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Has the EU Commission found its true north?

Ursula von der Leyen's Competitiveness Compass promises a new economic doctrine for Europe, but social and regulatory concerns remain

Former ECB President Jean-Claude Trichet liked to say that the central bank had only one needle in its compass. He meant price stability. Most people agree that a compass with multiple needles is not a good idea, but it doesn't follow that public policy should be aligned to a single, unwavering goal.

Ursula von der Leyen has now unveiled a 'Competitiveness Compass'. According to the Commission president, 'the Competitiveness Compass transforms the excellent recommendations of the Draghi report into a roadmap. So now we have a plan.' Her executive vice-president, Stéphane Séjourné, claimed the Compass was the Commission's 'economic doctrine for the next five years'.

Peering through the mixed metaphors, what is to be made of this new initiative? And can it make sense to focus so exclusively on a single goal?

The good, the bad and the ugly

Let us start with the positive. Properly understood, competitiveness is a valid policy goal. The one-sided drive to resolve the euro crisis through 'competitive disinflation' – depressing wages and prices – in the countries under the yoke of the troika was a disaster. But the Draghi report was, and the new Compass is, right to insist on the importance of faster productivity growth and at least maintaining Europe's place in a geopolitical race for dominance in strategic sectors. That is not about lowering costs, and not just an issue for business, but a precondition – especially given tight labour markets and Europe's demographic prospects – for many social goals, for living standards, pensions, fiscal sustainability, quality jobs and more; in principle also for both the political acceptance and technological feasibility of decarbonisation.
To give some examples from among the potpourri of initiatives, there are

encouraging signs that the Commission seeks to go beyond traditional 'horizontal' industrial policy to focus efforts on strategic sectors; such 'vertical' industrial policy had long been taboo. Thus, sector-specific legislation is promised to support AI, cloud computing, biotechnology and advanced materials. Merger rules are to be revised so as to enable European companies to achieve the required scale to compete globally. A European preference in public procurement for strategic sectors and technologies is proposed. Of course, it remains to be seen exactly what will be put forward under these headings, but these examples – and more could be given – suggest that policymakers have indeed moved on from a naïve faith in competition policy and free trade towards a more realistic agenda that engages with modern realities.

The problematic aspects of the Compass are of two types: the measures foreseen to achieve the competitiveness goal (and those not envisaged) and concerns that, in pursuit of competitiveness, other policy goals will be sacrificed.

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Particularly concerning is the misplaced faith that deregulation (under the beguiling term 'simplification') will jump-start productivity growth without sacrificing important public policy objectives. Both the Letta and Draghi reports are right to see fragmentation in the form of 27 national legal regimes as a costly barrier to firms scaling up their activities. National authorities hang on tenaciously to their prerogatives. There is a case for differentiating between large corporate players and SMEs who face difficulties in shouldering administrative burdens, at least on some issues. However, the trick is not to throw out the baby with the bathwater, nor delude citizens that lessening the burden of reporting and form-filling, which employers complain about, will unleash a burst of new investment. If approval processes take too long, a better solution than scrapping a process that serves a public-interest goal is to adequately staff and equip the relevant public administrations.

Among the simplification initiatives mentioned, the proposal for a 28th, presumably radically simplified, corporate law regime threatens to undermine established legal practices, for instance on the information and consultation of workers. If the harmonisation achieved by a 28th

regime is based on minimalism rather than best practice, it would represent a triumph of 'negative' (i.e. abolition of cross-border barriers) over 'positive' (i.e. adoption of common standards) integration that EU critics have long posited as a worrying feature of the integration process. It is vital that any simplification agenda includes clear provisions to consult with relevant actors, including social partners and civil society organisations, and avoids arbitrary numerical targets for reducing the administrative burden.

One 'supply-side' measure not put forward, but that would help drive productivity growth, would be to ensure greater coverage of sectoral collective pay agreements. That would avoid weaker firms being able to offset their sluggish productivity by paying below collectively agreed rates. Meanwhile, the goal of 80 per cent collective bargaining coverage set out in the directive on Adequate Minimum Wages is now under threat following the opinion of the Court of Justice Advocate General that the directive contravenes the EU Treaty. If that view is upheld by the Court itself, it will weaken a potentially important 'productivity whip'.

Similarly, the Compass does not mention the use of 'social conditionality' clauses, which would tie public subsidies given in the context of industrial-policy or decarbonisation programmes to objectives such as respect for collective agreements or longer-term employment or investment commitments by recipient firms. This would prevent wasteful use of public money, support quality jobs and undergird public support for needed restructuring and decarbonisation measures.

As with the Draghi Report, arguably the most serious weakness of the Compass comes with its failure to envisage measures commensurate with the laudable goal of bringing about a very substantial increase in investment; Draghi called for up to €800 billion a year, an increase of five percentage points of GDP. On this, the needle of the Compass spins in circles.

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It criticises the EU's reliance on bank lending to finance private-sector investment, favouring US-style capital markets. But that is a long-term structural feature of European finance, which applied also when investment was at the levels, as a share of GDP, that Draghi says are necessary. It totally mischaracterises how banks work. They do not need to mobilise European savings, as is claimed. They can and do make loans *ex nihilo*, out of nothing. What they need

is firms with good business prospects (and/or collateral). If the reasons for weak demand for capital (like high energy costs, policy uncertainty, sluggish expected aggregate demand growth, a lack of financial support for decarbonisation-linked investments that are not yet profitable, etc.) were properly addressed, then European banks would lend more, as they have in the past.

On public investment, the new fiscal rules, while an improvement, will scarcely create any space for additional investment. Meanwhile, the proposals for EU-level investment funds (the existing STEP programme and a mooted European Competitiveness Fund) have nowhere near the required volume. This is all the more worrying given that the Recovery and Resilience Facility support for investment runs out in 2026.

In short, the competitiveness goal, focused as it is on productivity, is indeed an important one, although it is far from the only policy objective and there may be trade-offs. There are some promising-looking initiatives. But, not for the first time, Commission over-promising seems set to be followed by under-performance and political disaffection. Overcoming fragmentation is a worthy goal but will prove hard in practice, as the endless discussions about Capital Markets Union testify. Most importantly, there is still no recognition of the fundamental need to establish the fiscal resources at the federal level that Europe's global competitors have at their disposal. A clear orientation towards achieving that goal would be worth much more than all the myriad detailed initiatives set out here.



Andrew Watt
Brussels

Dr Andrew Watt is the Director General of the European Trade Union Institute (ETUI). He was Head of the department Macroeconomic Policy Institute in the Hans-Böckler Foundation. He was previously Senior researcher at the European Trade Union Institute, where he coordinated

research on economic, employment and social policies.