

THE ELECTRIC ENDGAME: EUROPE'S CLEAN PATH OUT OF VASSALAGE

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SUMMARY

- How the EU navigates the energy transition will shape its geoeconomic power. The bloc's recent moves to dilute climate regulation and prioritise short-term competitiveness could cause long-term damage.
- Stay this course and by 2040 Europe risks industrial stagnation, weaker exports and deeper dependence on imported energy and Chinese technology.
- Regulatory standards, clean-tech production and climate finance are tools of power. They can build rule-setting authority, market share and political influence in the age of electrification.
- This means another future for Europe is possible. To bring it to pass, the EU should shield strategic sectors and invest in innovation. It should also tie trade more firmly to standards alignment and deploy climate finance with purpose.
- That way, the EU can convert its climate leadership into lasting competitiveness and economic autonomy.

Brussels's blunder

It is February 2040. In Brussels a chill is in the air, and it has nothing to do with the weather. The green signs outside pharmacies read 14°C. It is a warm day for winter, but not unusually so. These days, global temperatures are hitting 2.3°C higher than pre-industrial levels. Policymakers in the European quarter have long since shed their puffer jackets. Inside the Berlaymont, they have also dispensed with Europe's environmental leadership. The EU's goal to achieve climate neutrality by 2050 has been postponed indefinitely.

Over the last 15 years, the conservative forces that have come to power in most EU member states have made two successful arguments against climate action: that it unduly restricts the competitiveness of European industries, and that reliance on Chinese-made clean technologies serves the EU up to Beijing on a plate. The bloc has since scrapped most of its emissions targets for the industrial sector. To counter dependence on China, the EU has also adopted a 100% tariff on imports of Chinese clean tech, from electric vehicle (EV) batteries to solar panels. And, after the European Commission decided back in 2025 to water down its ban on sales of new petrol and diesel cars, it scrapped the controversial policy altogether a few years later.

The turn against green policy had some short-term benefits. It produced surface-level trade agreements with third countries that had objected to “unfair” policies like the carbon border adjustment mechanism (CBAM). It also kept alive domestic car sales for European producers and prevented mass layoffs from industries threatened by the green transition.

But the turn had many unintended consequences, too. Faced with stiff competition from China, the decline of overseas sales forced car manufacturers, among others, to cut their workforces. Europe's green sector in particular has experienced big job losses, especially among those working on the expansion of the electricity grid. Meanwhile Chinese solar panels are still entering the market since—even with tariffs—they remain cheaper than most European alternatives.

On top of that, the sharp reduction in climate finance has shut European firms out of opportunities abroad, even if it has freed up some cash for Europe's governments to subsidise domestic industry. But with the continent largely reliant on costly natural gas and clean tech from overseas, European industries are still struggling to compete. They are lagging on innovation and know-how too, given they lack incentives to develop cleaner and more efficient technology. Europe's retreat has also damaged its regulatory power. As China is the dominant producer of green technology, often the first mover, and the main trading partner of emerging economies, it has overtaken Europe as the main rule-setter.

In short, the two arguments for delaying Europe's energy transition and abandoning climate action have proven false. Europe is in no way more competitive than it would have been otherwise and most of its firms are living on borrowed time. Overseas partners are turning away, and Europe has very little to offer them in terms of new technologies. Nor is the bloc more autonomous: it still depends heavily on imported gas and technology, and it has lost markets and partners in the global south. This is hardly a world in which Europe is more secure or more powerful.

The EU's climate policy will shape its geopolitical place in the world. The decline laid bare in the above scenario is just one of infinite possible futures. But it is a plausible one, given the trajectory of Europe's climate debate.

In the European Parliament, a new alliance of the centrist European People's Party and right-wing forces has already reduced firms' requirements to report on environmental measures. The European Commission has postponed its 2035 ban on sales of new cars with internal combustion engines (ICE) by downgrading the mandated 100% reduction in car emissions to 90%. It is also planning to delay the phase-out of exemptions under the emissions trading system (ETS), diluting previously agreed climate action.

More and more voices within European politics seem to be questioning the worth, speed and scale of the EU's energy transition and climate funding. For some, it is purely a matter of new spending priorities like defence and economic security. Others are concerned about Europe's ability to adapt rapidly, and the reliance on external, primarily Chinese, suppliers of components and technology. Europe's industrial sector, meanwhile, wants regulations to change because of the cost of the transition and the struggle to remain competitive. Then there are those who argue green regulation is preventing the bloc from concluding quick and easy free-trade deals.

Europe is indeed facing a difficult transition. It is becoming increasingly complex for policymakers to strike the right balance between sustainability, affordability and energy security. But, as this paper argues, the EU must continue. This is because the fight against climate change is about the bloc's global economic power, too. Other powers are developing and implementing emissions regulations and environmental standards with the aim of applying them around the world. Trade in clean-tech components has created dependencies, from the extraction of critical minerals to the sale of finished products abroad. Climate finance for developing and low-income countries gives donors sizeable geoeconomic influence.

Powers that excel in all three domains—regulation, technology and finance—will gain substantial economic clout in the coming decades. By 2040, the world is forecast to reach peak

oil demand, and renewable energy will be used on a large scale. How the EU and its member states have adapted by then depends on policies they make today. Take environmental regulation and emissions trading schemes: early adopters set the rules of the game. This gives domestic companies a head start over foreign producers that must become familiar with the rules and adapt their production facilities to be compliant. Clean-tech manufacturing also brings an enormous amount of geoeconomic leverage—just think of China’s market dominance in solar panels (in 2024, China built 87% of photovoltaic cells globally) and EV batteries (over 70%). This competitive advantage can then be reinforced through economies of scale, leading to greater innovation. And a savvy use of climate finance can strengthen global soft power, sparking profitable trade agreements and infrastructure deals in destination countries.

The countries able to strategically embrace the energy transition through regulatory, industrial and financial measures over the next decade will thus be the winners in the multipolar world of tomorrow. Those that delay, or worse, roll back, climate action risk exclusion from regulatory decision-making, major industries, commercial opportunities and the soft power that comes with them. This may leave them with weak industries powered by fossil fuels that come from inconvenient powers and dependence on clean tech from strategic rivals.

Europe is already facing a decline in geoeconomic might. The continent is projected to account for just 9% of global GDP by 2050, down from 16.5% in 2024. This is not to mention the consequences of its ageing and shrinking population. But European leaders still have time to change course. By playing to the EU’s regulatory strength, investing in key technologies where European companies are still competitive, and maintaining significant climate financing abroad, Europe can remain powerful today and develop precious geoeconomic leverage for a hotter and more uncertain future.

The power of regulation

2040: The EU has abandoned climate clauses in its trade agreements, including the notoriously sensitive CBAM and the anti-deforestation law. But Europe’s regulatory pause means the bloc has effectively ceded leadership to China, which has been quick to fill in the gap by promoting its own climate rules and standards that favour its domestic players.

The pause has allowed the bloc to rapidly conclude free trade deals with emerging economies including Malaysia, Nigeria and Thailand, whose environmental regulation is weaker than Europe’s. But the difficulties in rolling back domestic European regulations to the level of developing countries mean these agreements are shallow. They also exclude several sectors from free trade, including agriculture,

minerals and food products. At the same time, European industrial producers are being undercut since scrapping the environmental part of trade agreements has made foreign, more polluting products more competitive in the single market.

Moreover, the slowdown in green regulation has disincentivised European industries from developing smart and efficient solutions through which they could have promoted stronger economic cooperation with developing countries. Instead, most European firms have optimised existing technologies rather than innovating.

Writing the rules

2026: Those who write the rules have a better chance of shaping the outcomes. And for a long time, the EU has been the dominant rule-maker: to have access to the EU's huge consumer market, exporters must abide by its climate regulation. This means the bloc sets standards that its businesses are better prepared and resourced to meet than importers. In other words, the bloc's climate standards give its firms a competitive advantage over the actors required to meet them. But things are changing, and the geoeconomic order will change with them.

China is taking note of this regulatory power. For example, back in 2005, the EU established the world's first large-scale carbon market, the ETS, to cap greenhouse gas emissions and allow the trading of permits among industrial players. China initially copied from the European example, applying it to the power sector and using an emissions-intensity model that allowed overall emissions to grow alongside the economy.

But Beijing is now tightening and expanding its system beyond the energy sector. From 2027, it plans to move towards an absolute cap with a fixed ceiling on total emissions. This shift is partly a response to the EU's CBAM. It aims to ensure that Chinese exporters pay taxes to Beijing, not at the European border, and that its firms are not disadvantaged in carbon-priced markets.

The effect is broader than EU-China trade alone. If both the EU and China embed carbon pricing at scale, exporters in third markets will increasingly need to internalise carbon costs to maintain access their markets. Europe is now sharing its regulatory influence: China is no longer simply adapting to European rules but incorporating carbon pricing into its own industrial strategy, keeping tax revenues, encouraging low-carbon innovation, and gradually shaping standards across its supply chains.

Most of the world is now moving—albeit at different speeds—towards the adoption of domestic climate standards and are necessarily basing their models on existing systems. Even major

fossil fuels exporters like the UAE are introducing compulsory reporting and emission regulations as part of their transition strategies.

At the other end of the spectrum, US president Donald Trump is tearing up environmental standards and waging a war against America's domestic wind industry. The geoeconomic costs are a warning sign. After halting the green tax credits introduced under the Biden-era Inflation Reduction Act, the first quarter of 2025 saw \$7.9bn worth of clean-tech projects cancelled, more than in 2022-2024 combined. The president's love for fossil fuels is diminishing America's ability to compete in new technologies. This domestic regulatory rollback, combined with America's withdrawal from nearly all international climate and environmental organisations, is eroding US regulatory power. American businesses hoping to export will now have to abide by foreign regulation with little domestic help (and that is before factoring in tariffs).

Even if the EU does not have the US to worry about, China is a growing challenge to its regulatory influence. Beijing dominates clean-tech markets in Asia and is now expanding its influence into the regulatory realm. In particular, it offers its system of carbon trading and taxation to developing countries as a model to address greenhouse gas emissions while growing economically. Here Beijing is using a cheaper alternative to the EU scheme to answer an implicit fear of many governments in the global south that emissions reduction is not compatible with economic growth. This could encourage Asian countries follow its model and adopt emissions reporting and trading standards that favour Chinese firms over European ones.

A standards clash

On the other side, Europe's trade partners are keen for the bloc to roll back its climate regulation, to avoid dealing with its environmental standards and emissions reporting. The most demanding of these is the CBAM, which, as of January 2026, forces importers into the EU to pay a fee on the carbon content of goods—unless those emissions have been taxed in the country of origin. This means developing countries with weaker carbon pricing regimes will face higher costs for trading with the EU. The mechanism has sparked accusations of undue protectionism from much of the global south. Trade partners have also voiced concerns over the EU's anti-deforestation law which bans the imports of agricultural goods linked to forest destruction abroad as of December 2025.

European officials are painfully aware of these complaints. Climate protection proved a contentious point in EU-India trade negotiations, and the agreed upon deal limits liberalisation in climate sensitive areas like agriculture and steel, although the EU did hold firm on CBAM. To finalise the EU-Indonesia Comprehensive Economic Partnership Agreement, the bloc had to

carve out an exemption for smallholder farmers.

Prospective partners have objected to other climate-connected unilateral measures from the EU. One example is the late 2025 doubling of steel tariffs and reduction of import quotas. The move, which protects clean European manufacturers from cheap and highly polluting imports, was intended to be both a negotiating tool against similar US tariffs on European steel and a first step towards an international clean steel club (comprising members who impose tariffs on external imports of “dirty” steel). But the EU’s hasty decision has angered advanced economies and developing countries alike.

While the EU has been persistent on CBAM, elsewhere extended delays of the EU deforestation law, the carve out for Indonesia, and sustainability frictions in the India deal suggest European policymakers are tempted to soften climate rules for quicker deals. This temptation to scrap significant environmental commitments or regulatory harmonisation in trade negotiations is likely to grow as the EU courts emerging economies whose standards differ significantly from those of advanced economies.

To be sure, the EU can hardly ask prospective trade partners to abide by its climate standards across the entire value chain the day after signing a deal—especially if the EU does not share the technology needed to reach those standards. Adequate and incremental timelines for implementation with embedded flexibility are a sensible choice when negotiating trade deals.

What does not make sense is severely weakening regulation for short-term benefits like marginally higher growth in exports following a free trade agreement. This would come at significant cost not just to the environment, including higher emissions and deforestation in partner countries, but to European producers who will likely be undercut by cheaper and less environmentally friendly imports by developing countries. The EU’s regulation, if consistently enforced, gives it a competitive advantage.

The influence of innovation

Finally, domestic decarbonisation efforts allow a country to export not just standards but also innovative climate solutions. Installing record-breaking renewable capacity or developing clean solutions at the industrial level is a matter of influence as well as international headlines. And once again, the trend favours China. Between January and May 2025, the country added 198 gigawatts (GW) of new solar capacity and 46GW of wind, enough to cover the entire electricity generation of a large, industrialised country like Turkey or Indonesia. In the same period of time, Germany—Europe’s biggest solar-energy power—added just 7GW

Europeans cannot compete with China on total capacity. But they should be aware that the country's record-breaking pace means it is continuously developing new solutions to meet new energy demand, primarily in renewables and nuclear. Between 2016 and 2020, China produced the lion's share of the world's green and digital patented innovations at 31.4%, followed by America, Japan, South Korea and then Germany at just 3.8%. This is important as the primary concern in many developing countries besides cost is how to decarbonise when electricity demand keeps rising. Beijing is showing them the way, leading in innovation on clean energy by developing new technologies and reducing the costs of established ones. But the good news for Europe it is not just about quantity. The quality of European innovation leads China in some key sectors like wind, and innovation rankings still put European countries at the top—but China is improving here too.

Weaker decarbonisation rules would spell weaker global influence for European firms. With no incentive, they would have little or nothing in terms of green innovation to offer partner countries, making China the only game in town. The EU's domestic firms would likely struggle as emerging economies keep improving capacity and development in legacy sectors and undercut European industries. In such a world, it becomes clear that retreating from domestic climate commitments would hardly serve Europe's geoeconomic interests.

Technologies for a cleaner world

2040: The rollback of the EU's climate regulation means most of the bloc's carmakers still produce cars that run on fossil fuels. This means they maintain domestic sales levels and only slightly increase sales of EVs, which now lack subsidies. ICE car manufacturers have managed to hold onto some jobs, as have the myriad firms that produce components for those cars. But overseas sales are lagging: Chinese EVs now dominate sales in most high- and middle-income countries. The know-how gained in making EVs has spread to ICE cars, and China now produces much cheaper gasoline and hybrid cars than Europe with similar quality. For households in developing countries, the choice is a foregone conclusion. European players can only compete in the high-end sector, but this is unsustainable.

Europe's domestic decarbonisation industry has similarly stalled as tariffs have made Chinese solar panels too costly for many households and small firms, yet they remain cheaper than most domestic production which never quite got off the ground. The end of subsidies has also made the installation of clean energy sources more expensive. Some of this money was used to reduce energy prices for energy-intensive firms—a necessary measure given the reliance on natural gas and frequent prices hikes linked to spot contracts and geopolitical disturbances in export countries.

A new battleground

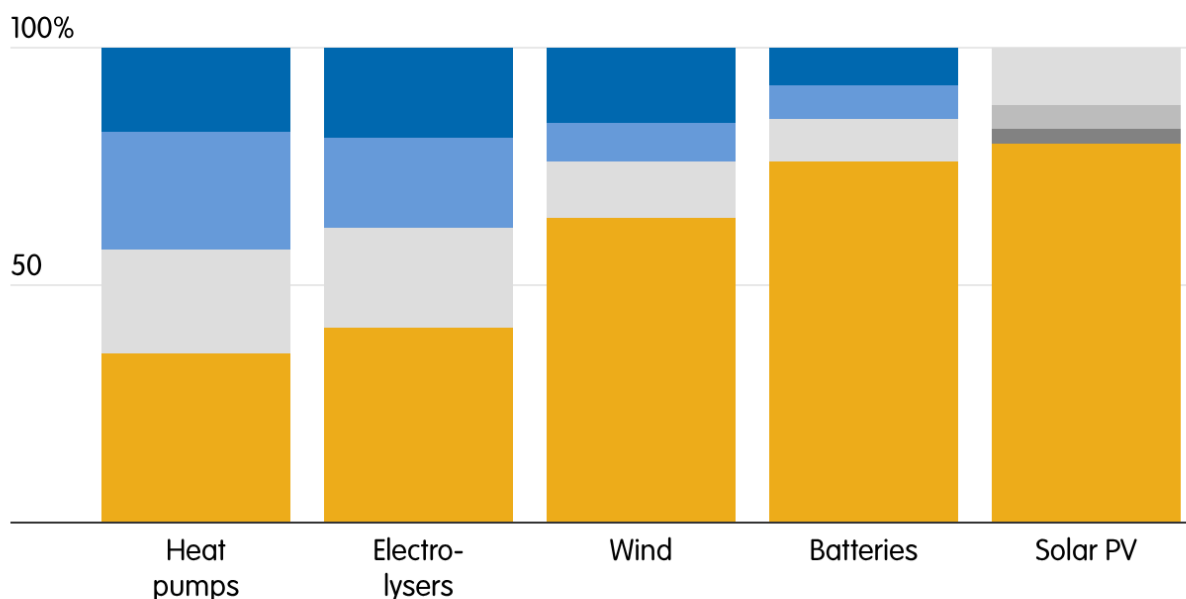
2026: The manufacturing and trade of clean tech is the second key geoeconomic battleground of the future. As more countries integrate renewables into their energy supply, the market for clean-tech components, electrification solutions, and EVs will soar. By 2040, the combined value of clean tech, critical minerals, green industry materials and green services could reach \$11trn. While the forecast is based on the International Energy Agency's net zero by 2050 scenario, a trajectory that today looks unlikely, it underlines the economic importance of these sectors. Even in a less climate-friendly scenario that assumes none of the currently planned environmental legislation will enter into force, electric vehicles would account for 40% of global car sales by 2035, and based on currently proposed and pledged policies, they would make up more than half.

Renewables are set to grow faster than any other energy source. As installations of solar panels and wind turbines increase, so does the geoeconomic power of the countries that produce them and extract and refine the raw materials they require. The EU is hardly a heavyweight in any of these industries. Several European carmakers have recently scaled back plans to transition to EVs and the scrapping of the ban on sales of new ICE cars has been hailed as a major victory by legacy carmakers across the continent. But with this, the EU risks being left out of the rapidly growing EV market. A similar logic applies to other clean industries: without domestic demand, many European firms would struggle to reach the scale necessary to compete globally.

China already dominates the clean-tech industry. The country is the top refiner in most energy-related minerals, holding above 80% of the world's gallium, graphite, manganese, rare earths and silicon. Besides that, Chinese firms are expanding their footprint in mining operations abroad, going upstream in the mineral value chains. They are going downstream too, accounting for 95% of solar-grade polysilicon production, for example. This dominance of clean-tech value chains and China's massive industrial capacity mean that climate action will only strengthen the country's global position. As the world moves towards electrification, countries able first to electrify rapidly and second to provide quality electrification solutions at scale will gain huge overseas sales and with them, geoeconomic leverage.

Global manufacturing capacity of key clean-energy technologies 2022, in %

China EU US India Vietnam Other countries



Source: IEA
ECFR · ecfr.eu

Developing dependency

At its core, the clean-tech race is about strategic autonomy. As the global economy electrifies, control over clean tech is becoming the new foundation of energy security—especially for countries lacking vast fossil fuel resources. Countries that cannot depend on their own clean-tech industry will be far more vulnerable to the whims of oil producing countries and to suppliers of key technologies.

Already, politically strategic oil-producers like the Arab Gulf states are developing clean tech and researching new solutions to remain relevant in the energy scenarios of the future. They are also ramping up the electrification of their domestic economies. Backwards-looking ones like Russia, meanwhile, are continuing to base their economic model on fossil extraction, hampering opportunities down the line. Similarly, America's decision to boost oil and gas and cut support for cleaner sources means it will trade increased revenues today for a weaker position in clean-tech supply chains tomorrow.

As for Europe, nearly half of its electricity and a quarter of its total energy comes from renewable sources, a figure that is steadily growing. However in 2024, 73% of the clean tech needed to produce this energy came from China. The continent's energy security is not only bound up in reducing reliance on fossil suppliers, but increasingly on clean-tech suppliers too—whether it moves with the trend or against it.

Even though fossil fuels will play a geopolitical role for a long time yet, as legacy energy sources they will benefit little from innovation; the geoeconomic leverage that comes with their production is declining. Indeed, while oil and gas demand is set to rise in the coming years, nearly 90% of upstream oil and gas investment since 2019 has been dedicated to offset production decline rather than demand growth. Meanwhile electricity demand is rising faster than total energy demand. In the coming years, manufacturers of clean tech will not only be secure in their own energy supplies. They will also increase their export revenues and geopolitical leverage. The countries able to dominate the clean-tech industry at the global level will have the geoeconomic advantage over those that do not. Indeed, these “electrostates” are the new powers of the future.

China is often described as the first electrostate, an unchallenged leader in clean-tech industrial products and almost all related materials like refined rare earths. With this, it is shoring up its geopolitical power. As it provides the materials and technological know-how to emerging economies seeking to decarbonise, Beijing is becoming an indispensable partner for many countries' decarbonisation and electrification.

Under its “south-south” model of cooperation, China has already built an energy ecosystem in South-East Asia, where it is the main provider of industrial inputs and technological know-how across clean energy supply chains. In Latin America, it is expanding cooperation on energy and infrastructure to include green solutions. And in Africa, 59% of China's energy projects are now for renewables. By embedding its firms and clean-tech products into the energy transitions in these regions, China is converting infrastructure investment into durable geopolitical influence.

Although on a smaller scale, the Arab Gulf states are increasingly using clean energy to extend their influence in Africa, too. The UAE, Saudi Arabia, and Qatar are financing solar, wind and green-hydrogen projects, while Gulf firms provide technical expertise and investment in supporting infrastructure. These initiatives allow Gulf states to position themselves as reliable partners for African governments as they balance decarbonisation with growing electricity demand. By linking finance, technology and energy planning, they are creating channels of influence and embedding themselves in emerging cleanenergy markets.

Amid this competition, the EU risks losing ground. Through initiatives such as Global Gateway, European institutions and firms are financing clean energy projects, sustainable infrastructure and technology transfer in Africa, Asia and Latin America, aiming to link decarbonisation with economic development and climate standards alignment. However, Europe’s industrial footprint in mass-manufactured clean tech is far smaller than China’s, and its investment is often dispersed across markets rather than concentrated in dominant supply chains. As a result, the bloc’s influence is shaped more by regulatory weight and finance than by export driven leverage, reinforcing a model of strategic partnerships rather than industry dominance.

A disappearing industry

These dynamics put Europe in a precarious position across many industries, but none is more threatened than its automotive sector—one of the EU’s biggest employers with 2.4 million direct jobs. Laggards in EV production (in 2024 the EU produced only 2.4 million EVs compared to China’s near 13 million), EU car manufacturers have long relied on mechanical excellence and have seen China as a market for their sales. But this is quickly changing. China’s electric revolution presents a double threat: Chinese EV makers are increasingly squeezing EU carmakers in the Chinese market and EU carmakers are facing growing Chinese competition in the European market. Europe has already become the largest export market for Chinese EVs by far, representing half of foreign sales in the first nine months of 2025.

Chinese brands’ battery EV registrations in Europe*

Brand	August 2025 registrations	YoY change
BYD	7,109	+114%
MG	2,562	-16%
Leapmotor	2,019	new
Xpeng	1,094	+62%
Omoda	664	new
Zeekr	463	+188%
All Chinese brands**	14783	+89%

*EU27 and UK

**Excludes Chinese-owned Volvo, Polestar, Smart and Lotus

Source: Jato Dynamics; Bloomberg

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A third threat is also appearing: once looked down upon as bad quality and poorly engineered by their European counterparts, Chinese gasoline vehicles are now seeing a boom of exports to emerging markets. Besides manufacturing scale and cheap labour, two dynamics are behind this trend. First, after diminishing domestic sales, Chinese ICE-vehicle producers are shifting to markets that are more receptive to gasoline-powered cars. And second, manufacturers are using the software and electronic know-how acquired through EV production to produce higher quality ICE vehicles that compete with European rivals in technology and appeal, but sell for a fraction of the price.

In this context, the EU's decision to lift the ban on new ICE car sales by 2035 is hardly a victory for Europe's struggling carmakers. While in theory the decision removes a hard-to-reach deadline and provides producers with more breathing space, the underlying risk is that the delay might just be used to ensure a few years' more sales rather than to put forward a radical transformation of the sector if there is no immediate incentive to do so.

By the late 2030s, it is extremely unlikely that European ICE producers will see sunlit uplands, either domestically or internationally. In a low EV adoption scenario, battery powered EVs are estimated to make up 64% of the global new vehicles fleet by 2040; while ICE vehicles will have an shrinking market share, both in Europe and abroad. If European carmakers do not use the additional years provided by the shift in policy to rapidly adapt and become highly competitive in EV and hybrid car production, they might find themselves even worse off. At the same time, emerging economies with limited purchasing power will just opt for Chinese brands—both in EVs and ICE cars—as they will likely be cheaper and of similar quality to European counterparts.

In wind power too, Europe is barely holding on to its position. Much like solar power, Europe was a pioneer in wind power technology, both in research and manufacturing. And just like solar power, the sector is now coming under huge competitive pressure. Once the undisputed world leader, in 2024 Denmark's Vestas accounted for only 10.2% of combined (onshore and offshore) wind commissioned capacity globally and was the only non-Chinese producer in the top five.

Even the good news for European industry is short lived. Growing demand for legacy energy sources, in part driven by AI data centres, is temporarily boosting the profitability of European makers of gas turbines like Siemens. But this trend is largely down to gas demand and at the mercy of its future fluctuations. Plus, the profitability only lasts until the turbines are sold, then someone else gains the revenues and the geopolitical influence that comes with the gas they use.

In the coming years, at risk is not just the fate of some companies but of European industries. If rising political pressure prevents the EU and its member states from deploying effective industrial policies to support the sector, important know-how and capabilities could be lost. In an increasingly electrified world, Europe would struggle even more to provide partners with solutions to electrify and decarbonise their economies, leaving room for other powers—namely China—to deliver them instead. Worse, the EU could find itself more and more dependent on foreign suppliers of energy solutions, too.

Funding a greener future

2040: The EU and member states have largely reduced the climate finance they provide to contribute to poorer countries' mitigation and adaptation measures, hailed by many conservative voices as a way to stop wasting money abroad. While Europeans maintain their binding commitments to international institutions, their retreat as major climate donors has whittled away European soft power and the opportunity to shape recipient countries' decarbonisation efforts. In just a few years, China has stepped into the void and wasted no time in presenting itself as the defender of the poorest, providing loans and offering its own products and components for climate change solutions.

America down and out, China racing ahead

2026: Climate finance—the public and private funding to support climate mitigation and adaptation measures—is the third channel through which climate will shape the geoeconomic balance of the future. It addresses the needs of developing countries and redistributes some wealth from richer and historically more polluting countries to poorer economies that often face the negative effects of climate change first.

Climate finance is also a powerful geoeconomic tool: by providing financial resources, countries gain reputational benefits and get a say in recipient countries' climate action. Criteria that define how grants and preferential loans should be used mean donors can partially orientate their climate finance towards their interests in a region, for instance fending off geopolitical rivals, as well as introducing standards that would favour their own industry. In an increasingly contested world, climate finance is a way to protect the environment, and a battleground for influence.

The landscape of international climate finance dramatically transformed over the course of 2025. Trump's decision to freeze and then permanently close the US Agency for International Development (USAID) slashed more than 2% from the world's total funding for climate resilience. The absence of the US from COP30 in Brazil makes the commitment reached in Belém to triple adaptation financing for developing countries harder to reach. Then, the January 8th US Treasury decision to withdraw its funding of \$4bn to the Green Climate Fund, the largest multilateral climate-finance fund, signalled the end of US public contribution to climate finance, at least for the remainder of Trump's term. In one fell swoop, the US left the global south without support to fight the worst effects of climate change and destroyed the soft power and geoeconomic leverage that came with it. This is particularly evident in the Indo-Pacific, where China, while not filling the gap left by USAID, is rapidly winning in terms of narrative and gaining the trust of countries abandoned by America.

In recent years, China has ramped up its contributions to international climate finance primarily through its flagship infrastructure development strategy, the Belt and Road Initiative (BRI). Through the BRI, China has focused on loans rather than grants (which were just 6% of China's bilateral climate finance between 2000 and 2022) and energy and transport received the bulk of this funding. Still, China is among the world's top ten donors through multilateral institutions, providing approximately \$10.4bn between 2015 and 2022, just behind Canada's \$11.03bn. Besides bilateral and multilateral contributions, China is also rapidly expanding its foreign direct investment in clean tech, with more than \$220bn invested abroad since 2022. While this cash is not strictly climate finance, it can play a similar role by increasing energy availability in developing countries, where demand is growing, and ensuring at least a part of this is met by clean sources. In the first six months of 2025, Chinese projects for power generation abroad added 4.9GW in solar and 4.4GW in wind energy.

Through much of its bilateral climate finance, China has advanced its own geoeconomic interests, creating customers for its oversupply of clean tech and ensuring the energy transition in developing countries relies on Chinese-made components. It also helps China cast itself as a desirable partner in the developing world's fight against climate change—a strategy that is all the more powerful at a time when developed countries' pledges for climate finance have been repeatedly missed: only in 2022 was the 2016 Paris agreement's \$100bn target met and COP29's target of \$300bn per year in climate finance was confirmed at COP30.

A test for Europe

America's withdrawal and China's advance in climate finance puts the EU in a peculiar position. On the one hand, the union and its member states are still by far the world's largest donors in

international climate finance, with €31.7bn contributed in 2024 by the EU's institutions, member states and European multilateral development banks. Such leadership has encouraged regulatory harmonisation in recipient countries, although Europe does not have a clean-tech industry like China's to answer newly created demand.

On the other hand, US policy has created a gap in funding that European public finances are unable to fill, all the more so when a growing number of voices within the EU—especially, but not exclusively, on the far right—are calling for a reduction in climate finance commitments. The growing relevance of the far right in European politics is already reshaping the narrative about international climate finance agreements. In 2025, for example, Alternative for Germany ran on a climate-sceptical platform calling for a reduction of international development cooperation and the exit of Germany from the Paris climate agreement.

Given the urgency to dedicate more resources to improving the bloc's defence capabilities, international climate finance is unlikely to be a top priority in the EU's next seven-year budget. The scaling back of several measures and targets in the European Green Deal and calls for a more reserved approach to climate action and the energy transition suggest that supporting mitigation and adaptation efforts in the developing world might be reduced too. But significantly cutting European climate finance commitments would merely save some financial resources in the short term and produce an array of negative effects just as quickly.

First there would be reputational damage, not to mention anger from many developing countries that had been counting on European support for their mitigation and adaption needs. This would serve Beijing a narrative victory on a silver platter, allowing China to claim the title of the defender of the global south countries abandoned by Europeans—even though China is the world's biggest emitter of CO2. Second, without providing the funding, Europeans would be unable to influence the direction of climate efforts in developing countries. Such countries would then have no incentive to follow European guidelines nor to rely on European hardware or components for their clean-tech adoption or clean-energy production.

This reasoning also applies to environmental standards: without European financial support for their climate action, developing countries would likely adapt to the standards of their remaining donors, which in turn would make future climate cooperation with Europe more difficult. European firms producing clean tech would have a harder time selling their equipment in those countries and would struggle to be competitive in those markets if the standards landscape had been shaped by rival powers. Beyond all this lies the detriment to the global fight against climate change—which goes against every country's interest—that would likely come from a substantial reduction in European funding.

Another future is possible

It is 2040 and the weather in Brussels is grey and mild for February, but the geoeconomic clouds are not as dark as they could have been. Just over a decade earlier, policymakers in the city doubled down on the EU's strengths to protect the bloc as much as possible in this brave new, electrified, world.

There is no denying China's dominance in clean-tech production, and much of South-East Asia follows its climate standards. But the EU has partially held onto its reputation as a regulatory superpower. It has continued to link its trade deals to climate standards. And, thanks to the size of its consumer market, many emerging clean-tech manufacturers like India, Mexico and Vietnam are abiding by them. The EU is also working with these economies by sharing know-how and climate funds to collaborate on green manufacturing without China. Europe is a few percentage points short of its target of a 90% reduction in greenhouse gas emissions, but it is getting there.

Meanwhile, European manufacturers used delays on policies like the transition to EVs to prepare their industries to maintain their advantage where possible. China is still the world's largest EV producer and, thanks to low prices, dominates sales in emerging economies. But European producers have been able to develop luxury models and smaller cars with high efficiency and world-class mechanics. These are appealing to the middle class in and beyond the single market. The know-how gained in developing those models has also created more opportunities for clean cooperation with other parts of the world. The car industry is somewhat smaller than it was 15 years earlier, and much more automated, but it still exists.

Climate finance is not what it was since Trump's second term. American funds never recovered and Europe's appetite to spend remains small. In the gap, Chinese and Gulf investments flowed into Africa, Latin America and South-East Asia in particular. However, the EU's move to link debt forgiveness to clean energy investments and governance standards have improved both its reputation and climate mitigation efforts. This has paid off against Beijing; global south leaders are increasingly wary of getting into debt with or becoming dependent on China.

Back in 2026, Europe faced a difficult transition. Its fiscal space was constrained, and its room for manoeuvre even more so by those questioning the priority and viability of climate action. But through pragmatic and forward-looking policies, the EU protected its geoeconomic future as best it could.

Below are recommendations for how the EU can make this alternative future a reality.

Build international partnerships

The EU and member states need to cooperate internationally if they are to maintain their role in the future global order. This will not be easy to do in a world where interdependencies are weaponised, America has retreated from climate action and China is more assertive. Yet Europe's domestic market is a powerful asset, and the EU can use China's self-sufficiency drive to its advantage. While keen to export its clean tech, Beijing seems extremely wary of sharing know-how and transferring technology. And on the import side, it is only interested in raw materials and other commodities China cannot produce at home. For many emerging economies, improved trade with China thus amounts to it buying raw materials and dumping cheap goods.

The EU, on the other hand, can provide access to a rich market and support developing countries' aims to move up the value chains in clean tech. Here, European policymakers should better combine trade, climate finance and environmental regulations. New types of free trade agreements, like the Deep and Comprehensive Free Trade Agreements, already embed significant climate components. But the EU can and should do more. One option would be for the bloc to strengthen the conditions that relate to market access. It should place a stronger focus on companies and countries adopting similar environmental regulation to the bloc, while adding preferential climate finance for countries that sign free trade agreements that significantly align their climate standards. Another would be for the EU to work more closely with these economies by providing technical expertise, and expand the "Made in Europe" policy that favours European-made goods in public contracts, by adding "Made with Europe" as a secondary preference.

This would serve three parallel European goals. First, it would expand the EU's network of trade partners, reducing reliance on China. Second, it would help the bloc maintain influence thanks to the provision of climate finance and technology sharing. Third, it would incentivise emerging economies to follow European climate standards and regulations. Together, this would create a network of preferential trade agreements with regulatory harmonisation and more access to climate finance, creating incentives for countries to join the network rather than staying outside and face higher tariffs as well as less financial support. To make this politically palatable, European policymakers who care about competitiveness should savvily package climate regulation as trade, manufacturing and financial gains.

Diversify energy

The EU and its member states should double down on diversifying their energy supplies and electrifying their industrial systems. This would allow them to reduce reliance on capricious fossil fuel providers while preparing their countries for an age of electrification. It would also help them avoid the disruptions caused by sudden shifts. In this regard, natural gas will remain an important energy source in the short and medium term. But, directing it primarily to electricity generation would help contain its emissions, as is the case for Germany's new gas-fired power plants. This can improve resilience and allow for a smoother phase out once enough clean power is available. To support this switch, Europe needs to repair and strengthen its electricity grid, which it can fund as a security measure under the NATO funding requirement of 1.5% of GDP be spent on critical infrastructure and preparedness.

Use time wisely

European companies were global pioneers in many clean technologies. But they are now lagging behind China in most of them, either in terms of innovation or in manufacturing capabilities. In some others, like the wind industry, European players are still competitive in their domestic market but struggle to fend off Chinese rivals abroad. To address this double challenge and protect domestic producers, while recovering some of the gap, time and protective measures could help.

The EU's postponement of some key transition deadlines like the ICE ban or extending some emissions-cutting targets can only help prevent excessive dependence on Chinese-supplied tech if it is accompanied by actions to make European firms more competitive. The EU should ensure any such preventive measures happen within limited, incremental timeframes. They should not be deployed indefinitely as if the world is not entering an age of electrification.

Some industrial players might be interested in just kicking the can down the road and extracting the maximum revenues from additional years of sales on ICE cars. Here, European policymakers should provide clear guidance and directions. They should design these to push enterprises to use the time to develop competitiveness in sectors where they are still behind like EVs or to make sure that alternative fuels like biofuels or e-fuels are economically competitive.

In this regard, Europe's deregulation drive, supported by the European Commission and many member states, should not go to extremes: the commission should take into account the competitiveness concerns of firms, but Europeans would do well to remember that in a system without rules, China is more competitive, not less.

Adopt clever protectionism

Protectionist measures only make sense if there is something worth protecting. Tariffs on solar panels, save for the most advanced ones, would likely be pointless. This is because Chinese manufacturers' advantage is massive, and European firms have little chance of catching up. But the wind power sector, electric furnaces and recycling solutions, among others, are worth defending with tariffs to maintain a competitive edge. On top of these, the EU's demand-side measures like targeted public incentives should give a direct preference to equipment made in the bloc or at least within the G7.

The EU will have to carefully balance any protectionist stance, even if driven by the best intentions, with its need to maintain and defend open multilateral trade. This would help reduce the risk of the bloc antagonising emerging economies with excessively stringent trade measures. In this regard, countries that have free trade agreements with the EU or that are "like-minded partners" should not be subject to tariffs on green-tech components. Japan and South Korea, for example, are key players in EV batteries, while India—which recently agreed a free trade agreement with the EU—could provide a large-scale manufacturing alternative to China. Canada, a longstanding European ally, should also be included in industrial cooperation initiatives.

Find the right balance

Climate action is not cheap, and conflicting priorities will limit the availability of resources the EU can devote to supporting its clean tech or containing climate change abroad. With less resources available, Europe should be savvy in crafting this course of action. In climate finance, a greater use of debt for climate swaps—in which parts of developing countries' debts are forgiven in exchange for climate commitments—would help Europeans to support mitigation and adaptation efforts abroad without committing new resources.

Developing countries' debts are growing rapidly and are for the most part becoming increasingly difficult to recover. Instead of undertaking painful debt restructuring discussions that carry the risk of alienating partners, Europeans should offer debt-swap agreements to countries in distress. Those agreements, where possible, should include clauses that require recipient countries to use European equipment and standards in their adaptation or mitigation efforts, thus reducing the risk that recipients' climate action increases their dependence on China or other players. Debt for climate swaps would constitute an effective counter-offer to Chinese loans: despite recent openings, Beijing has a long history of reluctance towards debt relief and restructuring. As financial constraints could reduce the amount of European money available for climate finance, Europeans should try to get the most out of every euro spent (or forgiven) abroad.

Europe's green gambit

The decisions Europeans make about their environmental regulations, clean tech and climate finance today will shape Europe's place in the world in 2040 and beyond. Slowing the pace of transition might buy the EU some time, but it needs to use this time well given America's climate retreat is leaving Europe almost alone and China has a massive head start on many clean technologies. Europeans cannot just stop the clock.

Listening to the many arguments against climate action will not serve European interests. At best, the EU could score some quick trade deals, buy a few more years for European industry, and free up some money to use on areas like defence. But it would soon become clear the bloc is in a worse position to face the future, and by then, its rivals will be almost out of sight.

Rather, with some pragmatic policymaking, international cooperation and clever innovation, the EU can sketch out a different future for itself. One in which, even if China is ahead, Europe's global influence and industries can survive and maybe even thrive.

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