GLOBAL TRADE AND ECONOMIC TENSIONS

MARIO NAVA
Director General, DG Employment, Social Affairs and Inclusion – European Commission

Putting people first to unlock Europe's competitiveness

Over the years, the EU has clearly demonstrated its resilience in times of crisis. The world of today asks once again to show that the EU is not only an economic and peace project, but our best bet for a safe and prosperous future.

The global order is shifting. The world of international cooperation turns into a race with increasing competition. It is imperative for the EU to increase its competitiveness, while considering the different opportunities and challenges in the Member States.

Respecting national, regional and local diversity is key for a fair and just transition. Member States are impacted by global shifts differently, depending on reliance on energy exports and global trade. Their economies also face specific transition paths, depending on industrial specialisation that leads to different labour market and skills needs.

President Von der Leyen outlined in her Political Guidelines *"Our threats are too great to tackle individually. Our opportunities too big to grasp alone."* The best way to do so is by leveraging the EU's unique assets – the single market, the EU's social model and its people.

People are at the centre of Europe's strategy for competitiveness, but the EU is still facing skills shortages and gaps. Despite a record high employment rate of 75.8% in 2024, European companies struggle to find the staff that they need. Four in five SMEs report skills challenges and 70% of businesses report that the lack of right skills hampers their investments.

This calls for a step up in ambition and action to invest in people. This is the objective of the recently adopted Union of Skills that sets out over 40 actions to upskill and reskill the workforce, underpinned by governance and investment. It provides a framework for action, but its success depends on a joint effort.

Member States play a central role in this. The persistent skills shortages must be addressed via structural reform, with skills strategies that link policy to skills needs and funding.

Empowering adults to upskill and reskill is a must. EU leaders agreed on the target of 60% of adults participating in training every year by 2030, today we stand only at 39.5%. Individual Learning Accounts – digital wallets with training entitlements – could help reach this target, with more than half of the Member States exploring this. Skills Academies – EU-wide training initiatives in strategic sectors - are also a powerful tool to help fill skills gaps, when traditional education and training cannot keep pace with the change, especially in strategic sectors, such as net-zero industries.

It is key to provide a platform to engage key stakeholders in industry and develop a sectoral perspective on skills. Employers lack resources to develop training content, especially SMEs. Creating partnerships between businesses, education and training providers and governmental actors in industries helps leverage resources. The Pact for Skills and its Large-Scale Skills Partnerships in all industrial eco-systems and across regions is an excellent example.

Another imperative is to activate everyone, especially those furthest away from the labour market. This calls for targeted support measures, with a central role for Public Employment Services, for high quality career guidance, and validation of skills.

Investing in people's skills is key to Europe's competitiveness.

To be effective, these measures must be well-informed and funded. Currently, skills intelligence remains fragmented. Available data must be coordinated and used better, to help define skills needs across Europe. The European Skills Intelligence Observatory, part of the Union of Skills, will play an important role. Effective skills measures also need sufficient funding. The current EU budget invests 150 billion in skills, complemented by national and private funding. Looking ahead, the Commission proposals for the next EU multiannual financial framework put a strong accent on skills development and investment in human capital.

Work remains, and we can build on lessons learned over the years, adjusting coordinated action to the fast-paced reality of today. Skills are a high political priority, put centre stage at EU level already during the European Year of Skills 2023 – 2024. We continue our efforts to show that skills are an investment that pays off many times over.

ALFRED KAMMER
Director, European Department –
International Monetary Fund (IMF)

Europe's blueprint for higher and more resilient growth amid global uncertainty

A deteriorating external environment weighs on Europe's outlook. Sustained high trade policy uncertainty, tariffs, and rapidly shifting geopolitical developments continue to cast a shadow over the continent. Front-loading of exports to avoid tariffs lifted growth early in the year, but the underlying picture remains broadly unchanged. As this temporary boost fades, Europe is headed for a slow grind as the negative effects of fragmentation add to the long-standing decline of productivity growth and rising fiscal pressures.

Yet Europe has the blueprint for higher and more resilient growth. When access to foreign markets is curtailed, expanding Europe's internal market to its full scale would open new avenues for growth and enhance resilience through greater risk diversification. Over the past three decades, the EU has made remarkable progress in deepening its single market. But momentum was lost. Policymakers understand the untapped potential, but plans to complete the single market remain tentative, narrow, and lack ambition matching the challenge. In short, recognition still needs to be translated into action.

A deeper single market could unlock enough European growth potential to counter global headwinds. Divergent regulatory frameworks and a lack of political consensus have stalled progress toward fuller integration. Achieving a Savings and Investments Union (SIU)—one key ingredient—requires overcoming these obstacles. Capital could then be allocated more effectively across borders and spur innovation by offering risk funding for start-ups and upscaling. Reducing the still sizable remaining barriers to goods, services and labor mobility—another key ingredient—would provide startups and innovative firms a large market to grow at scale and use inputs more efficiently. A more integrated energy sector could also improve energy security and reduce dependency on non-European suppliers. An IMF recent study shows that such a package of tangible reforms could raise GDP by 3 percentage points.[1] It would also strengthen resilience against external shocks through increased EU interconnections.

Domestic structural reforms are a crucial complement to single market integration. Ambition also pays at the national level. Closing just half the gap to the most growth-friendly structural policy settings across EU countries could raise GDP in the EU over the medium term by almost 6 percent.[2] Combining domestic and EU-level reforms would amplify Europe's economic potential more than either alone. For example, making progress on the SIU would greatly magnify the benefits of domestic efforts to raise private investment by giving firms easier access to risk capital.

Another lever to raise Europe's growth and resilience is broadening its global trade partnerships. The EU has benefited enormously from the open, rule-based trading system. Policymakers should strive to preserve it and use trade defense measures judiciously. Meanwhile, the EU can forge deeper trade ties with others, encouraging investment and job creation. Examples include ratifying the trade agreement with Mercosur, building deeper relationships with the UK and Switzerland, and concluding the bilateral FTA with ASEAN member countries.

> **Plans to deepen the single market remain narrow; they need more ambition and need to be acted on.**

Turning this blueprint into action will take strong political leadership and bundling reforms to ensure shared gains. Much like the NGEU overcame deep-seated reluctance to share fiscal resources by packaging grants and loans with conditionality, EU growth reforms could also be bundled to offer net gains for everyone. In addition, the EU's Multiannual Financial Framework (MFF) needs to be scaled up. Our estimates suggest that to adequately support the provision of European public goods (EPGs), the spending on these should increase by 0.5 percent of GNI annually, more than in the current proposal. A small budget risks foregoing EPGs or pursuing them inefficiently through national budgets. On national reforms, the MFF's mainstreaming of performance-based budgeting is welcome. These efforts should be combined with strategies deployed in successful reform cases—such as, for example, Sweden on private savings and Germany on labor markets—including clear communication, strong institutional setups, proper sequencing, and buffering adjustment costs.

Europe should act now–when costs are still manageable–rather than deferring reforms until persistently sluggish growth and further rising spending pressures force disorderly adjustment.

This article was co-authored by Xiangming Fang (IMF).

1. *Lifting Binding Constraints on Growth in Europe: Actionable Priorities to Deepen the Single Market, IMF/WP June 2025.*
2. *Europe's National-Level Structural Reform Priorities, IMF/WP May 2025.*

CARMINE DI NOIA

Director of Financial and Enterprise Affairs – Organisation for Economic Co-operation and Development (OECD)

Systemic uncertainty: a threat to EU integration?

European economies are navigating significant systemic uncertainty largely related to trade policy and global conflicts. It is tempting to point to the exogeneity of these factors and describe European policymakers as simple "price-takers". However, this would be only one side of the coin. On the other side, past policy actions have determined how resilient the European economic system is to systemic uncertainty today.

A brief overview of the main European macroeconomic indicators reveals two main long-term trends that undermine the EU's capacity to face geopolitical and trade tensions: overindebtedness and underinvestment. It is important to note that borrowing poses fewer risks when used to boost growth-enabling investments, yet this has generally not occurred.

On indebtedness, the latest edition of the OECD Global Debt Report shows that public debt has been on a rising trend over the last decades. It increased sharply during the global financial crisis and the COVID-19 pandemic to fund countercyclical economic policy measures. The result is that many governments are concerned that additional borrowing to fund measures to tackle systemic uncertainty could deteriorate market confidence, widen spreads and, in the worst case, even trigger a sovereign debt crisis.

On investments, the volume of productivity-enhancing investments has been disappointing in the EU since the early 2000s, worsening following the global financial crisis. After the crisis, non-financial companies' total investments in capital assets and R&D declined and recently stagnated. At the same time, many governments restrained investments partly to avoid aggravating their fiscal balance. These were short-sighted choices which, in the long term, led to weak growth and, consequently, less sustainable debt burdens.

Geopolitical and economic fragmentation add to and may worsen high debt and low investment trends.

Geoeconomic fragmentation has steadily been among the top sovereign debt managers' concerns over the last few years. This is particularly important as foreign investors are a significant source of demand for European sovereign bonds. Global tensions may cause a sudden drop in demand from these investors and heightened volatility, resulting in higher borrowing costs and a shift in resources from growth-enhancing investments to interest payments.

In general, geopolitical and economic fragmentation can disrupt foreign investments. Foreign investors may be less inclined to invest in countries politically less aligned with their own. Moreover, recipient countries may want to limit investments from abroad when they perceive them as a threat to national security.

This trend is exemplified by the widespread adoption and strengthening of FDI screening mechanisms across the European Union, as well as the new EU Recommendation (2025/63) on outbound investments. Today, all EU countries adopt or are discussing whether to adopt screening mechanisms. This is also due to the encouragement from the Commission. It is important to utilise these instruments to effectively address national security threats, instead of pursuing unwarranted state interference in the economy.

It is not possible to foresee the evolution of international trade policy and global conflicts. However, we can observe that these tensions have already contributed to a change in mentality among European policy makers who now seem to no longer judge economic globalisation as an inherently beneficial trend driven by politically neutral market forces. It is plausible to expect that this new mindset will keep affecting European policymaking in the future.

Geopolitical and economic fragmentation add to and may worsen high debt and low investment trends.

National security is now a key factor in decisions of EU policy makers on themes such as fiscal discipline, capital markets liberalisation, and state economic interventionism. This is good, as being able to better leverage the national security exception makes the EU more resilient to future shocks. However, the risk is that security-driven policy stances may lead to excessive fragmentation of the Single Market, foregone investment opportunities, and capital misallocation.

Against this backdrop, international coordination among partner governments continues to be essential, and the OECD remains one of the best fora to this end.

MICHAEL WEST
President – Moody's Ratings

Will geopolitics catalyze decisive European reforms?

Europe's long-standing economic model - built in an era of increasing global trade and investment links and a relatively benign regional security environment - faces geopolitical challenges.

The European Union's size gives it a considerable advantage in navigating these challenges. It is the world's third-largest economy. At 16%, its share of global trade surpasses that of the largest two economies, US and China. The Euro's 40% share in international trade invoicing matches that of the US Dollar.

However, these statistics mask an underlying fragmentation among EU member states that has inhibited the economic benefits of Europe's scale. Geopolitics may well catalyze collective action that bolsters Europe's growth, by providing an imperative for overcoming narrow differences to meet broader common goals.

Higher US tariffs are an example of external pressures on Europe's growth. On the surface, Europe's size is a buffer. US-bound gross value-added exports account for just 1% of EU GDP. Looking deeper, however, reveals that tariffs will negatively affect some large, employment generating sectors in Europe.

Of the more than 900 companies we rate in EMEA, about 10% are highly exposed to tariff related disruption through their revenue exposure to the US, global supply chains and limited pricing flexibility. An example is the auto sector, which relies on the US market for 20% of exports. Its reliance on imports from the rest of the world exposes it to tariffs beyond Europe. Moreover, the European auto sector also faces considerable global competition as EV technology and pricing shift.

The security environment is another source of pressure. Europe's NATO members have pledged to raise core defense spending to a minimum of 3.5% of GDP, with total defense spending expected to reach 5% over time. This buttresses national security, but at a fiscal cost. We estimate it could increase debt-to-GDP ratios by 3.5-5 percentage points by 2029 across Europe's four largest economies - adding strain to public finances already stretched by the pandemic shock and unfolding demographic trends.

European defense manufacturers will benefit from this boost to spending, with spillover effects on growth in related sectors. However, Europe does not currently have the capacity to fully meet its defense needs, so some portion of this spending will go to imports, including from the US, rather than the domestic economy.

Each of the growth and security challenges outlined can be mitigated by channeling more private and institutional capital into productive investments. This, in turn, requires financial deepening that serves a three-fold objective: stronger growth and security, new investment opportunities for Europe's substantial pool of savings, and greater financial resilience to market volatility.

The recent securitization proposal, among the measures to develop the Savings and Investment Union, aims to support such financial deepening. It could also support Europe's private credit markets, and their interlinkage with the broader financial sector. Private credit already accounts for around $500 billion in assets under management in Europe —nearly 30% of global private credit AUM. Our survey of 32 global banks shows that while current exposure of banks to private credit is modest—just 4% of loans in Europe—it is growing in line with the expansion of private credit itself.

Geopolitics could catalyze collective action that bolsters Europe's growth.

With its access to long term funds, private credit brings the potential for matching long-term liabilities to long term assets. It also serves to diversify sources of funding for borrowers, alongside banks and public debt markets. However, compared to these financial segments, it is less transparent and has a more limited track record in multiple credit cycles. As in other areas, the role of policy and regulation will be to support private credit growth that increases long term investment and diversification while building guardrails against the risks associated with opacity and a shorter track record.

Today's juncture of geopolitical and market shifts offers Europe an opportunity to unleash its full potential. It will require collective policy actions that channel funds to productive activities while enhancing the European financial system's shock-absorption capacity.

LAS OLSEN
Chief Economist and Head of Macro Research – Danske Bank

Nordic economic outlook amidst global trade and economic tensions

While Donald Trump made his plans of imposing tariffs widely known well before last year's election date, few could have imagined the scale of trade uncertainty that followed in 2025. Particularly the Nordics, as small, open and cyclical economies have been exposed to the risks.

A pessimist sees the tariffs as another negative shock following years of pandemic restrictions, high interest rates, energy shortages and a war in Ukraine – all of which have affected the Nordics more than others. But at the same time, the renewed impetus for fiscal policy driven investments, whether for defence, alternative energy sources or shifting supply chains, have all sparked a welcome jolt of optimism particularly for the region's stagnant manufacturing sector.

Danske Bank continues to forecast recovering growth for the Nordic economies despite the trade war and seemingly high tariffs imposed by the US. We emphasize two factors that support the cautiously optimistic view:

1. While the US has played an outsized role in driving export growth over recent years, the growth outlook does not rely just on exports. Slowing inflation and recovering real incomes will provide support for households' consumption. With high share of variable interest rate loans in Sweden, Norway and Finland, the decline in central banks' policy rates has already begun to provide tangible support for households and businesses alike.

2. We believe the US will struggle with decreasing its import dependency given the limited labour supply. As Nordics and broader Europe seem to avoid the highest tariff rates relative to global peers, the trade war does not automatically weigh on export competitiveness as long as final demand holds up.

European politicians have shared varying opinions on the recent trade deal between the US and the EU, but at the very least, the easing uncertainty will allow businesses to finally start adapting to the new landscape. While parts of the deal related to tariff carveouts for specific sectors remain unclear at the time of writing, we estimate that the EU will face a trade-weighted average tariff of around 12-13%. This is below the trade-weighted average tariff on all US imports, which hovers close to 20%, meaning that the EU exports continue to face tariffs below the global average.

In our baseline scenario, we expect the euro area economy to grow by 0.9% this year and 1.2% in 2026. Similarly, we forecast Danish growth at 3.2% and 2.5%[1], Swedish at 1.6% and 2.5%, Norwegian at 1.7% and 1.6% and Finnish at 0.9% and 1.7%, respectively.

Further escalation in trade tensions could still weigh on the growth outlook indirectly, particularly if more expensive tariffs end up weighing on US final demand. The negotiations between the US and China were extended by another 90 days in late July, meaning the risk of renewed tensions persists. In a worst-case scenario, if the US were to reimpose the 145% tariffs that it held against China earlier in the spring, the average trade-weighted tariff rate of all US imports could rise above 30% - and tilt the US economy into a recession roughly comparable to the burst of the dotcom bubble in 2001.

In such a scenario, we would expect both Nordics and the broader euro area to avoid an outright recession, but the growth outlook would still be clearly downgraded. Within Nordics, Denmark faces perhaps the most uncertain situation given the country's large pharmaceuticals sector and its' still unclear tariff level. That said, while the US is by far the Denmark's largest export market, more than 75% of the exported Danish goods are actually manufactured outside the country's borders, and often within the US itself.

US is relatively smaller, though still important market for Swedish and Norwegian exporters, with a share of around 8-9 % of total export value. Sharp strengthening of the local currency has been an additional headwind especially for Swedish export competitiveness, with USD/SEK rate declining by nearly 12%. That said, we do not expect the SEK appreciation turning into a longer-term trend. Finland stands in the middle of the pack when it comes to US exposure in its exports, with a share of around 11%. The Finnish economy is recovering from a much more fragile starting point than its Nordic peers, as the end of trade with Russia as well as the steep downturn in local construction sector pushed the economy into an outright recession in 2023.

We expect the Swedish Riksbank to maintain its monetary policy unchanged over coming months, but if the escalating trade war would increase the downside risks for the economy, we see room for 1-2 more rate cuts. Norges Bank initiated its rate cutting cycle only this summer – significantly later than its peers. We expect rate cuts to continue later this year and into 2026 irrespective of the trade war, dampening further risks for the Norwegian economy.

1. *There has been a major revision to Danish historic data since this forecast was made in June. This implies that growth will be lower in 2025 than what is forecasted here. Our next forecast will be published in September.*