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PERSPECTIVES ON THE EU ECONOMY AND THE IMPORTANCE OF
ENHANCING COMPETITIVENESS*

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Ministers

Distinguished Guests

Ladies and Gentlemen

Thank you for the invitation to contribute to this exchange. I am grateful to Minister Keravnos and to the organisers for the opportunity to engage with you on matters of critical importance for the EU's economic policy framework in the context of the Cyprus Presidency of the Council of the EU.

Allow me to share some observations informed by research and by long standing engagement with EU policy debates.

A major point suggested by the analytical material prepared for this meeting indicates that the EU's post crisis export performance has to a significant extent masked underlying structural weaknesses, particularly in productivity and innovation and that the current global environment is now exposing these constraints more visibly.

This interpretation is important but it is not sufficient on its own. It captures part of the reality but not the full complexity of the current European economic conditions. The issue is not only that productivity has been weak. Moreover, the economic paradigm of the EU has produced uneven outcomes, including pressures on social cohesion, divergence across member states and structural vulnerabilities that extend beyond productivity indicators.

* *Speech by Professor Andreas Theophanous at the Informal ECOFIN meeting which took place on May 22, 2026.*

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Competitiveness as a Systemic Outcome

Competitiveness has long been a shared objective of the EU as it is reflected in successive strategies. What has changed is the environment within which it must now be pursued.

We are operating in a context characterised by geopolitical fragmentation and conflict, structurally higher energy costs, tighter financing conditions and intensified technological competition. These characteristics define the current realities.

In this setting competitiveness should not be understood as a narrow outcome measured by exports or cost indicators. It is a systemic outcome. It reflects how institutions, investment patterns, innovation capacity, energy structures and financial systems interact over time.

This also implies that competitiveness is shaped not only by efficiency but by how adjustment processes are distributed across societies. In this respect it must be acknowledged that the current EU economic paradigm has in several cases been associated with increasing inequality, pressure on the middle class and growing social fragmentation. These developments directly affect the sustainability of economic policy.

Productivity, Investment and Structural Reality

The emphasis on productivity is justified. However, productivity does not exist in a vacuum. It is embedded in a broader economic and institutional context.

European productivity growth has been weaker in comparison to competing economies. Addressing this gap is not simply a question of increasing investment or deepening capital markets. There is a tendency to assume a relatively direct relationship between investment, financial deepening and productivity outcomes. In reality the relationship is far more complex.

Productivity also depends on institutional quality, regulatory efficiency, the structure of finance, the capacity of firms to scale, the broader governance framework and of course energy prices. In addition, the issue is not only how much capital is mobilised but how effectively it is allocated and utilised.

It is also important to recognise that the relationship between productivity investment and competitiveness is not purely mechanical. The reallocation of resources toward more productive sectors, the deepening of capital markets and

the expansion of private investment operate within institutional and social settings that shape their effectiveness.

Adjustment processes may involve transitional costs across sectors, regions and labour markets. These dynamics can influence both the pace and the sustainability of reform. The challenge is therefore not only to accelerate productivity growth but to ensure that the conditions under which it is achieved do not undermine cohesion or the long-term sustainability of the competitiveness agenda.

Innovation, Bureaucracy and the Business Environment

The EU does not lack knowledge or human capital. It faces constraints in translating these into innovation and scale.

A central issue is bureaucracy and regulatory fragmentation.

European startups operate within multiple legal systems, fragmented markets and complex administrative procedures. These conditions slow down innovation, delay scaling and create incentives for firms to relocate.

In order to advance competitiveness the EU must reduce unnecessary administrative burdens, simplify regulatory frameworks and improve the speed and predictability of decision making. This is not a marginal issue. It is central to the capacity of the EU economy to generate and retain innovation.

Energy, the Green Transition and the Standard of Living

Energy is a central dimension of competitiveness. European energy prices remain structurally higher than those of key competitors. This affects industrial activity, investment decisions and household welfare.

The Green Deal is a necessary objective. However, its implementation must be carefully re-designed. If the transition significantly increases the cost of living, weakens industrial competitiveness or places disproportionate burdens on certain member states, it will be associated with serious economic and political constraints. The issue is not whether to proceed but how to proceed.

Energy policy must place greater emphasis on affordability, stability infrastructure and security of supply. Without addressing the energy cost issue, broader competitiveness objectives will be difficult to achieve. And inevitably these issues also involve political dimensions and decisions.

Divergence and Structural Diversity

Competitiveness must also be assessed in the context of divergence within the EU. Member states differ significantly in their economic structures, institutional capacities, energy profiles and fiscal space. A one size fits all approach is therefore not appropriate.

Policies designed at the EU level must take into account structural diversity and allow for differentiated implementation where necessary.

Cyprus illustrates this clearly. As a small and geographically peripheral economy it is particularly exposed to energy costs, financing constraints and scale limitations.

These structural asymmetries became especially visible during the 2008 crisis, when adjustment within the Eurozone was not experienced uniformly across member states. In the case of Cyprus, the 2013 package included harsh measures such as the depositor haircut.

Recent reflections by senior European officials, including Juncker and Dijsselbloem, on the management of the Greek crisis have also contributed to a broader recognition that, in some cases, adjustment policies may have been excessively severe. This underlines the importance of ensuring that future crisis management combines financial stability with proportionality and social cohesion.

The Role of the State

We must acknowledge that the role of the state is important.

The state must perform its strategic, social and referee role. The objectives include supporting economic growth and development, social cohesion, stability and fairness. Preventing excessive inequality and social exclusion are also particularly important. We should also ensure that public spending leads to the best possible results.

The same level of expenditure can lead to very different outcomes depending on how it is allocated and implemented.

Labour Markets, Wages and Social Sustainability

There is a need for caution regarding labour market deregulation and wage restraint as instruments of competitiveness. While flexibility can support

adjustment, excessive reliance on wage compression and precarious employment can lead to increased inequality and social instability.

Such developments can also have long term economic consequences including weaker domestic demand and reduced incentives for family formation. This is particularly important in the context of an ageing EU population.

Competitiveness cannot be built on social erosion. It must be based on productivity innovation and a stable social environment.

The External Dimension and the Role of the EU

Competitiveness is also affected by external conditions. Geopolitical instability and conflict have significant economic costs. They affect energy prices, trade flows, expectations, investment and overall economic confidence. Wars are costly.

For this reason, the EU must strengthen its geopolitical and diplomatic role in order to enhance its capacity to contribute to de-escalation and stability. This is not only a political objective. It is an economic necessity as well.

Governance and Trade Offs

Competitiveness is also influenced by governance.

The EU is pursuing multiple objectives simultaneously; these include the green and digital transitions, fiscal sustainability, social cohesion and global competitiveness.

These objectives are legitimate but their interaction must be carefully managed. If trade-offs are not addressed explicitly, they will be resolved indirectly often in ways that increase divergence and weaken policy effectiveness.

Concluding Remarks

The competitiveness challenge confronting the EU is not simply one of addressing productivity issues. It involves reconciling a more demanding external environment with an internal economic and institutional framework that was shaped under different and in many respects more favourable conditions.

The challenge is therefore not only to raise productivity and mobilise investment. It is to do so in a way that does not increase inequality, does not undermine social cohesion, does not weaken the productive base and does not ignore structural diversity across member states.

Competitiveness must be economically effective, socially sustainable and institutionally coherent.

At the same time, it is important to recognise that the credibility of the EU's economic strategy will ultimately depend on its capacity to deliver tangible improvements to living standards, to maintain social balance and to ensure that economic transformation is perceived as fair and sustainable across all member states.

Thank you very much