

Growth and competitiveness challenges and priorities in the EU

Introduction

The Chair observed that the European Union is clearly facing significant challenges in terms of growth and competitiveness. While the competitiveness gap between Europe and the US is gathering, Europe excels in terms of stability. In 2024, half of the world's population participated in elections, including many EU member states. These countries delivered relatively positive outcomes, maintained political stability, and experienced no substantial shifts in policy direction.

It required instability in the US for Europe to realise how positive its stability is compared to others. The same is true with regard to income inequality, which in Europe is the lowest in the world. Unlocking higher growth will come from adding scale in the single market, and bold national reforms.

1. The time to act is now

1.1 Europe's prosperity is in peril

An official remarked that the World and Europe in particular have been exposed to an exceptional series of shocks. The world experienced a pandemic and the Russian invasion of Ukraine. The disruption to Russian gas supplies had a significant impact on Europe. Europe now faces tariffs imposed by the United States and heightened global trade tensions. These developments have exacerbated longstanding structural challenges within Europe. In order to sustain its living standards and uphold the social contract, Europe must address its poor medium-term growth prospects while contending with long-term fiscal pressures. European per capita GDP is currently 30% lower than that of the United States, with 70% of this disparity attributed to a persistent productivity gap.

1.2 Europe's competitiveness gap with the United States has become a priority issue for all EU leaders

An official referred to the Polish proverb, 'Strength lies in peace'. Ongoing global challenges, including the trade war between the United States and China, have left Europe somewhat sidelined. However, political stability within Europe is a valuable asset, and potentially a financial one. Europe is not engaging in radical reforms. Figures such as Valdis Dombrovskis are tasked with pursuing simplification agendas, carefully analysing the practical impact of EU legislation on businesses. The Commission is maintaining a stable regulatory environment, which is a key advantage for business confidence. While no radical changes are underway, ongoing negotiations on files such as the Corporate Sustainability Reporting Directive (CSRD) and

the Crisis Management and Deposit Insurance (CMDI) framework are progressing steadily.

20 years ago, similar concerns were raised regarding Europe's competitiveness gap with the United States. What has changed is the degree of urgency and political attention. Competitiveness is viewed as central to Europe's future. As a result, it has become a core theme of the Polish EU presidency, and a frequent subject of discussion at Economic and Financial Affairs Council (ECOFIN) meetings.

1.3 Many of the challenges confronting Europe are long-standing, but recent developments may serve as catalysts for change

An industry representative stated that many of the challenges confronting Europe are long-standing, but recent developments may serve as catalysts for change. The imposition of tariffs on trade increases the risk of recession in both Europe and the United States. This heightened vulnerability reinforces the need for Europe to act as a unified single market and exert global economic influence.

While the response to these shocks must be coordinated at the EU level, there is also a critical role for national governments. These must move beyond a traditionally cautious approach and adopt more proactive strategies to promote a business-friendly environment and incentivise private investment.

1.4 Broadening investment opportunities for European businesses

An industry representative noted near-unanimous agreement on the current assessment and desired outcomes, thanks in part to the Letta, Draghi and Noyer reports. The emphasis must now shift to action and defining a concrete roadmap. For decades, Europe has concentrated on consumer protection, but going forward the emphasis must be on production, enabling Europe to become a global powerhouse alongside the United States and China. The objective should be to cultivate 450 million producers, not merely 450 million consumers.

2. Lowering internal trade barriers, especially in services and achieving the Savings and Investment Union (SIU)

2.1 A deeper single market is essential

An official highlighted that the remedy identified by Draghi, Letta and others lies in strengthening the single market. European firms currently lack economies of

scale, and the level of business dynamism remains insufficient. Numerous barriers within the internal market prevent companies from scaling effectively. The cross-border trade in goods imposes an ad-valorem equivalent cost of approximately 44%, while the figure for services stands at 110%. According to the IMF, lowering intra-EU trade barriers and services to US levels could boost productivity by nearly 7%.

The solution is well understood. If internal barriers within the single market were reduced by 10% then overall GDP output would rise by 7%. This assertion is supported by the experience of the 2004 EU accession: 15 years after joining the EU, new member states recorded a 30% increase in GDP per capita, while existing members also benefitted from market enlargement, gaining an additional 10% in GDP per capita. Deepening the single market is essential, as it offers a pathway to resolving productivity shortfalls and enhancing economic resilience.

The single market requires decisive action, urgency, and a comprehensive approach. Eliminating internal barriers will only be effective if firms also have access to capital to support growth. Structural reforms at the national level are indispensable, particularly given the scale of transformation required. The EU budget could be made conditional upon performance based milestones, as exemplified by the Next Generation EU (NGEU) initiative. Europe has no alternative; both growth and resilience are essential. Public spending is expected to increase by 5¾% of GDP in advanced economies and 8% in emerging markets due to demographic pressures, healthcare, defence, and the green transition.

An official stated that internal market barriers remain a major challenge. While the Commission disputes some figures, internal barriers currently equate to an effective tariff of 44% for goods and 110% for services. The high cost of cross-border service provision significantly undermines growth. This issue will be central to the informal ECOFIN discussions. Removing internal market barriers would constitute the most significant political and economic initiative available to the EU at this juncture. It is a smart and strategic response to growing protectionist pressures.

The missing element in the single market discourse has been focus. There is now a broad consensus that attention must be directed toward the energy market, financial services, and defence integration within the single market.

The Chair added that the single market ensures the recognition of qualifications, such that a ski instructor in Sweden is also considered a ski instructor in France. Domestic reform and the single market must advance hand in hand.

2.2 Achieving a genuine SIU to drive growth

2.2.1 Boosting productivity

An official explained that eliminating finance-related barriers to upscaling through a well functioning SIU would be indispensable for boosting productivity.

Capital markets in the EU remain highly fragmented. Private pension funds and insurance companies in the EU manage only around \$11.9 trillion in assets, which is a fraction of the \$42.5 trillion held in the US. The lack of long-term capital hurts EU scale-ups. Despite Europe's vast savings and financial integration in global markets, investment levels remain insufficient, and capital allocation remains inefficient constrained by national silos. This fragmentation further limits private cross-border risk sharing and compounds the problem.

Capital markets in the US smooth consumption across states at four times the rate seen in the EU. A more integrated SIU would address these inefficiencies. Channelling savings into risk capital would help start-ups and upscaling of larger firms, while ensuring financial futures for households. It would also strengthen the financial ecosystem, making it more resilient to economic shocks.

An industry representative noted that Europe experiences an annual outflow of approximately €300 billion in savings from its financial system. Redirecting this capital towards private investment could unlock substantial potential for growth. Nordic countries have already demonstrated success in encouraging household savings to support private investment and infrastructure. There is a clear opportunity for other EU member states to replicate such models.

The Chair added that the Letta report states that consumers will always go to a single market if an existing market has been fractured. Europe has the most savings in the world, but before transforming it into investment it needs to go to the United States before it comes back as investment.

2.2.2 Driving growth

An industry representative argued that the EU must vigorously defend the principles of a free market, particularly as the US increasingly questions them. The policy discussion must expand beyond labour markets and social spending. It must also include strategic investment priorities at the EU level. Europe has two key ingredients for competitiveness and growth, which are talent and savings, but it has failed to effectively align them. What is needed is the political will to remove barriers and build a financial system that truly works for growth. European citizens are highly educated and entrepreneurial but are constrained by an ecosystem that hampers innovation. Factors such as taxation, regulatory burdens, and labour market rigidity discourage entrepreneurship.

Europe generates ample savings but lacks mechanisms to deploy them efficiently. Institutional investors face regulatory obstacles. Since the 2008 crisis, Europe has produced four times more financial regulation than the United States and Canada. Additional supervisory layers impose capital burdens far beyond what is written in legislation. Regulatory stability must be balanced with growth and lending objectives. There is a need for a robust banking union (BU), a fully developed capital markets union (CMU), and a retail investment strategy (RIS). Regulatory incentives should favour long-term financing and equity.

2.3 Priorities and key success factors for an effective SIU

An industry representative urged a reconsideration of how Europe functions in light of significant geopolitical shifts. Future historians may characterise the period between 2022 and 2024 as a turning point marked by the United States' strategic pivot towards Asia. If Europe is to secure its economic future and maintain prosperity, then a fundamental reboot is needed.

2.3.1 A bottom-up integration approach is needed to accelerate decision making

An industry representative argued that the EU legislative process is no longer fit for purpose, as the current model often produces suboptimal legislation that then falls to regulatory agencies such as ESMA to implement. According to the Draghi report it takes an average of 19 months to finalise EU legislation. Speed must be prioritised. Bottom-up integration is needed. Industry-led initiatives, such as International Swaps and Derivatives Association (ISDA) contracts, have already transformed the derivatives market. Similar efforts should be replicated across sectors to establish common standards and enhance market functionality.

2.3.2 Reviewing prudential ratios, developing pension funds and equity financing

An industry representative observed that the prudential regulatory environment currently in place reflects the post-2008 environment of excessive risk, but the challenge today is that there is too little risk capital in the system. Europe must revise therefore its prudential frameworks and solvency rules to unlock capital for equity financing. The United States will not apply Basel standards, and the United Kingdom has postponed implementation. Europe cannot afford to remain constrained. Another source of untapped capital lies in household savings. Governments need to decide whether to continue incentivising sovereign bond purchases, or to provide equivalent incentives for equity investment. Prioritising local investment and 'buying European' is a strategic shortcut to drive capital into domestic innovation and industry. Governments must rethink how European savings are transformed into investment. Pension tax incentives and more accessible investment accounts will be a game-changer.

2.3.3 Accelerating the unification of the European regulatory framework

An industry representative highlighted that Europe's financial markets suffer from excessive fragmentation, making cross-border investments and liquidity management unnecessarily complex. The divergent national implementations of EU directives create multiple interpretations across the EU and inefficient gold plating. A true level playing field requires the establishment of ESMA as the single supervisor for market infrastructures and asset managers that have cross-border operations. For the SIU to succeed, Europe must embrace three essential principles: simplification, speed and bottom up initiatives from willing partners.

An industry representative added that reconnecting savings with investment is critical. Reindustrialisation

and enhanced competitiveness depend on the presence of strong European investment players. It is vital to eliminate national biases that limit scale within the EU, to strategically leverage the power of an integrated market as a 'base camp' in the global economy. European asset managers already allocate 15% more to EU investments than their international peers. Long-term investment should not be equated with low cost. Funding for small and medium-sized enterprises (SMEs), infrastructure, innovation, and the green transition requires strategic and patient capital. EU-level mechanisms, including pension reforms and auto-enrolment, are essential.

2.3.4 EU Presidency priorities for financial services

An official stated that there is a growing consensus that Europe must recalibrate its financial regulatory framework. The Polish Presidency is determined to move quickly, especially in advancing reforms to the securitisation market, which remains a critical yet underdeveloped component of the financial ecosystem. Progress on the CMDI package is also essential. While the CSRD and the Corporate Sustainability Due Diligence Directive (CSDDD) have been concluded, more ambitious revisions are required. The Polish presidency has been in dialogue with the Commission to propose radical improvements to the Carbon Border Adjustment Mechanism (CBAM), which currently excludes approximately 200,000 European companies. Furthermore, an agreement has been reached with the Danish Presidency to continue prioritising simplification, as this is now widely recognised as the most pressing policy priority.

Regarding external trade, there is a complex global landscape. The EU's initial restraint in imposing tariffs is a moderate and measured approach. While retaliatory tariffs have been introduced on specific goods such as steel and aluminium, these remain limited in scope compared to measures adopted by the United States. The EU's objective remains to promote free trade and avoid further escalation. Energy trade, particularly the import of liquified natural gas (LNG) and equipment from the United States, is another piece of the broader puzzle.

3. National reforms must match EU ambitions

3.1 Comprehensive reforms at the national level should further accelerate growth

An official highlighted that structural reforms at the national level have stagnated over the past 15 years. Supply-side reforms are crucial for improving productivity. The labour market and regulatory environment should be prioritised, as these areas directly complement the single market. A better trained workforce and more market flexibility are key to lifting productivity and seizing new technological opportunities. Most advanced European economies would also benefit from simplifying or harmonising product market regulations, deepening capital markets that improve access for startups or small firms and implementing innovation

and digitalisation policies. Better governance would amplify the impact of reforms, particularly in Central, Eastern and Southeastern Europe (CESEE) countries.

An industry representative noted that domestic reforms include reducing bureaucratic obstacles, encouraging private investment, enacting structural reforms in public administration and education, and enhancing labour market flexibility. These national efforts should be aligned with the broader EU-level simplification agenda. A predictable and stable policy environment is essential. A careful balance must be maintained between regulatory oversight and the need for a business-friendly framework that facilitates the implementation of reforms. National authorities should engage in continuous dialogue with regulators to ensure effective implementation and necessary adjustments. If the EU is to pursue a Savings and Investments Union (SIU) then it must be supported by national measures that encourage households to allocate savings to risk-bearing assets.

Germany's recent defence and infrastructure package marks a historic shift in its fiscal policy and demonstrates the government's willingness and capacity to act decisively. Although the package will increase Germany's debt by nearly 10%, reaching around 72% of GDP by the end of the decade, this level remains consistent with the criteria of a Aaa credit rating. Germany therefore enjoys more fiscal flexibility than countries such as Canada or the United States. The package is expected to initially raise Germany's real GDP by at least 0.5%, with further increases projected over time. Although some of this growth may be offset by tariffs, it is still likely to support domestic demand.

3.2 National opposition to the single market

An official reflected on long-standing advocacy for the benefits of the single market. Despite its clear advantages, the reality is that the European Union has supported free trade selectively, often only when it serves specific interests. Much of the progress made in single market integration has been driven by the judiciary rather than by political will. There is always a political rationale when member states resist deeper integration. The hope remains that a genuine political impetus for a fully realised single market will emerge, though this appears unlikely given opposition to external trade deals such as Mercosur. In addition, differences in labour markets and social policies between European countries are difficult to overcome.

Labour markets vary significantly across the EU. Some Member States have dynamic and flexible employment systems, whereas others are more rigid. Jurisdictions where dismissal requires a court order represents a considerable hiring disincentive. This structural rigidity is not addressed at the European level, as labour market reform falls within national competence. Since 2000, social spending as a share of GDP has increased on average by 6 to 7% across OECD countries. This figure exceeds the €800 billion cited in the Draghi report. There is a growing concern that escalating social expenditure is crowding out other critical public investments.

Social policy remains firmly a national responsibility. Taxation is another area of divergence. Some member

states maintain relatively low tax-to-GDP ratios, while others impose much higher levels. When attempting to attract international talent, high marginal tax rates can deter potential recruits. For instance, if the top tax rate reaches 55% it significantly increases the cost of employment compared to jurisdictions like the United States. The Competitiveness Compass highlights the importance of collaboration between academia and the private sector. In the United States, institutions like MIT serve as hubs where firms collaborate, even as competitors, to produce network effects. Emulating this in Europe is difficult under current tax regimes that deter research and innovation.

The Chair stated that despite institutional constraints many European countries have achieved impressive employment results. In 2000, the EU set a target of a 70% employment rate by 2010; the new objective is 78%, and several countries now exceed 80%. Europe is responsible for half of global social spending, which may enhance its appeal as a destination for talent. Success in health and education outcomes is also evident. Education is a public good in Europe, with significant investment in training, upskilling, and reskilling. Through the European Social Fund, 38 million individuals have received training over the past seven years. The Pact for Skills aims to upskill around 25 million people by 2030 through private sector engagement. Proactive labour policies are essential. Labour market dynamics are being reshaped by artificial intelligence and digitalisation. Recent announcements, such as the closure of Cora in Belgium, have caused shockwaves.

Concluding remarks

A market expert challenged Europe's persistent inability to act on well-diagnosed economic and strategic issues. Referring to repeated contributions by European figures such as Letta, Draghi, Monti, and Giovannini, the market expert argued that while Europe consistently identifies its problems and formulates solutions, it repeatedly fails in execution. The problem is Europe's collective hesitancy to act decisively.

The Trump administration has been a catalyst for European awareness and response. Trump's approach forced Europe to react, which is something it tends to do better than acting independently. However, Europe's initial responses, such as proposing reciprocal zero tariffs, miss the strategic context of current US policy. The United States is no longer focused primarily on trade; it is undertaking a broad strategy of autarky, which is re-establishing domestic control over industrial, technological, and defence capabilities. The shift reflects deep-rooted concerns about future geopolitical confrontation, particularly with China, potentially supported by Russia. The current US mindset is one of consolidation and preparation, not cooperation.

Europe cannot continue its pattern of forming new unions to patch individual problems. Instead, it must pursue a proactive, comprehensive strategy to build a truly integrated and capable Union. The European Union was born out of the ashes of war through

industrial cooperation. Today's imperatives, particularly in digital, defence, and infrastructure, require a similarly foundational approach.

There is some scepticism regarding Europe's readiness to meet these challenges, particularly when comparing its firms to their American counterparts. Deutsche Telekom remains dwarfed by US technology firms, both in investment capacity and strategic scope. Without substantial reinvestment and policy shifts, Europe risks strategic dependency.

The market expert has restructured their own investment approach to support European resilience, divesting a majority US equity holdings, maintaining only diversified exchange-traded funds (ETFs) and created two long-term investment portfolios. The first is Make Europe Great Again (MEGA), which is focused on rebuilding Europe's industrial and technological capabilities. The second is Make European Finance Great Again (MEFGA), which is concentrated on reinforcing Europe's financial institutions and capital markets. At the end of Q1, the industrial MEGA portfolio had returned 40%, driven by firms identified for their potential to substitute US leaders in defence, technology, and digital services. However, such results reflect early momentum and should not be interpreted as sustainable without broader systemic support.

There is strategic relevance in services and capital flows. Applying US methodologies for calculating goods

autonomy to services yields a -38.5% equivalent tariff for Europe. As a net exporter of services, the US views its dominance in this area as a competitive advantage. Europe continues to export capital via pension funds and institutional investments into US equity markets, reinforcing American corporate leadership. This misallocation of capital reflects a fundamental misunderstanding; by investing abroad, Europe neglects its own development and erodes its economic sovereignty. Strategic reallocation of European capital is essential for fostering innovation and resilience within its own borders.

A market expert strongly supported the development of a European defence capability. However, such ambitions require far more than political declarations; they demand sustained financial commitment and structural reform. Defence, digital infrastructure, industrial production and financial markets must all be viewed as pillars of strategic autonomy. With the Polish EU presidency and the war in Ukraine intensifying Europe's geopolitical exposure, Europe must be prepared for a range of outcomes, not only the most optimistic. Europe must recognise the scale of the strategic transformation underway and act with urgency, clarity and unity.