Balancing the risks and benefits of the European Economic Security Strategy

The case of the electric vehicles industry
On 20 June 2023, the European Commission (EC) published its first ever Economic Security Strategy (ESS). The document is groundbreaking in many ways, with Brussels appearing to be breaking away from old conceptions of the global economy, and the role it plays within. Prior laissez-faire economic doctrines are now being displaced by a seemingly more directed and interventionist approach.

In the new strategy, the concept of economic security centres on resilience across supply chains, critical infrastructure, strategic industries and the weaponisation of interdependences. At the core is the notion of de-risking – i.e. reducing economic risks from unreliable and competing states – by applying the ‘Promote–Protect–Partner’ approach. Specifically, the ESS strives to promote the competitiveness of European strategic industries and the industrial base, protect its economy from economic coercion and unfair practices, and partner with other (like-minded) states. The strategy brings together legislative pieces passed in recent years, while providing guidance for future policies. It articulates how the European Union (EU) intends to position itself as a geoeconomic actor for the near future.

Critics have been quick to question the ESS, given that the EU has been perceived as ‘a geopolitical herbivore in a word of geopolitical carnivores’; it is seen by some as a harmless giant struggling to hold its ground in a world of realpolitik.

However, this short perspective piece argues that, like any other great power, the EU does act as a ‘carnivore’, seeking its own interests and protecting its members. The ESS provides a framework to guide European actions in this new geoeconomic environment. This commentary offers insights on the European economic security approach and highlights key obstacles to the pursuit of economic security, as well as potential responses based on a case study of the electric vehicle (EV) industry. It does not derive from a single piece of RAND research, but seeks to offer a reflective perspective on the issues by drawing on selected published research by RAND Europe and others.

The evolving strategic context

The global economy has become a venue for great power competition. The Covid-19 pandemic and the Russian invasion of Ukraine are reminders that global supply chains have a ‘hub and spoke’ topography, where asymmetric
dependencies can become a liability and be weaponised by adversaries. Great powers such as China do not hesitate to resort to economic coercion to pressure other states to accept their demands. More generally, mounting techno-industrial competition between the United States and China is increasingly perceived as a near zero-sum game in which relative gain is king. Due to the highly networked architecture of the global economy, this competition will have global repercussions. Disruptive technologies, ranging from green tech and electric batteries to semiconductors, or artificial intelligence to quantum computing, create uncertainties for long-standing Western incumbents, who risk being displaced by newcomers like China.

On the global stage, states are adapting to this new environment by turning their attention to the pursuit of greater economic security. Levers at their disposal range from standard-setting strategies, minilaterals and economic alliances, to coercive and anti-coercive measures, redirecting supply chains, trade tariffs, import and export controls, inbound and outbound investment screening, and industrial policies. One example of a policy development in this field is the US outbound investment screening regime that intends to prevent US investors from investing in Chinese sensitive technology companies, and activities considered as threatening national security interests.

Some countries are already a step ahead of others. For example, Japan has a Minister of State for Economic Security, and in 2022 passed the Economic Security Promotion Act, which involves a six-step item-specific process to ensure the security of critical items. The process includes the designation of critical items, the formulation of an action plan for each item and the approval of applications by companies. Similarly, South Korea has a Foreign Economic Security Strategic Committee, and has been identifying overdependencies from foreign countries with a quantitative focus. If South Korea’s dependency for a specific item is over 50 per cent, it will be included in an early warning system to anticipate supply chain disruptions. China has been developing an economic security apparatus for several years. Recent policies include the 2022 new Export Control Law, which has been described as the country’s ‘first comprehensive legal framework for export controls’ that ‘embodies China’s focus on economic security’. The newly formed Russia–China axis also offers de-risking opportunities from the West for both parties.

**European economic security: The example of the EV industry**

To illustrate how these geoeconomic forces apply in practice, and what economic security measures can bring in terms of benefits and risks for the EU, this piece explores the EV industry as a case study. The case of the EV industry shows how Brussels intends to use economic security instruments to be a leader in this strategic sector. However, potential risks are also associated with a security-driven economic approach.
Given that new internal combustion engine (ICE) vehicles will be banned in the EU by 2035, producing electric batteries and EVs is a strategic imperative for the European Union.

**The importance of the EV industry to the European Union**

The automotive sector is a key component of the European economy. It employed 13.8 million people around the Union and accounted for 7 per cent of its GDP in 2022. Some European countries, such as Germany, France, the Czech Republic and Slovakia, heavily depend on this industry in terms of employment gross value, and more generally to sustain their economic growth. Given that new internal combustion engine (ICE) vehicles will be banned in the EU by 2035, producing electric batteries and EVs is a strategic imperative for the Union. However, as EVs rely on technologies fundamentally different from ICE vehicles, Western automotive incumbents fear being displaced by Chinese newcomers.

Within the policy circles of Brussels, China is increasingly perceived as the elephant in the room. Not only does it produce more than 60 per cent of electric batteries, but it also recently surpassed Germany as the world’s second largest car exporter in 2022, and might soon be set to become number one. This has come as a shock for many within a sector that has not seen such drastic changes for almost three decades. In 2023, Chinese car manufacturers began to penetrate the European car market, accounting for 8 per cent of electric vehicles sold in the EU, and could even reach 15 per cent by 2025. The EU becoming a prime target for Chinese EV exports and battery investments has raised fears across the West that the Union might be losing this technological race. As Chinese Carmakers are expanding their hold on the EV industry, calls for economic security measures – especially from France whose less reliant on the Chinese market for its automotive exports – have gained momentum across the bloc.

**Economic security and the EV industry**

Promote

In the EV industry, economic security links closely with industrial policy and investment. French President Emmanuel Macron summarised the desired aim as follows: ‘We [Europeans] need more factories and fewer dependencies. “Made in Europe should be our motto”.’ In pursuit of this aim, and in the wake of the EC’s 2018 Strategic Action Plan on Batteries, several policy levers were created.
For example, projects defined as Important Projects of Common European Interests (IPCEIs) allow public subsidies to fund advances in batteries. The European Battery Alliance and the European Investment Bank also serve as platforms to de-risk investments across the whole EV value-chain by promoting public–private investments and collaborative research. As of 2023, around 50 gigafactory projects have been planned around Europe to produce electric batteries.

**Protect**

Economic security is also pursued through defensive measures. Brussels is developing a multiscale economic security toolkit to resist economic coercion and respond to unfair economic practices. For example, to alleviate its dependency on Chinese critical raw materials supplies, the new EU-wide Batteries Regulation has set up requirements for battery components recycling, supply chain due diligence and sustainability standards. Other EU measures include procurement and anti-coercion instruments, regulations on foreign subsidies, and screening inbound and potential outbound investments. For example, the Foreign Subsidies Regulation enables Brussels to act against market distortion caused by subsidies given to foreign firms competing against their EU counterparts, and the Anti-Coercion Instrument allows the EU to retaliate if a country uses economically coercive measures to interfere in its political process. However, an ongoing challenge is that the economic security agenda is splintered between the EU’s responsibility over external economic relations and member states’ authority in national security, with member states needing to give their legal approval and political support for any legislative and policy advances. The EC assesses risk, puts forward legislations and other measures, and supervises the implementation of its Economic Security Strategy. After adopting specific instruments and regulations, member states decide (or not) to implement certain parts of the ESS at the national level. This might result in discrepancies between the theoretical strength of an economic security policy and its limited impact in practice.

**Partner**

Partnering is the last priority. By expanding its web of economic alliances, the EU aims to de-risk the European economy by reducing imports from countries deemed unreliable. For example, the strategic alliance recently struck with Uzbekistan on critical raw materials such as titanium and lithium, both used in the production of EVs, aims to help mitigate the EU’s asymmetric dependence on Chinese critical raw materials. Economic alliances also reflect new geoeconomic alignments across the international system. Recently, the European Battery Alliance and the US Li-Bridge Alliance established a transatlantic electric battery alliance to consolidate industrial synergies. Minilateral are also important, with the G7 increasingly becoming a platform among Western democracies to coordinate geoeconomic policies. Brussels’ ambition to set up critical raw materials clubs with like-minded countries such as Canada or Australia to de-risk global critical raw materials supply chains is another example of this trend.
The risks and challenges of economic security policies

The benefits of security-focused economic policies must be carefully balanced against their associated risks. A recent development in the EV sector illustrates potential drawbacks to such policies. Fearing that Chinese EV might structurally displace European carmakers, the EC launched an anti-subsidy investigation to determine whether to impose punitive tariffs against Chinese EV exports to the EU on the grounds that Chinese firms benefit from unfair state subsidies. As Laurence Boone, France’s Europe Minister, noted, ‘We [Europeans] won’t let our market be flooded by over-subsidised EVs that threaten our companies as happened with solar panels.’ While this timely move aims to force China to revise its unfair subsidy scheme, unintended consequences could harm European car manufacturers. If China were to retaliate by restricting access to its internal market, some European carmakers could face high financial losses – a fear largely shared by German carmakers who have high stakes in the country.

At the geopolitical level, China has already shown resolve to respond in a like-for-like manner and reacted swiftly with retaliatory measures by conditioning access to its critical raw materials – including gallium and germanium. As the world’s leading graphite producer, on 20 October 2023 Beijing announced new export restrictions on certain types of graphite that are key to making EV batteries. Furthermore, given that France has largely lobbied behind the scenes to launch this anti-subsidy probe, China retaliated by opening its own anti-subsidy investigation against the alleged dumping of French cognac and brandy in China. Such economic security dynamics create further ripple effects on European firms. Given that the EC has since launched new anti-subsidy investigations, these dynamics could escalate further.

From an economic perspective, the potential costs attached to this dynamic are evident, even if poorly understood by governments and decisionmakers. Due to the interconnectedness of the global economy, protectionist measures in the EV sector might produce negative spillovers and reverberate across the wider economy. Arguably, the influential nature of the EV sector and related supply chains make the risks of negative economic impacts potentially systemic. To better understand how these risks manifest and how much they may cost the global economy, or a regional economy such as the EU, decisionmakers should have at their disposal tools and approaches to assess the benefits and costs associated with geoeconomic policies.

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Tools to prepare for and anticipate the impact of economic security measures

As the ESS continues to shape the future of European economic security, European officials would benefit from a clear understanding of the potential impact of their own and their competitors’ measures to avoid a ‘what does this button do?’ approach to economic security. Previous RAND research offers examples of methods and tools that could help inform analysis of how the ESS impacts sectors of interest. For example, tabletop exercises were recently conducted with US officials and industry stakeholders to assess the geopolitical implications of Taiwan’s dominance over the semiconductor sector.

The study revealed that stakeholders lacked clarity on how interconnected the industry is globally and the costs required to reduce risk. Similar simulation exercises could be applied to the EV industry or other sectors of interest to improve understanding of market structure, assess the cost of disruptive scenarios and examine the impact of potential countermeasures.

Quantitative models provide an alternate means to estimate spillover effects from disruptions to particular firms or sectors. Input–output models have been developed to study systemic risk and could be adapted to assess how geoeconomic policies targeted at one or more sectors may impact other sectors and, ultimately, the economy. Computable general equilibrium (CGE) models are a related class of model equipped to tackle similar macroeconomic questions. By mixing economic theory and country data, a CGE model could help determine the impact of macroeconomic economic shocks on a pre-determined geographical zone. Alternatively, a CGE model could be used to test whether and how geoeconomic policies lead to increased unit costs for goods and services within affected sectors, and how related price changes might impact GDP growth via changes in supply and demand behaviour.

Conclusion

In recent years, the EU has joined other countries in its efforts to safeguard its economic activity against perceived economic security threats. The EC’s first ever ESS aims to promote the competitiveness of European strategic industries, protect the Union’s economy from economic coercion and unfair practices, and partner with other countries on the global stage to strengthen its position. This perspective piece has explored the various policy instruments and applications of this European approach to economic security, with a particular focus on the EV industry. It demonstrates that the EC and EU member states will need to develop a robust understanding of both the benefits and risks associated with economic security measures if they are to avoid harmful unintended consequences for their own economies.
Notes

1 European Commission (2023d). The June ESS has been followed by an update in January putting forward new economic security tools. For more on this, see European Commission (2024a).

2 European Commission (2023e).

3 Lefebvre (2021).

4 Farrell & Newman (2019); Mhalla (2022).

5 Frederick et al. (2022).

6 Drezner et al. (2021).

7 See for example: Allison (2023); Australian Strategic Policy Institute (2024); Citton (2023); Funaiolo et al. (2023); Miller (2022).

8 Ghiretti (2023).

9 Ghiretti (2023). According to Theil (2023), minilaterals can be defined as 'nimble, pragmatic coalitions that overcome multilateral paralysis without being formal alliances.'

10 The White House (2023); Benson & Mouradian (2023).


12 UK Parliament (2024).

13 Ghiretti (2023).

14 Ghiretti (2023).

15 Ghiretti (2023, 5).

16 Lin (2023).

17 European Commission (2024e).


19 European Court of Auditors (2023).

20 Citton (2023).

21 Mazzocco & Sebastian (2023); White, Song et al. (2024).

22 Mazzocco & Sebastian (2023).

23 Hancock et al. (2023); Kratz et al. (2023); Sebastian (2024); Xie (2024).

24 Kratz et al. (2023); Gregor (2023); Mazzocco & Sebastian (2023).

25 Duthoit (2023).

26 Macron (2023).


28 European Commission (2024d).

29 European Commission (2024b).

30 Transport & Environment (2023). It is worth noting that due to the US Inflation Reduction Act, many of these projects are threatened to never materialise.

31 Benson & Mouradian (2023).

32 European Commission (2023d).

33 Matthijs & Meunier (2023).

34 European Commission (2024c).

35 Benson & Allen (2023).

36 Benson & Allen (2023).

37 Benson & Denamiel (2023).

38 Kessler (2023).

39 European Commission (2023a).

40 European Commission (2023b).

41 Frederick & Shatz (2023).

42 European Commission (2023c).

43 Blenkinsop (2023).

44 Hancock (2023).

45 Allenbach-Ammann et al. (2024); Campbell & Nilsson (2024).


47 Benson & Denamiel (2023).

48 White, Klasa et al. (2024).

49 For example, the EC announced mid-February the launch of a new anti-subsidy probe against a Chinese train maker benefiting from subsidies that put European train makers at a competitive disadvantage. For more, see Bounds (2024).
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About this Perspective
This perspective offers insights on the European economic security approach and highlights key obstacles to the pursuit of economic security, as well as potential responses based on a case study of the electric vehicle (EV) industry. It does not derive from a single piece of RAND research, but seeks to offer a reflective perspective on the issues by drawing on selected published research by RAND Europe and others.