

# The Inflation Reduction Act: US-EU Relations

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The Inflation Reduction Act (IRA) is a turning point in US economic and climate policy and has reenergized conversations in Europe about transatlantic relations and domestic competitiveness. Firms seeking to benefit from the policy will need to carefully engage with different stakeholders in the US and Europe. With the issue likely to remain front and center this year, Brunswick Geopolitical convened key experts across sectors and geographies to discuss the IRA.

## Heavy on carrots, light on sticks

The IRA is the largest US investment in clean energy by several orders of magnitude. With its raft of incentives and limited penalties, it is said to be “heavy on carrots while light on sticks.” There are concerns, however, about how quickly funds will be distributed. The Joe Biden administration has linked tax credits to social and economic goals. The Treasury may take time to craft rules in areas where tax cuts and incentives for renewable energy coincide. This may lead to delays in permitting and implementation.

## Securing funds

There is no one-size-fits-all approach for companies hoping to secure IRA funds. Engagement is necessary at the national, state and local levels.

**National:** Firms should present their project as a solution to issues agreed on by most US voters: reshoring jobs and countering China’s grip on critical supply chains. There remain partisan divides on decarbonization.

**State:** States have differing approaches to the environment, with some like California more receptive to communications linked to decarbonization, while others will react poorly.

**Local:** Engaging local communities by highlighting the economic and employment benefits of a project is critical. With many local groups taking a “not in my backyard” starting stance to manufacturing plants, firms will need to work hard to bring local communities on board.

## Concerns

**China:** Bipartisan hawkishness toward China means companies must be prepared to answer detailed questions about any partnerships with Chinese firms.

**Anti-IRA politics:** Congressional Republicans will look to highlight projects deemed controversial or struggling as means of discrediting a flagship White House policy.

**Environmental justice groups:** the IRA will provide funds to environmental justice groups as a check on the subsidies going to businesses. Companies should engage the non-profits supporting these activists.

## EU Competitiveness

The EU is already at a competitive disadvantage to the US due to a weaker euro, higher energy prices, non-harmonized EU funds and complex regulation. The IRA could trigger further business relocation to the US in key industries. European companies could use the US policy to push for action from Brussels on competitiveness, although firms should be wary of being perceived by both governments and consumers as attempting to play national policies against each other.

## EU Response

Brussels is still working toward a unified response to the IRA, something similar in size and structure and supported by the European Commission, which is resurgent after its central role in handling the response to COVID-19 and Russia's invasion of Ukraine. The EU continues to accuse the US of protectionism. It is still unclear whether there is scope for a US-EU free trade agreement granting Brussels similar exemptions to Mexico or Canada.

### EU Council Meeting

The European Council met on March 23 and 24 to discuss, among other things, maintaining European competitiveness in response to the IRA.

In a brief statement put out after the conclusion of the meeting, the Council reiterated its commitment to "close coordination of our economic policies, with a view to increasing the resilience of our economies," and indicated the importance of "attracting sustained investment, supporting innovation and job creating, and fast-forwarding our green and digital transitions." These statements serve to push the conversation on an EU response forward without solving fundamental differences between richer and poorer member states on how to act.

As expected, Berlin and Paris' respective attempts to adjust a 2035 ban on vehicles with combustion engines and include nuclear energy in the EU's Net Zero Industry Act exacerbated tensions at the meeting, with German Chancellor Olaf Scholz [claiming](#) that the EU was attempting to back out of a "promise made long ago" on a synthetic fuels loophole.

## Transatlantic relations: avoiding a race to the bottom

Neither Washington nor Brussels wants to disagree on the IRA to the point that they cannot agree on issues like the war in Ukraine or the perceived threat from China. But there is a very real risk of a race to the bottom on subsidies. The UK, outgunned financially by its neighbors, will need to carefully consider how to make the most of its post-Brexit flexibility and whom to align with.

### WTO

If US-EU relations substantially worsen, Brussels could raise the IRA's perceived rules violation at the WTO. While this could allow both sides to park the topic in a protracted process to focus on bigger geopolitical issues, it would mark a serious deterioration in relations.

## IRA: adaptable but here to stay

A rollback of the IRA is unlikely even if the Republicans retake the White House and Congress in 2024, since Republican states will disproportionately benefit from the subsidies. But companies would be wise to secure planning permissions for their projects before January 2025, given the possibility of a changed US political environment subsequently. Exemptions to address European, South Korean and Japanese concerns are possible in the long term. Some loopholes have already been inserted into Treasury guidance to address Asian disquiet, including exemptions for leased vehicles.

### To continue the conversation:

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