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Ambition Without Precision: Why the Industrial Accelerator Act Falls Short*

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Industrial Policy Lab

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Abstract

Presented by the European Commission on 4 March 2026, the Industrial Accelerator Act (IAA) marks the Commission's most ambitious initiative to strengthen the Union's industrial base, aiming to raise manufacturing to 20% of EU GDP by 2035. Framed as a response to decarbonisation pressures, geopolitical fragmentation and competitiveness concerns, the IAA combines, among others, strategic sector designation, the creation of green lead markets, local content requirements (LCRs) and foreign direct investment (FDI) requirements. It thus marks a significant shift in the EU's industrial policy paradigm towards more conditional and more geopolitically targeted intervention.

This policy brief evaluates the economic coherence and proportionality of the IAA's design. We argue that the Act combines heterogeneous objectives on decarbonisation, geopolitical concerns and competitiveness, without sufficiently distinguishing their respective economic rationales. This lack of precision is already visible in the definition of strategic sectors. In particular, to pursue competitiveness and geopolitical goals, the IAA lacks a sufficiently forward-looking approach. The newly introduced industrial policy instruments of LCRs and FDI requirements primarily respond to China. Over the last decade, China has built up a rising industrial base through state-coordinated industrial policy, thereby increasing competitive pressure on the European economy. To limit risks associated with these new instruments, such as higher input costs along value chains or retaliation under international trade rules, the IAA requires clearer objective prioritisation, more precise targeting of instruments and a continued commitment to openness towards trusted partners within a rules-based trading system. At the same time, the objective of raising manufacturing to 20% of EU GDP by 2035 is neither a meaningful economic objective in itself nor one that the IAA is realistically designed to achieve.

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Abbreviations

AI	Artificial intelligence
EEA	European Economic Area
ETS	Emission Trading Scheme
EU	European Union
FDI	Foreign Direct Investment
FTA	Free Trade Agreement
GPA	Agreement on Government Procurement
GATS	General Agreement on Trade in Services
IAA	Industrial Accelerator Act
LCR	Local Content Requirement
NACE	Nomenclature of Economic Activities
R&D	Research and development
U.S.	United States
WTO	World Trade Organization

1 Introduction

Presented by the European Commission on 4 March 2026, the Industrial Accelerator Act (IAA) marks the Commission's most ambitious recent attempt to strengthen Europe's industrial base (European Commission, 2026b). It combines an explicit objective of raising manufacturing from 14.3% of EU GDP to 20% by 2035 with a broader effort to respond to decarbonisation pressures, geopolitical concerns and competitiveness challenges. In this sense, the IAA is presented as a strategic industrial policy initiative that seeks to address multiple structural challenges through a coordinated policy framework.

Figure 1 places this ambition in a broader international context by showing the changing distribution of global manufacturing value added over time. The geopolitical and economic backdrop of the IAA is clear. As the figure illustrates, the relative decline of the European Union's (EU) share in global manufacturing value added is striking, while China's marked rise over the past two decades has fundamentally reshaped the global industrial landscape.

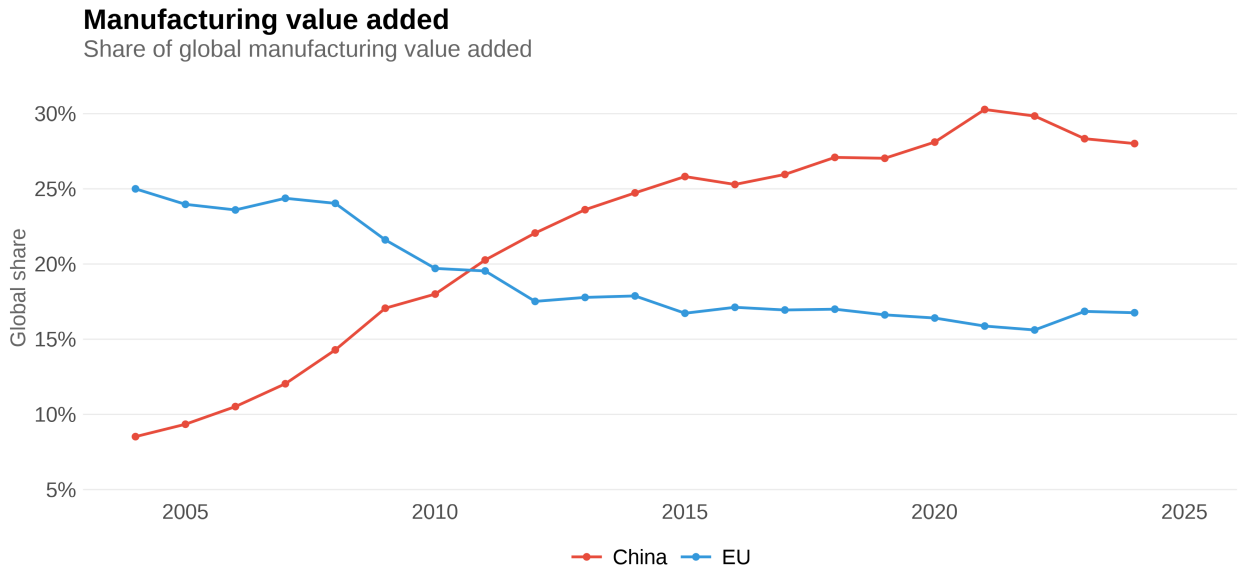


Figure 1: Share of global manufacturing value added for China and the EU over time. Kiel Institute based on World Bank (2026).

China has long pursued a state-coordinated industrial policy aimed at technological upgrading and control over critical value chains (Bickenbach et al., 2024a). At the same time, the United States (U.S.) has expanded its own industrial policy toolkit, most prominently through the Inflation Reduction Act and related support for domestic clean-technology manufacturing (The White

House, 2023). Under President Trump, U.S. economic policy has also become more protectionist and less predictable, with a stronger reliance on tariffs, trade measures and unilateral trade actions, which has added to uncertainty in transatlantic economic relations (Mahlkow et al., 2025; Hinz et al., 2026). In this context, EU industrial policy is no longer conceived primarily as a tool to correct market failures, for example in climate policy, but increasingly also as an instrument to strengthen industrial competitiveness and reduce external vulnerabilities.

To understand the focus of the IAA on clean technologies and the decarbonisation of energy-intensive industries, it is important to recall its origins in the Industrial Decarbonisation Accelerator Act under the Clean Industrial Deal. While the reference to decarbonisation was later dropped from the title to reflect a broader industrial ambition, this earlier focus remains visible in the architecture of the final proposal. The core operative instruments concentrate on creating lead markets for selected low-carbon products in energy-intensive industries, while also placing strong emphasis on the automotive sector. Beyond accelerated permitting and coordination of support schemes, the IAA introduces demand-side instruments in public procurement and links both procurement and public support to low-carbon and Union-origin requirements. It further establishes requirements for foreign direct investment (FDI) in selected emerging sectors, including key green technologies.

At the same time, the IAA raises important questions about the design of European industrial policy. In this policy brief, we distinguish between three broad objectives addressed under the Act: decarbonisation, geopolitical concerns and competitiveness. The category of geopolitical concerns covers objectives framed in the proposal in terms of economic security, resilience, strategic autonomy and the reduction of strategic dependencies. Our core argument is that the IAA combines these objectives under a common framework without sufficiently distinguishing between them or aligning instruments accordingly. It is ambitious, but often insufficiently precise to support the fulfilment of a specific objective.

In the sections that follow, we analyse the IAA's main design features and derive policy implications for the broader debate on European industrial policy. We begin with the definition of strategic sectors and examine whether the final proposal provides a sufficiently focused basis for industrial intervention. We then turn to the economic rationale and limitations of local content requirements (LCRs), before analysing the IAA's proposed FDI requirements, which go beyond traditional security screening by introducing conditional approval requirements in selected emerging strategic sectors. Finally, we use China as the main country case to assess how firms from today's leading global manufacturing power may respond to these requirements in practice.

Our central insights are threefold. First, the IAA's strategic sector definition is broader than its

operative instruments and risks blurring distinct policy objectives, while at the same time giving insufficient space to future-defining technologies that are increasingly central to Europe's long-term competitiveness and geopolitical position. Engaging in the global competition for those technologies will be unavoidable for the EU, but doing so effectively requires a more forward-looking, precise and criteria-based approach to strategic designation that targets technologies where Europe can build on its existing industrial and research strengths while including investments in necessary cross-cutting enabling technologies.

Second, LCRs can only be justified if they are tightly linked to clearly defined objectives. In the IAA, they are implemented more selectively than under a general market-wide localisation regime and do not follow a purely Union-only logic, since certain partner countries may be treated as equivalent to Union origin. Even so, if they are applied without clear objective prioritisation, they may still generate higher input costs, administrative burdens and unintended distortions. This is particularly important because these instruments are used not only in the context of geopolitical goals such as resilience and dependency reduction, but also to pursue competitiveness and decarbonisation goals.

Third, the proposed FDI requirements are institutionally significant, but their effectiveness and proportionality remain uncertain. In practice, they are primarily designed with China in mind. Rather than overburdening a single instrument with multiple goals, European industrial policy should rely on a clearer distinction between objectives and a more careful matching of instruments to the specific problems they are meant to address.

2 The Broad and Insufficiently Differentiated Scope of Strategic Sectors Under the IAA

The definition of strategic sectors under the IAA is broad and heterogeneous. Annex I defines the Act's core sectoral scope and indicates which parts of the economy fall within its broader scope of policy intervention. The Annex covers energy-intensive industries, the automotive sector and net-zero technologies. At the same time, the proposal presents the Act more broadly as serving decarbonisation, competitiveness and geopolitical objectives. Table 1 summarises the main policy instruments applied under the IAA and their relation to the designated sectors.[1]

What is missing in the final IAA proposal, however, is a clearer forward-looking angle to support competitiveness and respond to geopolitical concerns. Earlier leaked versions of the IAA pointed

1. Art. 17(2) in Chapter V (Foreign Investment Contribution) contains an additional list of industries (emerging strategic sectors) for which FDI requirements shall apply. We discuss the list and the industrial policy tool in Section 4.

to a broader strategic perimeter that also mentioned advanced technologies relevant to the EU's economic security, including semiconductors, artificial intelligence (AI), quantum technologies, biotechnologies, robotics and advanced materials. Even there, however, these technologies were not at the centre of the IAA's practical design. The main instruments were already focused much more clearly on energy-intensive industries, automotive and net-zero technologies, while the advanced-technology category played a more supplementary and signalling role. In the final proposal, these technologies are no longer part of Annex I.

This narrowing may improve legal precision, but it also makes the IAA less forward-looking. To be sure, EU industrial policy does not begin and end with the IAA. The EU already pursues future-defining technologies through other policy initiatives beyond the IAA. But the IAA still stands out because of the breadth of its stated ambition: it presents itself not merely as a sectoral instrument, but as a response to decarbonisation, competitiveness and geopolitical pressures bearing on Europe's industrial base. Against that ambition, its weak focus on key future technologies is striking. If European industrial policy is meant to strengthen long-term competitiveness and reduce geopolitical vulnerabilities, it should not primarily be anchored in the support of incumbent industrial structures, but more clearly in those technologies potentially to shape future productivity, innovation and strategic autonomy, especially in a global context in which such technologies are already central to industrial policy in the U.S. and China.[2] However, rather than simply mirroring the technological priorities set by other governments, the EU should ground its strategic sector selection in a careful assessment that reflects it's interests regarding future growth opportunities and resilience. In an era of intensifying global competition and active industrial policy, Europe risks becoming a bystander in emerging sectors once again by not making them a priority in it's policy.

Looking more closely at the covered sectors, the breadth of this strategic perimeter raises economic concerns. Sectors and technologies differ substantially in their technological maturity, market structure, exposure to global competition and potential for learning spillovers. Applying a common strategic label across such diverse activities risks diluting focus and weakening the link between policy objectives and the instruments used to pursue them.

At the same time, the broad sectoral scope should not be conflated with automatic support. Inclusion in Annex I does not mean that all firms in each sector benefit from subsidies, procurement guarantees or localisation advantages. The IAA's more interventionist tools remain more selective. Product-specific low-carbon and Union-origin requirements apply only in de-

2. AI and advanced computing infrastructure, semiconductors, quantum technologies, biotech as well as critical minerals and to a lesser degree advanced materials, autonomous systems and space technologies are top priorities for both the U.S. and China according to recent policy documents. While China places more emphasis on new energy and advanced manufacturing, the U.S. has a stronger military technology focus, on which however China might be less explicit in official documents (Xinhua, 2025; State Council of China, 2026; U.S. Congress, 2022; The White House, 2025a; The White House, 2025b; National Science and Technology Council, 2024).

fined cases under Annex II and Annex III and strategic project designation requires additional assessment at project level. The economic concern therefore does not arise from blanket support, but from the breadth of the strategic label relative to the more selective and conditional operation of the Act's instruments. This issue becomes visible across the three main Annex I categories.

In energy-intensive industries, the strategic rationale is closely tied to decarbonisation and the role of upstream materials in wider industrial value chains. Yet the proposal relies on broad two-digit NACE categories, which group together firms with very different technologies, production processes and decarbonisation challenges. Within basic chemicals, for example, activities range from bulk chemicals with high process emissions and major green hydrogen or electrification needs to other chemical products with very different cost structures, innovation dynamics and strategic relevance.

This broad categorisation is also difficult to justify because parts of the policy rationale for energy-intensive industries are already addressed through existing EU climate-policy instruments, in particular the EU Emission Trading Scheme (ETS) and the Carbon Border Adjustment Mechanism, which target decarbonisation incentives and carbon leakage more directly. Against that background, defining entire two-digit sectors as strategic risks stretches the concept too far. At that level of aggregation, the strategic label may cover activities with very different relevance for industrial decarbonisation, while omitting firms outside the category that may be more directly linked to specific decarbonisation bottlenecks.

In the automotive sector, the logic is different. Here, the IAA is less about broad sectoral classification and more about direct intervention in a specific value chain. Annex III introduces Union-origin requirements for certain vehicles and components, especially in the electric vehicle segment. Compared with the broader treatment of energy-intensive industries, this is more operationally targeted. At the same time, it illustrates a broader problem of the IAA: decarbonisation, competitiveness and geopolitical concerns are addressed within a single strategic framework, even though they may call for different policy tools.

Figure 2 and Figure 3 place Annex III in an international trade context by showing how the share of electric vehicles and batteries in total exports has evolved across major countries and regions. The figures clearly illustrate the sharp rise of China's export share in batteries and electric vehicles, the two product areas most directly addressed by the IAA's automotive-related Union-origin requirements.

A related concern applies to the category of net-zero technologies. They are clearly central to Europe's decarbonisation strategy and long-term industrial competitiveness. However, the category itself remains highly heterogeneous. It includes technologies with very different innovation

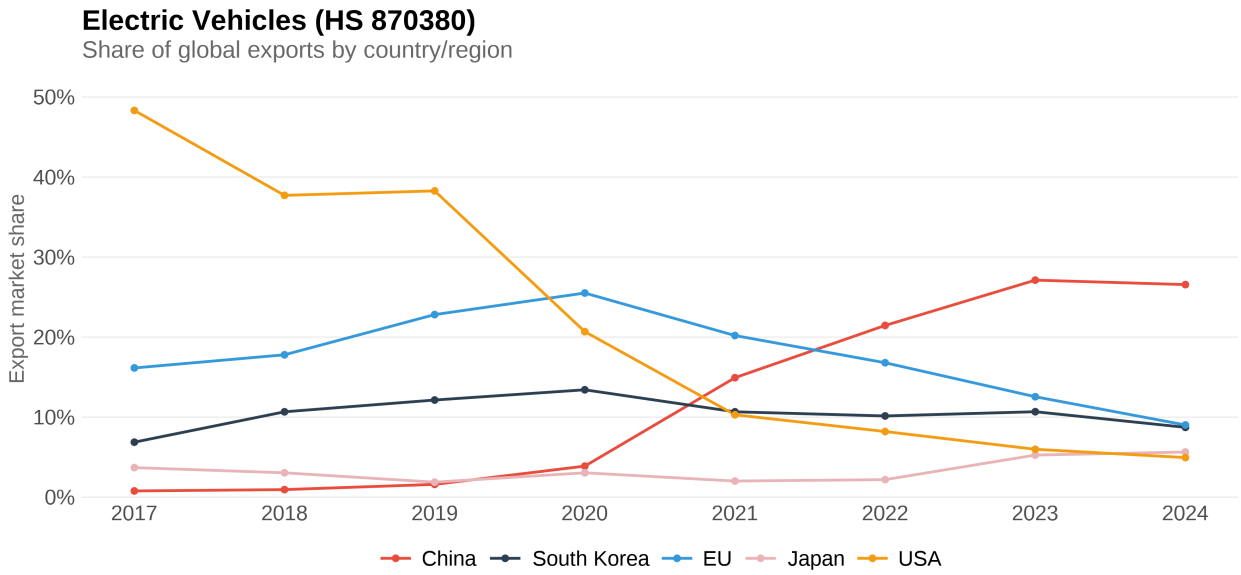


Figure 2: Share of electric vehicles in total exports across major countries and regions. Kiel Institute based on BACI (2026)

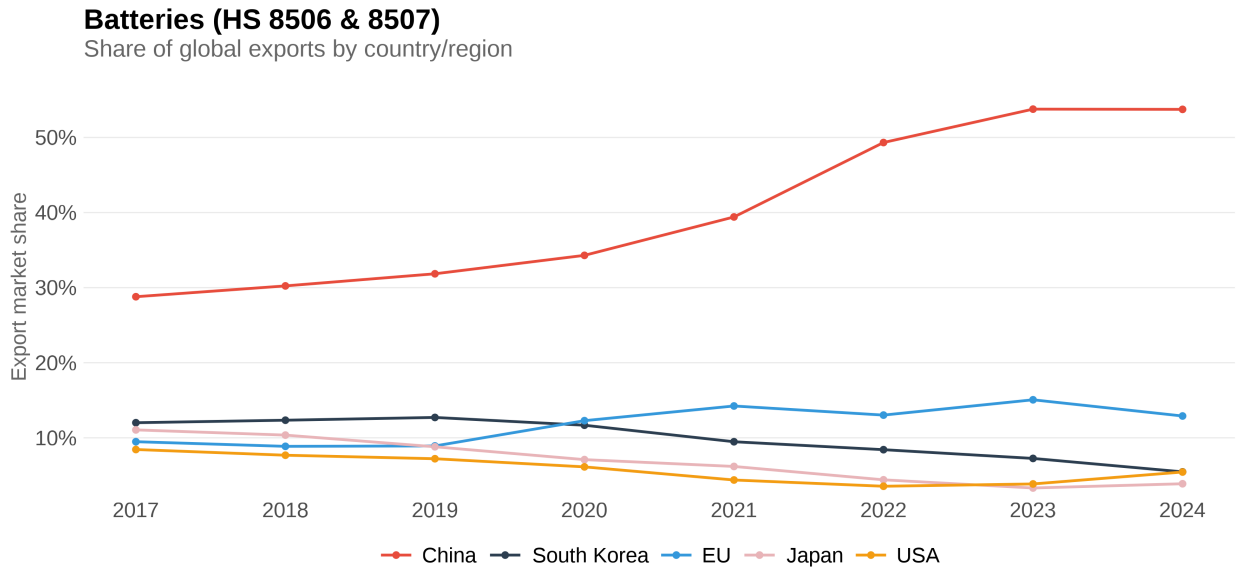


Figure 3: Share of batteries in total exports across major countries and regions. Kiel Institute based on BACI (2026)

dynamics, scale economies and dependency structures. In economic terms, strategic relevance often attaches not to an entire technology family, but to specific bottlenecks, key components, advanced materials or process technologies. A broad strategic label may obscure where intervention is most justified and where market-based sourcing remains more efficient.

Overall, the problem is therefore not simply that the IAA identifies a broad set of economically relevant sectors. Rather, it combines decarbonisation, competitiveness and geopolitical goals under a common framework without sufficiently distinguishing between them. At the same time, the final proposal does not sufficiently cover future-defining technologies that are increasingly central to global industrial competition. This creates a tension at the heart of the IAA: it is broad in its sectoral scope, but not sufficiently forward-looking in relation to the technologies most relevant for Europe's future competitiveness and geopolitical position. Strategic designation should therefore rely on more transparent and differentiated criteria that distinguish clearly between decarbonisation, competitiveness as well as geopolitical goals and link each of them to proportionate instruments.

This lack of strategic focus also casts doubt on whether the IAA is well designed to achieve its headline manufacturing objective to reach 20% of EU GDP by 2035. Missing this target would not necessarily be a problem in itself. Europe's future competitiveness may also be driven by successful developments beyond the industrial base, including in high-value service sectors that can likewise generate quality employment. For that reason, such aggregate sectoral targets have limited economic value in themselves. They become even harder to justify considering the IAA's comparatively weak focus on the future-defining technologies most likely to shape long-term productivity and competitiveness.

Based on the discussion above, we derive the following policy recommendations for the forward-looking design of industrial policy:

Policy recommendations: Drop the target that manufacturing represents at least 20% of EU GDP by 2035.

Build industrial policy on a clear distinction between objectives relating to decarbonisation, competitiveness and geopolitical concerns.

Define strategic sectors more narrowly and transparently, using objective and activity-based criteria and placing greater emphasis on technologies than on broad sectoral classifications.

Focus more strongly on future-defining technologies when pursuing competitiveness and geopolitical goals, rather than primarily supporting incumbent industrial structures.

3 Local Content Requirements Defined in the IAA

Chapter III of the IAA introduces local content requirements (LCRs), which constitute the most operationally significant element of the IAA's 'Made in Europe' approach. Conceptually, LCRs require a defined share of domestic value added, production or sourcing as a condition for access to public procurement, financial support schemes or, in certain cases, regulatory advantages. In the IAA, this logic is operationalised mainly through a combination of low-carbon requirements and Union-origin requirements. Importantly, Union origin also includes certain third countries, as discussed in more detail in the next sub-section. These requirements are not applied horizontally across all strategic sectors listed in Annex I, but primarily through Annex II and Annex III. Annex II links public procurement and public support to low-carbon and, for selected products, Union-origin requirements, while Annex III introduces detailed Union-origin thresholds for electric vehicles and selected components of the battery value chain.

Through these provisions, the IAA ties EU public resources more closely to production within the Union. This marks a shift from largely neutral framework conditions towards conditional industrial support linked to geographic production patterns. For public support schemes, the IAA also requires Member States to apply the relevant criteria to at least 45% of the national budget covered by Annex II schemes and to 100% of the national budget covered by Annex III schemes (Art. 12(1)). At the same time, the proposal allows exceptions where compliance would lead to disproportionate costs or significant delays and, in public procurement, also where it would create technical incompatibilities or insufficient competition (Art. 11(3) and Art. 12(3)).

However, its broader significance lies in establishing localisation-related criteria more firmly as a policy tool within the EU's industrial policy architecture. The IAA's localisation logic also reflects a broader international trend towards conditional industrial policy, as seen for example in the U.S., where the Inflation Reduction Act combines support for clean technologies with domestic-content incentives and domestic manufacturing support (The White House, 2023).

The objectives underlying this approach are heterogeneous. LCRs are expected to strengthen European value chains, reduce strategic dependencies and support industrial competitiveness. In the context of the green transition, they are also intended to create lead markets for low-carbon products, facilitate learning-by-doing and scale effects in emerging industries and anchor critical segments of new value chains within the Union. In addition, the instrument is often framed as a response to foreign subsidies and perceived unfair competition.

From an economic perspective, these rationales are distinct. The justification for LCRs depends fundamentally on the type of objective being pursued: addressing geopolitical concerns, decarbonisation or competitiveness. Each objective implies different design requirements and differ-

ent benchmarks for success. Combining these aims without explicit prioritisation risks overburdening a single instrument and weakening its effectiveness.

In the following, we discuss major caveats of the LCRs set out in the IAA and the economic risks associated with their implementation. While our analysis focuses on the IAA in its current form, we also consider the broader implications of embedding localisation-related criteria more firmly within the EU's industrial policy framework.

Defining Union origin: a central design question

A foundational issue in the implementation of LCRs concerns the definition of what qualifies as Union-origin content. In the IAA, this question is operationalised through the concept of Union origin. Determining whether a product meets a 'Made in Europe' criterion therefore requires the specification and verification of value-added thresholds or component origin shares. In globally fragmented value chains, where production stages are distributed across multiple jurisdictions, such measurement is technically complex and administratively demanding. The calibration of threshold levels, the treatment of intermediate inputs and the verification procedures will determine both the effectiveness and the cost of the instrument.

Beyond administrative feasibility and its bureaucratic burden, the definition of Union origin has strategic implications. A narrow interpretation that strictly limits eligibility to production located within EU territory would effectively amount to a protectionist instrument. Even though the IAA adopts a broader approach, earlier stages of the debate pointed in the direction of a tighter definition, which underlines that the precise scope of Union origin remains politically relevant while negotiations continue. By contrast, the IAA provides that, in public procurement and certain forms of public intervention, content originating in selected third countries may be treated as equivalent to Union origin. This is a central clause. It opens the possibility of a differentiated approach that preserves openness towards closely integrated partner economies rather than applying a rigid Union-only logic.[3]

Figure 4 provides an overview of the EU's trade agreements and their current status where relevant for the respective instruments of the IAA. The map illustrates that the EU maintains a broad network of trade agreements, with particularly dense coverage across parts of Africa, Latin America and East Asia. Closely integrated partners such as Turkey and the European Economic Area (EEA) states are linked to the EU through different forms of deep economic integration, including

3. See Articles 7, 8(1)-(2) and 9(1)-(2) of the IAA proposal. Article 7 defines Union origin. Article 8 provides that, in public procurement, content originating in third countries with which the Union has concluded a free trade agreement or customs union, as well as countries party to the Agreement on Government Procurement (GPA) where relevant Union obligations exist, shall be deemed to be of Union origin, subject to possible exclusion by delegated act. Article 9 provides equivalent treatment for other forms of public intervention for third countries with which the Union has concluded a free trade agreement or customs union, again subject to possible exclusion by delegated act.

the customs union in the case of Turkey and single-market participation in the case of the EEA (European Commission, 2026a). Beyond trade agreements, Article 8 extends Union-origin equivalence in public procurement to countries that are parties to the WTO Agreement on Government Procurement (GPA), which notably includes the U.S. and Australia, two strategic partners that currently lack a free trade agreement with the EU.[4] At the same time, the trade arrangements of the EU differ substantially in the depth of trade and investment liberalisation they provide. As a result, the precise definition of Union origin might shape the scope for relocating production stages within value chains and, with it, the balance between openness and localisation.

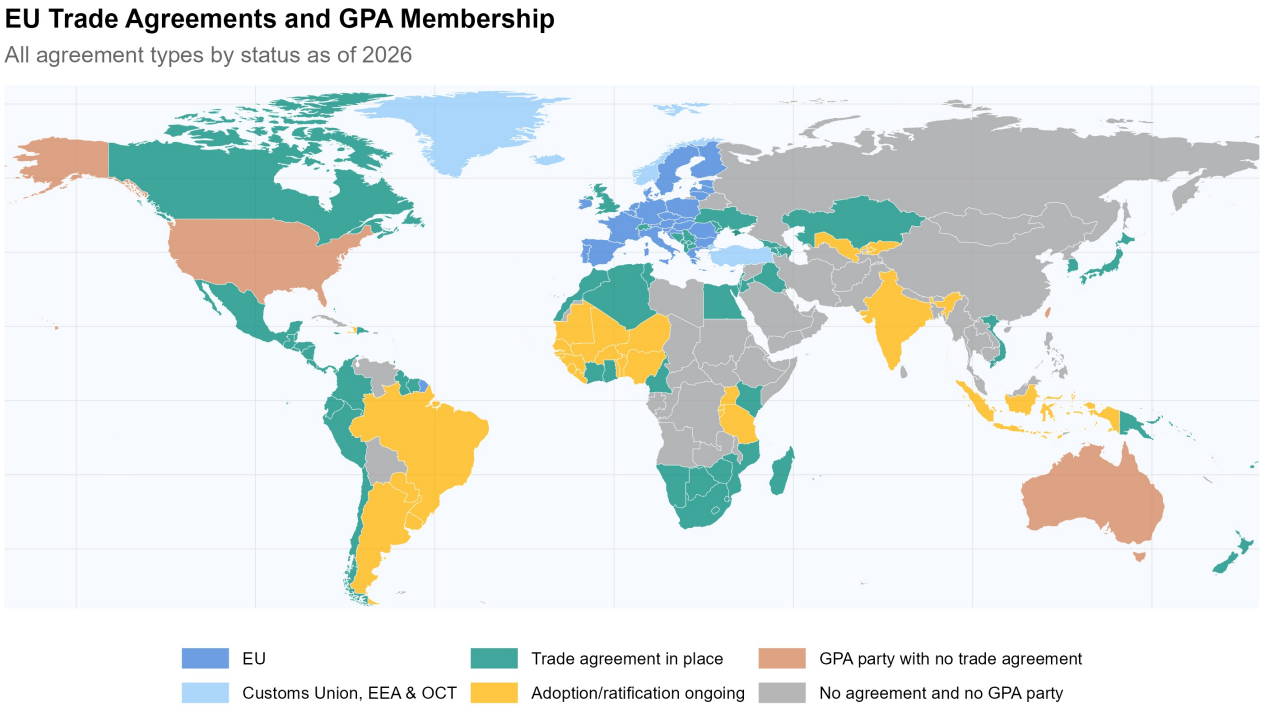


Figure 4: Overview of EU trade agreements and their current status. Kiel Institute based on European Commission (2026a) and WTO (2026)

From an economic and strategic perspective, maintaining openness towards trusted partners is essential. The EU's industrial base is deeply embedded in global value chains and supported by trade agreements with partners such as South Korea, Japan and Canada. As Figure 4 illustrates,

4. Hong Kong's status as an independent GPA party could theoretically allow Chinese firms to route production through the territory to obtain Union-origin equivalence in EU public procurement. However, Article 8(2) of the IAA provides the Commission with delegated authority to exclude any third country from origin equivalence, including on grounds of supply security concerns, which would close such potential loopholes. A similar logic could also matter for future partner countries. For example, although EU-India FTA negotiations were concluded in January 2026, India would fall under Articles 8 or 9 only once such an agreement is in force or provisionally applied and to the extent that relevant commitments exist. Even then, the Commission could exclude India, in whole or in part, by delegated act under Articles 8(2) or 9(2), for example in narrowly defined cases involving serious supply-security concerns or insufficient national treatment under the relevant agreement.

the EU is also advancing trade agreements and partnerships across a wide range of regions. This is an important direction and should be intensified further to build a broader alliance committed to a rules-based trading system. Important partners and markets in this regard include India, Mercosur, Indonesia and African countries, most notably Nigeria. Taken together, these regions represent substantial economic weight and significant market opportunities for the EU. A rigid localisation requirement, whether under the IAA or more broadly in EU industrial policy, that excludes partners committed to rules-based trade would risk raising input costs, weakening strategic partnerships and undermining resilience through greater fragmentation.

Policy recommendations: To define Union origin, continue to follow a pragmatic 'Europe plus trusted partners' approach, ensuring that trade-related benefits are preserved while taking geopolitical realities into account.

Deepen trade agreements and strategic economic partnerships to build a broader alliance committed to rules-based trade, expand market opportunities and strengthen resilience through diversification.

Objective coherence and proportionality

The relevance of how Union origin is defined illustrates the importance of clear and coherent objectives. Across the three underlying goals, addressing geopolitical concerns, decarbonisation and competitiveness, openness towards trusted partners remains important. For geoeconomic-related objectives such as security or supply chain resilience, the relevant benchmark is not autarky, but risk diversification and reduced vulnerability to coercion. This implies that 'local' should not be defined narrowly as EU-only, but rather as EU plus trusted partners.

For decarbonisation, abstracting from transport-related emissions, the climate impact of a technology does not depend on its geographic origin. From a global emissions perspective, it is not decisive whether low-carbon aluminium is produced in Europe or elsewhere. For competitiveness objectives, access to a larger integrated market is essential to realise scale effects, foster competition and sustain innovation. A restrictive origin definition may therefore undermine, rather than strengthen, the very competitiveness it seeks to promote.

A central design challenge of the IAA's localisation requirements therefore lies in aligning the instrument with clearly defined objectives. If LCRs are justified on resilience grounds, their calibration should be based on measurable dependency risks, such as import concentration, substitutability and geopolitical exposure. If justified on competitiveness grounds, they should target

segments characterised by learning-by-doing, scale economies or coordination failures. If justified on climate grounds, they should complement, rather than distort, the EU ETS.

Without such differentiation, localisation requirements risk being applied as a general industrial support tool rather than as a targeted response to clearly identified vulnerabilities or market failures. This raises concerns about proportionality. The broader and less differentiated the application of LCRs, the greater the risk that they are applied to sectors where resilience risks are limited, learning effects are weak or support may slow structural change towards more future-defining activities.

Policy recommendation: If LCRs are applied, each of them should be linked explicitly to a clearly defined objective, whether to address geopolitical concerns, competitiveness or decarbonisation, and justified ex ante based on measurable criteria.

Risk of higher input costs and downstream distortions

LCRs can increase production costs if Union-origin suppliers are more expensive than international alternatives. This risk is particularly relevant in sectors characterised by global scale economies and intense price competition. However, under the current design of the IAA, localisation criteria are primarily tied to public procurement and certain public support schemes rather than imposed as a general market-wide obligation. The immediate price effects are therefore likely to be concentrated in publicly supported transactions rather than affecting the entire market.

Nevertheless, even procurement-based localisation requirements may have indirect effects along value chains. If publicly supported demand is redirected towards higher-cost suppliers, this may influence market structures, investment and innovation incentives as well as relative price signals.

Higher input costs may in turn weaken the competitiveness of downstream and export-oriented industries. More generally, restricting access to lower-cost imports may slow parts of industrial transformation and, with it, the pace of the green transition.

From a structural perspective, localisation requirements may also affect the allocation of resources across sectors. If comparative advantages lie elsewhere due to place-based factors such as energy costs, resource endowments or established industrial clusters, conditioning public demand on domestic production may slow reallocation towards more competitive segments. While

this may be justified in cases of clearly identified strategic vulnerabilities, it risks preserving incumbent production structures where efficiency gains are limited.

The proposal itself acknowledges these trade-offs by allowing exceptions where compliance would cause disproportionate costs or significant delays and, in public procurement, also where it would create technical incompatibilities or insufficient competition. In procurement, cost differences above 25% may be presumed disproportionate, while in support schemes this threshold is 30%; delays beyond seven months may be presumed significant (Art. 11(3) and Art 12(3)).

The cost and delay exceptions make the IAA less binding than a strict localisation regime. In sectors where foreign suppliers retain a large cost advantage, they may substantially limit the practical effect of Union-origin requirements. At the same time, the IAA still gives these requirements a formal legal basis and concrete operational role in procurement and public support schemes.

Risk of reduced competitive pressure and innovation

Especially in technology- and knowledge-intensive sectors, firms need to cooperate with leading partners and institutions worldwide and remain exposed to international competition. Overly restrictive localisation requirements and the protection of incumbents may weaken competitive pressure and reduce incentives to innovate, increasing the risk of rent seeking rather than strengthening long-term competitiveness.

Maintaining or creating overly closed value chains in Europe, or across countries treated as equivalent to Union origin, can also impose significant costs. A key source of value creation in global value chains is that different locations contribute their respective advantages at different stages of production (Dohse et al., 2019). Even the more limited objective of ensuring that value chains are controlled from Europe may be costly, since welfare gains from participation in global value chains can arise without control over all stages of production.

Administrative and compliance burdens

The implementation of LCRs requires verification, documentation and monitoring of origin shares and value-added thresholds. In globally fragmented value chains, these requirements can generate substantial compliance costs, particularly for small and medium-sized enterprises.

Reducing bureaucratic burdens while simultaneously introducing detailed origin and content verification systems is administratively challenging. The effectiveness of LCRs therefore depends not only on their economic rationale, but also on administrative feasibility and enforcement

capacity. More broadly, if some sectors benefit from accelerated administrative treatment under the IAA, capacity constraints within public administrations may also create indirect delays and uneven treatment elsewhere.

Retaliation and legal risks under international trade rules

Institutional constraints further shape the feasible design of LCRs. Their compatibility with Single Market principles, consistency with World Trade Organisation (WTO) obligations and the differentiation between trusted and non-trusted trading partners impose legal and political boundaries on their application.

Overly restrictive localisation requirements may trigger retaliatory measures from trade partners, complicate ongoing trade negotiations and undermine the EU's credibility as a defender of a rules-based trading order. Even if the IAA aims to align with WTO rules, the practical design of origin thresholds and procurement conditions will determine whether the instrument remains defensible under international law.

Resilience should therefore not be equated with economic isolation. A strategy based on diversification and trusted partnerships is more advantageous for achieving both geoeconomic objectives and long-term competitiveness.

4 Foreign Direct Investment Requirements Under the IAA

In addition to LCRs in public procurement and support schemes, Chapter IV of the IAA introduces foreign investment requirements in selected emerging strategic manufacturing sectors. While the immediate scope of this chapter is narrower than that of the localisation provisions, its institutional significance is considerable. It marks a shift from a purely security-oriented screening approach towards a more strategic alignment of FDI with broader industrial objectives, including knowledge and technology transfer as well as the reduction of geopolitical dependencies.

Scope and legal design

The FDI chapter applies to FDIs exceeding EUR 100 million in four defined emerging strategic manufacturing sectors:

- battery technologies and its value chain for battery energy storage systems;

- pure electric vehicles, off-vehicle charging hybrid electric vehicles and fuel cell electric vehicles, including components related to electrification and digitalisation;
- solar PV technologies;
- and extraction, processing and recycling of critical raw materials (Art. 17(2)).

It applies where more than 40% of global manufacturing capacity is held by the third country of which the foreign investor is a national or undertaking. Investments within scope may not be implemented unless explicitly approved by the designated Investment Authority or, in some cases, the Commission. The IAA therefore introduces a formal ex ante authorisation requirement for qualifying transactions.

At the same time, the chapter is not designed as a general foreign investment control system. It does not apply horizontally to all strategic sectors listed in Annex I, but only to the narrower set of emerging strategic manufacturing sectors set out in Article 17. It also excludes investors and investments covered by economic partnership agreements and free trade agreements in force or provisionally applied by the Union, to the extent relevant commitments have been made under those agreements, as well as services investments and portfolio investments (Art. 17(3)). These exclusions reflect an attempt to preserve differentiated treatment of partner countries and to remain compatible with the Union's international commitments.

A further important design feature is that the IAA does not merely require notification and review. Investment Authorities shall approve covered investments only if they fulfil four out of six value added FDI requirements (Art. 18(2) and Art.18(3)). These include limits on ownership and control, the possibility of joint ventures with Union entities, licensing and co-ownership rules for intellectual property and know-how, minimum research and development (R&D) spending in the Union, workforce requirements and commitments to strengthen Union value chains through local sourcing. One of these conditions, that at least 50% of the workforce be made up of Union workers across all workforce categories, is mandatory for approval in all cases.

Figure 5 illustrates the global distribution of manufacturing capacity across the emerging strategic sectors covered by the IAA. The blue colour refers to the manufacturing capacity of the EU and the red colour to that of China. In addition, the horizontal line marks the 40% benchmark set by the proposal. At first glance, the figure strongly suggests that the chapter is primarily designed with Chinese investment in mind. China dominates manufacturing capacity across most value chain segments in solar, batteries and electric vehicles. The picture is more differentiated for critical raw materials, where resource-rich countries such as Australia are highly significant at the extraction stage, while China remains dominant in refining and processing. Here, however, the legal design leaves some ambiguity. The proposal refers to more than 40% of global

manufacturing capacity in the sector concerned, but does not fully clarify how this should be assessed across heterogeneous value chain segments. If concentration in one segment were sufficient, countries such as Australia could in principle fall within scope for parts of the critical raw materials supply chain. On the basis of the current treaty framework, Australia does not appear to be excluded under Article 17(3), which applies only to investors covered by an economic partnership agreement or free trade agreement in force or provisionally applied by the Union, to the extent that relevant commitments have been made.

Taken together, the design of the FDI chapter indicates a targeted and conditional regime rather than a comprehensive investment control system. The distinctive feature of the final proposal is not only that it screens investments, but also that it conditions approval on their contribution to industrial upgrading within the Union.

From screening to conditional alignment

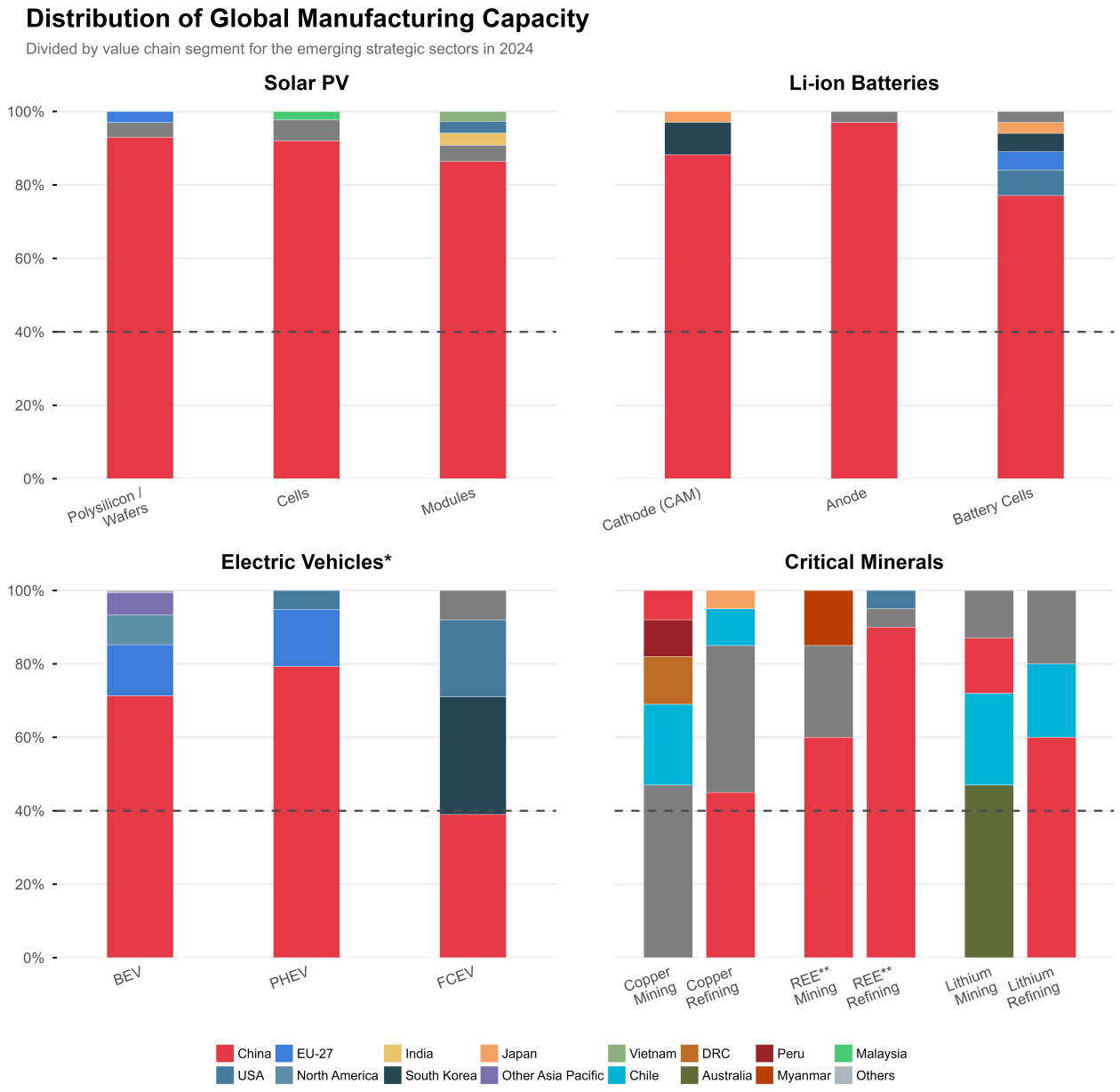
The European Union already coordinates an FDI screening framework aimed at protecting security and public order. That framework is primarily defensive. It allows Member States and the Commission to assess and, where necessary, block acquisitions that pose security risks. The IAA goes beyond this logic. Rather than merely preventing undesirable transactions, it introduces a rule-based authorisation regime designed to steer foreign investment towards specific forms of contribution to the Union economy. In this sense, the Act complements security screening with industrial policy conditionality.

The focus on countries holding more than 40% of global manufacturing capacity in a given sector signals that the concern is not only firm-level behaviour, but also systemic dependency and global production concentration. At the same time, the six approval conditions show that the chapter is not confined to resilience alone. It also seeks to shape ownership structures, retain knowledge and intellectual property, increase R&D development spending in the Union, support Union employment and strengthen local value chains. The chapter therefore combines geopolitical and competitiveness objectives within a single investment regime, with industrial upgrading acting as one of the main intended channels.

Intended objectives

The FDI provisions appear to pursue several interconnected objectives:

- Enhancing resilience in sectors characterised by high global manufacturing concentration;
- strengthening European value chains in emerging clean technologies;



Notes: Electric Vehicles*: PHEV and FCEV show sales shares as proxy as no direct production breakdown available. FCEV data refers to 2023.
REE**: Only rare earth elements used for permanent magnets.

Figure 5: Distribution of Global Manufacturing Capacity for the defined emerging strategic sectors, divided by value chain segments. Kiel Institute based on IEA (2022); IEA (2024a); IEA (2024b); IEA (2025a); IEA (2025b); IEA-PVPS (2025); Rhodium Group (2025); USGS (2025); Statista (2024)

- supporting technological upgrading and innovation capacity;
- and aligning foreign investment with broader industrial policy goals.

Implicitly, the regime also reflects concerns about systemic dependencies, global production concentration and the strategic use of investment in globally highly concentrated sectors. From an economic perspective, however, these objectives are heterogeneous. The rationale for FDI requirements differs depending on whether the primary goal is dependency reduction, competitiveness or industrial policy coordination. Each objective implies different benchmarks for evaluating effectiveness and proportionality. The proposal's design does not clearly separate these rationales. Instead, it relies on one common set of approval conditions to pursue several goals at once.

Economic considerations and effectiveness conditions

FDI can generate substantial benefits for host economies, including technology transfer, productivity spillovers and integration into global value chains (Alfaro, 2017). These effects, however, are not automatic. They depend on domestic absorptive capacity, competitive markets that allow spillovers to materialise, and the broader institutional and economic environment in the host economy. Where governments seek to tie FDI to specific policy conditions, effectiveness may additionally depend on credible monitoring and enforcement mechanisms.

In the European context, these conditions are likely to be only partially met. The EU market is large and attractive, which strengthen its bargaining power. At the same time, its openness and dense network of trade agreements allow firms to serve the EU market from third countries, which may weaken the leverage created by conditionality. If the regime becomes excessively restrictive, some investment could be redirected to neighbouring economies or partner countries with preferential access to the Union market.

The design of the approval criteria also raises more specific economic questions. Some of the conditions, such as R&D spending, licensing of intellectual property, workforce commitments and local sourcing strategies, may under certain circumstances support domestic capability building. But they are also demanding and potentially costly. Their effectiveness will depend on whether they respond to genuine market failures or strategic vulnerabilities and on whether they can be economically monitored and enforced over time. It should also be kept in mind that, while conditionality may foster spillovers, there is a risk that the regime imposes substantial conditions on investments without consistently generating the intended spillovers.

The governance of the regime is institutionally demanding. Member States must designate Investment Authorities, while the Commission may issue opinions, require more detailed assess-

ment where national decisions diverge from its view and in specific cases undertake the assessment itself, including for investments above EUR 1 billion or where several Member States are affected. Effective implementation will therefore depend on close coordination between national authorities and the Commission.[5]

Preliminary assessment in the context of the IAA

The final proposal does not create a blanket prohibition on foreign investment in strategic sectors. Its scope is limited to specific sectors, investment sizes as well as origin criteria and it excludes some partner-country investments as well as services and portfolio investments. Nevertheless, the regime goes well beyond the current FDI screening framework. It conditions the approval of covered investments on a mandatory set of value-added requirements, thereby treating FDI not only as a source of capital, but also as an instrument for advancing industrial policy objectives within the Union.

This makes the FDI chapter one of the most economically sensitive parts of the IAA. Its institutional significance should therefore not be underestimated. At the same time, its economic justification depends critically on objective clarity and proportionality. Where geopolitical concerns are central, the focus should be on clearly identified dependency risks and coercion vulnerabilities. Where competitiveness is the objective, the case for intervention should rest on demonstrable spillovers, learning effects or coordination failures. Without such differentiation, the regime risks overburdening one instrument with several goals and weakening both openness and effectiveness.

Policy recommendation: Preserve the EU's openness to foreign direct investment to sustain knowledge transfer, spillovers and integration into global value chains. Where geopolitical concerns arise, apply clearly defined and proportionate conditions linked to measurable vulnerabilities and ensure that any investment requirement remains narrowly targeted, transparent and consistent with existing screening mechanisms.

5. See Arts. 18, 20 and 21 IAA proposal. Article 18 requires Member States to designate Investment Authorities. Article 20 allows the Commission to issue opinions and requires more detailed assessment where national authorities diverge from those opinions. Article 21 allows the Commission, in specific cases, to undertake the assessment itself, including for investments above EUR 1 billion or where the investment has significant effects across more than one Member State. Article 19(6) also requires coordination where targets or assets are located in more than one Member State.

China as an FDI source country under the IAA

In assessing the EU's proposal to introduce conditions on foreign investment as part of the effort to accelerate European industrial capacity, a key question is how foreign investors would respond to these new requirements. Although Chinese investments account for only a relatively small share of total inward investment in the EU, the Chinese case warrants particular attention. China differs markedly from Europe in its political system and in the role of the state in economic governance. It is precisely these features that make its likely response especially relevant. In addition, ongoing concerns about strategic dependencies and the legacy of the 'China shock' further reinforce the importance of this assessment.

In China's political system, the state plays a central role in planning, coordinating and steering economic and industrial development. This party- and state-led governance model has been further reinforced under President Xi Jinping, through the call to build a 'new type of whole-nation system' (新型举国体制) in 2022 (NDRC, 2023). While often discussed in the context of innovation policy, the concept more broadly reflects the intensification of centralised Party leadership in mobilising and coordinating national resources to achieve strategic development objectives and safeguard national security.

Against this background, Chinese firms' outward investments cannot be understood solely as business- or market-driven decisions. The Chinese government possesses a wide array of regulatory and economic instruments through which it can influence, guide, constrain or promote firms' overseas investment behaviour. These instruments shape both the approval and the financing of outward investment. Outward investment projects are subject to registration and approval procedures, during which firms that apply for investment approval must report on the potential implications of their investments for national interests and security (NDRC, 2017). Country-specific guidance catalogues and sectoral policy documents further shape investment priorities. Capital controls and a tightly regulated financial system limit the free movement of funds, while China's major commercial and policy banks are state-owned or state-controlled and operate within governance and regulatory frameworks aligned with national development strategies. In addition, the planned development of a National Comprehensive Overseas Services System to support Chinese firms' international activities (MOFCOM, 2025) is likely to further strengthen the state's capacity to coordinate and steer outward investment.

Recent investment developments illustrate the relevance of these policy mechanisms. Rising Chinese outward investment into countries participating in the Belt and Road Initiative (e.g., Du et al., 2018) and into sectors designated as priorities under the Made in China 2025 strategy (e.g., Zenglein et al., 2019; Xia et al., 2021) suggest a close alignment between China's policy objectives and outward investment patterns. More recently, amid intensifying technological tensions with

the U.S., particularly in the semiconductor sector, China's 2023 government report presented outward investment in mining and critical raw materials as a strategic priority (Bickenbach et al., 2023). These examples suggest that overseas investment decisions are embedded in broader state-led development strategies rather than being driven solely by firm-level commercial considerations.

Future Chinese investment in Europe, and its response to the proposed IAA, must therefore be assessed not only through corporate cost-benefit calculations, but also in light of China's broader strategic development agenda. This is particularly relevant where the IAA conditions approval on ownership structures, technology-related provisions, local employment and supply-chain commitments. For the period 2026-2030, China's overarching development objectives include advancing 'high-quality development' and strengthening technological self-reliance. In this context, the Chinese leadership has emphasised the need to manage overseas investments more effectively, promote the integration of trade and investment and guide the orderly cross-border development of industrial and supply chains (State Council of China, 2026).

This policy orientation suggests that outward investment is expected to contribute to the integration of trade and investment and to the orderly cross-border development of industrial and supply chains. In practical terms, overseas investment is encouraged where it helps Chinese firms serve foreign markets more effectively and stabilise trade relations. This approach is consistent with the current economic context, which is characterised by rising geopolitical tensions affecting Chinese exports, weak domestic demand and overcapacity in several industrial sectors (Bickenbach et al., 2023; Bickenbach et al., 2024b). Under these conditions, outward investment can also facilitate the relocation of parts of production abroad in order to preserve market access and alleviate domestic pressures.

Such investment, however, is not intended to weaken China's domestic industrial base, but to support its upgrading through the controlled expansion and restructuring of value chains. More concretely, cross-border industrial and supply chains are expected to be configured in ways that remain consistent with China's domestic industrial policy goals: strengthening control over key value chains, increasing technological self-reliance, fostering advanced manufacturing clusters at home and supporting the development of strategic emerging industries such as next-generation information technology, new energy, new materials, intelligent connected new-energy vehicles, robotics, biomedicine, high-end equipment and aerospace (State Council of China, 2026). Investments that would significantly weaken China's technological position or undermine these objectives are unlikely to receive policy support.

From this perspective, the EU remains an attractive destination for Chinese investment because of its large market size and relatively high purchasing power. This attractiveness matters not

only at the firm level but also from the standpoint of the Chinese government, which has an interest in maintaining access to advanced markets. Stricter European requirements concerning ownership structures, technology transfer, local employment or supply-chain integration may therefore not automatically deter Chinese investment.

However, the response of Chinese firms, potentially supported by state coordination, could take several forms. Firms may comply selectively, for example by localising production while limiting the transfer of frontier technologies. Alternatively, investment strategies may shift toward third countries such as Morocco or Turkey, from which firms can continue to serve the EU market while potentially facing lower regulatory constraints and production costs. In such cases, the direct impact of the IAA on China's broader industrial and trade strategy may be more limited than anticipated.

5 Discussion

The IAA reflects a timely ambition to strengthen Europe's industrial base in a context of decarbonisation, geopolitical tensions and intensifying international competition. At the same time, the analysis in this policy brief suggests that the Act faces important design and implementation challenges. Its central weakness is not a lack of ambition, but a lack of precision. The IAA combines decarbonisation, geopolitical and competitiveness goals under a common framework without sufficiently distinguishing their respective economic rationales or aligning instruments accordingly.

The first challenge concerns the broad and heterogeneous scope of the strategic sectors covered by the IAA. The final proposal defines a wide strategic perimeter, while no longer giving a prominent place to key future-defining technologies that are increasingly central to global industrial competition. This creates a tension at the heart of the Act: it is broad in sectoral scope, but insufficiently forward-looking in relation to the technologies most relevant for Europe's future competitiveness and geopolitical position. Strategic designation should therefore rely on clear and more transparent criteria, both to define what is strategic and to distinguish more consistently between decarbonisation, geopolitical and competitiveness goals. In addition, there will be no way around for the EU then to engage in the competition for the emerging technologies that both the Chinese and U.S. governments have signalled as primary interests. However, this does not make every single one of these technologies a necessary strategic priority for the EU. There will be no-regret options such as cross-cutting enabling technologies like AI and its underlying infrastructure with semiconductors, datacenters, and cloud services. Moreover, areas

such as biotechnology, robotics, aerospace or advanced materials could built on strong existing ecosystems already present across Europe. Yet, the identification of strategic emerging sectors and technologies requires a thorough and honest assessment grounded in clear and transparent criteria that needs to be precise and reflect Europe's own industrial and research strengths, dependencies and long-term interests.

A second challenge concerns the use of local content requirements (LCRs). In the IAA, these are mainly operationalised through low-carbon and Union-origin requirements in public procurement and certain support schemes. While their immediate scope is narrower than a general market-wide localisation regime, they still mark a significant shift towards more conditional industrial support. Particularly in Annex III, these instruments are also best understood against the background of China's growing strength in electric vehicles and the battery value chain. Such instruments may be justified under specific conditions, for example where lead markets are needed to support the scaling of emerging technologies or where measurable dependency risks are present. However, their justification depends fundamentally on the objective pursued. A geopolitical rationale differs from a competitiveness-oriented rationale, just as both differ from a decarbonisation rationale. Without such differentiation, localisation requirements risk increasing input costs, weakening downstream competitiveness and creating administrative burdens without effectively addressing the specific policy problem they are meant to solve. Preserving openness towards trusted partners remains essential, since resilience is better achieved through diversification than through rigid Union-only approaches.

A third challenge concerns the IAA's new foreign direct investment (FDI) requirements. These are limited to selected emerging strategic manufacturing sectors and therefore much narrower than a general investment control regime. Yet their institutional significance is considerable. In practice, these requirements are best understood as being designed primarily with China in mind. The chapter moves beyond the current FDI screening framework by conditioning investment approval on a set of value-added requirements linked to ownership structures, intellectual property, research and development, employment and local sourcing. In this way, the IAA treats FDI not only as a source of capital, but also as an instrument to advance industrial-policy objectives within the Union. This is a significant step, but one where economic justification depends critically on objective clarity and proportionality. If geopolitical goals are central, the focus should be on clearly identified vulnerabilities and dependencies. If competitiveness is the primary objective, it remains unclear whether the FDI requirements support knowledge and technology spillovers or instead hamper them by creating barriers to FDI inflows.

The case of China illustrates these limits particularly clearly, not least because the newly introduced FDI requirements, and to some extent also the LCRs under Annex III, are best understood against the background of China's growing role in strategic manufacturing sectors. In China,

where outward investment is embedded in a broader state-coordinated development strategy, stricter EU conditionality may not simply deter investment. It may instead lead to selective compliance, limited technology transfer or investment diversion towards third countries that still offer access to the European market. This underlines that the effectiveness of the IAA depends not only on its legal design, but also on how foreign investors may adapt in practice.

Overall, the IAA points to a broader shift in European economic policy towards more targeted and more conditional industrial policy intervention. That shift is understandable in light of rising geopolitical tensions and economic competition pressures. But successful industrial policy requires more than ambition. It requires a clear distinction between objectives, a careful matching of instruments to those objectives and a continued commitment to openness where this strengthens rather than weakens Europe's long-term competitiveness.

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APPENDIX

Table 1: Strategic sectors and targeting instruments under the Industrial Accelerator Act (Annex I)

Category	Sector / Technology	NACE Code / Description	Main Instruments Applied under IAA
Energy-intensive industries	Paper and paper products	C17	Inclusion in Annex I for industrial manufacturing acceleration areas; potential administrative acceleration. No product-specific Annex II requirement directly tied to this sector as such.
	Coke and refined petroleum products	C19	Inclusion in Annex I for industrial manufacturing acceleration areas; potential administrative acceleration. No product-specific Annex II requirement directly tied to this sector as such.
	Chemicals and chemical products	C20	Inclusion in Annex I for industrial manufacturing acceleration areas; potential administrative acceleration; possible future demand-side requirements for selected chemical products by delegated act.
	Rubber and plastic products	C22	Inclusion in Annex I for industrial manufacturing acceleration areas; potential administrative acceleration. No product-specific Annex II requirement directly tied to this sector as such.
	Other non-metallic mineral products	C23	Inclusion in Annex I for industrial manufacturing acceleration areas; potential administrative acceleration. Annex II includes product-specific low-carbon and Union-origin requirements for concrete and mortar.
	Basic metals	C24	Inclusion in Annex I for industrial manufacturing acceleration areas; potential administrative acceleration. Annex II includes product-specific low-carbon requirements for steel and low-carbon plus Union-origin requirements for aluminium.
Automotive industry	Motor vehicles, trailers and semi-trailers	C29	Union-origin requirements for electric vehicles in procurement and support schemes (Annex III); component-level thresholds; super credits for small zero-emission vehicles; inclusion in Annex I for industrial manufacturing acceleration areas.
Net-zero technologies	As defined in Article 4(1) of Regulation (EU) 2024/1735	Cross-reference	Inclusion in Annex I for industrial manufacturing acceleration areas; amendments to Net-Zero Industry Act rules on public procurement and resilience; origin requirements in auctions and other forms of public intervention under the amended Net-Zero Industry Act framework.

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