Brussels, 24 June 2024

Orgalim key recommendations on investments

Policy proposals for the upcoming EU legislative period

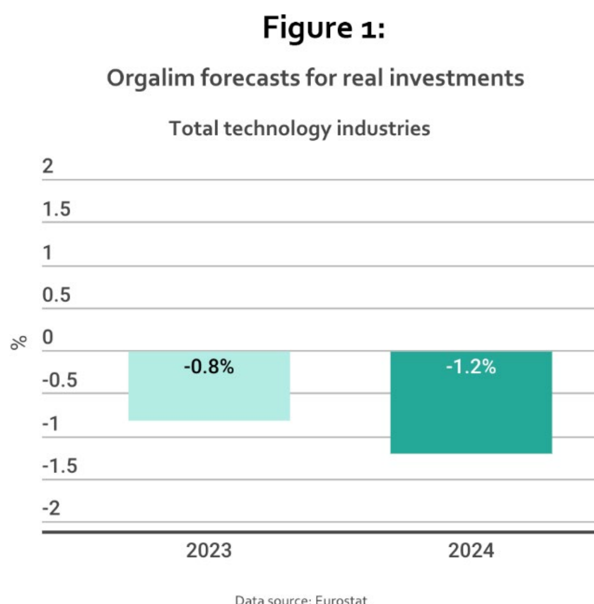
Investments in Europe's technology industries are decreasing, while global competition for technological leadership is fierce. A number of factors discourage technology businesses in Europe from investing in RDI, new products and services, including excessive regulatory burdens and an increasingly prescriptive legislative framework together with the complex processes required to benefit from existing EU financial instruments. In addition, we are concerned about the risks of a subsidy race both at global level and internally among EU Member States. To reverse the current underinvestment crisis and address the risks of a subsidy race in the EU, we must revitalise the EU's investment climate through **a long-term tech investment vision** and **an overhaul of the EU's investment landscape** that removes barriers, strengthens framework conditions and creates the best possible environment for industry to prosper here in Europe.

Introduction

Europe's technology industries provide the solutions that drive the transition to a sustainable climate-neutral economy and the digital transformation. However, in the face of increased global competition for technological leadership and rising geopolitical tensions, investments in Europe's technology industries are decreasing[1], which can in turn seriously impact our industry's enabling role for the twin green and digital transitions. Inflation, interest rates, multiple crises, declining demand in some sectors and a complex regulatory framework with heavy bureaucratic burdens are squeezing profitability and creating significant uncertainty for companies, thereby hindering their ability to invest. Additionally, structural issues such as energy costs and fragmented capital markets are further exacerbating the investment climate for companies.

[1] Orgalim Economics & Statistics report, 4 June 2024 see figure 1

Figure 1:



To remain competitive and resilient to external shocks businesses need to invest in RDI as well as new production methods, products and services. However, the uncertain business environment is forcing some companies to rethink their investment decisions, ultimately postponing and slowing down investments in Europe. For example, recent OECD data shows that R&D investment grew much faster in the US than in Europe, with 27 % versus 16 % growth of R&D expenditure as a share of GDP during the period 2000-2022[2]. Of even bigger concern, due to lack of investment we are witnessing an increasing number of bankruptcies linked to the lasting impact of COVID-19 and more restrictive financial conditions[3].

To support industry in a time of multiple crises and counterbalance subsidies from third countries, there has been an increased reliance on state aid in several Member States. In some cases, state aid has enabled certain companies to set up or keep their production activities in the EU instead of relocating outside, while in other cases Member States have reported that companies are bargaining with several Member States to get the best financial conditions for their investments. The latter could clearly lead to an internal subsidy race, creating further inequalities among Member States, inefficient allocation of resources and distortions within the single market.

If these trends continue, they will seriously impact the competitiveness of our industries in the long run, and – indirectly – the ambitious net-zero and green transformation in Europe.

Revitalising investments in Europe's technology industries

To reverse the current underinvestment crisis, creating a favourable climate to attract investments in new technologies, beyond just those considered "strategic", will be crucial. This will need to happen on three levels:

1. **General investment conditions**

[2] OECD Database gross domestic spending on R&D 07/012/2023
[3] OECD FINANCING SMES AND ENTREPRENEURS 2024: AN OECD SCOREBOARD 13/03/2024

2. **Private investments**

3. **Public investments**

General investment conditions

Investors need stable and favourable framework conditions. Europe cannot deliver on sustainability without investing in technological solutions, both at the innovation and deployment stages. Over the last five years, the EU has put in place a series of initiatives to deliver on the Green Deal and support critical technologies in Europe, such as the Net-Zero Industry Act (NZIA), the Strategic Technologies for Europe Platform (STEP), and the advanced materials initiative. Yet, on their own such measures will not make the EU's investment conditions competitive with other regions. These measures are often compared with the Inflation Reduction Act in the USA, but this Act is generally considered much more efficient when it comes to giving support to companies.

The EU´s investment landscape needs **a complete overhaul of framework conditions,** based on a **cohesive and long-term tech investment policy**:

- **Establish framework conditions which attract private investment**
  To unleash investment, any strategy must focus primarily on the review and improvement of the framework conditions for and the removal of obstacles to private investments. Key measures include substantively reducing bureaucracy and over-regulation, reducing barriers to trade by expanding partnerships and concluding free trade agreements, and ensuring an innovation-friendly legislative framework to facilitate market uptake and scalability. An overly prescriptive legislative framework makes the regulatory environment less agile when adapting to the latest technological advancements – which in turn creates barriers to market entry, thereby limiting investments.

- **Create a cohesive and long-term tech investment policy**
  Currently, the EU has a patchwork of investment instruments and funds aimed at supporting manufacturing and related technologies. Many of these were created as a reaction to the recent consecutive crises including the COVID pandemic, or to new policies announced by other economies such as the US Inflation Reduction Act. These instruments have targeted technologies such as microchips, batteries and net-zero technologies that were identified as "strategic". While responding to external shocks is critical, so is having a long-term tech-investment policy, as this gives businesses certainty. In the long run, such a vision would contribute to increasing the confidence of private investors for large green-field investment and brown-field investment in a wide range of technologies that are important to Europe's strategic goals, even if they may not be labelled as "strategic" in a narrow sense. Investments in the technology industries should be a priority, since this sector provides almost 12 million direct jobs in Europe and is at the core of Europe´s continued prosperity and competitiveness. Limiting investment policy to a top-down approach of identifying a narrow set of "strategic" technologies or sectors is ultimately likely to distort competition, lead to displacement effects and the reallocation of resources from areas where European industry is competitive. Therefore, we need an anticipatory and technology-neutral vision, building on our current strengths such as advanced manufacturing and electrification, instead of only reacting to global trends outside of our control. In particular, the EU's investment policy should aim to increase investments in manufacturing and electrification technologies by raising investments in, for example, infrastructure, defence and security. Moreover, public procurement should be utilised more when encouraging investments in infrastructure, defence and security.

Private investments

Both the EU and Member States should focus on boosting private investments. It is evident that we need to rely on a significant amount of private investment, as public money will not be sufficient to support industry and achieve the twin green and digital transitions. The European Commission has embarked on a series of initiatives ranging from sustainable finance to launching the Capital Markets Union, CMU. Nevertheless, given the significant decline in private investments our industry is experiencing, we call for the following urgent actions:

- **Leverage private investments**
  The biggest share of investments in technologies must come from the private sector. Invest EU is an example to follow, aiming to facilitate more than €372 billion in private investments to support broader EU policy priority areas. Open calls contributing to such wider policy objectives should be favoured. Collaboration in European Research and Innovation (R&I) communities, and between industry and policymakers such as the public-private partnerships (PPPs), has shown its value as an appropriate tool to ensure dialogue and involvement of industry. So far, PPPs such as Made in Europe and the Smart Networks and Services Joint Undertakings have been successful for both sides. We need to continue improving the model with business-led PPPs to strengthen the impact of research on economic growth. Identifying priorities together with industry leads to work programmes that are better aligned with actual industrial needs – which increases the probability of uptake of results as well as efficient budget use and increased incentives for private capital in R&D. We recommend expanding them to reap the full benefits of the PPP model.

- **Include enabling technologies in the EU taxonomy in 2025**
  To mobilise private investment into the green transition, the manufacturing of a wide range of state-of-the-art technologies, systems and services must be reflected in the technical criteria under the delegated acts of the EU's taxonomy, to be updated in early 2025. For example, energy efficient equipment and machinery enabling circularity, pollution prevention in industrial processes, together with services under the circular economy such as repair or refurbishment and digital solutions should count as green for investors. Without support and access to affordable financing for all technologies enabling sustainability, Europe's strategic goal of the net-zero and green transformation simply will not happen.

- **Complete the single market for capital**
  The EU Banking Union and Capital Markets Union are moving in the right but more needs to be done by both policy makers and market participants to complete the Capital Markets Union. Financial integration in the EU is increasing but must be further improved.

Public investments

To close the investment gap between the EU and the USA, the consultancy firm McKinsey suggests sharply increasing private and public investments in Europe including 400 billion euros per year in corporate investments[4]. While we recognise the important role of public investments for industry's competitiveness, we are concerned that ever-increasing levels of state aid also carry structural risks for the long-term competitiveness of Europe's economy and its public finances. State aid that artificially supports non-competitive industries is counterproductive, as it restricts the "creative destruction" of non-profitable companies which is important for the optimal use of resources in the economy.

The EU has traditionally financed activities where, due to a crisis or when single Member States failed to react, there was an urgency to react jointly. A set of various funding instruments currently exists to help EU economies; nevertheless,

[4] McKinsey: "Accelerating Europe: Competitiveness for a new era" 16/01/2024

synergies between different EU funds are often missing and access to funding remains complex. To ensure that public investments contribute to the long-term competitiveness of the EU the following actions should be executed:

- **Review existing funding instruments**
  Existing instruments need simplification, increased predictability and more transparent and competitive processes. We would recommend a comprehensive critical review of the effectiveness of existing EU funding instruments, mapping them against relevant stages in the innovation and deployment process and assessing their contribution to achieving key EU policy goals. This comprehensive review should be undertaken in consultation with the industrial sectors concerned and should include an assessment of whether current financial instruments may result in side effects, such as distortions in the single European market. It should also assess whether companies have equal opportunity to access financing regardless of size and Member State of origin. If the results point to a sub-optimal system, we call for a coherent reform of the various European funds favouring excellence to drive industrial policy objectives. Such an analysis should be carried out before the launch of a potential new funding instrument.

- **Prioritise tax incentives to achieve broader policy goals**
  If public money is to be allocated to an industry-driven project, it is more efficient if the public investment takes the shape of tax incentives rather than subsidies. Compared to subsidies, tax incentives have the potential benefits of decreasing both tax levels and transaction costs since the money stays where it was first generated. They also provide equal access and predictability for recipient, thus strengthening the incentives to invest. National tax incentives should be coordinated at EU level to increase impact and avoid contradicting policy goals.

- **Create a level playing field for European and national public investments**
  To prevent an internal subsidy race between EU Member States, national state aid should be lower than 2% of GDP. The Commission should apply EU state aid guidelines strictly and conduct a more comprehensive impact assessment to ensure that state aid does not damage the functioning of the single market. State aid above 2% of GDP should be pooled into a joint EU fund that is channeled to projects according to performance-based criteria such as, for example, the excellence criteria – and not based on the geographic location of the project. We strongly caution against public investments that would require an increase in the net tax burden for companies taxes or new debt. This means that public investments should be the result of a redistribution within public finances.

- **Recommit to technology neutrality and excellence**
  Any politically identified lists of "strategic" technologies risk overlooking essential enabling technologies and value chains, such as robotics, automation and other advanced manufacturing technologies and components critical for unlocking new competitiveness opportunities for all industrial sectors. The award of public financial support must be based upon excellence and competitive selection processes, as is the case with the EU's Innovation Fund. Priority should be given to company-driven technology projects within ecosystems, clusters, value chains and infrastructure rather than awarding support to a single company or a single technology.

- **Ensure strong innovation support**
  Research, development and innovation should be prioritised when it comes to both national and European funding instruments. The EU should at least double the budget for Europe's next Research Framework Programme (FP10) to €200 billion to stimulate European competitiveness. This increase in the EU research and innovation budget should take place without creating any new EU debt and without increasing taxes. Moreover, innovation support should follow the example of the Innovation Fund, which is clearly targeted to one policy objective but technology neutral. We would like to highlight the need for providing funding to pre-competitive research and development programmes to build long-term competitiveness, while outlining principles such as addressing market failures and conditions for sharing risk when providing support closer to market implementation and cautioning against support for mass production as a means to be competitive.

- **Radically simplify access to EU public financing**
  An increasing number of EU companies find it challenging to access EU funds due to their complex application procedures. For example, to seek funding from the EU Innovation Fund, European companies must submit a 300 page document, which typically takes a year of preparation. In contrast, a US based company needs to provide a 30 page project document when applying for the Inflation Reduction Act benefits. Streamlining EU funds application processes and ensuring transparency will contribute to increased participation and effective use of available funds. This would also require heavier penalties for those who misuse funds.

- **Create a clear definition of market failure**
  Given that "market failure" is often cited as a justification for state aid, we call for a clear definition of market failure to be developed by the European Commission.

Links to Orgalim publications

Orgalim Policy Agenda and key recommendations for the upcoming EU legislative period 2024-2029

- Orgalim Policy Agenda for a European high-tech manufacturing base for the 2024-2029 legislative cycle
- Orgalim key recommendations on the single market for the 2024-2029 legislative cycle
- Orgalim key recommendations on the circular economy for the 2024-2029 legislative cycle
- Orgalim key recommendations on digital policy for the 2024-2029 legislative cycle
- Other Orgalim key recommendations for the 2024-2029 legislative cycle will soon be available on the Orgalim website.

Orgalim represents Europe's technology industries, comprised of 770,000 innovative companies spanning the mechanical engineering, electrical engineering, electronics, ICT and metal technology branches. Together they represent the EU's largest manufacturing sector, generating annual turnover of €2,835 billion, manufacturing one-third of all European exports and providing 11.7 million direct jobs. Orgalim is registered under the European Union Transparency Register – ID number: 20210641335-88.

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