

BDI and Confindustria

October 14, 2016

“Reviving economic growth and social cohesion in Europe”

Executive summary

Anxiety and uncertainty about the future, as well as perceived impoverishment and lack of trust in political and business elites are deeply shaking European society.

We, the entrepreneurs of Germany and Italy here represented by BDI and Confindustria, share these feelings and sense our high responsibility in front of our fellow citizens in building a better future for them and our children.

The outcomes of the UK referendum and of other elections in many European countries testify European citizens' hardship which reflects extraordinary tough times. In Europe, there are more than 22 million unemployed today and there are millions more at risk of poverty or social exclusion.

However, these electoral outcomes of their protest do not alleviate their sufferings and do not increase the number of jobs available. They can even worsen the social and economic outlook. The only way forward to create growth and jobs is to build on our strengths.

The EU is one of the strongest economic areas in the world. It has only 7.3 per cent of the world's population but it accounts for 23 per cent of global GDP. Even without UK, it will continue to be of such pre-eminence.

The single market is at the basis of its strength. Thanks to its size and the presence of rich and sophisticated buyers, it creates the optimal environment to develop innovations and reach the production scale that European companies need to compete globally and to penetrate new markets.

Notwithstanding these numerous achievements, the outcome of the British referendum and the implementation of border checks suggest that, for the first time since the signing of the Treaty establishing the European Coal and Steel Community, the European project may unravel. Without decisive action, the public goods of the EU (peace, freedom, security, democracy, prosperity, welfare and the single market itself) could be put at risk.

The business community can and wants to play an active role to avoid that present and real danger. We want to set the tone, providing policy makers with appropriate suggestions about the necessary measures to sustain competitiveness and growth in Europe.

As matter of fact, manufacturing industry is the pillar of the economic power and development of Europe. It provides the bulk of export goods, it generates and spreads innovation and it creates highly skilled and well paid-jobs. As the source of growth and jobs, industry can help us to overcome the identity crisis that the EU is facing today.

To survive stronger and stronger Chinese competition, EU companies need to pioneer the production frontier. In this context, BDI and Confindustria are putting forward a comprehensive Competitiveness Agenda for the European industry.

While traditional structural and macroeconomic policies are an essential component of a competitiveness agenda, they do not provide sufficient comfort and need to be supplemented by strong industrial and innovation policies.

To this end, we recommend to the governments of Germany and Italy to start a bilateral process of work of identifying key industrial policy projects that require robust national action and/or parallel European-level efforts. The major aim is addressing emerging policy issues or horizontal issue-areas that need to be tackled to fully embrace the potential of value-added and employment of new global developments and new technologies or business models.

In that regard, we recommend specifically the following points:

- 1. to define a horizontal strategic framework at European level for industry modernization;*
- 2. to strengthen the joint work on Industry 4.0, promotion schemes for investment in these fields, data protection and IT security;*
- 3. to review innovation policies at the national and EU level;*
- 4. to make better use of existing innovation funds;*
- 5. to support interregional cooperation and to coordinate investments related to industrial modernisation;*
- 6. to implement the unitary patent;*
- 7. to strengthen broadband infrastructure investment and establish an industrial Giganet until 2025;*
- 8. to develop a joint understanding on new and advanced mobility services such as automated driving, e-mobility and sharing services;*
- 9. to pursue joint projects of common European interest (IPCEIs) on key enabling technologies;*
- 10. to develop a comprehensive policy approach towards product market regulations;*
- 11. to encourage entrepreneurship and new industrial business models;*
- 12. to address the financing requirements of EU enterprises.*

“Reviving economic growth and social cohesion in Europe”

I. Why restarting the European engine is crucial for legitimacy and efficiency

Anxiety about the future, uncertainty concerning their own and their children’s jobs, perceived impoverishment, lack of trust in political and business elites, demands for protection, insecurity: these feelings are deeply shaking European society.

We, the entrepreneurs of Germany and Italy here represented by BDI and Confindustria, well understand these feelings, both as individuals and as entrepreneurs, because we share them. Every day we experience exasperated levels of competition, increasingly fast-paced changes and a degree of uncertainty that has no precedent in the post-war period. Many among us work side by side with many employees and know their worries and anxieties.

We sense our high responsibility in front of our fellow citizens, in building a better future for them and our children.

In fact, those feelings reflect extraordinary tough times. In Europe, there are more than 22 million unemployed today. On a broader definition of unemployment, the number is twice as high. There are millions more at risk of poverty or social exclusion.

The outcomes of the UK referendum and of other elections in many countries demonstrate that European citizens democratically express their hardship and their protest at the ballots.

However, these outcomes of their protest do not alleviate their sufferings and do not increase the number of jobs available. They can even worsen the social and economic outlook. The only way forward to create growth and jobs is to build on our strengths.

The EU is one of the strongest economic areas in the world. It has only 7.3 per cent of the world’s population but it accounts for 23 per cent of global GDP. Even without U.K. it will continue to be of such pre-eminence.

The single market, which is the result of increasing European integration and enlargement following the signing of the Treaty establishing the European Coal and Steel Community in 1951, is at the basis of its strength.

With more than 500 million consumers and 21 million companies, Europe has the largest common marketplace in the world. This is at the very heart of the competitiveness of its companies. This has contributed greatly to European growth, spurring employment and inward investment. Value chains are inextricable linkages that cross national boundaries and are vital for our competitiveness.

Thanks to its size and the presence of rich and sophisticated buyers, both on the final consumption and on value-chain sides, the single market creates the optimal environment to develop innovations and reach the production scale that European companies need to compete globally and to penetrate new markets.

We, German and Italian entrepreneurs, are increasingly concerned about the potential unravelling of the European project. The outcome of the British referendum and the implementation of border checks are outstanding examples of it.

This trend must be reversed soon. We must build on achievements of European integration. We have to rediscover the public goods of the EU: peace, freedom, security, democracy, prosperity, welfare and the single market itself. These goods are both at the root and the result of the unification process. However, these goods are not here to stay forever and could be put at risk if the unification unravels.

The business community can and wants to play an active role to avoid that present and real danger. We want to set the tone, providing policy makers with appropriate suggestions about the necessary measures to sustain competitiveness and growth in Europe.

As matter of fact, manufacturing industry is the pillar of the economic power and development of Europe. It provides the bulk of export goods, it generates and spreads innovation and it creates highly skilled and well paid-jobs.

As the source of growth and jobs, industrial companies are the glue of the society and our best answer to fear and rise of nationalism. That can help us to overcome the identity crisis

that the EU is facing today, due to some of the biggest challenges since the end of the Second World War: terrorism and security threats, international conflicts, the slowing down of world growth, high unemployment and the asylum and migration crisis.

Only industry can provide solutions to today's big global challenges such as environmental and climate change, ageing society and energy shortage. To survive stronger and stronger Chinese competition EU companies need to pioneer the production frontier.

In this context, BDI and Confindustria are strongly supporting a comprehensive Competitiveness Agenda for the European industry.

The new industrial revolution is radically transforming our economy. To exploit it fully to the benefit of the European society we have to promote high investment and productivity levels and an increase in the skill-intensity of European production in order to make high added-value products and services.

BDI and Confindustria, representing the companies of the two biggest manufacturing countries in the EU, believe that industry is the cornerstone from which to start to re-launch the economy; in this sense, they consider essential the adoption of a clear EU strategy for a smart, innovative and sustainable industry, supporting its modernisation and transformation.

The development of an "ecosystem", facilitating the cooperation between various industrial players and between them and other actors (universities, research institutes, public institutions) represents a key element for filling the innovation gap and supporting industrial transformation.

BDI and Confindustria are really asking for an EU industrial policy strategy, starting with the boost for Industry 4.0. Adequately supporting innovation and digitalisation plays a fundamental role in the transformation of industrial processes. Full implementation of the European Action Plan for the digitalisation of industry has to be ensured with no delay; in particular, we need a harmonized regulatory framework allowing free movement of data in the EU, addressing the related issues of data protection, IT security and business models based on high-quality standards in these fields. Moreover, in order to accelerate the

adoption of ICT in the European industry, we call for a renewed relationship between public and private players through the rapid development of digital innovation hubs and competence centres and the establishment of all appropriate connections among them.

More and more, industrial technologies – key enabling technologies in particular – represent a driver for innovation across industries (e.g. automotive, energy, aerospace) improving the development of new goods and services. In this context, a coherent and simple EU regulatory framework is needed in order to ensure the full uptake of technologies by industry (including SMEs). Financial schemes such as Public Private Partnerships and Joint Technology Initiatives established under Horizon 2020 play an important part in scaling up the economic impact of industrial investments and must be supported further.

The lack of investments hampers EU growth. BDI and Confindustria welcome the Commission's decision to extend the duration of the European Fund of Strategic Investment (EFSI) and to substantially increase its financial capacity. Individual projects and investment platforms should be selected according to their potential impact on the economy and their ability to boost value chains at European level. In parallel, EU and national efforts to remove regulatory obstacles and improve the overall investment climate in Europe must be stepped up.

It also appears essential to assess the effectiveness and impact of EU financing programmes supporting industrial investment. Their review must fully take into account industrial priorities and needs and enhance all possible synergies between them. Also, stronger synergies between public and private financing must be encouraged.

Likewise, the case for infrastructures investments has been strong for a long time, but it gets stronger with each passing year, as government borrowing costs decline. They can create jobs, provide economic stimulus and expand the economy's capacity in the medium term, increasing investment attractiveness. They are crucial for the competitiveness of firms and territories.

If all these issues are not swiftly tackled, Europe's collapse will become inevitable. We entrepreneurs are ready to fight to avoid this disastrous result. Starting by doing consciously our own job: to invest, to innovate and to explore new markets around the world. We are

aware of the need to work even harder to improve the performance of our companies. For the good and to the benefit of all European people.

II. A call to action: specific proposals for a bilateral agenda on competitiveness

Comprehensive action at both the national and the EU level will be required to lift the European economy to higher levels of economic growth, job creation and competitiveness. The European G20 partners committed to that goal at the Brisbane G20 summit in 2014, and our two government leaders committed to a “Pact for Competitiveness” at the bilateral meeting in Maranello on August 31st. While traditional structural and macroeconomic policies are an essential component of a competitiveness agenda, they do not provide sufficient comfort and need to be supplemented by strong industrial and innovation policies.

To this end, we recommend to the governments of Germany and Italy to start a bilateral process of work of identifying key industrial policy projects that require robust national action and/or parallel European-level efforts. The major aim is addressing emerging policy issues or horizontal issue-areas that need to be tackled to fully embrace the potential of value-added and employment of new global developments and new technologies or business models.

In that regard, we recommend specifically the following points:

Recommendation 1: Defining a horizontal strategic framework at European level for industry modernization

Jobs, growth and competitiveness must remain at the centre of the EU's efforts. Beside the on-going EU specific strategic initiatives – such as the Digital Single Market, the Energy Union, the Capital Market Union etc. – a horizontal strategic framework at European level is required to strengthen and modernize Europe’s industrial base. In line with the letter the Friends of Industry countries (including Germany and Italy) sent to Vice-President Katainen and Commissioner Bieńkowska last 26th of September ahead of the Competitiveness Council, Confindustria and BDI call on the Commission to include a dedicated Communication on

industrial policy in its work programme for 2017. This Communication should set out an action plan - including concrete deliverables and deadlines - to tackle the main challenges that industry is facing, supporting its transition towards a smart, innovative and sustainable industry. Concrete actions need to be developed in the following priority fields: regulatory framework fit for stimulating investments in Industry 4.0, adequate support to future industrial technologies and their uptake by enterprises (including SMEs), financing instruments promoting investment in R&D, innovation and skills (including investments platforms industry-driven focusing on close-to-the market projects such as the S3 Platform on Industrial Modernization), and stronger cooperation between various players within industrial ecosystems.

Recommendation 2: Strengthen the joint work on Industry 4.0, promotion schemes for investment in these fields, data protection and IT security

We understand that the recent initiatives of both governments are similar in nature and should be fully implemented. We urge our governments to focus on this important topic in their bilateral work, also to the aim of promote shared projects reinforcing companies' cooperation along the value chains, and to discuss the regulatory framework on standards, data protection and IT security. We applaud the recent plans for digital modernization of industry by the Italian and German governments and consider these as first steps towards a comprehensive approach for industrial rejuvenation and job creation in our countries.

Recommendation 3: Review innovation policies at the national and EU level

Innovation is a crucial requirement for maintaining economic competitiveness, and thus is a growth engine for the national and European economy. Regulation has a strong influence on it and the priorities of innovative companies. Well-drafted legislation can stimulate innovation. However, poor legislation can also stifle it. Excessive precaution and regulation which concentrates on risk avoidance and fails to consider both risks and benefits stifles technological innovation. This takes place at the expense of more basic research and

innovation, and therefore also at the expense of future competitiveness. A balanced approach to risk is a key factor in enabling innovation. Germany, Italy and Europe suffer from rather risk-adverse attitude and societies. This does not contribute to the societal conditions and acceptance needed for (disruptive) innovation.

The EU should continue to foster and implement an “Innovation Principle” as a complement to the Precautionary Principle. Innovation Principle means that potential risks but also the potential benefits of a new technology /innovation are fairly balanced. Enterprises and people should be encouraged to develop new ideas, technologies while ensuring that related risks are managed appropriately.

The EU Competitiveness Council has recommended EU member states in its resolution on May 27th 2016 to install an “Innovation Principle” in member states as well as at the European level. The European Commission set up voluntary “innovation checks” by DG Research and Innovation for any new piece of legislation which comprises innovation (the so called “toolbox 18”). This approach has to be deepened by making the use of the toolbox18 mandatory for all new legislative EU proposals. Finally, the Innovation Principle should be included in the EU Treaty on the same level as the Precautionary Principle.

In Germany, BDI demands to install an innovation check as well for all legislative proposals at the national level and has developed a concrete “innovation check” with relevant questions and criteria. In the next months, the Commission will launch the Interim Evaluation of Horizon 2020 to assess the socio-economic impact of R&I funding, both at national and EU level, and examine the need to review policies and instruments. In this context, a strong dialogue between the competent ministries of our respective countries should be considered in order to bring coordinated input and proposals in the process and to ensure that German and Italian industry R&I priorities will properly be taken into account in the design of future policies and instruments. The same should apply as far as the definition of the 2018/2020 work programme of Horizon 2020 is concerned.

Recommendation 4: Making better use of existing innovation funds

Funds existing at EU, national and regional level play a crucial role to stimulate economic development. EU institutions, Member States and regions should work closely together to ensure

real synergies between these funds and allow industrial innovation projects to be co-funded, making the best use of available resources, be it Horizon 2020, EFSI, ESIF or national/regional funds. Nevertheless, it is fundamental and urgent to deal with the problems deriving from different funding mechanisms, aligning the procedures according to a simplification objective: in this regard the proposal of the High Level Group on simplification presented by the European Commission last 27 September offers first concrete solutions to ease access to the EFSI, also through better synergies and an effective combination of funds.

Recommendation 5: Supporting interregional cooperation and coordinating investments related to industrial modernisation

Beside synergies between structural funds and Horizon 2020, Confindustria and BDI look with great interest at the recently launched Smart Specialisation Platform for Industrial modernisation where the Commission is considering possible ways to combine structural funds with the EFSI. Open to regional and national authorities as well as industrial actors, the Platform aims at starting partnerships in specific priority areas, scaling-up common innovation projects and investment platforms that have the potential to be a business driver across regions. We support these efforts aiming at coordinating investments related to industrial modernisation and targeting support from EFSI and ESIF. At Italian and German level, some regions are already quite active on the side of interregional cooperation: Lombardy and Baden-Württemberg participate (together with Catalonia and Rhone-Alpes) in the activities of the Four Motors for Europe. Also, Lombardy, Emilia-Romagna, Saxony, Baden-Wuerttemberg and North Rhine-Westphalia are partners of Vanguard Initiative, one of the best practices among the various regional cooperation initiatives. The Vanguard Initiative brings together regions committed to mobilise – in alignment with their smart specialisation strategies – resources and ecosystems with the aim of supporting the development of interregional networks that co-invest in new, interconnected European and global value chains.

Confindustria and BDI share the Commission’s vision according to which Smart Specialization Strategies and Thematic Platforms may be considered as a key industrial policy mean for

favouring a stronger cooperation between regional territories and their respective economic systems and for accelerating the development of new industrial value chains on the basis of a *mutual-leverage* and risk-sharing logic. The political commitment of regional and national authorities is a fundamental condition to work in this direction. At the same time, industry involvement in the S3 implementation plays a key role; this is why, BDI and Confindustria express their will to work together in this field.

Recommendation 6: Implement the unitary patent

Intellectual Property (IP) protection is at the core of innovation and value creation for innovative businesses. *IP-intensive* industries account for one in three jobs and 39 per cent of total economic activity (*GDP*) in the *EU*. Innovation and patent protection in particular are crucial to address not only the current stagnant growth but also some of the major challenges Europe will be facing in coming decades (e.g., healthcare and medical technologies for an aging population, fighting climate change, improved sanitation).

This is why innovative businesses need to fully rely on IP protection at a reasonable cost. The new Unitary Patent and Unified Patent Court will finally open a new opportunity for companies to protect their innovations.

Still the Unitary Patent is not yet a reality for companies and inventors with negative repercussions for innovation, growth and job creation in Europe. Since 2012, EU Member States have been focusing on the technical implementation of the Unitary Patent and Unified Patent Court project. We understand that the final touches to the new system will be established in due course. With the necessary ratifications of the Unified Patent Court Agreement having almost been completed there have been valid expectations from companies that the new system would become operational in the first semester of 2017. However, we are still missing a few key ratifications for this to happen.

This is why, we urge all EU Member States that have not ratified yet the Unified Patent Court Agreement to do so urgently. No other considerations should jeopardise this major

contribution to the industrial renaissance of Europe. This is too important for Europe to let it fail.

Recommendation 7: Strengthen broadband infrastructure investment and establish industrial Giganet until 2025

We suggest developing national action plans for the industrial Giganet with specific timetables for ultimate implementation, financing and investment options and joint regulatory initiatives with a view of broadening the bilateral cooperation swiftly to other partners.

The emergence of a robust Giganet is both required for reliable and secure data transactions of businesses, consumers and the public sector. The Giganet has strong characteristics of a public infrastructure and requires alongside private investment a substantial amount of public funding through many different mechanisms (direct investment, co-funding, financial incentives for private investment, risk-sharing and so on). Also, we recommend making full use of spectrum allocations for mobile internet (5G) and harmonizing national plans for spectrum allocations. A particular emphasis should also be place on ensuring the smooth continuation of services across borders.

Recommendation 8: Develop a joint understanding on new and advanced mobility services such as automated driving, e-mobility and sharing services

Mobility is subject to major changes. Traditional structures in mobility are changing and new technologies, providers and services come to the market place. At the same time, we are faced with the challenge to achieve a better reconciliation of the growing demand for mobility with the need to respect environmental, climate, social, safety and resources protection. In the medium term, we have to recognize the great role played by mature technologies (such as gas) to achieve sustainability targets. Therefore, a new impetus for a common approach of the EU is essential to reach the 2030 goals.. After all, the interdependence of our individual mobility and our freight services are so diverse and

international that national stand-alone solutions will fail in the medium and long term. With regard to aviation and shipping even European solutions fall short. Both require global solutions.

At the European level much has been achieved. A number of initiatives such as GEAR 2030, C-ITS, AIOTI, ERTRAC or "Declaration of Amsterdam" were successfully launched. There is already a substantial amount of research on these topics. We expressly welcome this very much. Nevertheless, these diverse initiatives should be brought together again in order to continuously assess progress. A joint initiative has to take into account questions of an intelligent networking of transport modes and the increasing digitalization of transport. This particularly addresses the automated driving.

The existing EU legal framework covers most of the liability, data protection and data security's issues. The need for any further legislation should be carefully assessed and be evidence-based, in order not to freeze innovation in this field.

In addition to existing platforms and research initiatives extended pilot applications and introductory projects are needed. The German "digital A 9 motorway test bed" might be used as best-practise example. Furthermore, the focus should be set on electro-mobility and alternative fuels in general. The success of e-mobility depends not only on the advancements in vehicle technologies but thus on the availability of charging infrastructures, an adapted urban planning and harmonized norms and standards to ensure interoperability and user-friendliness. This is largely recognised by the European Commission. Still, it needs continuous efforts to establish those alternative mobility concepts on a large scale. R&D support to optimise vehicle components, public tendering and tax incentives to make alternative fuels and powertrain technologies more attractive for consumers and the extension of public charging points can contribute to an increased share of renewable energies in the transport sector.

The future urban mobility is of paramount importance. In addition to effectively networked transport modes different concepts of car-sharing play an important role. A common understanding of basic requirements could reduce the barriers to market entry for providers significantly.

Recommendation 9: Pursue joint projects of common European interest (IPCEIs) on key enabling technologies

The governments should work together on two Important Projects of Common European Interest (IPCEIs) that should also be submitted for financial supported from the EFSI. The first IPCEI project covers investment on first production and R&D for the full manufacturing supply chain of micro- and nano-electronic components in an integrated way. The project involves different actors belonging to several countries: Germany, Italy, Austria, Belgium, France, the Netherlands, UK, through an industry consortium. The second IPCEI on HPC (High Performance Computing) and Big Data enabled applications has been launched by France, Italy, Luxembourg and Spain and should include Germany.

Recommendation 10: Develop a comprehensive policy approach towards product market regulations

Well-established regulatory systems in product and services markets often act today as an implicit barrier to innovation and competition. We urge our governments to take stock of the new competitive environment in a comprehensive fashion and to make recommendations on specific changes to the European and national regulatory and competition environment for those new products, services and business models. As an interim step to an action plan, the governments of Germany and Italy might set up a small expert group to develop. Business should be consulted early on and contribute to the policy process.

Recommendation 11: Encourage entrepreneurship and new industrial business models

We recommend the establishment of an expert group of government officials, academics, experts and industry representatives to address the broader issues of industrial entrepreneurship in times of rapidly changing business models with a view of meeting and even leading those changes at industrial companies. The purpose of the group should be to

develop recommendations within one year after resuming its work on company experience, structural shifts in business models, corporate options of responding to those new environments and public policy requirements for meeting those challenges.

Further arguments: In many industrial sectors, issues of true entrepreneurship, i.e. risk-taking under conditions of uncertainty, have become more salient in recent years. There are two main factors driving the changes: one is increasing competition in final goods and services markets by companies from emerging markets and the second one is the impact of new technologies, in particular ICT, on long-established business models ranging from automotive and logistics to tourism and travel. We witness an increasing gap between top-firms or best performers and many a SME struggling to adapt in time. This process puts stress on organizational structures, established financing relationships, the supply chain and customer relations and requires strong top-down leadership based on a clear vision of required changes to the business model.

Given the recent nature of those pressures it would be desirable to study the various changes, to gauge the impact on industrial business and value added and to consider broader public policy parameters that either facilitate and support changes or effective defences of business models or that inhibit and hinder changes. Similarly, intra-corporate issues in change management and culture should also be addressed.

Recommendation 12: Address the financing needs of EU enterprises

Smooth financing of companies is crucial for the economic recovery in the EU. However, despite huge liquidity injections by the ECB and historically low interest rates, the credit mechanism does not function properly. To give powerful and lasting impulses for investment and growth in the EU, it is essential to revamp the credit market, which is instrumental especially for small and medium-sized businesses. SMEs remain largely reliant on bank-related lending to finance their activities. While only a robust and profitable banking sector can serve the economy and finance the growth of our enterprises, additional regulatory constraints would further increase financing problems. We advocate for a more balanced

regulatory approach that takes the specific financing needs of our companies more into account.

Among other things, the capital reduction factor for loans to SMEs (the so-called SME supporting factor), which was introduced in 2013 to neutralise tougher capital requirements imposed to banks as a response to the crisis, should be made permanent and the 1.5 million euro limit removed. Given regulatory and balance sheet pressures, there is a significant risk that as economic growth picks-up banks will be unable to meet companies funding requirements on the desired scale. Therefore, financial structures of companies must be adapted to the new setting. Companies will have to raise funds through alternative channels. In particular, they will have to increasingly capitalize on their own resources. Companies need to increase their equity/debt ratio through external capital injection, helped by tax incentives and strengthened venture capital markets. In this context, we underline the fact that the crisis has caused a deep fragmentation of the European banking system. There is a lack of confidence that creates inefficiencies and disruptions in the European credit market. Therefore, we call for urgent action to go on without delay towards the creation of a Capital Markets Union.



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