

COMPETITIVENESS AND EUROPEAN GOVERNANCE

Posted on 06/05/2025 by Naider

Europe must invest. The Letta and Dragui reports state this in black and white, and important steps are being taken in this direction. However, I am afraid that the **main initiatives currently underway reveal important contradictions in European policy.**

First of all, the European Commission has drawn up and published in January 2025 the '[Competitiveness Compass for Europe](#)'. On its first page, the compass makes a rough diagnosis of the situation, which leaves no doubt about the seriousness of the patient's situation, and sets a **very ambitious target, highlighting the need to invest** in the electricity grid, in the mobility system, in several sectoral plans, in defence, and so on.

"What is at stake for Europe is not just economic growth, but the future of its model. If Europe does not increase its productivity, it risks being trapped on a low-growth path, with lower incomes for workers, less welfare for the disadvantaged and fewer opportunities for all".

"Europe must be the place where tomorrow's clean technologies, services and products are invented, produced and marketed, while staying the course towards climate neutrality."

Secondly, the same Commission, responding to political demands for a significant strengthening of defence capabilities and in line with its competitiveness compass, presented in March 2025 [the ReArm Europe Plan/Readiness 2030](#), in which it proposes to mobilise more than EUR 800 billion in defence spending. 800 billion in defence spending, most of which will come from **relaxing national fiscal rules**, allowing countries to exclude defence spending from their net expenditure paths (a maximum of 1.5% of GDP per year for up to four years).

Finally, **Germany**, which suffers particularly from competitiveness problems and has technically been in recession since the beginning of 2024, has lifted its own constitutional constraint and will launch a **major fiscal expansion plan** of more than one trillion euros over the next ten years, significantly increasing its investment in both defence and security, as well as in improving its infrastructure.

In all three cases, the need for investment is clear, but so are the contradictions of European policy.

In order to invest in defence, Europe is prepared to make an **exception** similar to the one it made to combat the consequences of a structural crisis such as the Covid 19 pandemic and **to allow European countries to take on more debt** than the fiscal rules that will come into force in April 2024. However, a compass is on the table to correct the major problem of competitiveness that is hampering the future and the welfare of citizens. It shows the way forward, but does not clarify **where the economic resources will come from to tackle the serious innovation backlog and resolve the obvious contradictions between decarbonisation and competitiveness.** In my view, and in line with the Letta and Dragui reports, Europe urgently needs additional resources for investment, because more coordination, more protectionism, new plans, strategies and laws and promises of less bureaucracy are no longer enough.

The hope that this will be the case comes from the step taken by Germany. Its expansionary fiscal policy, despite the escape clause for defence investment, is **in clear contradiction with European fiscal rules** (Germany would move from a debt-to-GDP ratio of 63% in 2024, which is already above the set standard, to a long-term ratio of over 100%; see Bruegel '[Germany's fiscal rules dilemma](#)'). However, there is no doubt that the train wreck between Germany and the Commission will be resolved in favour of the former. It is inconceivable that the promises of the new German coalition government, backed by the ballot box and its parliament, will come to nothing on the pretext of the need to comply with European rules.

On the other hand, it is unrealistic to think that the Commission is prepared to put European unity itself at risk in a situation where it may be legally right but not legally strong: Europe needs to invest, Germany has the capacity to do so and, moreover, it is good for all countries without exception, as the financial markets are already discounting it.

In any case, this does not detract from the fact that it is a good time for countries that have had to endure the rigours of austerity prescriptions in recent times, imposed among others by Germany, to point out the double standards that are used when the crisis directly affects the most powerful.

How will the problem be solved in the end? No one knows, but in the short term the simplest and most straightforward way would be for the Commission to arbitrate an escape **clause from fiscal rules that gives all countries the freedom to invest in competitiveness** in the same way that has already been allowed for defence spending. This would give Germany a free hand to deploy its policies and open the door to the necessary investments of countries like Spain, France and Italy whose budgets are severely constrained by European fiscal rules (their public debt stock is above 100 per cent of their GDP in 2024), putting them all on an equal footing.

In the long term, however, Europe needs to **rethink the adequacy of its fiscal rules**. As the Great Depression of 2008 showed, and the current situation makes it all too clear, they are nothing more than 'sticks in the wheel' that hinder and slow down the fight against severe crisis situations and end up jeopardising European unity itself.

It is time to recognise once and for all that fiscal rules and European economic governance itself are useless. I fear, however, that **the countries of the Union are far from being ready to cede sovereignty and move forward in the construction** of a more federal Europe, which is the true and, almost certainly, **the only effective solution** for the 'Old Continent' to continue to play a relevant role in the global concert of countries. For the time being, I fear we will have to settle for **a short-term solution that provides the means to be able to invest**.

