EUROPEAN COMPETITIVENESS

Status Report & Economic Policy Implications

The European competitiveness is being put to the test. In addition to persisting **efficiency problems,** which, for example, materialize in an **incomplete and fragmented single market,** there are **structural challenges** to consider, including the green and digital transition and demographic change. On top of that, geopolitical shifts—in particular the deviation of foreign economic powers from the liberal international order—jeopardize the core of the European economic model. These developments have led to an increasing emphasis on resilience over economic efficiency. Due to **one-sided dependencies,** particularly on **strategically important goods** such as (critical) raw materials, semiconductors and special pharmaceutical ingredients, Europe is forced to readjust its place-based, industrial and trade policy.

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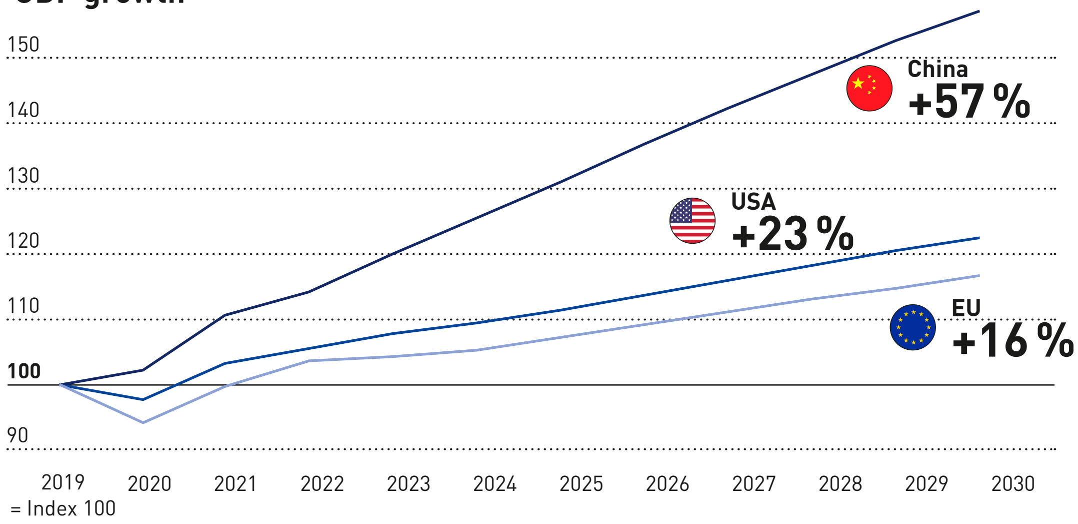
At the top of the world's largest economic areas, Europe competes with the US and China. Projections indicate that the EU will grow at a relatively slower rate than the other regions until 2030. This will widen the gap in per capita income compared to the US. Meanwhile, China is expected to continue catching up.

GDP growth



Source: OECD

	EU	USA	China
Share of global GDP (2022)	16.6	25.2	17.8
GDP growth 2024, change compared to previous year in %	0.9	2.1	4.7
GDP growth 2025, change compared to previous year in %	1.7	1.7	4.2
GDP/capita (2022, PPP in current international USD)	54,636	76,330	21,483

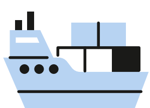
Source: World Bank, OECD Interim Report February 2024, EC Winter 2024 Economic Forecast

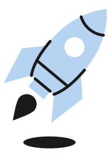
Dimensions for strengthening European Competitiveness


European Single Market


Green Transition


Workforce & Labor Market


Trade


Innovative Industry & SMES

Capital & Investments

European Single Market

The European single market has helped to position the EU as one of the most powerful trading blocs in the world. Apart from the single market for goods in the US, the EU is far more integrated in trade in both goods and services than other major economic areas, whose main sources of trade lie mainly outside their own territory.

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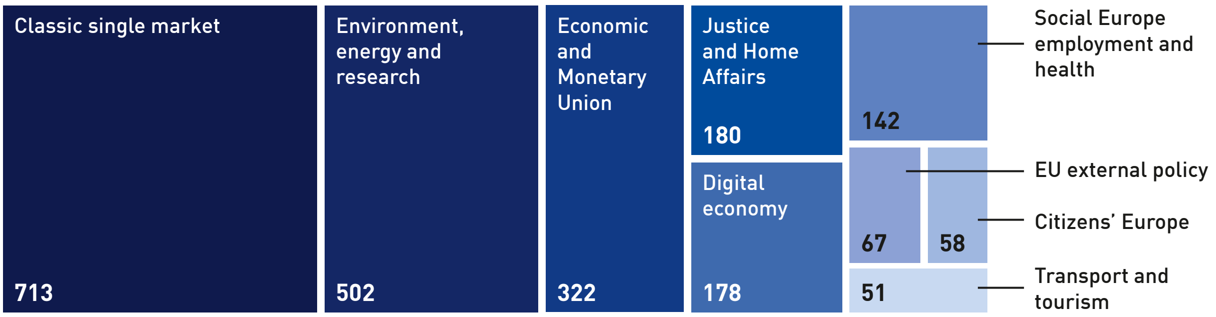
> **447 million People**
> **23 million Enterprises**
> **GDP (2022): 16,494 bill. EUR**
> **17.2 % of global GDP**

Cost of non-Europe (policy action), in EUR billion (annually)



Source: European Parliament

Goods

- Between 1999 and 2022, trade in goods between countries within the single market grew by 254 % (EUROSTAT).
- In 2022, 26.3 % of EU's GDP was traded as goods on the single market (European Commission).
- Differences between member states: While Slovakia, for example, traded 66 % of its GDP on the single market for goods in 2022, France's share was only 14 %. In the same period, Austria traded goods worth 25 % of its GDP within the single market.
- EUR 183 billion per year = untapped potential due to the incomplete integration of the single market for goods (European Parliament).

Services

- Growth in intra-EU service exports from 2010 to 2022 by 142 % to EUR 1,294 billion (EUROSTAT).
- In 2022, services amounting to 7.5 % of EU's GDP were traded on the single market (European Commission).
- EUR 297 billion per year = untapped potential due to the incomplete integration of the single market for services.

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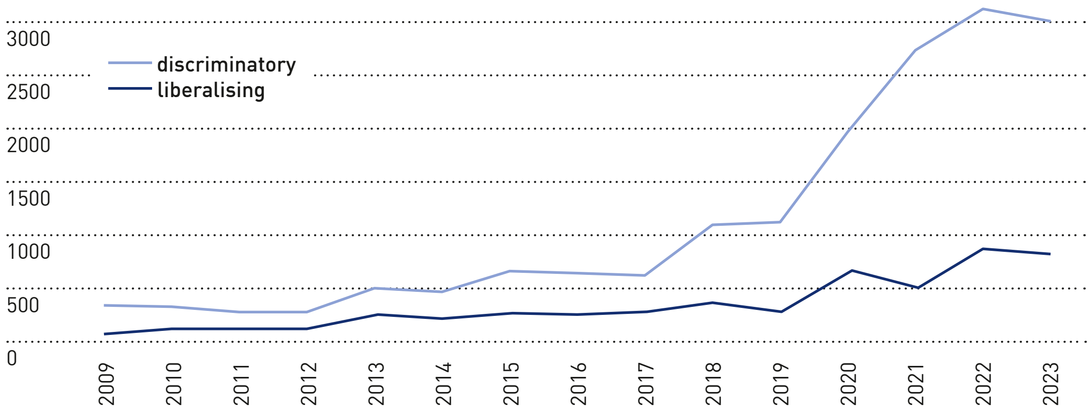
> **According to the European Parliamentary Research Service (EPRS), the European single market offers annual growth potential of EUR 713 billion by the end of 2029.**

ECONOMIC POLICY IMPLICATIONS

- Deepening and expanding the European single market with a focus on the single market for services
- Increasing resilience through uniform application, implementation and enforcement of existing single market regulations
- Cutting red tape for businesses

Trade

Number of new trade interventions, 2009–2023



Source: Global Trade Alert

In the past, the EU's common trade policy has led to significant welfare-enhancing effects.

- In terms of total exports and imports of goods and services, the EU is more open than the US or China.
  - → While China's trade openness has been on a downward trend since the mid-2000s, the EU's has been on an upward trend.
  - → Overall, the EU is now 30% more open to trade than the US and 70% more open than China (McKinsey).
- While economic measures become increasingly linked with social and security policy objectives in China and the US, the EU often defines social and environmental policy objectives as a prerequisite for trade policy initiatives.
- Currently, liberal trade principles are in decline, while protectionism and state aid are on the rise. The number of global discriminatory trade measures has increased significantly in recent years, with the EU being affected to a far greater extent than other economic areas (IMF).

Four of the eight countries most affected by new discriminatory trade interventions since 2019 are EU member states. As a small, open economy, Austria is ranked 26th in terms of its exposure to trade discrimination.

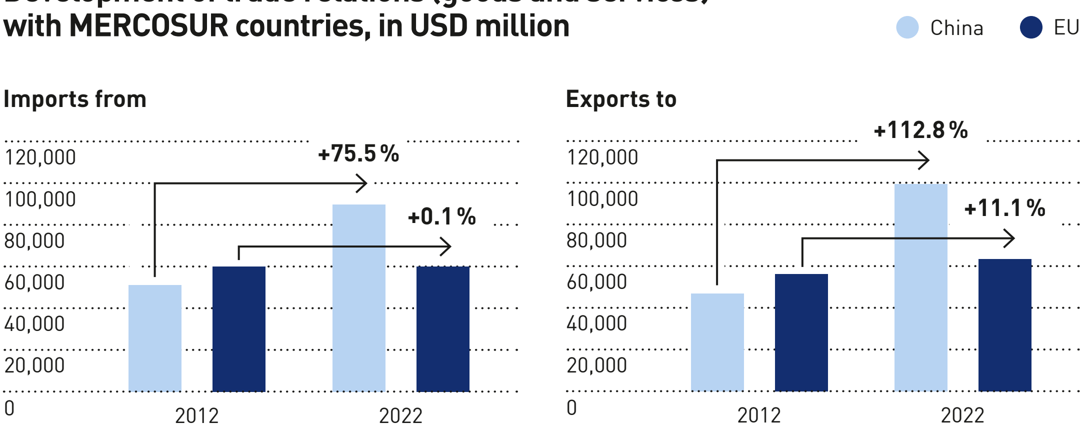
With a new wave of regionalism, Europe is in danger of losing out on trade compared to other economic powers. This is evidenced by the expansion of trade with the MERCOSUR countries, where China has been much more successful than the EU. While China has been able to increase its exports to MERCOSUR by as much as 75.5 % over the past ten years, the EU has seen a de facto stagnation in trade.

Countries most affected by discriminatory interventions, 2019–2023

1.	China	2,250
2.	USA	2,114
3.	Germany	1,892
4.	Italy	1,779
5.	United Kingdom	1,674
6.	France	1,645
7.	Netherlands	1,572
8.	South Korea	1,551
26.	Austria	1,010

Source: Global Trade Alert

Development of trade relations (goods and services) with MERCOSUR countries, in USD million

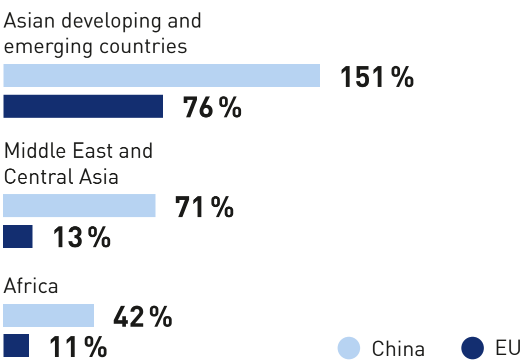


Source: IMF, own calculations

China also increased its trade volume **with developing and emerging Asian countries** twice as much as the EU between 2012 and 2022. Furthermore, China has fostered stronger economic ties with the Middle East and Africa than the EU.

> **Europe's trade relations are characterized by one-sided dependencies on other countries and economic areas.**

Change in trade volumes (imports + exports) 2012–2022, in %



Source: IMF, own calculations

In addition to its heavy dependence on fossil fuels from Russia, this is particularly true for its economic relationship with China.

- In terms of both imports and exports of goods, the **EU** is **more exposed to China than the US.**
- Over the past two decades, **EU imports from China** have increased almost **three times as much** as imports from the **rest of the world.**
- **The composition of imported goods has become "increasingly strategic",** too: in 1995, 40% of all EU imports from China were considered "potentially critical". Today, according to the European Commission, 70% of all imported product groups—ranging from electronics to pharmaceutical ingredients—fall within this category.
- One-sided dependencies often concern **future technologies** that are of crucial importance for the twin transition.

ECONOMIC POLICY IMPLICATIONS

- Pursuing an active trade policy
- Securing open strategic autonomy
- Ensuring security of supply

Green Transition

Between 2010 and 2020, Russia accounted for approximately 40 % of European natural gas imports, around 30 % of oil imports and over a third of coal imports (EUROSTAT).

To ensure a future-proof gas supply in Europe, initiatives have been taken to increase European port capacity for the arrival of LNG carriers.

- As of 2020, before the Russian war of aggression, LNG made up only 22 % of the EU-27's gas supply.
- By the end of November 2023, this share had risen to 42 %, while imports of Russian natural gas fell from 43 % to 9 % over the same period.

For European companies, the switch to LNG imports has resulted in **gas prices three times higher than in the US** in the medium term and **greater price volatility,** as the EU will have to compete with other (primarily Asian) consumers in the LNG market.

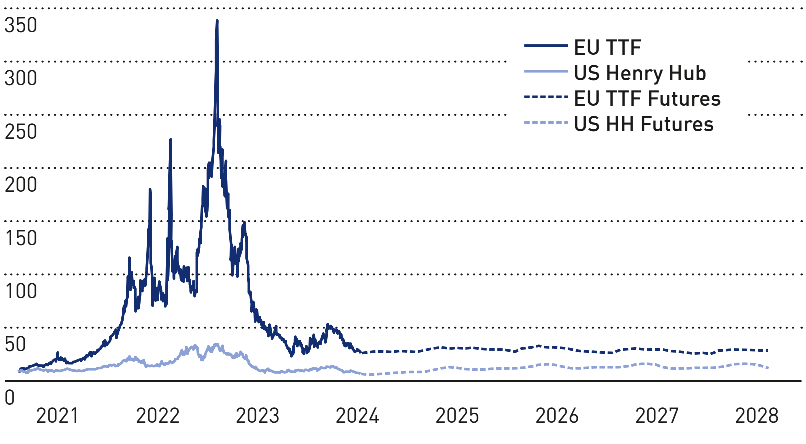
Electricity prices have multiplied in 2022, too. Especially energy-intensive industries face a significant price competitiveness disadvantage.

With a net import share of 63 % of its primary energy consumption in 2022, the EU remains **heavily dependent on third countries** to cover its energy needs. Some member states, such as Germany and Austria, are even more dependent on energy imports at 69 % and 74 %, respectively.

At the same time, the growth of **renewable energy** in the EU has been slow, accounting for only 23 % of gross energy consumption in 2022 and 14 % in 2010. Although individual countries such as Austria (share of 33.8 %) are making faster progress, the overall expansion remains insufficient.

Gas price development in the EU and the US

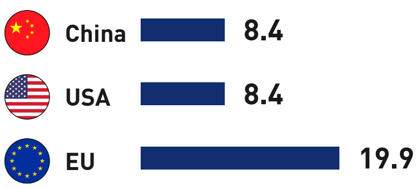
in EUR/MWh



Source: Trading Economics, Barchart

Europe remains heavily dependent on energy imports. Growth in renewables progresses slowly.

Average industrial electricity prices in EU countries and other countries in 2022, in Ct./KWh



Source: Prognos, vbw

ECONOMIC POLICY IMPLICATIONS

- Enabling the green transition
- Securing affordable energy prices
- Ensuring energy supply security

Innovative Industry & SMEs

The EU's industrial sector accounts for more than 20 % of the Union's economic output and 35 million jobs. Meanwhile, the Manufacturing Purchasing Managers' Indices (PMI) in the eurozone remained **below the growth threshold for twenty months now.** Apart from the cyclical economic weakness, mostly structural economic deficits put pressure on the competitiveness of the industrial sector.

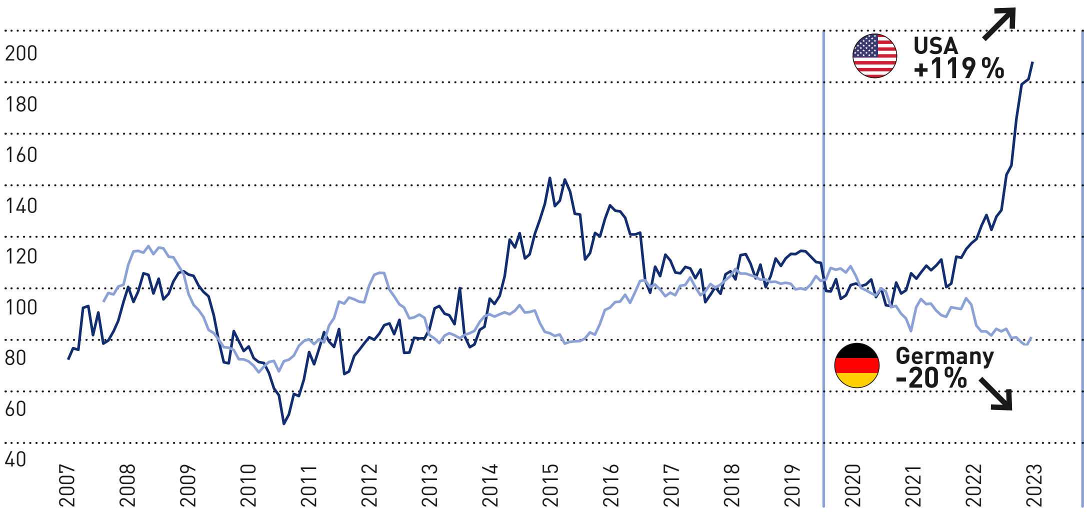
The industrial policies of other economic powers spill over and damage the price competitiveness of European companies. China and the **US** subsidize their industries with extensive funding programs.

- The **US Inflation Reduction Act (IRA)** targets the production of green energy technology—a key area in which European companies have previously been in the lead.
- The industrial policy instruments include, in particular, long-term (approx. 10 years) and uncapped tax credits (OPEX and CAPEX), which are linked to domestic content rules.

While the risk of deindustrialization grows in the EU, the US rapidly expands its industrial capacities.

- In this way, (price adjusted) investments in factory buildings in the US have more than doubled since 2021, even though the US economy is affected by high interest rates and construction costs, too. In comparison, real capital investments in the construction of new factories in Germany in 2022 were at their lowest level since the recession in the early 2010s.
- In 2023, USD 33.7 billion in federal funds (98 % of which in the form of tax credits) sparked green investments of a total of USD 220 billion, thus corresponding to a **multiplier of 5.5** (MIT CEEPR / Rhodium Group).

Real construction investments in factories, index 2020=100



Source: DESTATIS, Federal Reserve St. Louis

ECONOMIC POLICY IMPLICATIONS

- Pursuing an industrial policy offensive with simpler, more flexible and more comprehensive investment promotion instruments
- Simplification and acceleration of IPCEI and state aid procedures

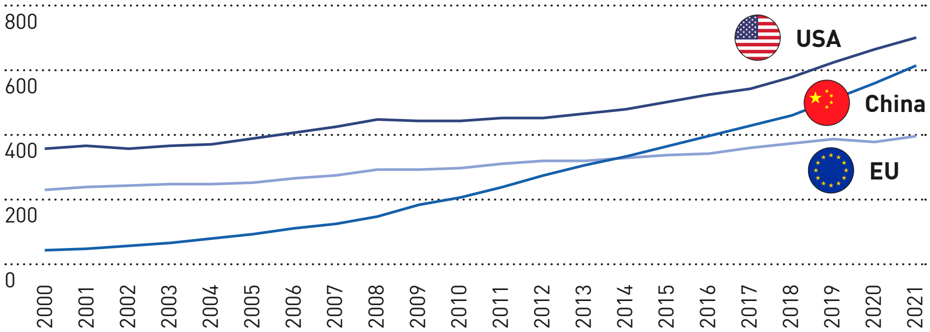
Innovation: decent starting position, but pressure is increasing. With **16 countries,** the EU has the largest number of innovation leaders in the top 25 of the Global Innovation Index 2023. However, a long-term observation shows that the **EU is losing touch with other economic areas in terms of R&D funding.**

- At the beginning of the 21st century, EU R&D spending accounted for 64 % of US spending but fell to 56 % by 2021.
- At the same point in time, China's R&D spending made up 17 % of EU spending. In 2014, China caught up with the EU. Nowadays, China spends 55 % more on R&D, thus, almost as much as the US.

These monetary figures are also reflected in the measurable output of the economic areas' R&D efforts. The EU's global share of patent applications related to the twin transition is declining, while China is rapidly catching up.

Development of gross expenditure on research and development

in USD billion



Source: OECD

ECONOMIC POLICY IMPLICATIONS

- Realizing a joint research and innovation agenda
- Implementing an EU framework program for international and interdisciplinary RTI-cooperation between industry and research

Workforce & Labor Market

The rapid increase in vacancies indicates a considerable shortage of labor and skilled workers.

Stagnating population growth in the EU, caused by demographic change, will continuously create a challenging labor market situation in the future. European population growth is very low and the group of 15- to 64-year-olds, i.e., the **working-age population, will shrink by 8 % by 2040 compared to 2015.**

The EU member states succeed only to a limited extent in integrating the existing workforce into the EU labor market. The US performs better in this regard.

The EU is lagging behind the rest of the world in terms of hours worked. It has not succeeded in recuperating the number of hours worked to pre-pandemic levels.

Average working hours per employee

in h/year

EU	USA	CHINA
1,593	1,681	2,136

Source: Prognos Economic Outlook

The digital and green transition has a huge impact on the labor market. While the demand for highly qualified workers is likely to increase, a loss of low- and medium-skilled jobs can be expected.

ECONOMIC POLICY IMPLICATIONS

- Leveraging the untapped potential of the European workforce
- Expanding skilled labor campaigns in third countries
- Increasing productivity

Capital & Investments

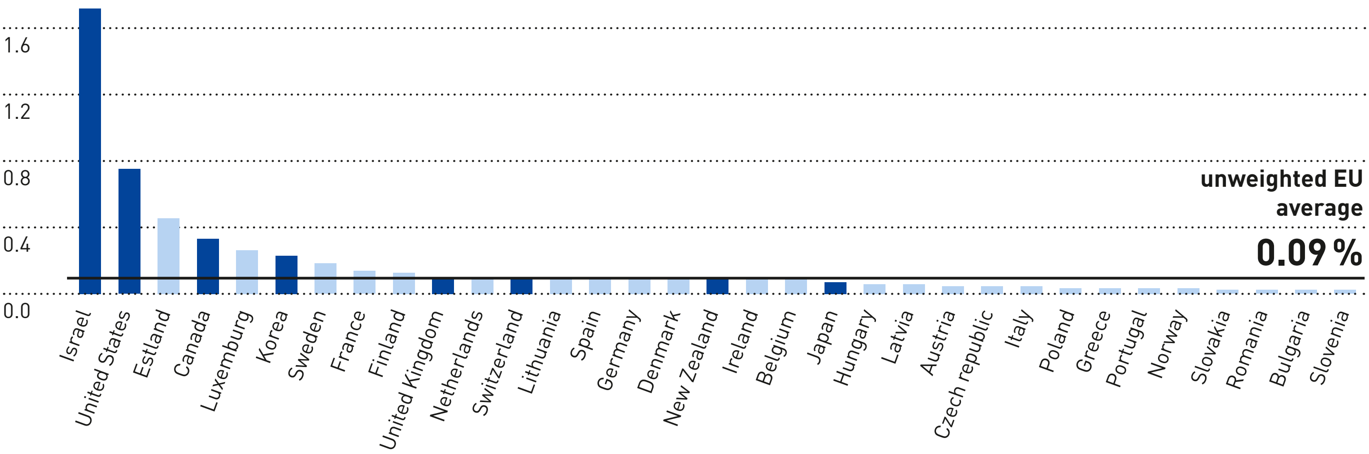
- Since the mid-2010s, the EU-27 have been recording **higher private gross fixed capital formation** than the US. In 2024, the private sector investment ratio of 18.9 % of GDP in the EU-27 will exceed that of the US by 1.5 percentage points.
- Since 2013, the ratio of public gross fixed capital formation to GDP in the EU-27 has been below that of the US, although there is a trend towards catching up. **Europe is becoming less attractive to foreign direct investment:** While the share of the EU-27 of the global FDI stock has remained constant at around 26 % over the last ten years, the US has shown a rise by around 5 percentage points, from 19.1 % to 24.3 %. Since 2013, the share of FDI in the OECD countries has also increased significantly to 67.2 %, while that of China has decreased to 7.7 %.
- **Capital markets in the EU are fragmented and undeveloped:** 4 of the top 6 countries for venture capital investment (Israel, USA, Estonia, Canada, Luxembourg, and Korea) are non-EU states. The unweighted average of venture capital investment in the EU countries included in the OECD data is only 0.09 % of GDP. In contrast, Israel (1.72 %), the USA (0.75 %) and Canada (0.32 %) display significantly higher figures.

ECONOMIC POLICY IMPLICATIONS

- Improving conditions for private investment
- Further development of the Capital Markets Union
- Ensuring sustainable public finances

Venture capital investments in 2022

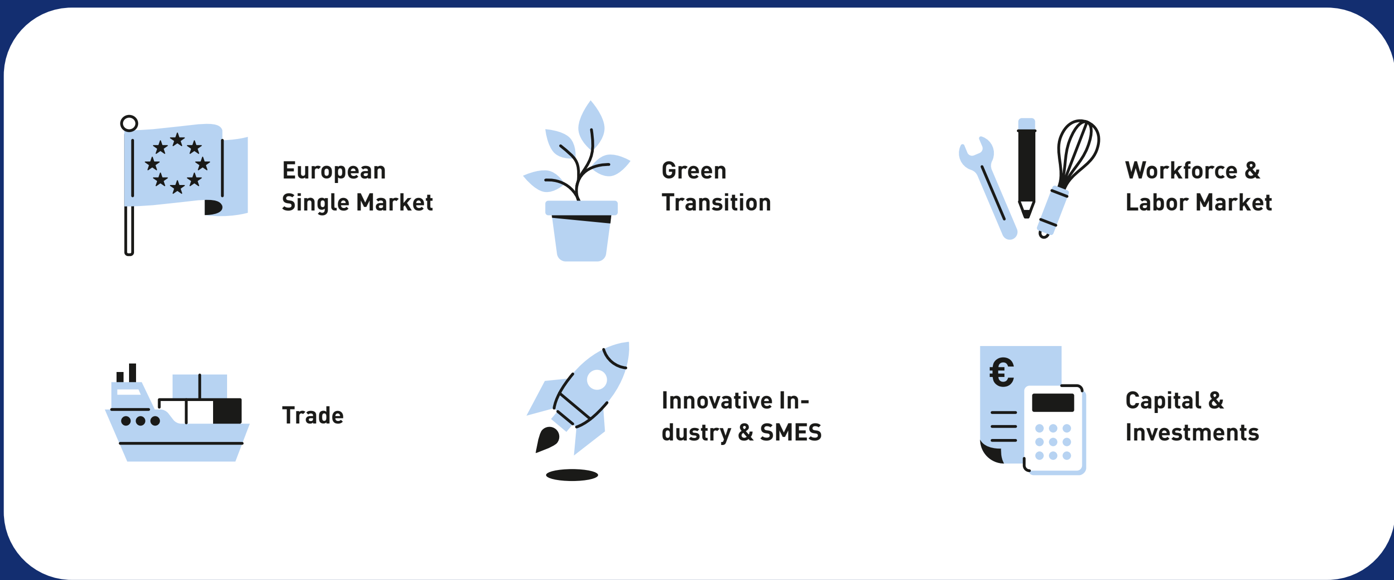
in % of GDP



Source: OECD

Conclusion

Dimensions for strengthening European Competitiveness



The European Economic Area, characterized by a single market based on free competition, a liberal trade policy and an investment-friendly environment, has ensured economic prosperity for decades. To continue this success story, swift action is needed to deepen the single market, pursue an active trade policy, secure energy supplies and set the course for industrial and innovation policy.

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