Report on

Industrial Policy in Europe

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Introduction

Europe has a strong industrial base that generates 75% of its exports and 75% of private research and innovation. Industry in Europe has managed to remain competitive on the international markets thanks to high levels of education, centres of industrial and academic excellence, strong legal systems, an Internal Market of over 500 million people and low levels of corruption.

Despite these strengths, it is becoming increasingly challenging for European industry to compete in the global market. High energy prices in comparison to the levels in the United States (US), weaken the competitiveness of a large part of European industry and in particular the energy-intensive industries such as steel and chemicals. The situation is different in the EEA EFTA countries Norway and Iceland where energy prices are relatively low and can offer industries an important competitive advantage. Complicated and slow administrative procedures disencourage entrepreneurs to undertake business opportunities. There is also a need for increased research and innovation to face the transition into a modernised economy based on new technologies and sustainability. This transition needs financing which, after the financial crisis, has only become more difficult.

Initiatives taken in the area of industrial policy in the European Union (EU) affect several other sectors such as trade, Internal Market, research and innovation, employment, and energy, environmental and climate policies. As the EEA EFTA States are deeply integrated in the Internal Market, many of the tools used for the EU industry also influence industry in these countries.

The purpose of this report is to highlight the main initiatives taken by the European Commission (Commission) over the last years in the area of industrial policy, and to take a look at the new Commission's plans for industrial policy.

Industrial policy in Europe from 2010 to 2014

The Lisbon Treaty establishes the competences for the field of industry within the EU, which are shared between the EU Member States and the Commission. In order to ensure the necessary conditions for the competitiveness of industry, the Member States and the Commission consult each other and are coordinated in their actions. The EU is therefore limited in what it can do in the area of industrial policy.

The Commission has set a goal that European industry should account for 20% of the EU’s gross domestic product (GDP) by 2020. Over the last five years, the Commission has launched three
communications on industrial policy. The overarching aim of these policy documents is to support policy goals and the flagship initiatives of the Europe 2020 strategy, which seeks to improve Europe’s economy in three main areas: knowledge and innovation, competitiveness and increased employment. The trend is also to have a more horizontal approach to industrial policy in Europe and view the initiatives in greater connection with policies in other areas such as competition, trade, innovation and energy, since all of these areas influence industry. This is a trend that could pose challenges for the EEA EFTA States since the consideration of what is and is not included in the Agreement on the European Economic Area (EEA Agreement) is based on a clear delineation of the sectors covered.

The reasoning behind this change of approach lies in the challenges that have been identified in the European industrial sector over the last decade, such as uneven progress in the sector, a weak internal demand and inflexible regulations. The latter is especially challenging for small and medium-sized enterprises (SMEs), since the burden created by administrative costs and regulations can be considerably harder for small companies to deal with. Lack of investment in innovation and high energy prices in Europe are also weakening competitiveness (Norway and Iceland are an exception to the latter with relatively low energy prices that can offer industries a competitive advantage).

In order for European industry to meet the global competition, the Commission has placed importance on investing in innovation, improving market conditions and ensuring access to capital and skills. Given that the industry is trading in both goods and services, maximising the potential of the Internal Market has also been an important factor. A particular focus in this regard has been on the implementation phase of existing initiatives, in order to exploit their full potential.

The new European Commission: the future of new initiatives

In November 2014, the new Commissioner for Industry and Internal Market, Elżbieta Bieńkowska, outlined her priorities for European industry. Four main pillars were mentioned as being necessary for industry. First, better access to markets, both in the EU and beyond; second, access to resources; third, the ability to invest in innovation and modernisation; and fourth, a favourable business environment.

The new Commission is continuing the horizontal approach, focusing on faster implementation of existing legislation and the potential of existing initiatives. It also points to the same challenges as the former Commission that need to be tackled by both the Member States and the EU in order to meet
the overall industrial policy goals. These include difficulty in finding new financing, in particular private investments in the sector, and the excessively high administrative burden in Europe. High energy prices, delocalisation of European companies and the need to modernise EU competition rules were also identified.

However, there has been an overriding shift in EU policy with the new Commission. One of the main changes is that the number of new initiatives has been reduced drastically. In his political guidelines for the Commission, Commission President Juncker mentions industry in his list of priorities, but not as a separate policy area. It is now included in the Internal Market section. Under the priority “A deeper and fairer Internal Market with a strengthened industrial base”, President Juncker reiterates the previous Commission’s goal that industry should account for 20% of the EU’s GDP by 2020, from 16% as it is today. He underlines that in order to obtain this goal there is a need to reinforce a strong and high-performing industrial base for the Internal Market. Important industry sectors in which the EU should be a global leader are the high-value sectors such as the automotive, engineering, space and pharmaceutical industries. The Commission wants to achieve this, among others, by stimulating investment in new technologies and improving market access.

In the Commission’s plan for new initiatives in 2015, five initiatives are listed under the Internal Market and industry section:

- Internal Market strategy for goods and services
- Labour mobility package
- Capital markets union
- Financial institutions framework
- Aviation package

This reveals that three of the former main initiatives for industrial policy have not been prioritised for this year, i.e. the previously announced roadmap for actions to support industry, the revised Small Business Act for Europe and the proposal to promote the circular economy.

If, however, we take a look at some of the policy areas that will influence industry, such as Internal Market policies in the area of goods and services, in the energy sector and on the regulatory side, we find several initiatives in the Commission work programme for 2015, some of which are cited as main priorities for the Commission. None of these are explicitly on industry policy, but they will nevertheless be important for the industrial sector, indicating how the horizontal approach has started to be embedded in this area.
Instruments for European industry

Market access and better regulation

The Internal Market has been a success for both the EU and the EEA EFTA States, as it provides companies in the EEA with a large home market. It does, however, have strong potential for further growth, especially if its rules are simplified.

In 2015 the Commission will present an Internal Market strategy for goods and services, aimed at improving standardisation in key areas in the industrial and services sectors and looking at the rules on professional qualification. A new initiative will also be launched on the Digital Single Market package, which will cover EU data protection, telecommunication, cyber security, copyright issues and mainstream digitalisation across several policy areas.

Legal predictability is crucial for business, and the need to have a business-friendly regulatory environment in the Internal Market is important. Harmonised standards and regulations across the Internal Market will minimise the burden on businesses. This work is high on the Commission’s agenda, and “better regulation” is the main portfolio of First Vice President, Frans Timmermans. One of his tasks is the programme for Regulatory Fitness and Performance (REFIT), where the main goal is to simplify EU law, reduce regulatory costs, and withdraw legislative proposals and repeal legislation that are no longer needed. During 2015, 79 REFIT actions will be taken, and the Commission has decided to withdraw or modify 80 pending proposals.

On the list of withdrawals are several proposals in the field of the environment, among them the legislative proposal on the circular economy (waste policy). This has stirred resistance both in the European Parliament and among ministers in the EU Member States. The Norwegian Minister of Climate and Environment, Ms Tine Sundtoft, wrote a letter to the European Commission in December 2014 where she asked for the proposal on the circular economy not to be withdrawn. She argued that the proposal was important for the transition to a greener economy. She also referred to a letter from 11 EU Member States arguing the same case.

In his response in February 2015, the Commissioner for the Environment, Maritime Affairs and Fisheries, Karmenu Vella, underlined that the Commission “is fully aware of the importance of environmental and economic challenges related to the circular economy”. It is the intention of the Commission to “withdraw the waste proposal in order to make way in 2015 for a more ambitious approach that can be more effective”. The aim is for the revised proposal is to better reflect the situation in different Member States, and through a broader approach to address all elements of the
cycle, “inter alia looking at supporting better product design and sustainable consumption on the one hand, and at facilitating the development of a market for recycled products and raw materials on the other hand”.

In a meeting with Commissioner Vella in Brussel in March, Minister Sundtoft underlined that the green transition represents opportunities for better productivity, more efficient and healthy cities and low carbon development. She supported the broader approach to the circular economy and stressed that ambitious, long term recycling targets are central policy instruments that stimulate the reuse of resources and the establishment of markets for reused materials. However, the targets should be designed in a way that they do not encourage recycling of prioritised hazardous substances.

Another initiative for 2015 is a proposal for an inter-institutional agreement on better law-making. This aims to update a common understanding within the EU when it comes to better regulation. The better regulation agenda is especially important for SMEs because the impact of regulatory and administrative costs is much higher on them than on larger companies. As deeply integrated members of the Internal Market, the EEA EFTA States are positive with regard to the initiatives taken by the EU in this field.

Increased access to external markets is also crucial for the growth of European industry. The EU’s negotiation of free trade agreements (FTAs) with strategic partners is key in this respect. The negotiations currently taking place between the EU and the US on a Transatlantic Trade and Investment Partnership (TTIP) are one such example. The four EFTA States also have a proactive trade agenda and are currently negotiating FTAs with strategic partners around the globe. Currently, EFTA has 25 FTAs in force covering 35 countries. The positive impact of FTAs can be well observed when looking at the example of South Korea. The trade balance of the EU with South Korea evolved from a deficit of EUR 3,8 billion in 2011 (prior to the coming into force of the FTA) to a surplus of EUR 4,0 billion in 2013. Within the same period of time the trade balance between the United States and South Korea deteriorated quite significantly. The EFTA States also have a FTA with South Korea since 2006.
**Energy and climate**

Between 2008 and 2012, EU retail energy prices for industry grew on average by 3.5% a year and gas prices by 1%. This makes industrial energy prices within the EU twice as high as those in the US and Russia. The development in energy prices is a great challenge for the competitiveness of energy-intensive industries.

The new Commission is continuing to underline that strengthening the Internal Energy Market could promote competition, increase energy security and reduce energy cost. The EEA EFTA States are part of this market through the EEA Agreement and are cooperating with the EU on a range of energy issues. Energy and climate policy also features regularly on the EEA Joint Parliamentary Committee’s agenda and the resolutions adopted at its meetings support the EU’s policy of completing the Internal Energy Market.

The fact that the new Commission has established the role of Vice President for Energy Union also underlines the importance of a more coherent energy policy for the EU. The priorities for the Energy Union were outlined in February 2015. This strategy has five mutually-reinforcing and closely interrelated dimensions designed to bring greater energy security, sustainability and competitiveness:

- Energy security, solidarity and trust;
- A fully integrated European energy market;
- Energy efficiency contributing to moderation of demand;
- Decarbonising the economy, and
- Research, Innovation and Competitiveness

Renewable energy is also a high priority for the EU and a growing industrial sector. European renewable energy businesses have a combined annual turnover of €129 billion and employ over a million people. EU companies have a share of 40% of all patents for renewable technologies.

Energy questions are of high importance for the EEA EFTA States, as both providers of energy and hosts of energy-intensive industry. Norway is also the main supplier of natural gas to the EU and the second biggest supplier of energy products (oil and natural gas taken together) after Russia. The considerable experience that Iceland and Norway have with renewable energy and the cooperation between the EU and Norway on carbon capture and storage also demonstrate the EEA EFTA States’ integration in Europe in the field of energy.
In February 2015, the Norwegian Government presented a White Paper on its climate commitments for the period after 2020 that aims to join the EU 2030 framework for climate and energy policies in order for Norway and the EU to jointly fulfil their climate targets. Norway will reduce emissions by at least 40 per cent by 2030 which is in line with the EU's climate targets and take the initiative to enter into an agreement with the EU about a joint fulfilment of the targets. Negotiations with the EU on the agreement are foreseen to start in 2016.

An important tool for achieving the targets set in the 2030 framework is the EU Emissions Trading System (ETS), which the EEA EFTA States already are part of through the EEA Agreement. ETS has an important influence on European industry covered by the trade of emission allowances.

In the EU's 2030 framework, emissions covered by the ETS shall be reduced by 43% in 2030 compared to 2005. Approximately half of Norwegian emissions are covered under this scheme. In the sectors not covered by the ETS, the EU will reduce overall emissions by 30% compared to 2005. Member States will need to reduce their emissions by between 0% and 40% according to their GDP. With the new policy, Norway will after negotiations with the EU also take on a specific emissions reduction target for the sectors not included in the ETS in line with the EU Member States.

The ETS is currently being revised and the outcome of this will influence the conditions and competitiveness for European industry – also in the EEA EFTA States. In order to tackle the supply-demand imbalance in the ETS, the European Commission proposed to introduce a "market stability reserve" (MSR), a mechanism that regulates the market against big fluctuations, for the period after 2020. On 22 January 2015, the Committee on Industry, Research and Energy (ITRE) of the European Parliament failed to agree on the MSR proposal due to lack of consensus on its start date. However the Committee on the Environment, Public Health and Food Safety (ENVI), which is the leading Committee on this topic, has voted in favour of introducing MSR in 2018, earlier than originally planned. The ENVI Committee also agreed on the transfer 900 million tons of back loaded emissions allowances, that were held back in 2014, to the reserve instead of re-entering them into the ETS market and the selling of 300 million allowances up till 2025 to finance industrial innovation. Trilateral negotiations between Commission, Council, and Parliament on this issue are supposed to take place in March and April. The negotiations are said to be challenging due to certain resistance in the Council to introduce the MSR before 2021. The Latvian chairmanship of the EU intends to conclude the negotiations by the end of its term in June 2015.
Liechtenstein is currently working on its commitments for the period after 2020. Energy and climate legislation plays an important role for Liechtenstein. Within 50 years Liechtenstein developed from a mainly agricultural state to one of the most highly industrialized countries in the world. The high value-added development until today is particularly due to the strong industrial sector and financial services, while the public sector of the national economy is comparatively small. From 1990 until 2012 the country’s GDP experienced a growth of about 140%, with an increase of population of around 25%. At the same time Liechtenstein managed to decouple its economic growth from its greenhouse gas emissions. Despite the growth of its economy and the increase in population Liechtenstein’s emissions are today below the levels of 1990. The implementation of EEA relevant climate legislation in the past such as the EU ETS or the introduction of emission limits for new passenger cars were and still are important drivers for a low carbon economy in Liechtenstein.

On 27 February 2015, Switzerland became the first country to submit to the UN a text outlining what its national contribution to limit climate change will be, ahead of climate talks in Paris in December. Switzerland is promising to reduce its greenhouse gas emissions by 50% in 2030, corresponding to an average reduction of greenhouse gas emissions by 35 percent over the period 2021-2030. By 2025, a reduction of greenhouse gases by 35 percent compared to 1990 levels is anticipated. Carbon credits from international mechanisms will partly be used. The intended nationally determined contribution (INDC) is subject to approval by Parliament. Since Switzerland submitted its INDC, the Latvian chairmanship of the EU and the European Commission have also done so on behalf of the EU.¹

Iceland has been harnessing renewable resources in a sustainable manner for more than 80 years. Today, 99% of space heating is from renewable resources and around 76% of final energy consumption. On climate commitments, Iceland aligns itself with the EU through the Kyoto Protocol and participates in the so-called “EU bubble” for the second commitment period of 2013-2020. Iceland will soon present its commitments for the post-2020 global climate change agreement to be signed in Paris this year.

¹ http://www4.unfccc.int/submissions/indc/Submission%20Pages/submissions.aspx
Research and innovation

Shortly after she came into office, the new Commissioner for Industry and Internal Market stated that industrial policy had to be built on knowledge and should play on Europe’s strengths, such as high levels of education and centres of industrial and academic excellence.

To manage the transition into a modern industry based on technologies that support a sustainable way of living, Europe needs more research and innovation. Further financial efforts are, however, necessary to support this and to achieve the Europe 2020 target of spending 3% of GDP on research and development in Europe. Several initiatives have already been launched in order to increase these efforts. The Horizon 2020 Programme will provide close to EUR 80 billion, and the Multiannual Financial Framework 2014-2020 makes at least EUR 100 billion available to financial investments by the EU Member States through the European Structural and Investment Funds.

The EEA EFTA States participate in Horizon 2020 through the EEA Agreement in addition to a range of other EU programmes. They also contribute with 1,8 billion euro in the current programme period to 16 beneficiary states in the EU through the EEA and Norway Grants. Several of these programmes focuses on areas of importance for the industry such as green technology, innovation and research.

Private capital and investment is also crucial for achieving increased research and innovation in Europe. Among the initiatives aimed to attract investment is the Commission’s EUR 315 billion investment plan for projects related to energy, transport, IT, infrastructure and SMEs. This package could potentially attract private investors and is one of the top priorities for the Commission. Furthermore, EU member states and possibly also third countries could contribute to this ambitious investment plan, in order to support projects of added common value across borders.

Another priority area is improving the regulatory conditions for innovation with measures for entrepreneurship, intellectual property and standards.

Concluding remarks

The priorities of the new Commission seem to favour an increasingly horizontal and integrated industrial policy approach than we saw with the former Commission. In order to overcome some of the challenges for industry in Europe, it might be constructive to look at industrial policy in greater connection with other policy areas, rather than as a separate policy. There is a risk, however, of an
industrial policy without any independent initiatives. It is therefore highly important that the industrial aspect is not forgotten when developing policy in other areas.

Blending the various policy initiatives with Internal Market policy could pose challenges for the EEA EFTA States since the consideration of what should and should not be included in the EEA Agreement is based on a clear delineation of the sectors covered. For the EEA EFTA States, it is important to monitor the development of industrial policy in the EU and the initiatives that influence the conditions for industries in the EEA. Overall, all envisaged measures should be in line with the goal to increase the competitiveness of the industrial sector inside the European Union and the EEA/EFTA countries compared to other competing regions in the world. Special attention should be given to the further development of the relations between the EU, the EEA countries and Switzerland.