

## A Commission of concrete steps rather than grand strategy

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**T**he von der Leyen Commission inherits a Union that has largely overcome its ‘polycrises’. The economy has stabilised and employment continues to grow, despite the slowdown in the global economy. Apart from some fluctuations in the risk premium on Italian government bonds, the financial markets are largely without tension. The flow of refugees has fallen to a fraction of the peak registered three and four years ago.

At the same time, trust in the EU and its institutions has increased steadily across most member states, reaching near-record values, and participation rates in the recent elections for the European Parliament also increased considerably. Against this background, it is not surprising that the various Eurosceptic parties did not do as well as expected in these elections.

In the absence of unforeseen major shocks, the EU institutions should now be less engaged in crisis management and more able to pursue a long-term strategic agenda. The President-elect of the European Commission has also set out her overall programme, which is highly ambitious in many respects, hits all the right notes in terms of policy prioritisation but, significantly, does not recognise any trade-offs between different goals.

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Recognising trade-offs is essential for policymaking. For example, protecting citizens from terrorist threats might necessitate limitations to their freedoms. Fostering a climate-neutral Europe has costs that might weigh on growth and be difficult to distribute fairly. Any concrete political strategy will need to address these trade-offs – which political leaders typically fail to do.

Part of an ongoing series of CEPS publications exploring how the incoming Commission can best approach the multiple challenges facing the EU.

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In a string of policy contributions, CEPS will continue to expand on the choices to be made and actions that are needed in different areas to achieve the lofty overarching goals of this new Commission.<sup>1</sup>

In this Policy Brief we limit ourselves to identifying the overall strategic backdrop against which the EU institutions must operate during their new mandate and single out two key challenges. They are not new but have taken on such importance that they are likely to represent long-lasting trends that should be taken into account in any EU policy.

These two issues are very different in nature and pose different problems. One is external and one is internal:

1. The fundamental internal issue is to counter the threat to the rule of law and democratic values in some member states.
2. The fundamental external issue concerns the geopolitical position of Europe in an increasingly disordered world, now seemingly dominated by a struggle for primacy between the US and China.

Safeguarding the rule of law is an essential element of the Union. But existing instruments are not sufficient to uphold it. The emergence of China, coupled with the rise of authoritarian regimes in other important countries poses an even thornier issue. Meeting this challenge would necessitate, first, a proper definition of the role the EU would like to play at global level, and then a realistic appraisal of the available policy instruments that could be used to transform the EU into a real global actor.

Our recommendations can be summarised as follows:

1. A key element in the changing global environment is the emergence of an increasingly assertive China as a major economic, political and technological power. This is unavoidable, given the huge investment in human and capital the country is undertaking. In our view, the Chinese state contributes little to economic success compared to the 'brute force' of this accumulation of the basic factors of production. The EU should not succumb to the temptation to create some ill-defined industrial policy just because China does so.
2. China is becoming increasingly authoritarian and will not necessarily be an easy partner or rival to deal with. Nevertheless, the EU should not second futile US efforts to limit China's development. The EU thus needs to conserve and strengthen its 'strategic autonomy'.
3. The rise of China is occurring at the same time as the world is becoming ever more digital. Digital technologies, such as 5G or artificial intelligence, have not only economic

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<sup>1</sup> See the contributions of CEPS staff to S. Blockmans (ed.), *What Comes After the Last Chance Commission? Policy Priorities for 2019-2024*, Brussels: CEPS Paperbacks, February 2019, and our designated [web page](#).

but also security implications, blurring the line between soft and hard power. To preserve Europe's autonomy and prosperity in this rapidly changing digitised global landscape concrete actions in a limited number of key areas are required. Without them 'strategies' often amount to little more than declarations of intent that member states ignore whenever their perceived national interests are at stake. Concrete action is needed in the areas of telecommunications networks, especially common auctioning and supervision of spectrum, common cyber defence, etc.

4. Efforts to safeguard the rule of law should be de-politicised. The Justice Commissioner, who should act independently of any national or ideological position, should be given the sole right to make proposals to initiate proceedings (as for Competition). The Vice President responsible for this area should not be allowed to interfere with this brief. The College would of course be free *not* to follow the proposal of the Justice Commissioner, but the proposal itself should be made public and the College would have to justify its reasons for not following the proposal.

### Safeguarding Europe's prosperity and security

The integration process has so far focused mainly on domestic issues. This was understandable while Europe's security was guaranteed by the trans-Atlantic Alliance, and major powers in the neighbourhood seemed to evolve towards democratic values.

Today it is not only Europe's neighbourhood that has become unstable. The entire geopolitical landscape is unsettled, with non-democratic powers on the rise. Promoting European interests and values on the global stage has become increasingly difficult under these circumstances.

### China a 'systemic rival'?

A recent [joint Communication](#) by the Commission and the HR/VP on China has rightly recognised that a more self-assertive China poses a challenge in several respects. It finds that China is:

... in different policy areas, a cooperation partner with whom the EU has closely aligned objectives, a negotiating partner with whom the EU needs to find a balance of interests, an economic competitor in the pursuit of technological leadership, and a systemic rival promoting alternative models of governance.

Labelling China a 'systemic rival' has revived the notion that Europe would somehow need to adapt its economic model to remain competitive at the global level. In particular, it has been argued that Europe needs its own industrial policy to nurture 'European champions' and that it should protect its strategic industries against takeovers from foreign state-owned or state-led enterprises that might acquire critical technology. The latter concern has led to the creation of a new investment- screening mechanism, which should be fully operational by late 2020.

However, a sober look at the numbers suggests that concerns about important parts of European industry possibly being ‘sold out’ to the Chinese seem overblown. A recent [detailed report of the JRC](#) shows that FDI by Chinese State Owned Enterprises amounted to only about €120 billion over the last 10 years. This is equivalent to about 2% of all FDI from third countries, and much less than investment by State Owned Enterprises from the Gulf region. Even if one were to classify all Chinese firms as ‘state led’, the total sums invested by Chinese entities

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remain below 1/20<sup>th</sup> of all FDI. Moreover, there is little evidence that Chinese investors have targeted ‘strategic’ sectors. There have been attempts (some successful, others stunted) at taking over European companies specialised in chips and robotics but the share of FDI from China in electronic and electric equipment and software is even lower than their overall share. There have been scattered investments in some peripheral port facilities (Piraeus) and roads and bridges in southeast Europe, but these cannot really be considered of strategic importance.

The attention the EU’s FDI screening mechanism has attracted seems to be out of proportion to its real-life importance. On present trends, it might have to deal with at most a dozen cases each year. Moreover, this screening mechanism only imposes some requirements on member states to provide information to the Commission. Its basic principle is that “[national security remains the sole responsibility of each Member State](#)” (Article 4(2) TEU). This means that all decisions on whether to block any particular FDI project on grounds of national security will remain at the national level, with each individual member state free to take its decision based solely on its own national interests and perception of national security.

### Limits of the state-led model

The description of China as “a systemic rival promoting alternative models of governance” refers to its state-led model of growth. However, in this case as well, a careful analysis suggests that this state-led model has its own serious drawbacks. Views of the role of the state (or, equivalently, the Communist Party) in China have undergone a remarkable about-turn. Not so long ago, the general advice to the Chinese authorities was to reduce the scale of state involvement in the economy because State Owned Enterprises (SOE) are generally far less efficient than the private sector. Today, the perceived wisdom is that it is the guiding role of the state that is behind China’s emerging dominance of some high-tech sectors. The Made in China 2025 programme is usually cited as the prime illustration of the role of the state in expanding its dominance in key technological sectors.<sup>2</sup> However, the reality remains that

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<sup>2</sup> Views of the role of the [Ministry for Industry and Trade in Japan \(MITI\)](#) also changed radically once Japan’s growth miracle petered out in the 1990s. During the growth spurt in Japan (the 1970s and 1980s) the MITI acquired almost mythical status and many countries were advised to copy this model of the state fostering growth by channelling resources to strategic sectors. When growth slowed after the bubble-burst of the late 1980s it became apparent that the MITI had also supported many sectors that did not succeed.

Chinese SOEs continue to have much lower profitability than private enterprises (about one third). They are thus unlikely to pose a systemic challenge to Europe's economy.

It is clear that in some individual sectors massive investment subsidies can give specific sectors a competitive advantage. But the cost of these subsidies has to be borne by the rest of the economy, which then becomes less competitive. The advantage of the few favoured sectors is more visible than the cost imposed on the rest of the economy. This is why a state-led investment drive can appear successful if one focuses only on those sectors that receive state support. Yet even massive support is not always sufficient to create 'champions'. The steel sector in particular has become a considerable drain on government finances. In this sector China seems intent on repeating the mistakes made in Europe during the 1980s when over-capacity was maintained for too long at a considerable cost to the economy.<sup>3</sup> This would suggest that the best way to slow down China would be to encourage a greater role for SOEs.

### Does Europe need to change its model?

A sober evaluation of the situation thus suggests that the rapid rise of China is mainly based on strong fundamentals, namely an extraordinary rate of investment in capital, including public infrastructure coupled with a high-quality education system, rather than the guiding role of the party/state. However, there is a strong feeling that Europe is losing ground in the global technological race and that something should be done about this.

*Modern industrial policy is not about the state 'picking winners' (be it the EU or its member states).*

A first answer is often to adapt Europe's 'industrial policy'. But this vague term can encompass many different aspects. It is now generally agreed that modern industrial policy is not about the state 'picking winners' (be it the EU or its member states). Fostering more investment in education, world-class research universities and more R&D in general are all uncontroversial ideas. They have been on the agenda for decades and should be pursued with renewed vigour. But the gap in investment is unlikely to be filled, even if a significant proportion of the EU budget is shifted to Research and Development. The relative decline of both Europe and the US is likely to continue for some time.

Competition policy is often cited as a key element of industrial policy and it has been proposed recently that European competition policy should be subordinated to the goal of creating European champions. This is not a new idea; it should be resisted today for the same reason that it was not accepted in the past. The purpose of EU competition policy is to block monopolistic or oligopolistic market structures on our internal market, which in the end do not foster growth. Other instruments such as anti-dumping mechanisms can be used if foreign enterprises benefiting from subsidies sell into the internal market.

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<sup>3</sup> Discussion about economic sovereignty for Europe is also not new; see F.A.M. Alting von Geusau & J. Pelkmans (eds.), *National Economic Security: Perceptions, Threats and Policies*, Tilburg: Transactions Publishers, 1982.

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The Siemens-Alstom case is often cited as an example of an industry (i.e. high-speed trains) where support from the Chinese government has led to the creation of a global champion that dwarfs these two European enterprises. However, the Commission finding that the size of the Chinese competitor was of little importance for the goal of preserving competition on the EU market was unanimously supported by all national competition authorities. The blocked Siemens-Alstom merger does not therefore provide an illustration of the need to relax EU competition rules to create European champions. When Chinese global champions dominate markets in third countries the best reaction would be to appeal to WTO rules and OECD guidelines on export financing.

More generally, one should keep in mind that the proposition that state intervention can foster economic growth can only make sense in sectors where there are economies of scale or scope. Experience has shown that this condition is satisfied only rarely. Artificial intelligence, with its reliance on large databases, might be such a sector. But in this sector the main obstacle is not EU competition policy, it is a fundamental issue of values.

### The EU and the Sino-US competition for strategic dominance

The rise of China also poses a wider challenge, beyond economics. Remarkably, the Joint Communication on China from March does not even mention US-China tensions or the impact the EU's China policy might have on transatlantic relations. This is a crucial oversight given the emerging conflict between America and China, which is becoming a struggle for geopolitical dominance.

This clash of the titans puts Europe in a difficult position. On the one hand, the EU shares the fundamental values embedded in the US Constitution and its strong democratic traditions. On the other hand, many of the recent unilateral measures of the US violate international norms and thus run counter to the EU's preference for rules and quiet diplomacy. A key issue is thus whether (and how) the European Union can develop its own strategic autonomy.

The feeling of a community of values across the Atlantic has so far survived the presidency of Donald Trump, who has professed little attachment to these values. Nevertheless, civil society and the system of checks and balances remains very much alive in the US, showing a grassroots adherence to democratic values. This is the key for a continuation of the Trans-Atlantic alliance.

*Confrontation with China is thus not an attractive policy for Europe.*

China, by contrast, is clearly moving towards an autocratic system in which freedom of expression is increasingly curtailed. The hope that rapid economic progress would lead to a more open China has not materialised. On this point the US and Europe agree. On the other hand, the US and Europe have a very different view of the potential threat China poses to national (or European) interests. The EU is not a Pacific power and does not see China as a geopolitical competitor. European interests in Asia in

general are mostly commercial. Confrontation with China is thus not an attractive policy for Europe.

The US, by contrast, is also a major Pacific power and thus perceives China to be the biggest threat to its own global pre-eminence. For the time being, it has chosen confrontation on a broad range of issues. This is not a path on which Europe should follow the US. Confrontation is anyway unlikely to slow down the economic progress China continues to make. A very high rate of domestic savings coupled with the extraordinary spread of high-quality education, especially in hard sciences, virtually ensures that growth will continue for some time and that the country will catch up in technology on a broad front. Given the millions of engineers and other scientists being churned out by Chinese universities it is inevitable that the country will dominate in some technologies. But even if, within a generation, China has as many scientists as Europe and the US combined, this does not mean that China will dominate all high-tech sectors. The raw numbers suggest that China will have the capacity to dominate a number of fields, but it remains to be seen whether tight political control over public opinion is compatible with innovative science and technology. The long-term advantage of a democratic system should not be underrated.

Yet China is not an entirely benign power. Increasingly authoritarian at home, it generally has little regard for human rights abroad. The official aim of the Belt and Road Initiative (BRI) is to improve connectivity between the two sides of the Eurasian landmass. It could, however, also be seen as an attempt to create a chain of vassal states. Even if this were the case, there is little point in an elaborate EU response. The most enthusiastic recipients of BRI financial support are countries with few economic prospects due to serious internal governance problems (especially in the so-called Stans). India, the only major economy between Europe and China, does not participate in the BRI.

The EU can limit the impact of BRI initiatives in Europe by insisting on its core principles of transparency, state aid and competition rules. Moreover, the EU should intensify its relations with India, which, while trailing China's development by about a generation, has a much higher economic potential than most BRI participants.

### The EU in the global power game: hybrid rather than soft power

The EU has often been portrayed as a big 'soft power', able to promote its rules and standards, but as lacking in 'hard power', i.e. the military. However, it now seems that 'hybrid power'<sup>4</sup> is becoming more important than either the purely soft or hard variety. Elements of hybrid power can be, for example, disinformation campaigns, cyber-attacks, export controls, and maybe even targeted strategic investment.

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<sup>4</sup> Nye has popularised the term 'smart power' which, in his view, represents a combination of soft and hard power. This term does not seem appropriate for the EU, which does not possess any hard power.

It is in these new areas that Europe is being challenged and must find ways to react, thus developing its own strategic autonomy. The traditional elements of soft and hard power remain relevant but the challenges in these domains are well known. Europe's soft power depends in the first instance on economic instruments such as the common trade policy and the attraction of the internal market. These elements remain important but are destined to decline in effectiveness as the share of the EU in the global economy shrinks.

A standard recommendation is that the EU should uphold the rules of the WTO and the multilateral trading system in general. This is certainly something the EU should aspire to, but it is unlikely that the EU can achieve much when both the US and China behave differently. The US complains openly about WTO procedures and is pursuing, at the same time, a China policy, which ignores all multilateral rules. China professes great attachment to the WTO and the multilateral trading system but has so far refused to budge on key points such as the role of SOEs or the opaque nature of the state's role in the economy. This is unlikely to change much given that these are essential features of the 'Chinese model'. These are some of the real-world limits to the EU's soft power.

*Cyber security is the hybrid domain par excellence whose importance can only increase over time.*

The EU is now also taking steps towards hard power, but they are limited to coordination in research and procurement – an approach that has actually received a boost from an aggressive Russia, the America First policy and Brexit. A 'European army' remains a vague and distant goal, shared by few. By contrast, the EU should be able to acquire its own instruments of hybrid power. Cyber security is the hybrid domain par excellence, whose importance can only increase over time.

## Concrete steps

What could be done to safeguard the prosperity and security of Europe in this challenging global environment?

There is little need to create new structures. The weakness of Europe is in many ways a result of the very uneven integration of markets and the desire of member states to retain the exercise of competences they regard as key to protecting their sovereignty.

The best way forward remains thus the Monnet method, as quoted by the President of the ECB in a recent speech:

The problems that our countries need to sort out are not the same as in 1950. But the method remains the same: a transfer of power to common institutions, majority rule and a common approach to finding a solution to problems are the only answer in our current state of crisis.

What is needed today is not a wholesale transfer of competences, which is politically unattainable in many sectors anyway, but concrete steps in key areas where political will does exist.



A notable example is the crossroads between telecommunications and cyber defence, where important benefits can be obtained to strengthen the strategic autonomy of the EU.

At present, every member state keeps its own network regulation and supervision under national control. The allocation of frequencies for the 5G network has been conducted entirely at the national level, with widely different rules and conditions. As a result, there is no integrated market, which hinders the emergence of European champions in this industry.

Moreover, the defence against cyber-attacks, disinformation etc. of the (national) networks is managed at national level, with only a very weak coordination function by the European Union Agency for Network and Information Security (ENISA). This EU agency has few staff (less than 100) and has been located at the very periphery of the EU (in Crete). This set-up damages both security and the economy. Telecommunication networks are highly integrated across borders and many cyber-attacks will involve more than one member state or might pass through several member states in order to hide the origin of the attack. There are obvious economies of scale to be gained from integrating cyber defence across the EU. At present each national authority has only imperfect knowledge of what is happening in the rest of Europe. What is needed is thus a true European cyber-defence capability.

How this is achieved is secondary. A radical upgrading of the functions of ENISA would be one way. The creation of a new Union body would be another way. Such a European Cyber Defence Authority would not only enhance cybersecurity in general, helping to pin down the origins of attacks; it could conduct the tests of suppliers of 5G and certify them for the internal market, avoiding the duplication inherent in the present situation.

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The cyber domain thus offers a vivid illustration of the way progress could be made through concrete and circumscribed transfers of competence. There is no need to develop grand strategies or to subject all of economic policy to geostrategic objectives. The best basis for prosperity remains an open and competitive internal market. European security can best be safeguarded by common action in key areas.

## Defending the rule of law

There is an erosion of the basic tenets of the rule of law in some member states. This is a slow-moving development but its continuation threatens the foundations of the Union. The EU is not just an association pursuing material goals it is also a community of shared values. Moreover, most EU policies are implemented by member states. A functioning rule of law and its implementation on the ground is thus essential if a common policy is to produce the desired impact throughout the Union's territory.

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## The separation of powers

Threats to the rule of law come from two directions. First of all, some member states have recently enacted reforms of their judiciary that would appear to give governments more political control. This contradicts the principle of separation of powers. An independent, politically neutral judiciary constitutes the basis of rule of law.

However, in reality, the separation of powers can never be absolute. The executive provides the financing for the judiciary and ministries of justice have important managerial roles concerning, for example, the careers of judges and the assignment of cases. There is thus a considerable grey area between a totally independent judiciary and an unacceptable degree of political interference with its operation. Moreover, in many cases governments with illiberal tendencies use formal rules or regulations that also exist in other countries but are exercised with self-restraint, resulting de facto in an 'a-political' judiciary. The application of rules with a clear political intention is what counts in practice.

A second threat to the rule of law arises from the malfunctioning of the management and application of justice. The basic form is the simple corruption of individual judges or magistrates to serve private interests. But in some countries this phenomenon has gone beyond occasional bribes to secure a favourable judgment. The infiltration of private interests into prosecutorial services has gone so far that criminal and other investigations can be directed at particular individuals, often those tasked with combating corruption. This problem, often called state capture, is fortunately limited to only a few member states. But corruption and other forms of private influence are more diffuse and even more difficult to measure, let alone combat.

A key challenge for the EU will thus be to uphold the principle that the rule of law requires an independent and effective judiciary. This will be an uphill struggle. Improving the administration of justice in countries where it is mired in corruption or hobbled by mismanagement leading to excessively long proceedings should become a second leg of a rule of law strategy. Of course, the administration of justice remains an exclusive member state competence but peer pressure (for example an annual report on corruption and more publicity to scoreboard indicators) could be combined with offers of technical assistance from the Structural Reform Support Service.

## Upholding the rule of law: Article 7 versus the ECJ

The procedure under Article 7 of the EU Treaty is of limited use. First of all, it constitutes an 'ultima ratio' mechanism and requires unanimity minus one, which is impossible to achieve, as experience has shown, if more than one government is trying to limit the independence of the judiciary. Secondly, the Article 7 procedure is intrinsically political. It can easily be perceived as unfair when it is directed against governments from a particular political family.

The attempt to link access to Structural Funds to the rule of law, which was first proposed by the Juncker Commission, seems more promising. But it also has a number of drawbacks. First, it would be asymmetric, as it would be most efficient against poorer countries. Richer countries, which receive few Structural Funds, would be immune from this 'punishment'. Second, the

underlying problem of the Structural Funds is the proper spending of EU money, which is not always the same as general malfunctioning or undue influence over the judiciary for broader political reasons. The controversy surrounding the involvement of the Czech Prime Minister in firms that were alleged to have misused Structural Funds and the reaction of the Czech government to an investigation into this matter is an example that underpins the notion that the rule of law is a necessary condition to protect the financial interests of the Union. But this does not have to be the case everywhere. At any rate, there are already strong safeguards for the financial interests of the Union in the form of OLAF and EPPO. The latter will soon start work and will have to prove its effectiveness. The problem which remains is that both OLAF and EPPO can only look into specific cases of corruption, misuse of Structural Funds or large-scale cross-border VAT fraud, not into the state of rule of law in general.

The only institution that has so far been able to have an impact is the Court of Justice. The ECJ has recently declared some aspects of a controversial Polish law on the Supreme Court of the country as contrary to EU law and a breach of the principle of the irremovability of judges and thus that of judicial independence. This precedent-setting judgment establishes the principle that the independence of the judiciary is part of the fundamental principles of the Union and therefore subject to judicial review in Luxembourg.

*The fight to uphold the rule of law cannot be left to the ECJ.*

But the fight to uphold the rule of law cannot be left to the ECJ. Threats to the rule of law result ultimately from systemic problems, which cannot always be linked to a few specific and identifiable laws or regulations and a discretionary decision by a 'political' Commission to pursue infringement procedures before the ECJ.

## De-politicising the enforcement of the rule of law

Upholding the rule of law will require a sustained effort by all institutions and a broad-based commitment by member states. Given that the Council will continue to be dogged by internal problems in this area, a key role will fall to the Commission and European Parliament. However, care needs to be taken that the Commission does not appear to become 'politicised' in the sense that its infringement actions are influenced by party political considerations.

One solution would be to strengthen the position of the Justice Commissioner inside the College. The Commissioners for Competition and for ECFIN have specific prerogatives inside the Commission in that they are the only ones who can make proposals for action in their area. This principle should be applied for rule of law issues as well. The Justice Commissioner, whose independence and impartiality vis-à-vis the member state under investigation must be guaranteed, should be given the sole right to make proposals to initiate proceedings (a similar arrangement already exists for Competition cases and for proposals under Excessive Deficit procedure). The Commissioner should rely as much as possible on impartial outside advice, such as from the Venice Commission, the Council of

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Europe, the European judicial network, etc., and his/her proposal would have to be made public. The College would of course be free *not* to follow that proposal, but it would have to 'motivate' its reasons for not doing so. As such, the final choice of whether or not to initiate a 'Rule of Law' infringement procedure against a member state would depend less on the discretionary judgement of a '(geo)political Commission'. The appointment of a Vice President responsible for Values and Transparency risks muddling the responsibility of the Justice Commissioner responsible for the rule of law since the (non-executive) Vice President is in principle supposed to have an oversight role in this area as well. This blurring of responsibility should be avoided. The Commission should clarify that the Justice Commissioner for the rule of law will act in full independence.

## Conclusions

Announcing a "geopolitical Commission", President-elect Ursula von der Leyen expects her restructured institution to be better equipped to tackle the global forces unleashed by a protectionist America First policy and an increasingly assertive China. It remains to be seen, however, whether the new Commission will be able to maintain its role as guardian of the Treaties on issues pertaining to the protection and enforcement of the rule of law.

Our overall conclusion is thus simple: implementing concrete, if limited, steps in these two crucial areas will do more good for the EU and the European integration process than taking refuge behind resounding rhetoric and grand strategies.



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