# THE THREATS TO THE EUROPEAN UNION'S ECONOMIC SOVEREIGNTY

## Memo to the High Representative of the Union for Foreign Affairs and Security Policy

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# 1 STATE OF AFFAIRS

Your predecessors rarely spoke to economists, let alone received memos from them. High Representatives deal with wars, conflicts and human disasters – and how to avoid them. Economists, and your colleagues in charge of economic issues within the Commission, deal with peacetime concerns: growth, inflation, jobs, public finances, trade, competitiveness. Every now and then, economic mismanagement results in a country entering your orbit (like Venezuela currently). Every now and then, an opposite transition takes place and economic development must be supported after peace or civil concord has been restored. But otherwise there has not been much communication between the foreign affairs and security sphere and the economic sphere. It is becoming clear, however, that in the current context increasing interlinkages between economics and power politics mean you must play a greater role in reinforcing and defending Europe's economic sovereignty. This memo summarises and expands on Leonard *et al* (2019) a June 2019 Bruegel and European Council on Foreign Relations paper that discusses in detail the economic sovereignty issue.

There were good reasons for the division between the foreign policy sphere and the economic sphere. Through the first decades of its history and up until very recently, the European Union took it for granted that the global system provided a functional framework for international economic relations. For sure, the economic rules were determined by power relations in the wake of the second world war. But in the years that followed, even the United States by and large kept to them. It regarded economic integration as conducive to the strength of the free world, and it stood by this principle even after the Soviet Union ceased to exist and was no longer a security challenge.

The EU has always believed in the primacy of economics. As a consequence, sovereignty for the EU as a whole was and remains first and foremost *economic* sovereignty. The collective capacity of the EU and its member countries working together to preserve their economic independence underpins the bloc's value to Europe's citizens. That argument is bolstered by the EU's ability to participate in defining the rules of the game for the global economy – what Chancellor Merkel calls *Handlungsfähigkeit* and the

were designed under the assumption that external economic relationships would be ringfenced from the interference of geopolitics. In this new context, it will be your responsibility and that of your Commission colleagues to redefine for the EU its concept of economic sovereignty and the instruments it intends to use to defend and promote it.

## 2 CHALLENGES

European economic sovereignty faces many threats, ranging from structural demographic and technological trends to lone-wolf hackers in their parents' basements revealing state secrets. But China and the United States represent specific and particularly difficult problems.

### China

China simultaneously pursues economic growth, technological development and geopolitical influence. For this reason,

about the reliability and implications of that alliance. Moreover, the Trump administration has actively reduced the support it gives to the multilateral order and has used its unique position within the global economic order to extract immediate economic gains or secure geopolitical goals. The dollar, the US's financial system and its current role as a hub for the global digital architecture provide the US with an unrivalled ability to use the global system to serve its own security goals.

On Iran – over which the crisis appears to be deepening at the time of writing – a 1996 EU regulation (Regulation (EC) No 2271/96) is intended to protect European companies from US enforcement of including trade, foreign direct investment, finance and currency internationalisation. But what it needs is a more encompassing strategy for the new context in which partners and competitors are prepared to let economic relationships serve broader geostrategic goals. Such a strategy should be based on, first, a definition of what the EU considers the key tenets of economic sovereignty; second, on a clarification of the EU's goals and strategy for achieving them; and third, on a review and reform of the EU toolkit so it has the right instruments.

The starting point should be a confirmation that it is in the EU's interest to remain highly open and intertwined with international partners. In the US, there is a growing debate about decoupling from China. But a decoupling strategy cannot be in the EU's interest. First, EU prosperity critically depends on global economic exchange. Second, China is set to become an increasingly relevant trading partner for the EU and it is therefore in the EU's interest to engage with China. Third, while the US is in direct geopolitical confrontation with China, the EU is not. The central challenge for the EU is therefore to uphold its economic sovereignty while staying highly intertwined with both the US and China.

## 3 RECOMMENDATIONS

The EU needs a change of mindset to address threats to its eco-

both economic growth and national security. State aid intended to maintain technological competitiveness can easily become ine cient jobs programmes. E orts to broaden the use of the euro could easily morph into subsidies for favoured banks. ese risks imply that such measures need to result from a considered process that is capable both of weighing the trade-o s between economic e ciency and national security and of maintaining a reasonable distance from special interests.

To both achieve a change in mindset and to give it institutional expression, we recommend a four part strategy for the EU:

1. **An economic sovereignty agenda**
2. **A reformed policy toolkit**
3. **Effective machinery**
4. **A flexible implementation strategy**

### An economic sovereignty agenda

As a priority, we suggest that when you take o ce you start by monetary giant whose initiatives measure up to those taken by other major powers. It has done this while ensuring levels of transparency, integrity and effectiveness that meet the best global standards.

But the EU has to adapt its policy toolkit to cope with the new reality of greater geopolitical and geo-economic competition. New initiatives are necessary in several key fields, some of which concern you directly:

1. Building on a strong and independent competition policy, the EU should define precise procedures to take into account economic sovereignty concerns in competition decisions. European Commission merger control and the abuse of dominant position decisions should continue to be based on economic criteria and on independent, legally-grounded assessments. Importantly, competition policy exists to protect consumers not producers. The EU needs to avoid politicising competition enforcement or it risks capture by powerful producer interests. However, competition policy decisions should also take into account the broader scope of internationalised markets and whether incumbents' market power can be tamed by the threat of potential entry. To address cases in which competition policy decisions might raise security concerns, you as High Representative should be given the right to invoke a security clause and object to a decision proposed by the competition commissioner.

2. Because foreign investment gives access to the entire internal market, the EU cannot regard investment control as a purely national affair. It should develop a common approach and common procedures for the screening of foreign investments and empower the Commission with the right to recommend on security grounds the prohibition of certain foreign investments. The Council should be given the right to decide by qualified majority to block foreign investments based on a Commission recommendation, in which you will play a strong part. The current investment-screening mechanism is a step in the right direction

but it is insu cient to tackle the common dimension of decisions relating to foreign investment. e EU should also develop instruments, such as a dedicated investment fund, to o er member states alternatives when foreign investments are disallowed.

3.

### Effective machinery

European governance was not built to implement an encompassing economic sovereignty strategy, but rather to manage sectoral policies separately. Reforms are thus needed, as follows:

**A European Commission Economic Sovereignty Committee:** the European Commission has already prioritised making the EU a stronger global player. e priority area brings together several relevant European commissioners (foreign and security policy, neighbourhood and enlargement, trade, international cooperation and development, civil protection and humanitarian aid under your chairmanship). It would introduce an economic-security element by including key commissioners whose portfolios are not generally thought of as having sovereignty implications, including competition policy, economic and nancial a airs, and research, science and innovation. It will be important to create strong links with the sta of similar bodies in EU member states, to enable coordination of economic sovereignty e orts across the levels of governance.

In addition, a **Committee on Foreign Investment in the European Union,** sta ed by some of the economic sovereignty sta and containing representatives of relevant directorates-general, should be charged with making recommendations on the national security implications of large foreign (non-EU) investments or mergers in the EU. is committee would present its recommendations to you and the College of Commissioners. Also, an o ce of **Financial Sanctions Enforcement** sta ed by representatives of the European External Action Service, the Directorate-General of Economic and Financial A airs, and relevant member-state representatives, would closely coordinate with banks and other nancial institutions to ensure that European sanctions regulations are strictly enforced. It would also impose penalties on entities that violate sanctions.

### A flexible implementation strategy

**Implementing these changes cannot be just a Brussels-based EU-wide effort**. Many relevant powers remain with the member states and economic sovereignty issues can be divisive