

01|2026

REPORT

GOVERNANCE OF THE EUROPEAN UNION

CONCLUSIONS AND PROPOSALS



CONSEJO ECONÓMICO
Y SOCIAL ESPAÑA

NUMBER 01|2026

COLECCIÓN INFORMES

Ordinary Session of the Plenary Assembly on 29 April 2026

REPORT 01|2026 GOVERNANCE OF THE EUROPEAN UNION

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CONSEJO ECONÓMICO Y SOCIAL **ESPAÑA**
PUBLICATIONS DEPARTMENT
NICES: 905-2026

Colección Informes

Number 01/2026

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INTRODUCTION

Since the publication of the last report drafted by the Economic and Social Council (ESC) on the economic governance of the European Union, which was approved in May 2024, the EU's external environment has changed substantially, with geopolitical fragmentation intensifying at a global level due to an increase in armed conflicts. The latest of these, which involves the war launched by the United States and Israel against Iran, has triggered an escalation of hostilities in the Middle East. This conflict has reached as far as Europe's doorstep and led to widespread political and economic instability, the consequences of which remain unpredictable.

But beyond the economic impact and increasing uncertainty, the deepening fragmentation and increased conflicts place additional pressure on the European Union in its role as an international actor. They herald a new era for the EU, where it must deal not only with temporary crises, but above all, with structural changes.

In addition to the tensions arising from the conflict, the EU is facing a new era of rapid technological change and fierce geoeconomic competition, which has called into question its seemingly well-established relationship of trust and cooperation with the United States. The rise of China and the protectionist response of the US to the threat posed to the latter's hegemony –especially within the technological sphere–, the shift in the foundations of the European energy model in the wake of the war in Ukraine, and the need to boost security and defence, are shaping a new reality.

These changes in the global order have a particular impact on the European Union, as its model of growth and integration relies on a framework of international trade liberalisation, participation in global value chains, and a rules-based multilateral system. Furthermore, its global influence stems, above all, from its adherence to standards, markets and regulation.

Broadly speaking, the EU has the potential to be a major global player. To consolidate this potential, as pointed out in the Letta¹, Draghi² and Niinistö³ reports published in 2024, the Union must roll out an ambitious strategy that emphasises not only in-

1 Letta, E. (2024), *Much more than a market*.

2 Draghi, M (2024), *The future of European competitiveness*.

3 Niinistö, S. (2024), *Safer Together – Strengthening Europe's Civilian and Military Preparedness and Readiness*.

vestment and innovation, but also open strategic autonomy and security in its broadest sense, including defence. Only then will it be able to gain greater economic and geopolitical relevance, building on its strengths: its single market, its social and democratic framework based on the rule of law, and its defining values, in addition to its climate ambitions.

This is not to say that all its difficulties are due to external sources or arise unexpectedly. As a matter of fact, one might say that, on several occasions, the EU's problem stem from within. While it is true that in times of crisis, the EU has been able to overcome its internal limitations by delivering a unanimous and coordinated response, it has made only modest progress in certain areas, owing to conflicts in the decision-making process. This has been consistently pointed out by the ESC in successive reports. Providing a joint response is complex, since it requires negotiation, institutional adaptation and consensus, all of which prolong and complicate the decision-making process, thus rendering it ineffective within the current context.

In any case, European integration remains one of the greatest political, economic and social achievements in contemporary history. The fact that twenty-seven Member States, each with markedly different historical, cultural and economic backgrounds, have managed to cooperate within a common institutional framework is a remarkable achievement, more so given that this cooperation is based on shared democratic values and it upholds a social model that benefits all citizens.

These are the challenges facing the current European Commission (2024–2029), whose term officially began on 1 December 2024, once again under the leadership of Ursula von der Leyen. The President has clearly defined the priorities of the new Commission from the outset. She has announced the Competitiveness Compass, which aims to close the innovation gap with the US and China, boost security and independence, and decarbonise the economy. She reaffirmed the commitment to the goals of the European Green Deal and proposed a clean industrial deal, a dialogue on the future of the automotive industry, and the fostering of a competitive circular economy. Regarding armed conflicts in Ukraine, the Middle East and Africa, she emphasized that Europe must play a leading role and increase defence spending, reaffirming that European security would be a priority for the Commission.

Based on all the above, the ESC considers that now is the right time to draft a new report on EU governance⁴. On this occasion, it focuses on identifying and assessing the strategies proposed to boost the EU's influence and autonomy within the current global

4 Previous reports published by the ESC on this topic are as follows: ESC: Report 03/2012 on new economic governance in the EU and growth; Report 1/2014, *Evolution of the Economic Governance of the European Union: an update on the ESC Report 3/2012*; Report 1/2016, *Analysis of the Economic Governance of the European Union*; Annual Report 2/2017, *The Economic Governance of the European Union*; Annual Report 2/2018, *The Economic Governance of the European Union*; Annual Report 3/2019, *The Economic Governance of the European Union*; Report 3/2021, *The Economic Governance of the European Union. The impact of the pandemic*. Report 2/2023, *Governance of the European Union. Spanish Presidency 2023*; Report 2/2024, *Economic Governance of the European Union*.

context, intended to address technological, demographic, environmental and security challenges, while also continuing to fulfil the expectations of its citizens. To this end, the report is structured as follows:

The report begins with an overview of the situation in the European Union, compared to the United States and China. This analysis is based on a series of indicators selected to identify the main areas of significant difference between these global players.

Next, it examines the factors that have contributed to this situation. These factors include both external elements: derived from the reshaping of the global economic order; and internal elements: related to the building and evolution of the European project itself.

This leads to the identification of areas for improvement, which are described in detail in a third chapter, and deemed by the ECS as areas that require a special effort by the EU. This chapter also analyses and assesses the range of initiatives and proposals that have already been tabled, including the new Multiannual Financial Framework 2028–2034, evaluating their potential to address current challenges. It concludes with a series of reflections on the governance of the European Union and its ability to achieve its stated objectives.

CONCLUSIONS AND PROPOSALS

Europe at a critical crossroads that calls for decisive and swift action

The new international landscape, characterised by growing geoeconomic competition, continued trade tensions (including the tariff war), rapid technological disruption, the green transition, demographic challenges (ageing populations and migration) and the need to boost security and defence spending, poses a challenge for the EU with regard to making a qualitative leap in its capacity to act.

These changes in the global order have a particular impact on the Union, as its model of growth and integration relies on a framework of international trade liberalisation, participation in global value chains, and a rules-based multilateral system. Furthermore, its global influence stems, above all, from its adherence to standards, markets and regulation.

The EU must implement a strategy focused on investment, innovation, open strategic autonomy and security in the broadest sense. Promoting a robust, sustained and inclusive recovery in economic growth, boosting competitiveness, and mobilising the necessary resources (at both national and EU levels) are now an absolute priority. The EU must also make a significant commitment to strategic technology and industrial sectors. Only then will it be able to gain greater economic and geopolitical significance by boosting its single market. To do so, it must build on its strengths: its social model and democratic values, as set out in the Charter of Fundamental Rights of the European Union, and which are its hallmarks; its economic and territorial cohesion, and its firm commitment to environmental protection.

Europe stands at a crossroads that calls for an ambitious, sustained, decisive and agile strategy. Over more than a decade of successive crises, it has demonstrated its resilience and ability to adapt, and it must now once again prove that it is prepared to tackle these structural challenges. To this end, the report identifies five priorities for action: improving EU governance, achieving a genuine single market, promoting investment as an economic cornerstone, promoting open strategic autonomy, and strengthening its external influence.

1. Improving the governance of the European Union

Based on the Draghi, Letta and Niinistö reports, the new European Commission (2024-2029) has formulated a response whose initiatives must follow the EU legislative process, one that is not always successful or rapid enough to address identified needs.

The path set out appears to address recent problems, and the main challenge lies in ensuring that the priorities set and the corresponding actions planned are implemented effectively, thus moving beyond mere formal statements. This entails overcoming the sluggish pace of EU decision-making, at the same time ensuring that this speed is not achieved at the cost of social cohesion or the safeguarding of EU values.

Institutional inertia and the difficulty in keeping pace with the demands of the current environment are limiting the effectiveness of the EU's response. At present, the governance system poses a stumbling block to the EU's ability to tackle challenges and expand European integration in a sustained manner. Providing a joint response is complex, since it requires negotiation, institutional adaptation and consensus, all of which prolong and complicate the decision-making process, thus reducing its effectiveness.

Problem: institutional inertia and challenges of governance

Within this context, it is necessary to boost the EU's capacity for action and rapid joint decision-making, both of which require improvements to its governance. Even though amending the Treaties would be the most suitable course of action, both EU institutions and Member States lack the necessary political will and consensus to undertake such a sweeping transformation.

For this reason, perhaps the most realistic and practical solution would be to make pragmatic use of the instruments already provided for in the Treaties. Despite its limitations, "enhanced cooperation" remains the best option for resolving deadlocks and making progress in key areas which often have specific deadlines. This would enable willing Member States to move forward swiftly and in a coordinated manner without being held back by a lack of broad consensus. Far from fragmenting the European project, this approach can act as a driving force for integration, promoting a process of gradual convergence and demonstrating the EU's ability to deliver tangible results.

"Enhanced cooperation" as the way forward

This solution does not preclude the need to counter the re-nationalising trend stemming from the rise of Eurosceptic views within governments and parliaments, which prioritise national interests over those of the EU; if we are to safeguard the European Union's relevance and influence as a global player.

The active involvement of social partners in this drive to improve governance is key to boosting the legitimacy and effectiveness of the EU's institutional framework. Commitment to social dialogue, at both national and European levels, ensures that EU policies contribute

Participation of social partners

to inclusive economic growth that strengthens the welfare state and promotes more cohesive and inclusive societies to counter inequality.

2. Achieving a genuine single market

The single market is one of the greatest achievements of European integration and is recognised as the Union's most valuable asset. Nevertheless, its full development continues to be held up by obstacles that are difficult to overcome, which in turn affects its competitiveness.

Joint assessment of the EU's competitive disadvantages

From the very start of the century, and following the impact of the financial crisis, the pandemic, and the war in Ukraine, the European Union has found itself at a disadvantage compared to other major economies, especially the United States and China.

There are persistent internal market barriers (the "Terrible Ten") such as regulatory complexity and diversity, the fragmented goods and services markets, and the lack of mutual recognition of qualifications between Member States. All of this hampers the flow of cross-border trade within the EU and reduces its appeal to foreign investors.

Additionally, the EU not only faces higher energy costs than its main trading partners, but also relies heavily on external sources, which affects its competitiveness and strategic autonomy. This lack of strategic autonomy also extends to other areas such as raw materials and defence.

The EU still lags behind in terms of investment in R&D&I and intangible assets, as well as in digitalisation and company size, all of these are factors that also influence competitiveness.

There is a persistent financial fragmentation that makes it less attractive when mobilising investment within the EU and channelling existing savings into productive investment. Limited access to venture capital and other alternative sources of financing, as well as an excessive reliance on bank financing also pose challenges.

Speeding up financial integration

The ESC has constantly drawn attention to the lack of financial integration within the EU and the eurozone, as an element that hinders the free flow of investment, but also poses a risk to financial stability and the EU's own economic sustainability. Progress has been slow on both the Banking Union and the Capital Markets Union initiatives, and they are yet to be finalised.

The Banking Union project, launched over ten years ago, remains deadlocked, mainly due to lack of political agreement on the creation of a European Deposit Insurance Scheme. For its part, the lack of an integrated capital market makes it difficult to raise private capital. The fact that capital markets provide less funding than banks limits access to finance for young, innovative companies in the expansion phase.

Promoting innovation is key to achieving the EU's urgent goals of technological sovereignty, open strategic autonomy, increased resilience and restoring global influence, as well as closing the productivity-wage gap.

Innovation as a key driver of competitiveness

To this end, it is essential to promote an ecosystem that is conducive to innovation. One of the key elements of this ecosystem is the existence of specialised funding channels that are capable of absorbing the relatively higher risk and delayed returns that typically characterise innovation projects. This is the reason why the drive for innovation is closely linked to the integration of the European capital market.

Promoting talent is key to the EU's competitive leap, and to establishing the "fifth freedom" of the European Single Market, which is designed to boost research, innovation and education across the region. This objective requires greater investment in the abilities and skills of workers, business owners and entrepreneurs, with a particular focus on basic skills, essential for promoting higher levels of employability, and STEM skills, which are crucial for driving technological, digital and green transformation, and additionally, are affected by a significant gender gap.

Abilities and skills: the foundations of European innovation and competitiveness

There are skills mismatches within the EU, with high levels of over-qualified individuals, especially amongst migrants. It is therefore essential to promote talent mobility via the mutual recognition and portability of qualifications and skills. At the same time, all of this must be achieved without losing sight of the fact that education and training are a right and a public good and are key to personal development and civic participation.

Investment in lifelong learning must be channelled effectively to meet the current and future needs of the business sector. This requires better anticipation of skills and, from a systemic perspective involving social partners, matching the supply and demand of skills.

It is therefore essential to consolidate the EU's internal market to capitalise on economies of scale. Doing so facilitates business growth, especially in strategic sectors, and unlocks the full potential of the various forms of enterprise within the EU, including the social economy.

Strengthening the internal market, a strategic asset for the EU

The first steps towards regulatory simplification and eliminating administrative and bureaucratic barriers have been taken through the Omnibus Regulations. This simplification must be carried out in accordance with all relevant regulations and objectives, to order to ensure legal certainty. To this end, arriving at a shared definition of the concept and scope of this simplification is essential, as well as its implementation in a way that takes into account various economic, labour and social realities.

On a similar note, the EU Inc. set of rules has been drafted as part of the 28th regime in order to facilitate the creation and expansion of businesses by providing a legal framework that supports cross-border activities.

3. Investment as an economic cornerstone

The needs that have been identified for the EU to tackle the energy and digital transitions head-on, encourage cutting-edge innovation, and boost European security and defence, all with the goal of achieving open strategic autonomy, require increased investment. In 2024, Draghi estimated that between 750 billion and 800 billion euros would be required; a year later, the ECB revised this figure to 1.2 billion euros, with an estimated 57 percent to be provided by the private sector and the rest by public funding.

The Savings and Investment Union: a new attempt at stimulating private investment

A robust and competitive European banking sector and deep, diversified capital markets are key to providing financial resources and ensuring access to efficient and reliable sources of funding, regardless of location, and to supporting the required flow of private investment. All of this will, in turn, help to boost the international role of the euro and strengthen the EU's resilience and strategic autonomy.

In this regard, the adoption of the Savings and Investment Union strategy, which is based on a proposal from the Letta report, represents a fresh attempt by the Commission to revitalise financial integration. Despite the measures included and the urgent timeline outlined by the Commission in various proposals for regulatory reform over recent months, progress in many areas requires a firm political commitment by Member States.

The priority must be to create a genuine single market for capital.

While mobilising private investment is essential, given the limited fiscal scope within the European Union, it is also necessary to consider how public funding may

Increase public funding for strategic investments

be increased in order to meet challenges that Member States are unable to address with their own fiscal resources.

Furthermore, the provision of European public goods in the sectors of energy, defence, strategic supplies and raw materials, digital technology and the fight against climate change, take the form of investments with increased European added value; these require the mobilisation of significant resources and, at times, entail risks that are difficult to bear without public funding. It is therefore necessary to build up the financial muscle of a reinforced European public sector.

However, the new Multiannual Financial Framework 2028–2034 clearly lacks ambition in terms of scale, and is insufficient to close the EU's investment gaps in various sectors. As a matter of fact, a new state aid framework (CISAF) has been adopted which seeks to simplify regulations and facilitate public support, primarily for the energy

transition. This could once again create unfair competition between Member States, given their differing fiscal margins.

Moving towards greater budgetary integration would require a substantial increase in revenue managed by the EU. This would in turn involve strengthening its system of own resources as well as give serious consideration to the issuing of joint public debt as a legitimate and permanent means of funding common policies. This would also make the EU a leading financial player and strengthen the euro as a global currency.

*Greater budgetary
integration and the
issuing of joint public debt*

Furthermore, the creation of a deep and liquid Eurobond market would represent a major step forward in the EU's financial autonomy, as it would help to reduce public and private borrowing costs across all countries, channel European savings into strategic European investments, and meet the new global demand for safe-haven assets other than the dollar.

4. Promoting open strategic autonomy

With regard to the need to promote open strategic autonomy, the EU's proposed Industrial Accelerator Act is especially noteworthy. Overall, it strikes a positive note in that the proposal introduces resilience, sustainability and security of supply criteria, seeks to boost European production capacity, and promotes more balanced international competition through the strategic use of public procurement. However, strategic sectors such as agri-foods, amongst others, are notably absent, even though recent crises have also laid bare the fact that this sector is especially vulnerable to external dependencies in certain supply chains.

*Boosting strategic
sectors*

With regard to the promotion of the European preference requirement in public procurement ("Buy EU"), care must be taken to ensure that this does not lead to reduced competition and efficiency in tendering processes or to increased costs. Furthermore, a coordinated approach must be adopted in order to avoid distortions in the single market, and maintain vigilance to ensure that third countries do not introduce similar measures that may harm European companies operating abroad.

The euro is a mainstay of the European Union's open strategic autonomy. Within a context of globalisation, digitalisation of the economy, and rise of e-commerce at a time when the use of cash is becoming less frequent, introducing the digital euro would provide a platform for a pan-European retail payment system. This would lead to increased financial sovereignty, help deepen the single market and reinforce the international role played by the single currency.

*Promoting the
digital euro*

Making energy more affordable

Within the energy sector, the EU's Affordable Energy Action Plan undoubtedly represents a step in the right direction towards energy independence and reducing price volatility. However, there are significant economic, technical and bureaucratic obstacles to its implementation in the short-term; of which, the biggest obstacle is the need for a large-scale and rapid roll-out of electricity and gas grids connecting Member States. Without this critical infrastructure, it is impossible to create a truly resilient single energy market that can effectively distribute surplus renewable energy to high consumption areas.

Additionally, the *RESourceEU plan* could boost the EU's strategic autonomy by securing access to critical raw materials that are especially important for the roll-out of renewable energy infrastructure and therefore, for lessening external energy dependence. Positive aspects worth noting are its focus on risk management, coordination and supply diversification; however, its effectiveness will depend on proper implementation and the actual capacity to strengthen European value chains.

Increased security and defence capabilities

Given the deteriorating geopolitical environment, strengthening European defence policy has become essential. There is a need to promote greater investment, coordination and industrial integration in order to reduce dependencies, enhance capabilities, and move towards greater strategic autonomy.

In any case, achieving this goal requires overcoming persistent structural obstacles such as fragmentation, duplication, lack of interoperability and technological dependence on third countries. But above all, there must be genuine political willingness of Member States to coordinate their efforts, cede some degree of sovereignty, and define the scope of the EU's autonomy.

5. Strengthening the European Union's international business presence

Strengthening the European Union from within will revitalise its potential for growth and enhance its economic and social resilience, thereby strengthening its international presence. A more cohesive, agile and effective EU will be better placed to uphold a rules-based international order, promote multilateralism, maintain open trade on fair terms, and lead the transition towards a sustainable model of development.

Within the current context of fierce geopolitical competition and a trade war led by the United States, the EU has made significant progress in trade integration with the rest of the world. This international projection is of critical importance, and it is based on seeking reliable partners and diversifying to reduce critical dependencies, strengthen economic security and promote open strategic autonomy. In any case, when faced with coercion, the EU should not hesitate to deploy the anti-coercion instrument adopted in 2023.

The flood of trade agreements that have recently been concluded after several years of negotiations, such as the EU-Mercosur Agreement, not only demonstrates the urgency felt by both the EU and its trading partners to strengthen their international presence and promote trade and investment ties, but also proves that there are countries and blocs that remain committed to trade liberalisation and a rules-based international order.

6. A European Union that acts as a reference and is equal to the challenges posed

European integration remains one of the greatest political, economic and social achievements in contemporary history. The fact that twenty-seven Member States with different historical, cultural and economic backgrounds have established a common institutional framework that is the first of its kind, is in itself a remarkable achievement, more so given that this cooperation is based on shared democratic values and it upholds a social model that guarantees the welfare state and benefits all citizens. In fact, Europe continues to be a prosperous region that an increasing number of countries seek to join, as demonstrated by their applications for EU membership.

Yet, much remains to be done. Contemporary challenges –from geopolitical competition to energy, migration, economic and security crises– require a more decisive Europe that can overcome existing problems in its internal governance system. The EU must strengthen its capacity to respond by introducing more flexible and effective decision-making mechanisms that can swiftly translate political priorities into concrete actions with real impact.

To achieve this, a firm and sustained commitment by Member States is essential. Without a shared political will, any attempt to improve institutional effectiveness and deepen integration will be limited.

However, until this consensus is reached and despite its limitations, enhanced cooperation is the best means of avoiding a deadlock and making progress in key areas. Many of these areas, which are included in the Commission's roadmap and shared by the Council itself, have specific deadlines for implementation; thus, avoiding any delay in meeting these deadlines justifies the use of this enhanced cooperation.

Ultimately, a Europe that is capable of rising to challenges requires a combination of strategic ambition, operational effectiveness and political will. Only in this way can we strengthen the European project and ensure its relevance within an increasingly complex international landscape.