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Dynamics and Challenges of European Defence Industrial Integration.

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This Master's thesis explores the dynamics and challenges of European defence industrial integration, aiming to identify the key structural barriers to deeper collaboration within this domain.

The research begins with a multidisciplinary analysis of the dynamics shaping European defence integration, laying the groundwork for a better understanding of the issue. Challenges and obstacles are periodically identified all along this section

At a later stage, this thesis delves more closely into specific structural challenges such as national industrial interests, budget constraints and the influence of external actors. Throughout the thesis, connections are drawn to the ongoing political efforts and initiatives aimed at advancing European defence industrial policy, offering insights into the prospects for a more cohesive and resilient European defence industry.

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Dynamics and challenges of European defence industrial integration

1 Introduction

The European defence industry stands at a critical moment, where the conjunction of geopolitical pressures, technological competition and a deteriorating security environment induce a rethinking of traditional defence dynamics. As the European Union pursues its strategic autonomy agenda and seeks to enhance its security infrastructure, intensifying the Europeanisation of national defence industries through a more cohesive approach has become a critical and pressing endeavor. Having said that, numerous challenges and structural barriers stand in the way of further integration in this politically sensitive domain.

This thesis delves into the intricacies of “Europeanising” the defence industry. Despite significant strides in defence cooperation in the past decades, notably through initiatives such as the Permanent Structured Cooperation (PESCO) and the European Defence Fund (EDF), the path towards a more integrated European defence landscape remains obstructed by a series of obstacles. The aim of this thesis is not to provide an exhaustive and linear catalogue of challenges. In the first place, the favored approach will rather be to provide an academic outline of key institutional and economic dynamics underpinning the European defence industry. Proceeding in such manner will enable to punctually identify key impediments to further Europeanisation and apprehend them within a broader context, thereby facilitating a thorough understanding of the matter.

Subsequently, a closer focus will be adopted by individually considering specific challenges that constrain the perspective of more Europe in the military-industrial domain. First, the influence of member states’ domestic industrial interests over national and European decision-making in defence matters will be detailed. Then, we will examine the financial questions complexifying a greater Europeanisation of defence industrial matters. Finally, we will take a closer look at foreign influences and considerations. Most notably, the transatlantic relations and their ramifications will be investigated.

2 Legal and institutional overview of defence industrial matters

The defence industry is politically sensitive and characterised by a tight grip from national governments over decision-making. Indeed, military capabilities remain under the purview of member states. Historically, European military integration could have been realised had the European Defence Community (EDC) Treaty been adopted in the 1950s. The EDC would have centralised military production and procurement under a supranational authority, implying that member states would have lost a significant facet of their sovereignty by ceding power in military matters. However, following the failure of the EDC Treaty, a contrasting approach was eventually instituted by the Treaty of Rome (1958). It established a common market characterised by competition rules and limited sovereignty of its signatories in economic matters. Nevertheless, the Treaty included a loose “armament exception”, granting the possibility for national governments to derogate from the application of the internal market regime when it came to the “production of or trade in arms, munitions and war materiel” if a member state “considered” it “necessary for the protection of the essential interests of its security”. If article 173 of the Treaty on the Functioning of the European Union (TFUE) gives the European Commission the authority to shape EU industrial policies, the vague wording of the “armament exception” opened the door to subjective interpretations by national governments. The result has traditionally been a sizeable use of the exception by Member States, leaving them much discretionary power to bypass EU competition rules and acting as a counter-force to European integration in defence matters by keeping military decision-making along national borders¹. Hence, defence industrial policy factually remained a national prerogative and most of the 20th century was characterised by a de facto absence of the EU in these matters. The 1990s nonetheless brought changes to the institutional status quo. Although the Treaty of Maastricht (1992) introduced a Common Foreign and Security Policy, defence industrial policy remained largely national, with military capabilities acquired unilaterally or through collaborative processes, notably in the NATO framework.

At that stage, a liberalised internal market for military equipment remained a complete utopia. Indeed, the Commission lacked the political legitimacy or even the competence to regulate and enact industrial policies in defence matters. Yet, since the 1990s, the agency of the European Commission has been on the rise and it has nowadays become a key player in defence industrial policy in the EU. In 2009, two important directives, also known as the

¹ Meershoek, N. (2021). *The Constraints of Power Structures on EU Integration and Regulation of Military Procurement*. European Papers, pp. 835.

“Defence Package” were adopted by the Council and the European Parliament, based on a proposal from the European Commission. These were the first legally binding European instruments in the military domain. One directive constrained the scope of the “armament exception” and the other promoted a more resilient and competitive European Defence Technological and Industrial Base² (EDTIB) notably through increased intra-EU defence trade. These two directives essentially targeted the liberalisation of the European defence market, notably by putting forward principles of the internal market such as non-discrimination based on nationality of the bidder in defence procurements³. The overarching goal was to stimulate cross-border collaboration. Nevertheless, the “armament exception” of article 346 TFEU kept on being widely used and the impact of these directives on the EDTIB remained marginal⁴.

The trend of greater European institutionalisation of defence industrial policy accelerated throughout the 2010s. In 2016, the concept of “European strategic autonomy” was introduced by the EU’s Global Strategy⁵. It emphasised the urgency of becoming a more credible defence and security player. The same year and in the same dynamic, the Commission issued the “European Defence Action Plan”, which outlined the essential character of a greater Europeanisation in defence in order to “act autonomously if and when necessary”⁶. To obtain such “strategic autonomy”, the strategy identified the need for a strong and integrated defence technological and industrial base (DTIB) capable of producing major weapon systems in Europe. This necessarily requires sufficient innovation and production capacities, which the plan found to be lacking, in part due to the inefficiencies of excessively running procurement programmes on a national and uncoordinated basis. Pursuant to the concept of strategic autonomy, EU member states should prioritise procuring weapons from European producers. When European producers lack required capabilities, joint development programs should be pursued⁷. Nevertheless, the willingness to pursue this objective is by no

² Faure, S. (2022). *EU defence industrial policy : from market-making to market-correcting*. In : *EU industrial policy in the multipolar economy*. Leuven Global Governance. Edward Elgar Publishing, pp. 383.

³ Fiott, D. (2024). *In Whose Interests ? Regulating Europe’s Defence Industry and the Politics of Exemptions*. CSDS Policy Brief. 3/2024. <https://csds.vub.be/publication/in-whose-interests-regulating-europes-defence-industry-and-the-politics-of-exemptions/>

⁴ Masson, H., Martin, K., Quéau Y. (2015). *The impact of the ‘defence package’ Directives on European defence*. Directorate-General for External Policies, European Parliament. doi:10.2861/719356. Pp.6.

⁵ European Union External Action (2016), *A Global Strategy for the European Union’s Foreign and Security Policy*. European Union External Action.

⁶ Meershoek, N. (2021). *The Constraints of Power Structures on EU Integration and Regulation of Military Procurement*. European Papers, pp. 838.

⁷ Mölling, C., Helmonds, S. (2023). *Security, Industry, and the Lost European Vision How Russia’s War in Ukraine Is Changing the European Defense Technological and Industrial Base*. German Council on Foreign

means a consensus among European actors as developed later.

Announced in the “European Defence Action Plan”, the European Defence Fund was established in 2017 as a financial instrument aimed at funding research and development related to the defence industry and thereby incentivise member states to cooperate on armaments programmes. The EDF stands out as the first occurrence of the defence industry being funded immediately from the EU’s own budget⁸. The Commission allocated €25 million in 2017, €90 million in 2018 and again €90 million in 2019 with a view to finance research and development (R&D). Beyond R&D, a “capacity component” was added to the EDF to fund the development stage of cooperation projects, granted that they comprise at least three companies from three different member states⁹. Such steering of the funding agenda by the Commission illustrates a trend towards a more supranational dynamic, despite the traditionally intergovernmental nature of the defence matters. Nonetheless, member states retained influence over EDF’s activities through the “work programme committee”, composed of national representatives¹⁰.

By the same token, the permanent structured cooperation (PESCO) was established on the basis of article 46 TEU in the CFSP framework. At first sight, the PESCO might be regarded as an incursion into the discretionary power of member states, due to the supposed legally binding nature of a list of commitments¹¹ regarding the collaborative approach in developing and jointly using capabilities. Yet, taking a closer look, these commitments remain vague and enforcement possibilities are limited given the absence of any sanction procedure¹². Participation in the PESCO ultimately takes place on a voluntary basis and is project-based. The framework thus remains intergovernmental in nature. Furthermore, in 2019, the Commission established a Directorate General for the defence industry and space (DG DEFIS), responsible for the management of the EDF. The conjunction of the EDF and DG DEFIS pursued the objective of enhancing the competitiveness of defence firms and the integration of the European defence market. These institutional developments manifested a growing agency of the European Commission. This proactive institutional stance would have

Relations. DGAP Report, pp. 9.

⁸ Faure, S. (2022). *EU defence industrial policy : from market-making to market-correcting*. In : *EU industrial policy in the multipolar economy*. Leuven Global Governance. Edward Elgar Publishing, pp. 383.

⁹ Ibid, pp. 398.

¹⁰ Csernaton, R. (2022). *The EU’s hegemonic imaginaries : from European strategic autonomy in defence to technological sovereignty*. *European Security*, 31:3, 395-414, DOI: 10.1080/09662839.2022.2103370. pp. 400.

¹¹ <https://www.pesco.europa.eu/binding-commitments/>

¹² Blockmans, S. (2018). *The EU’s Modular Approach to Defence Integration: An Inclusive, Ambitious and Legally Binding PESCO ?* CMLRev 1785-1826, 2018. Kluwer Law International. United Kingdom. Pp. 1788.

hardly been conceivable in the early 2000s. Neither did it come about without the opposition of several stakeholders. It has been argued¹³ that the progressive European institutionalisation of liberal defence industrial policy is partly the result of a decades-long political effort from the Commission. Also, an increasingly volatile geopolitical and security context surely provided a window of opportunity for the Commission to play a more proactive part in defence matters. Additionally, the strive for European autonomy in security and defence must be understood in a broader context where the future of Europe, its technological autonomy and its global competitiveness are largely discussed and debated. Furthermore, the progress of European defence policy agenda is also the outcome of an interplay between the Commission, defence industrial actors and interest and experts groups¹⁴.

Russia's invasion of Ukraine in 2022 provided a new impetus accelerating the Commission's involvement and the ongoing trend toward more Europe in defence matters. The European Commission presented a series of major documents pertaining to the investment in defence capabilities and the support to the European defence industry. The EU released the "Strategic Compass", its first ever defence strategy. One of the stated objectives was to develop the EU's military capabilities. Additionally, documents such as the Joint Communication on defence Investment Gaps¹⁵ and the proposed Regulation for the European Defence Industry Reinforcement through Common Procurement Act¹⁶ (EDIRPA) were published and both emphasise the pivotal character of common EU procurement. Although these policy initiatives might at first sight look like a significant move towards supranational integration, Daniel Fiott argues that the logic remains fundamentally intergovernmental¹⁷. He describes this push for common defence procurement at the EU level as being more a form of policy entrepreneurship than a real shift towards supranationalism or deeper EU defence integration¹⁸. Whatever the theoretical case may be - deepening of supranational integration or greater intergovernmental collaboration - the fact remains that the Europeanisation of defence industrial matters has gained further momentum since the Russian aggression on

¹³ Faure, S. (2022). *EU defence industrial policy : from market-making to market-correcting*. In : *EU industrial policy in the multipolar economy*. Leuven Global Governance. Edward Elgar Publishing, pp. 398.

¹⁴ Csernaton, R. (2021). *The EU's Defense Ambitions : Understanding the Emergence of a European Defense Technological and Industrial Complex*. Carnegie Endowment for International Peace, Working Paper. Pp. 5.

¹⁵ European Commission (2022) JOIN (2022) 24 final, *Joint Communication to the European Parliament, the European Council, the Council, the European Economic and Social Committee and the Committee of the Regions on the Defence Investment Gaps Analysis and Way Forward*. European Commission.

¹⁶ European Commission (2024), *The European Defence Industry Reinforcement through common Procurement Act*. European Commission.

¹⁷ Fiott, D. (2023). *In every crisis and opportunity ? European Union integration in defence and the War on Ukraine*. Journal of European Integration, volume 45, 2023. <https://doi.org/10.1080/07036337.2023.2183395>. Pp. 455.

¹⁸ Ibid, pp. 458.

Ukraine. Yet, several hurdles remain on the path to improved coordination and coherence in defence industrial decision-making.

In March 2024, the European Commission proposed a very detailed European Defence Industrial Strategy¹⁹ (EDIS) which mostly aims to diminish fragmentation in the European defence industry, increase collaboration in procurement, reduce arms imports and increase intra-EU defence trade. In many respects, the strategy appears far-reaching and raises questions that member states will have to debate and agree on.

¹⁹ European Commission and High Representative of the Union for Foreign Affairs and Security Policy (2024), JOIN 2024, 10 Final, *Joint communication to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the regions. A new European Defence Industrial Strategy : Achieving EU readiness through a responsive and resilient European Defence Industry*. European Commission.

3 Economic and industrial considerations pertaining to the European Defence Industry

Despite its strategic relevance, the European defence industry is highly fragmented on both the demand and supply sides, with significant heterogeneity among the various national industries. This fragmentation is a major concern, especially in an increasingly unstable geopolitical context and given the rising costs and complexity of defence equipment. Fragmentation along national lines is frequently singled out as the main impediment to a resilient, competitive and innovative European defense industrial base, hindering the achievement of economies of scale, causing duplications of capabilities and reducing interoperability. Furthermore, the technological complexity of modern armaments makes them too expensive or complex for single member states to develop independently, leading to capability gaps and a preference for off-the-shelf purchases from foreign suppliers over collaborative European processes. As military budgets increase, this could exacerbate Europe's inefficient and scattered defence spending, especially amid constrained public finances. Additionally, the war in Ukraine has prompted governments to prioritize quick replenishment of capabilities, often through imports, further impeding Europeanisation efforts.

In this chapter, we will endeavor to properly outline key economic, industrial and political considerations shaping the European defence industry's political economy. Although their respective dynamics are intrinsically related, we will first assess the demand side of the industry to finish by the supply side.

3.1 Demand side

3.1.1 Dynamics and stakes of defence procurement

On the demand side of defence markets, countries are typically the main actors. In the EU, member states tend to follow their own defence procurement policies, often prioritizing national suppliers in order to support their domestic industries. The 2022 Coordinated Annual Review on Defence (CARD) report indicates that only 18% of investment in defence programmes is actually collaborative²⁰ and emphasizes that “cooperation remains the exception rather than the norm”. This not only hampers the exploitation of economies of scale

²⁰ European Defence Agency (2022). *2022 Coordinated Annual Review on Defence Report*. European Defence Agency, pp. 11.

but also results in a lack of standardisation and interoperability among European armed forces, affecting the strategic weight of the EU. Further coordination of defence planning at the European level therefore conveys the prospect of faster and cheaper acquisition, as well as greater operational convergence and efficiency (e.g. ability to conduct joint operations). Because demand often shapes supply – especially in the defence sector – more European cooperation would also be instrumental in further rationalising the European defence industrial landscape (i.e. the supply side). The latter remains mostly structured along national borders.

The European framework corresponds to an insufficient share of the defence industrial collaboration by member states. The better part of defence investments actually takes place outside of the European structures, whether on a national or cooperative non-EU basis. Indeed, the 2022 Strategic Compass highlighted that “defence planning remains stuck at the national rather than at the European, or even Atlantic, level”. The Strategic Compass attributes the fragmented nature of Europe’s defence industry to this state of affairs²¹. Beyond the inefficiencies of such a fragmented demand, notably in terms of ramp-up or innovation abilities of the suppliers, the paucity of collaboration is an expensive issue. In 2023, a research report by the European Parliamentary Research Service estimated that from €24.5 billion to €75.5 billion per year could be saved through more EU collaboration, as a positive outcome of seizing economies of scales, savings in administrative costs and lower duplication of programmes²². Another study from 2014 estimated that up to €120 billion per year could be saved through a comprehensive EU army integration, that is, beyond industrial integration²³. Regardless of the accuracy of these figures, the cost of non-Europe in defence matters is significant and is closely related to the poor allocation of defence expenditures across the EU. As an illustration, in 2013, despite spending approximately the same amount, the US developed 3003 units of its Joint Strike Fighter while the German-Spanish-Italian-British consortium furnished only 707 Eurofighter jets²⁴.

²¹ European Union External Action. (2022). *A Strategic Compass for Security and Defence*. European Union External Action. Pp. 29.

²² European Parliament Research Service. (2023). *Increasing European added value in an age of global challenges. Mapping the cost of non-Europe (2022-2023)*, Brussels, European Parliament. DOI: 10.2861/144, pp. 312.

²³ Bertelsmann Stiftung (2014). *European Added Value of EU Spending: Can the EU Help its Member States to Save Money?* Pp. 96
https://www.bertelsmannstiftung.de/fileadmin/files/BSt/Presse/imported/downloads/xcms_bst_dms_38323_38324_2.pdf

²⁴ Briani, V. (2013). *The costs of non-Europe in the defence field*. Center for Studies on Federalism and Instituto Affari Internazionali. Pp. 28.

The EDIS²⁵ is the most recent endeavor to bolster collaborative defence projects. It notably proposes to establish a Structure for European Armament Programme (SEAP) in order to streamline defence cooperation between EU member states. In addition, the EDIS proposes the establishment of a Defence Industrial Readiness Board, a forum to “support the coordination and de-confliction of member states’ procurement plans and provide strategic guidance in view of more effectively matching demand and supply”²⁶. The Board would notably aim to identify European Defence Projects of Common Interests “to focus EU effort and funding programmes”²⁷.

3.1.2 Is collaborative procurement consistently the cheapest and preferable option?

The procurement of military equipment is still primarily done on a national basis, rather than through intergovernmental collaboration. Multiple factors influence the decision of European governments to collaborate or not on defence procurement. As later developed, these factors vary depending on the considered country. To name a few, different strategic cultures, languages, geographic imperatives, threat perception, external dependencies and alliances, domestic defence industrial interests and procurement habits are all elements likely to enter into account in the decision process and thereby constitute potential obstacles to collaboration. Besides, these factors also have an impact when it comes to setting requirements for a piece of equipment collaboratively procured. Under an ideal theoretical model of economically efficient collaboration, participating countries share the cost of development and procurement of defence capabilities. In turn, pooling research and development (R&D), development and/or production costs smoothly leads to economies of scale, increased production and reduced duplications, thereby enabling lower costs²⁸. The

²⁵ European Commission and High Representative of the Union for Foreign Affairs and Security Policy (2024), JOIN 2024, 10 Final, *Joint communication to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the regions. A new European Defence Industrial Strategy : Achieving EU readiness through a responsive and resilient European Defence Industry*. European Commission.

²⁶ Mölling, C., Hellmonds, S., Csernaton, R., Martins, B., Racz, A. (2024) *Sovereign, Capable, Innovative, Responsive: Prospects and challenges for EU security and defence policy in the 10th parliamentary term*. Policy Department for External Relations, Directorate General for External Policies of the Union, pp. 13.

²⁷ European Commission and High Representative of the Union for Foreign Affairs and Security Policy (2024), JOIN 2024, 10 Final, *Joint communication to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the regions. A new European Defence Industrial Strategy : Achieving EU readiness through a responsive and resilient European Defence Industry*. European Commission. Pp. 8

²⁸ Hartley, K. (2019). *The Political Economy of Arms Collaboration*. Cambridge University Press. <https://doi.org/10.1017/9781108348058.011> , pp. 242.

opportunity to obtain such savings is a recurring economic argument in favor greater armament collaboration in Europe.

However, the literature doesn't provide strong evidence of such savings being a systematic occurrence. In practice, it appears that cooperation hardly ever fails to depart from the theoretical model presented above. Joint development projects typically involve diverse inefficiencies such as costs overruns and delays, thus failing to provide the expected levels of economies of scale and cost savings. As previously described, such inefficiencies can proceed from national industrial interests and protectionist behaviors, operational and bureaucratic factors, etc. They can take the form of overly detailed and diverging national requirements. In multinational programmes, national requirements are indeed frequently instrumentalised to protectionist ends²⁹. Eventually, the lack of harmonisation of requirements can lead to a differentiated demand for a similar capability, thus putting a damper on the ability of the project to tap into potential economies of scale. Debates about work-sharing arrangements are also a typical source of frictions due to rivalries for leadership of the project. A recent example is the delaying of the multi-billion euro IRIS2 project, notably due to the German claims that the work was not fairly divided between France and Germany³⁰. Further, if this programme – aimed at producing a military satellite system to be used by European armies and spy agencies – was expected to average around €6 billion in costs, the latest figure stated in proposals revolves around €11.4 billion³¹. Besides, intellectual property rights and control of technology are also recurrent sources of complications in defence cooperative projects. By and large, the more participants, the more complex collaborative efforts tend to become. A telling example is the NH-90 military helicopter, which is produced in over 20 different versions³². Countries requesting that their national suppliers be involved in such or such quality in the project is also a factor driving higher costs and delays³³.

To streamline and manage collaboration on the demand side, several institutions have

²⁹ Darnis, J-P., Gasparini, G., Grams, C., Keohane D., Liberti, F., Maulny, J-P., Stumbaum, M. (2007) *Lessons learned from European defence equipment programmes*. European Union Institute for Security Studies. Occasional Paper, Pp. 25.

³⁰ Politico (2024). *EU's rival to Elon Musk's Starlink struggles to take off*. Available at : <https://www.politico.eu/article/eu-iris-satellite-plan-spacex-starlink-elon-musk-military-grade-space-rise-airbus-thales-alenia-space/>

³¹ Politico (2024). *EU's rival to Elon Musk's Starlink struggles to take off*. Available at : <https://www.politico.eu/article/eu-iris-satellite-plan-spacex-starlink-elon-musk-military-grade-space-rise-airbus-thales-alenia-space/>

³² Zandee, D. (2022). *Open strategic autonomy in European defence : what countries must do*. Clingendael. Netherlands Institute of International Relations, pp. 3.

³³ *Ibid*, pp.5.

been established. In the NATO framework, there is the NATO Support and Procurement Agency (NSPA), established in 1958. Then, there is the Organisation Conjointe de Coopération en matière d'Armement (OCCAR), which is the European organisation for the management of cooperative defence equipment projects. Established in 1996, its member states are Belgium, France, Germany, Italy, Spain and the UK. In the EU framework, the European Defence Agency is “ the Agency in the field of defence capabilities development, research, acquisition and armaments »³⁴. Cooperation between these agencies exists and can be beneficial due to an optimised use of their respective strengths and expertise.

At this stage, it is worth reminding that national programmes can obviously involve inefficiencies as well. Just like collaborative projects, they can be burdensome and time-consuming. Mention should also be made that less comprehensive forms of collaboration between countries are also common. A case in point are parallel acquisition processes whereby two or more countries set common specifications and cooperatively negotiate prices and delivery timelines, with the caveat that each country has its own contract and process, proofing the participants from potential delaying incidents and manoeuvres coming from one of their peers³⁵.

Arguably, despite these potential inefficiencies, collaboration remains many times the economically preferable option, especially when it comes to high cost equipment. This latter case is on the rise, given the trend of costs escalation affecting many types of defence equipment. Indeed, the increasing costs and complexity of state-of-the-art capabilities imply that no single member state can afford to develop and produce by themselves the whole range of necessary defence equipment. Furthermore, collaborative programmes also offer tactical and operational benefits ensuring greater interoperability and standardisation of their armed forces.

Notwithstanding the above-mentioned potential costs savings that can arise from collaboration, Member states might prefer to give priority to different (geo)political and industrial imperatives when considering the participation in a collaborative project, with pure economic gains sometimes taking a backseat. For instance, offset policies are frequently used by some countries to involve their companies in multinational projects and thereby stimulate their national industry. This is notably illustrated by the involvement of Dutch defence companies in the production phase of the US F-35 fighter plane. An offset basically means

³⁴ Andersson, J. (2023). *Buying Weapons Together (or not). Joint defence acquisition and parallel arms procurement*. European Union Institute for Security Studies. Brief 2023/7, pp. 6.

³⁵ *Ibid*, pp. 5.

that the prime contractors (here Boeing and Lockheed Martin) agreed to involve Dutch sub-contractors in the development and production of the equipment³⁶. In so doing, the project stimulated the Dutch domestic industry, something that would not have happened if the Netherlands had procured a cheaper available equipment (such as the Gripen planes offered by Saab in 2008) but without involving its industrial base. In addition, offsets frequently include some technology transfers, further benefiting the domestic defence and sometimes even civil industries. Therefore, the additional price paid can in the Dutch case be analysed as pursuing an industrial policy purpose³⁷. More importantly, as detailed later on, geopolitical considerations are not to be downplayed. For a country like the Netherlands, which cannot realistically aspire to autonomy in terms of defence capabilities, forging industrial and security ties with a global “superpower” conveys the advantage of strategic and geopolitical guarantees.

Finally, the increasingly pregnant concerns of alleviating supply chain risks and ensuring security of supply may at times take precedence over the acquisition of the cheapest equipment through competitive bids³⁸. To illustrate, France – in line with its long-time doctrine of national strategic autonomy - has ‘invited’ producers to re-shore some elements of their production to secure comprehensive supply chains domestically. For instance, while French firms previously used to import gun powder from Sweden, Eurengo has recently opened a new powder factory in Bergerac³⁹.

These few preceding remarks already give a glimpse into systemic elements that can constrain at the same time the efficacy of a market-based approach in the defence sector and the prospect of deeper Europeanisation.

3.1.3 In practice, is collaborative procurement such a negligible occurrence?

The fragmented nature of the European armament demand should be nuanced. In practice, there might be more European armaments cooperation than is commonly believed, although to variable degrees of cooperation. If anything, according to a study led by the

³⁶ Meershoek, N. (2021). *The Constraints of Power Structures on EU Integration and Regulation of Military Procurement*. European Papers, pp. 848.

³⁷ Ibid, pp. 849.

³⁸ Mölling, C., Hellmonds, S., Csernaton, R., Martins, B., Racz, A. (2024) *Sovereign, Capable, Innovative, Responsive: Prospects and challenges for EU security and defence policy in the 10th parliamentary term*. Policy Department for External Relations, Directorate General for External Policies of the Union, pp. 18.

³⁹ Bellais, R. (2024). *What are the main drivers of member states' defence procurement practices ? The French case*. Ares, Comment 98, pp. 6. <https://www.iris-france.org/wp-content/uploads/2024/06/ARES-98-Comment.pdf>

European Union Institute for Security Studies (EUISS)⁴⁰, there would be no scarcity of European defence cooperation. One stated reason for the underestimation of the amount of collaborative projects being that member states do not systematically publicly report data on arms procurement. Another consequence of this lack of precise data is that the extent to which member states have increased their collaboration on European procurement can hardly be properly assessed. The fact remains that several collaborative defence programmes take place at the EU level or between EU member states and foreign partners. The EUISS study actually identified more than 200 European defence partnerships. One caveat is that these projects do not only take place between EU member states but also involve allies such as the US or Norway⁴¹. Be that as it may, recent figures from the European Commission severely raise objections to the EUISS' narrative. Between 2021 and 2022, the procurement of new equipment increased by 7%. Yet, only 18% of the whole defence equipment expenditures was spent in the context of EU collaborative procurement programmes in 2022⁴². The recent European Defence Industrial Strategy (EDIS)⁴³ sets the target that European member states should procure at least 40% of defence equipment in a collaborative manner by 2030. The prospect of such benchmark being respected can strongly be questioned in view of its non-binding nature and considering past experiences in this regard. As a matter of fact, a 35% non-binding target already existed since 2007. According to the European Defence Agency, the closest European countries have come to reaching this benchmark was in 2021 when they allocated €7.9 billion to collaborative acquisition. Even so, €7 billion were still lacking in order to reach the 35% benchmark⁴⁴.

3.2 Supply side : the European Defence Industrial Base

3.2.1 Overview of the European defence industrial landscape

The concept of defence industrial and technological base (DTIB) basically includes actors involved on the supply side of defence equipment production such as research and development centers, arms-producing companies and their suppliers. The European Defence

⁴⁰ Andersson, J. (2023). *Buying Weapons Together (or not). Joint defence acquisition and parallel arms procurement*. European Union Institute for Security Studies. Brief 2023/7.

⁴¹ Ibid, pp.6.

⁴² European Commission and High Representative of the Union for Foreign Affairs and Security Policy (2024), JOIN 2024, 10 Final, *Joint communication to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the regions. A new European Defence Industrial Strategy : Achieving EU readiness through a responsive and resilient European Defence Industry*. European Commission. Pp. 8

⁴³ Ibid, pp. 10.

⁴⁴ European Defence Agency (2022) “*Defence Data 2020-2021: Key Findings and Analysis*”, European Defence Agency. Pp. 15. See: <https://eda.europa.eu/docs/default-source/brochures/eda---defence-data-2021---web---final.pdf>

Industrial and Technological Base (EDTIB) is marked by the heterogeneity of the national industries it comprises. They vary in size, competitiveness, and the array of products they provide. The lack of transparency as regards information-sharing in defence matters constitutes a major impediment to the assessment and mapping of the capabilities and size of the EDTIB. Consequently, informed European decision-making in the defence sector is a lingering issue⁴⁵.

The EDTIB is made out of a few large multinational companies, many mid-caps and more than 2000 small and medium-sized (SMEs) enterprises⁴⁶. According to the European Defence Agency, the turnover of the entire EDTIB in 2021 was around €84 billion. Moreover, the industry employs around 196 000 highly skilled workers and more indirectly around 315 000 workers, that is around 500 000 people overall⁴⁷.

Major players like France, Germany, Italy, Spain or the United Kingdom have the upper hand over the European defence industrial landscape. Their domestic companies possess strong and advanced industrial capacities able to furnish the quasi-totality of defence equipment across a wide range of sectors such as aerospace, naval, land systems, missile and space. Further, they produce the most technologically advanced and competitive products and are home to the major pan-European defence companies⁴⁸. Indeed, 97 out of Europe's 100 leading defence companies have their headquarters in one of these countries⁴⁹. Typically, these Western European countries are also involved in the biggest European joint development projects where their domestic industries usually assume leadership functions. Four out of the top eight arms exporting states are France, Spain, Italy and Germany, according to the Stockholm International Peace Research Institute⁵⁰.

In countries like the Netherlands, Sweden, Denmark, Greece or Norway, there are

⁴⁵ Mölling, C., Hellmonds, S., Csernaton, R., Martins, B., Racz, A. (2024) *Sovereign, Capable, Innovative, Responsive : Prospects and challenges for EU security and defence policy in the 10th parliamentary term*. Policy Department for External Relations, Directorate General for External Policies of the Union, pp. 16.

⁴⁶ Clapp, S. (2023). *Reinforcing the European defence industry*. European Parliament Research Service. Pp. 2.

⁴⁷ European Commission and High Representative of the Union for Foreign Affairs and Security Policy (2024), JOIN 2024, 10 Final, *Joint communication to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the regions. A new European Defence Industrial Strategy : Achieving EU readiness through a responsive and resilient European Defence Industry*. European Commission. Pp. 4.

⁴⁸ Mölling, C., Helmonds, S. (2023). *Security, Industry, and the Lost European Vision How Russia's War in Ukraine Is Changing the European Defense Technological and Industrial Base*. German Council on Foreign Relations. DGAP Report, pp. 7.

⁴⁹ Direction Générale L'armement (2024). *International Defence Companies Notebook, 2024 Edition*. See : <https://www.defense.gouv.fr/sites/default/files/dga/International%20Defence%20Companies%20notebook%2024%20edition.pdf>

⁵⁰ Wezeman, P., Gadon, J., Wezeman, S. (2023). *Trends in International Arms Transfers, 2022*. SIPRI. https://www.sipri.org/sites/default/files/2023-03/2303_at_fact_sheet_2022_v2.pdf

mainly mid-sized defence industries, frequently involved in European programmes for complex weapon systems, although not leading them⁵¹. Two out of the top 100 companies are from Scandinavia (Saab from Sweden and Kongsberg from Norway)⁵².

In the Baltic, central and eastern European countries, the defence industries are usually tilted towards less technology-intensive equipment such as ammunitions, light weapons and components production and maintenance. Some of their defence firms specialise and are competitive in niche domains, but their companies typically lag behind technologically and are unable to compete on the most technologically advanced products with the largest producing nations. In the aftermath of the Cold War, these former Warsaw Pact countries' defence industrial bases went through significant overhauls. A massive privatisations wave of state-owned defence industries took place. In addition, the plummeting demand for defence products that characterised this period inevitably shrunk their defence industrial base⁵³. In the 'region', Poland stands out as having the most diversified defence industrial base, due to the wide array of capabilities produced by its state-owned PGZ group. Additionally, major Western European and US firms have set subsidiaries in Poland, such as Lockheed (US), Leonardo (UK), Airbus and Thales (France)⁵⁴. Czech Republic also hosts a relatively significant number of defence SMEs.

To gain some perspective, drawing parallels with the United States (US) defence industrial base might not be a worthless endeavor. If 17 of the 100 world leading defence companies have their headquarters in the EU, the US counts 46. Further, the top five world leading defence companies are all US-based. In 2021, their combined turnover revolved around €193 billion, that is more than twice as much as the whole European defence industry⁵⁵. China has seven of its firms appearing in the top 100 (2021) while Russia only has one. These figures should nevertheless be considered with caution, due to the lack of transparency that characterises the defence sector.

As we will further develop, the discrepancies in size and expertise between the

⁵¹ Mölling, C., Helmonds, S. (2023). *Security, Industry, and the Lost European Vision How Russia's War in Ukraine Is Changing the European Defense Technological and Industrial Base*. German Council on Foreign Relations. DGAP Report, pp. 7.

⁵² Mölling, C., Helmonds, S., Csernaton, R., Martins, B., Racz, A. (2024) *Sovereign, Capable, Innovative, Responsive : Prospects and challenges for EU security and defence policy in the 10th parliamentary term*. Policy Department for External Relations, Directorate General for External Policies of the Union, pp. 8.

⁵³ Mölling, C., Helmonds, S. (2023). *Security, Industry, and the Lost European Vision How Russia's War in Ukraine Is Changing the European Defense Technological and Industrial Base*. German Council on Foreign Relations. DGAP Report, pp. 7.

⁵⁴ Béraud-Sudreau, L., Scarazzato, L. (2023). *Beyond Fragmentation ? Mapping the European Defence Industry in an era of strategic flux*. CSDS In-depth, n°2023/07, pp. 8.

⁵⁵ Clapp, S. (2023). *Reinforcing the European defence industry*. European Parliament Research Service. PE 749.805, pp. 2.

different European national defence technological and industrial bases, along with other factors, induce different perspectives on industrial policy and international cooperation.

3.2.2 Cross-border defence industrial ties

A complete overview of the European defence industrial base requires taking into account the fact that the largest firms of the large Western European states hold significant foreign direct investments across Europe. For example, in 2020, the foreign subsidiaries of the French firm Thales were among the top five biggest defence firms in ten other European countries than France⁵⁶. For smaller Western countries like Austria, the Netherlands or Belgium, these cross-border industrial ties are especially relevant. In Belgium, for instance, three of the biggest defence firms are actually foreign-owned subsidiaries. Regarding Central and Eastern Europe, direct foreign defence investments are rather limited. Poland once again stands out with three of its five largest defence firms being the subsidiaries of Leonardo, Airbus and Thales. In addition, it also appears that Central and Eastern Europe's arms industries have a limited incorporation within Western European supply chains and defence market, although they welcome a lot of subsidiaries from Western Europe⁵⁷. This notably derives from the fact that when entering NATO, most of former Warsaw Pact countries' companies were unable to adapt their defence production to NATO standards, de facto keeping them away from most European supply chains⁵⁸. It is important to mention that some countries such as Estonia possess dual-use capabilities that enable them to integrate into cooperative programmes and supply chains⁵⁹. Undeniably, varying degrees of integration represent a challenging element when considering the further Europeanisation of the defence industry.⁶⁰

On the other hand, a proper European defence industrial policy should also make the

⁵⁶ Béraud-Sudreau L. (2020) *Mapping the International Presence of the World's Largest Arms Companies*. SIPRI Insights on Peace and Security. <https://www.sipri.org/publications/2020/sipri-insights-peace-and-security/mapping-international-presence-worlds-largest-arms-companies>.

⁵⁷ Mölling, C., Hellmonds, S., Csernaton, R., Martins, B., Racz, A. (2024) *Sovereign, Capable, Innovative, Responsive : Prospects and challenges for EU security and defence policy in the 10th parliamentary term*. Policy Department for External Relations, Directorate General for External Policies of the Union, pp. 8.

⁵⁸ Mölling, C., Helmonds, S. (2023). *Security, Industry, and the Lost European Vision How Russia's War in Ukraine Is Changing the European Defense Technological and Industrial Base*. German Council on Foreign Relations. DGAP Report, pp. 7.

⁵⁹ Darnis, J-P., Gasparini, G., Grams, C., Keohane D., Liberti, F., Maulny, J-P., Stumbaum, M. (2007) *Lessons learned from European defence equipment programmes*. European Union Institute for Security Studies. Occasional Paper, Pp. 26.

⁶⁰ Béraud-Sudreau, L., Scarazzato, L. (2023). *Beyond Fragmentation ? Mapping the European Defence Industry in an era of strategic flux*. CSDS In-depth, n°2023/07, pp. 12.

most out of the different comparative advantages of countries and firms. In this regard, SMEs play a pivotal role, in particular by providing disruptive technologies and innovation in the defence industrial realm. The difficulty of cross-border access for European SMEs is an identified issue that notably stems from the lack of competitive tenders for sub-contracts by bigger industrial member states in their procurements⁶¹. The Commission seems to acknowledge this. Inter alia, European Defence Fund's (EDF) funding is leveraged to incentivise and stimulate cross-border cooperation involving SMEs. Indeed, one of the award criteria of the EDF programme is that there be cross-border cooperation involving SMEs. Additionally, financial bonuses may be granted depending on the level of participation of SMEs in the given project⁶². Beyond SMEs, the EDF also promotes cross-border collaboration by making financial incentives contingent upon the participation of at least three member states and three industries located in different EU countries⁶³. This reflects the pivotal stakes of enhancing the openness of supply chains when considering the larger goal of a more effective, competitive and self-resilient European defence equipment market. Other recent developments such as the EU Defence Innovation Scheme (EUDIS) or the Defence Equity Facility also illustrate the recognition of SMEs' value within the EDTIB.

3.2.3 A fragmented EDTIB.

In the defence markets, national governments occupy a monopsony position. That is, they are typically the only customers. In the EU, there is a largely insufficient coordination of demand and pooling of resources pertaining to defence products. As it happens, demand is considerably structured on a national basis through national programming⁶⁴. Unsurprisingly, the outcome is that the supply side is marked by a high level of fragmentation. Indeed,

⁶¹ Mölling, C., Hellmonds, S., Csernaton, R., Martins, B., Racz, A. (2024) *Sovereign, Capable, Innovative, Responsive : Prospects and challenges for EU security and defence policy in the 10th parliamentary term*. Policy Department for External Relations, Directorate General for External Policies of the Union, pp. 9.

⁶² European Commission and High Representative of the Union for Foreign Affairs and Security Policy (2024), JOIN 2024, 10 Final, *Joint communication to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the regions. A new European Defence Industrial Strategy : Achieving EU readiness through a responsive and resilient European Defence Industry*. European Commission. Pp. 19.

⁶³ Zandee, D. (2022). *Open strategic autonomy in European defence : what countries must do*. Clingendael. Netherlands Institute of International Relations, pp. 2.

⁶⁴ European Commission and High Representative of the Union for Foreign Affairs and Security Policy (2024), JOIN 2024, 10 Final, *Joint communication to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the regions. A new European Defence Industrial Strategy : Achieving EU readiness through a responsive and resilient European Defence Industry*. European Commission. Pp. 5.

defence companies remain for the most part organised along national borders, with a myriad of small defence markets instead of a single coherent and integrated one. In Europe, the rearmament effort taking place following the Russian war of aggression on Ukraine revived the long-time advocacy of many experts for more European cooperation on jointly manufacturing and procuring weapons. One aspect of this narrative is that more industrial consolidations should take place through national or transnational industrial mergers and acquisitions⁶⁵. The most stated and obvious rationale is the potential positive scale effect arising from a further consolidated defence industrial base involving fewer producers, among which some “European champions” rather than multiple national ones. The argument goes that such mergers would be a pivotal step towards a stronger and more competitive EDTIB, notably thanks to higher production volumes and the avoidance of costly duplications and multiplication of similar defence systems. According to the European Commission, the fragmentation of the EDTIB “greatly reduces its ability to improve its competitiveness through pooling of R&D and economies of scale in production”⁶⁶.

In a context where the European military industrial landscape stays fragmented mainly around large national (as opposed to Europeanised) companies surrounded by national small-size players⁶⁷, the intra-industry index remains low, meaning that bilateral trade flows are quite scarce⁶⁸. Yet, the point has also been made⁶⁹ in an EUISS report that the European defence industry would actually be less fragmented than commonly expected and that the number of key defence devices being produced in the EU is actually quite similar to that of the US (except for naval shipbuilding). Contrastingly, an European Parliament report⁷⁰ underscores an abundance of costly duplications, with for instance 17 different types of main battle tanks manufactured, procured and used in Europe, against only one in the US (the M1 Abrams). Another compelling illustration is the development of a sixth generation fighter jet, which is the most costly European defence project, estimated at more than €100 billion.

⁶⁵ Andersson, J. (2023). *Building Weapons Together (Or Not). How to strengthen the European defence industry*. European Union Institute for Security Studies. Brief 2023/20, pp. 2.

⁶⁶ Clapp, S. (2023). *Reinforcing the European defence industry*. European Parliament Research Service. PE 749.805, pp. 3.

⁶⁷ Schnitzler, G. (2023). *EDIRPA/EDIP : Risks and opportunities of future joint procurement incentives for the European Defence Market*. ARES, Policy Paper 81, pp. 4.

⁶⁸ European Parliament Research Service. (2023). *Increasing European added value in an age of global challenges. Mapping the cost of non-Europe (2022-2023)*, Brussels, European Parliament. DOI: 10.2861/144, pp. 312.

⁶⁹ Andersson, J. (2023). *Building Weapons Together (Or Not). How to strengthen the European defence industry*. European Union Institute for Security Studies. Brief 2023/20, pp. 2.

⁷⁰ Clapp, S. (2023). *Reinforcing the European defence industry*. European Parliament Research Service. PE 749.805, pp. 3.

Instead of having one development programme, two programmes are actually taking place⁷¹ simultaneously. These kinds of duplicated efforts also have the adverse effect of complexifying transnational military cooperation and interoperability. Furthermore, as will be developed later on, domestic considerations such as diverging national requirements and competing industrial and political interests induce member states to favor national over European programming. Even when international or European collaboration does take place, these national considerations and interests too often act as a hindrance to further rationalisation of the EDTIB⁷² through the coordination of defence planning. A case in point is the fact that transnational projects in the defence sector often tend to lead to “multi-domestic” consortia rather than multinational companies⁷³. Notably, offsets often imply fragmentation due to the inclusion of various domestic companies within the supply chains, typically more on the basis of national industrial interests than pure economic efficiency considerations⁷⁴.

3.2.4 Supply-side consolidation of the European defence industry: preferable in any case?

In light of the above, the question may be asked whether a reduced number of suppliers in the European defence industrial base is in any circumstance something to wish for. Following the end of the Cold War, a wave of mergers and acquisitions took place within the US defence industry. This consolidation was ordered by the Under Secretary of Defence William Perry. The US defence industrial base saw the number of its suppliers shrink in a significant manner. The objective was to anticipate concomitantly a decline in military budget (due to the end of the Cold War) and the “escalation” of the cost of defence equipment given the advances of technology⁷⁵. However, in a 2022 report, the Pentagon outlined the downsides of having too few suppliers. “The lack of diversity of suppliers decreases the kind of competition that spurs innovation and lowers prices paid for defence equipment by the taxpayer”⁷⁶. The Pentagon emphasises the essential character of upholding competition within

⁷¹ Clapp, S. (2023). *Reinforcing the European defence industry*. European Parliament Research Service. Pp. 3.

⁷² Andersson, J. (2023). *Building Weapons Together (Or Not). How to strengthen the European defence industry*. European Union Institute for Security Studies. Brief 2023/20, pp. 4.

⁷³ Meershoek, N. (2021). *The Constraints of Power Structures on EU Integration and Regulation of Military Procurement*. European Papers, pp. 862.

⁷⁴ Ibid, pp. 862.

⁷⁵ Faure, S. (2022). *EU defence industrial policy : from market-making to market-correcting*. In : *EU industrial policy in the multipolar economy*. Leuven Global Governance. Edward Elgar Publishing, pp. 386.

⁷⁶ US Department of Defense Report. (2022) *State of Competition within the Defense Industrial Base*. Office of

the defence industry in order to reap benefits such as improved costs, schedule, performance and innovation, all these features participating to the competitiveness of any defence industry. By the same token, it has been argued that competitiveness doesn't necessarily derive from consolidation, and that competition is the prevalent driving force of competitiveness⁷⁷.

Furthermore, another important criticism that can reasonably be levelled at consolidation is the reduced ability to ramp up production in war times. If the rationalisation (merger or exit of the market) of production capacities might reduce overcapacity, trigger economies of scale and gather technological knowledge, a limited number of producers may also potentially involve strategic and security implications. Finally, consolidation of some industries implies a stronger market power for the merged entities. Therefore, there is a risk that increased consolidation reduces competition⁷⁸ and thus potentially leads to negative outcomes for the market. In this respect, it is essential that further consolidation does not excessively affect small or mid-sized niche capability companies.

3.2.5 What market approach to favor?

Traditionally, the Commission has positioned itself along the line of a market-driven liberal approach, favoring competition policy over mergers as a means to pursue economic integration⁷⁹. Competitive biddings within liberalised and transparent public procurement processes (demand side) are meant to be a central tool of such integration effort of the defence industrial base (supply side). The Commission has previously argued that if Member States would collaborate more closely and refrain from too often buying domestically, the supply side (EDTIB) would be incentivised to cooperate or even integrate to match the demand, thereby enabling positive scale effects⁸⁰. In reality, several political and economic considerations have significantly constrained the efficiency of such a market-based approach. Notably, diverging national requirements, design stipulations and industrial interests make it complex and burdensome to agree on large pan-European programmes properly concentrating

the Under Secretary of Defense for Acquisition and Sustainment, February 2022, pp.1. (<https://media.defense.gov/2022/Feb/15/2002939087/-1/-1/1/STATE-OF-COMPETITION-WITHIN-THEDEFENSE-INDUSTRIAL-BASE.PDF>).

⁷⁷ Andersson, J. (2023). *Building Weapons Together (Or Not). How to strengthen the European defence industry*. European Union Institute for Security Studies. Brief 2023/20, pp. 4.

⁷⁸ Darnis, J-P., Gasparini, G., Grams, C., Keohane D., Liberti, F., Maulny, J-P., Stumbaum, M. (2007) *Lessons learned from European defence equipment programmes*. European Union Institute for Security Studies. Occasional Paper, Pp. 26.

⁷⁹ Meershoek, N. (2021). *The Constraints of Power Structures on EU Integration and Regulation of Military Procurement*. European Papers, pp. 862.

⁸⁰ Ibid, pp. 860.

demand. In addition, Member States very often invoke the “armament exception” to circumvent the transparency and competition obligations imposed by the two 2009 European Directives regarding access to defence procurements. All of that notably translates into a lack of predictability of demand, which further constrains the supply side of the EDTIB in its ability and willingness to create synergies. Indeed, European arms producers traditionally refrain from producing equipment until orders have been issued⁸¹.

In a climate of growing geopolitical tensions, the EU has taken a geopolitical turn, illustrated notably by the strategic autonomy narrative or by the return of industrial policy at the forefront of the policy agenda. Given the current context where global interdependencies increasingly appear as vulnerabilities, the EU moved toward a more interventionist industrial policy which constitutes a paradigm shift away from traditional market mechanisms. To illustrate this change in governance in the defence sector: if the two 2009 Directives embody a liberal approach based on the precepts of openness and competition, the 2021 EDF aims at shaping the competitiveness and self-reliance of the EDTIB through the use of subsidies and financial incentives⁸² in a view to foster the cross-border structuring of defence supply chains. The EDF is also a big step for the EU in terms of defence industrial policy considering that it invests into research and development to boost innovation. Moreover, administrative coordination and regulatory policies are two other important tools of the EU’s interventionist attitude⁸³. Another illustration of the new paradigm comes from the recent EDIS recently presented by the European Commission, which proposes the maintenance of residual production capacities or “ever-warm” capacities⁸⁴ to be able to swiftly react if and when necessary. Manifestly, this type of policy is more driven by a strategic logic than an economic one. At this stage, one caveat must be made and relates to the inherent limitations of such a European interventionist approach, in light of the dissensus regarding the role of the EU in defence matters as well as the limited funding available.

All in all, a major challenge for the EU is to strike the right balance between its thrust for a more liberalised defence market and the need to put together an efficient industrial

⁸¹ Clapp, S. (2023). *Reinforcing the European defence industry*. European Parliament Research Service. Pp. 5.

⁸² Hoeffler, C. (2023). *Arming Fortress Europe ? Spaces and Instruments of Economic Patriotism in EU Armament Policy*. Politics and Governance (ISSN : 2138-2463) 2023, Volume 11, Issue 4, pp. 156.

⁸³ McNamara, K. (2023). *Transforming Europe ? The EU’s industrial policy and geopolitical turn*. Journal of European Public Policy, 31: 9, 2371-2396, pp. 3.

⁸⁴ European Commission and High Representative of the Union for Foreign Affairs and Security Policy (2024), JOIN 2024, 10 Final, *Joint communication to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the regions. A new European Defence Industrial Strategy : Achieving EU readiness through a responsive and resilient European Defence Industry*. European Commission. Pp. 17.

policy⁸⁵. The difficulty of such endeavor is even greater given the specific nature of the defence sector, where competing political and industrial interests of the various stakeholders have a considerable weight in decision-making.

3.2.6 War in Ukraine and necessary ramp-up in defence production capacities: capability and industrial gaps

The new strategic reality owing to the return of high-intensity warfare on European soil has exposed several vulnerabilities of the European armament production capacities and dependences on global supply chains. Manufacturers have been unable to adequately respond to the surge in demand for defence materiel, mainly as regards munitions and land systems. As a reminder, deliveries of equipment to Ukraine partly explain the magnitude of the demand. A considerable part of this demand ended up benefiting non-EU suppliers such as the United States while also allowing a greater penetration of the EU defence market by emerging defence players⁸⁶ like South Korea or Israël. A 2023 study by the ARES Group⁸⁷ revealed that from a total of €75 billion spent by European member states between June 2022 and June 2023, 78% was procured from non-EU suppliers. Out of these purchases, 80% came from the US, 13% from South Korea, 3% from Israel and the United Kingdom together⁸⁸.

Used to deal with a relatively low demand, European manufacturers suddenly had to cope with a transition from a peacetime production level to a quasi-wartime one. This notably resulted in a strong price inflation. Furthermore, while European member states had promised one million rounds of ammunitions to Ukraine within 12 months, only half of it was actually delivered in due time⁸⁹. As recognised in the Joint Communication on Defence Investment Gaps of 18 May 2022, the EU experienced an accumulation of capability gaps in the collective military inventories, along with industrial production capacity shortfalls⁹⁰. The

⁸⁵ Fiott, D. (2024). *In Whose Interests? Regulating Europe's Defence Industry and the Politics of Exemptions*. CSDS Policy Brief, 3/2024.

⁸⁶ Maulny, J-P. (2023). *The impact of the war in Ukraine on the European Defence Market*. Ares Group, IRIS, Policy Paper 2023/09, pp. 17.

⁸⁷ Ibid.

⁸⁸ Ibid, pp. 15.

⁸⁹ Grand, C. (2024). *Defending Europe with less America*. European Council on Foreign Relations, Policy brief ECFR/545, pp. 7.

⁹⁰ European Commission (2022) 24 final, *Joint Communication on the Defence Investment Gaps Analysis and Way Forward*. European Commission, pp.2

main cause of such state of affairs is the overall⁹¹ significant under-investment in defence prevailing since the end of the Cold War during the decades of “peace dividends”. Obviously, the lack of coordination of those investments made the matter worse. European defence industries have also long been focused more on lucrative exports than on domestic demand. Furthermore, the inability to ramp-up and cope with a sudden surge in demand was only exacerbated by the relative consolidation of the defence industrial architecture having taken place in the 1990s, with firms either merging or exiting the market⁹². In the urgency of a rapid ramp-up to support Ukraine and to refurbish national inventories and capabilities, the EU and its member states swiftly reacted by launching initiatives such as the Defence Joint Procurement Task Force, the Instrument for the reinforcement of the European defence industry through common procurement (EDIRPA), the reconditioning of the European Peace Facility (EPF) and the Regulation on supporting ammunition production (ASAP). It is worth mentioning that these European efforts to scale-up defence-industrial production came up against the reluctance of some major defence producers to invest in ramping-up production. One notable reason is the unpredictability of both demand and governmental long-term financing. This uncertainty has triggered fears of potential overcapacity conveying the risk of diminished profits⁹³. Noteworthy also is the fact that European member states massively turned to foreign producers to satisfy their capability needs.

⁹¹ In this regard, countries differ in their profiles. France, for instance, had a relatively small defence investment deficit compared to other European countries. On the matter, see : <https://www.iris-france.org/wp-content/uploads/2024/06/ARES-98-Comment.pdf>

⁹² European Commission (2023). *Consultation on the new European Defence Industrial Strategy. Issue Paper 1.*

⁹³ Mölling, C., Helmonds, S. (2023). *Security, Industry, and the Lost European Vision How Russia's War in Ukraine Is Changing the European Defense Technological and Industrial Base.* German Council on Foreign Relations. DGAP Report, pp. 8.

4 Structural challenges to further defence industrial integration

The European Defence Industrial Strategy (EDIS) proposed in March 2024 by the European Commission is an important step towards more Europe in defence industrial matters. However, negotiations will undoubtedly prove lengthy and difficult. Indeed, given the sensitive nature of the defence industry, each member state will be willing to carefully tackle the issue with a view to get the most out of the future overhaul of the defence industrial policy. Getting member states to sign off on a common defence industrial strategy will necessarily entail overcoming several political and economic challenges at the roots of the low-level consensus that characterises Europe's defence industrial integration.

4.1 National economic and industrial interests

The current thrust for more Europe in defence-industrial matters must be weighed against the implications of the fact that security and defence policy is a fundamental aspect of national sovereignty and remains under the purview of member states through the Council of the EU. If these countries' inclinations are all genuinely influenced by security concerns, none of them will likely lose sight of the economic and industrial gains or losses that could arise from further Europeanisation of defence industrial matters. European governments' defence-related policies and attitudes tend to hinge on the nature of the relationship they entertain with their military-industrial players. Historically, governments' protection of their defence industries has been a recurring impediment in cooperative programmes⁹⁴. Given the previously described heterogenous profiles of the national defence industries composing the EDTIB, government-industry relations differ between European states. Hence, governments have dissimilar incentives and constraints and pursue disparate strategies, which typically complexifies decision-making. Pursuant to an EUISS report, the typical pattern would be that the lower the level of affiliation between the military and the domestic defence industry, the more a country will tend to favor competition and liberalisation. Conversely, countries might adopt more protectionist stances in negotiations when they have an especially close relationship with national defence firms. In any case, defence industries are closely linked to their respective governments, which are their main customers. The depth of such connection

⁹⁴ Darnis, J-P., Gasparini, G., Grams, C., Keohane D., Liberti, F., Maulny, J-P., Stumbaum, M. (2007) *Lessons learned from European defence equipment programmes*. European Union Institute for Security Studies. Occasional Paper, Pp. 3.

also tends to vary according to the considered defence sector. Beyond the government-industry relations, discrepancies in domestic industrial portfolios and positions in supply chains also influence the respective national perspectives on defence industrial policy. In light of the above, attitudes span over a wide spectrum and countries should therefore be differentiated. For simplicity purposes and accepting a certain degree of generalisation, European countries can be broadly gathered into different groupings.

First of all, there are the « big » states which possess autonomous and advanced national defence industries, namely France, Germany, Italy, Spain and the United Kingdom (UK). They tend to adopt what a recent German Council on Foreign Relations (DGAP) report⁹⁵ coined an « industry-driven approach ». When considering industrial policy or military procurement matters, their priority is usually to involve their domestic companies in projects and more generally to favor their defence industries' interests, even when it ultimately entails less optimal operational capabilities and readiness. Historically, France and Italy were the countries entertaining the closest relationship with their respective national defence champions, sometimes even holding ownership into some of them⁹⁶. With time however, the UK and Germany moved towards a comparable kind of relationship. Institutionally, these core countries usually favor intergovernmental governance. Indeed, they have traditionally defended a « sovereigntist » policy agenda⁹⁷ where states are meant to be the only actors competent to regulate defence matters. Therefore, they have traditionally been de facto opposed to the « liberal push » of the European Commission for a liberalised internal defence market based on competition precepts. They would rather have an intergovernmental setting which enables them to maintain a strong grip on defence matters and ensure that the industrial interests of their producers are served. Yet, over the last decade, most EU member states have come to adopt a less protectionist attitude and a more favorable stance towards an increased degree of European governance in defence. This renewed approach is notably due to the advocacy of large member states and of personalities such as Emmanuel Macron or Angela Merkel, notably following the 2016 Brexit referendum⁹⁸. Furthermore, large member states generally back initiatives such as the EDF or PESCO which are centered around

⁹⁵ Mölling, C., Helmonds, S. (2023). *Security, Industry, and the Lost European Vision How Russia's War in Ukraine Is Changing the European Defense Technological and Industrial Base*. German Council on Foreign Relations. DGAP Report.

⁹⁶ Darnis, J-P., Gasparini, G., Grams, C., Keohane D., Liberti, F., Maulny, J-P., Stumbaum, M. (2007) *Lessons learned from European defence equipment programmes*. European Union Institute for Security Studies. Occasional Paper, Pp. 24.

⁹⁷ Faure, S. (2022). *EU defence industrial policy : from market-making to market-correcting*. In : *EU industrial policy in the multipolar economy*. Leuven Global Governance. Edward Elgar Publishing, pp. 387.

⁹⁸ Csernaton, R. (2021). *The EU's Defense Ambitions : Understanding the Emergence of a European Defense Technological and Industrial Complex*. Carnegie Endowment for International Peace, Working Paper. Pp. 19.

research and development projects where their domestic industrial players can occupy prime positions. Naturally, they also take interest in the financial incentives that come with such projects. Some of them advocate for moderation in buying non-European⁹⁹. In the case of France, beyond the economic and industrial benefits that the French defence industry can reap from more European collaboration, there is the strategic ambition of more European sovereignty, mainly vis-à-vis non-European suppliers (e.g. USA, South Korea, Israel)¹⁰⁰. As it happens, recent off-the-shelf purchases by Germany triggered some tensions in the Franco-German relationship¹⁰¹. Furthermore, large producers countries have traditionally been making extensive use of the « armament exception » (which enables states to derogate from the rules of the internal market when it comes to defence equipment contracts) in order to maintain the prerogative of regulating defence collaborative programmes and thereby steer these in an industrially and economically-advantageous way¹⁰², notably in terms of the preservation of employment in the defence sector, security of supply concerns and the upholding of technological ownership within national borders. Nevertheless, as defence equipment costs and complexity escalate, nationally procuring the entire range of capabilities has become out of reach, causing a greater appeal for collaboration. In that regard and still in a view to help domestic companies, big member states are likely to favor European cooperative programmes over imports. Naturally, as previously described, economic and industrial interests typically reemerge within cooperative projects and tend to hamper their efficacy. Despite the broad common trends above-described, it remains hard to figure out how major European defence industrial nations will manage to unite over an integration strategy, considering that it will necessarily entail sacrifices for their respective industries.

On the whole, countries with a mid-sized industry like the Netherlands, Greece or Sweden often face the need to cooperate in order to get their domestic companies involved in international projects. Indeed, doing so is a critical means to foster their defence industrial base. Consequently, like the large defence producers states, they have a tendency to adopt an « industry-driven » approach and prioritise the interests of their producers, notably through the use of offsets.

Finally, Central and Eastern European states tend to follow a different approach,

⁹⁹ Mölling, C., Helmonds, S. (2023). *Security, Industry, and the Lost European Vision How Russia's War in Ukraine Is Changing the European Defense Technological and Industrial Base*. German Council on Foreign Relations. DGAP Report, pp. 8.

¹⁰⁰ Ibid, pp. 17

¹⁰¹ Ibid, pp. 17.

¹⁰² Faure, S. (2022). *EU defence industrial policy : from market-making to market-correcting*. In : *EU industrial policy in the multipolar economy*. Leuven Global Governance. Edward Elgar Publishing, pp. 389.

coined « capability-driven approach » in a DGAP report¹⁰³. In the main, their first priority is of a strategic rather than industrial nature. There are two main reasons that explain this state of affairs. First, they must deal with greater security concerns due to their geographical situation. Indeed, being physically closer to Russia prompts them to emphasise operational readiness and the development of resilient military capabilities. This is notably reflected in the fact that Eastern European countries are the ones having increased their defence spending the most following Ukraine's invasion. For instance, Poland's defence budget increased by 46% in real terms from 2022 to 2023. Second, their defence industrial bases are seldom able to significantly partake in and benefit from European projects or insert themselves in cross-border defence supply chains¹⁰⁴. Nevertheless, the particular attention given to capability acquisition doesn't preclude them from trying to support their respective domestic defence industrial base. Indeed, they still try to get involved in industrial partnerships and bring contracts and opportunities to their domestic firms. However, they tend to prefer to collaborate with third-countries like the US or South Korea and import equipment instead of cooperating on a European level¹⁰⁵. The major reason is that it is oftentimes faster, less costly and less burdensome. Besides, their industries are often quite unlikely to benefit much from European projects anyways.

In a word, national defence industries all occupy a special place within their state apparatus and typically endeavor to have their interests safeguarded and promoted, which can in many cases come at loggerheads with further European defence integration. To enhance government-to-industry concertation at the European level, the EDIS wishes to establish a European Defence Industry Group that would meet in sector-specific configurations and consult with the Defence Industrial Readiness Board (which should handle joint programming and procurement functions)¹⁰⁶.

In contrast, there have been forces advocating more European military-industrial solidarity, going back as far as the 1970s. Pioneer in this regard was Belgian prime minister

¹⁰³ Mölling, C., Helmonds, S. (2023). *Security, Industry, and the Lost European Vision How Russia's War in Ukraine Is Changing the European Defense Technological and Industrial Base*. German Council on Foreign Relations. DGAP Report.

¹⁰⁴ Mölling, C., Helmonds, S. (2023). *Security, Industry, and the Lost European Vision How Russia's War in Ukraine Is Changing the European Defense Technological and Industrial Base*. German Council on Foreign Relations. DGAP Report, pp. 8.

¹⁰⁵ Ibid., pp. 8.

¹⁰⁶ European Commission and High Representative of the Union for Foreign Affairs and Security Policy (2024), JOIN 2024, 10 Final, *Joint communication to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the regions. A new European Defence Industrial Strategy : Achieving EU readiness through a responsive and resilient European Defence Industry*. European Commission. Pp. 8

Leo Tindemans who emphasised the need for a common industrial policy on manufacturing defence equipment. Tindemans' recommendations fostered the emergence of a European vision of defence shared by different stakeholders. A case in point is the creation in 1979 of the Kangaroo Group. The group gathers influential business and defense industrial actors, academics, MEPs, Commission and Council representatives who are in favor of more cohesion in European projects. Nowadays, the Kangaroo Group notably includes representatives from sizeable European players such as the Safran Group, MBDA or Airbus¹⁰⁷. Two other groups of interests worth mentioning are the Group of Personalities on Security Research and the European Security Research Advisory Board. The existence of such public-private interests groups has undoubtedly played a part in the progressive emergence of the European Commission as a defence actor. Further, they remain forces to be reckoned with as one considers the ongoing evolution of the European defence industrial policy. Important as well is to remember that the national and industrial rivalries can also exist among the stakeholders present within such groups.

4.2 Financial challenges

4.2.1 How can national governments afford higher defence spending in the long-run given the constraints weighing on their public finance?

In a context of scarce financial resources, European governments need to find sustainable ways to achieve higher levels of defence spending. The deteriorating security environment, combined with a likely return of Donald Trump in the White House puts additional pressure on European states not only to reinforce their own military capabilities but also to increase their support to Ukraine in its ongoing conflict with Russia. What is more, other key imminent challenges also require important levels of public funding, not least the green and digital transitions. Consequently, European governments need to find fiscal space to finance these different endeavors. In addition, the sustainability of the increase in defence funding has to be credible. National governments and the EU must send the signal to the EDTIB that it will last, and that the risk of investing in the development of new capacities is minimal. This raises the question how to render available sufficient resources to finance higher defence spending in a sustainable manner? On a national level, states could basically

¹⁰⁷ Csernaton, R. (2021). *The EU's Defense Ambitions : Understanding the Emergence of a European Defense Technological and Industrial Complex*. Carnegie Endowment for International Peace, Working Paper, pp. 20-22.

do so by either issuing new debt, raising taxes or by shifting funds away from other policy areas towards defence¹⁰⁸.

National debt-making is a solution that appears unsustainable and detrimental to states in the long-run. Indeed, public debt ratios are already very high in several European countries, with rising interests putting additional strain on some governments' budgets. Taking on significant amounts of new debt and thereby increasing deficits would only increase the cost of refinancing the debt annually, which most governments cannot afford in a long-term perspective and is not wishable for the eurozone either. This also appears especially unsustainable when considering the progressive return into force of the EU Stability Pact in 2024 (public debt below 60% of GDP and government deficit below 3% of GDP). Furthermore, raising taxes might also be a complex endeavor considering the already important tax burden weighing on European citizens, as well as the adverse economic effects that can arise as a consequence of higher corporate taxes (e.g. negative effect on the attractiveness of European countries for business and investment, and on the competitiveness of European companies)¹⁰⁹. Finally, trade-offs in the allocation of government expenditures could lead to larger amounts available for defence. Since the end of the Cold War, European governments have significantly reduced their defence budget for the benefit of other policy areas such as social spending. By and large, this was allowed by the 'peace dividends' period. Against today's security backdrop, European governments have to decide what political trade-offs they are ready to make in order to steer more funds towards defence.

A long-term avenue to be explored in order to mitigate the burden put by defence spending on public finances is the increased efficiency that could arise from improved European coordination and collaboration¹¹⁰. However, most countries have a two-pronged budgetary approach as regards defence. They have their annual defence budget which must be approved on a yearly basis and is therefore liable to change every year. Then, there is their long-term defence investment plan, for which they commit a certain amount of money over a given period. The latter plans are usually de facto limited to the period of activity of the government and end with the next elections¹¹¹, thereby creating obstacles to collaborative efforts that most often need to be envisaged over several years. In particular, there is an inherent difficulty to aligning the views of different countries having different timeframes and

¹⁰⁸ Dorn, F., Potrafke, N., Schleppe, M. (2024). *European Defence Spending in 2024 and Beyond. How to provide security in an economically challenging environment*. CESifo GmbH. Policy Report 45/2024. Vol 8. Pp. 3.

¹⁰⁹ Ibid, pp. 4.

¹¹⁰ Ibid, pp. 4.

¹¹¹ Ibid, pp. 5.

investment plans. Furthermore, economic downturns can arise in the midst of a collaborative project running over many years, potentially leading some of the affected participating countries to withdraw their contribution to the project or at least delay its unfolding. Such issues remain present even in the context of European collaborative programmes such as the EDF, although their extent might be mitigated by a greater political and budgetary stability. These considerations are crucial: defence companies won't be incentivised to invest if they lack the guarantee that sufficient funds needed for a project will remain available as long as it takes.

The EU has the potential to play a very beneficial role in providing coordination, funding and guarantees to the European defence sector, but the current collaborative arenas often remain too unpredictable for member states to see defence collaboration as the most favourable option. Hence, the question remains how the Commission will manage to gather the political convergence needed for member states to channel sufficient funding towards the European framework.

4.2.2 How can sufficient funding be channelled towards the European level?

To materialise into an efficient policy, the EDIS needs to appeal to member states and thereby impact their budgetary and procurement decisions. At the same time, this won't be the case if such limited financial means are allocated at the European level. We have described the constraints currently weighing on national budgets in a period where defence spending must expand. In that light, because it is unlikely that member states will be able or even willing to fund the EDIS to a level sufficient to have the desired impact on the EDTIB, new solutions must be found to gather financial resources. The European Defence Industry Programme (EDIP), implementing the EDIS, aims to allocate funding to the tune of €1,5 billion and pursues the objective to provide grants to firms that engage in joint collaboration to strengthen their production capacities or make joint acquisition of equipment. The EDIP is actually the continuation of the EDIRPA¹¹², whose purpose is to financially incentivise joint procurement of equipment conducted by at least three member states, but which expires at the end of 2025. The EDIP is supposed to play the same role over the period going from the

¹¹² European Commission (2024), *The European Defence Industry Reinforcement through common Procurement Act*. European Commission.

expiration of EDIRPA until the end of the EU's current seven-year budget in 2027¹¹³. This quite short-term role has been stated to explain the timid €1.5 billion of funds provided in the instrument. In fact, this ill-funding is also due to the fact that the previous EU budget had not anticipated that a high intensity conflict would rage on European soil¹¹⁴. Further, the Commission's intention is that the potential positive outcomes deriving from the EDIP will convince member states to provide larger amounts of funding for the next MFF¹¹⁵. Yet, the case can surely be made that the current context commands some urgency in the endeavor of promoting further Europeanisation of defence production and acquisition. Decisions in defence matters bear over long periods and the impact on the integration of the EDTIB will remain limited or even detrimental if member states aren't dissuaded from relying on national solutions or faster and cheaper off-the-shelf acquisitions and imports. Providing public investment through the EU to finance or co-finance joint research, development and procurement of defence equipment of common interest is therefore a pressing matter.

In this regard, the possibility to collectively take on debt is a widely discussed and controversial topic in Brussels. This would allow to mobilise resources and would stimulate European collaboration. However, some fiscally conservative states such as Germany and the Netherlands see common debt issuance as an improper means to finance long-term structural reforms. Others, like Emmanuel Macron or former Estonian Prime Minister Kaja Kallas, are in favor of this funding strategy¹¹⁶. Furthermore, another considered course of action has been the utilisation of the European Stability Mechanism (ESM), which could establish dedicated credit lines at low interest rates for national defence expenditures¹¹⁷. The EDIS even suggests using the windfall profits generated by Russia's frozen assets to finance military equipment for Ukraine¹¹⁸. In addition, the strategic plans on granting VAT exemptions for defence equipment collectively developed and procured by member states through the Structure for

¹¹³ Malanska, L. (2024). *The imperative of cooperation: the European Commission's strategy for the defence industry*. Centre for Eastern Studies. <https://www.osw.waw.pl/en/publikacje/analyses/2024-03-18/imperative-cooperation-european-commissions-strategy-defence>

¹¹⁴ <https://www.euractiv.com/section/defence-and-security/news/explainer-how-to-make-sense-of-the-eus-defence-funds-and-programmes/>

¹¹⁵ Malanska, L. (2024). *The imperative of cooperation: the European Commission's strategy for the defence industry*. Centre for Eastern Studies. <https://www.osw.waw.pl/en/publikacje/analyses/2024-03-18/imperative-cooperation-european-commissions-strategy-defence>

¹¹⁶ Besch, S. (2024). *Understanding the EU's New Defense Industrial Strategy*. <https://carnegieendowment.org/posts/2024/03/understanding-the-eus-new-defense-industrial-strategy?lang=en>

¹¹⁷ Letta, E. (2024), *Much more than a market. Speed, Security, Solidarity. Empowering the Single Market to deliver a sustainable future and prosperity for all EU Citizens*, pp. 72.

¹¹⁸ European Commission and High Representative of the Union for Foreign Affairs and Security Policy (2024), JOIN 2024, 10 Final, *Joint communication to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the regions. A new European Defence Industrial Strategy: Achieving EU readiness through a responsive and resilient European Defence Industry*. European Commission. Pp. 23.

European Armament Programme (SEAP)¹¹⁹. Besides, the European Council has recently encouraged the European Investment Bank (EIB) to increase its support to defence-related activities. This notably resulted in the EIB Group Security and Defence Industry Action Plan in which the EIB changed its lending policy by renouncing to the previous requirement that projects eligible for funding obtain more than 50% of their expected revenues from civilian use¹²⁰. The EIB Group also modified its rules to enhance defence SMEs' financing and innovation capacities¹²¹. Additionally, it is worth mentioning that enhancing private funding is a recognised avenue to alleviate national and European budgetary means, as exemplified by the Defence Equity Facility¹²² (DEF) scheme, announced in 2024, whereby the European Investment Fund will invest €175 million into small defence-related firms and start-ups. Such funding and risk coverage aim to encourage private investors to increasingly target investment in the military sector¹²³. The same remark holds true as regards the modification of the EIB lending policies.

Furthermore, increasing and pooling defence investments at the European level necessarily entails reconciling varying positions on which defence capabilities the EU should acquire. Seeing eye to eye on the concrete direction that limited resources should take is a highly complex and political endeavor. Different geographical, cultural, industrial and strategic considerations influence the decision-making process in this regard. For instance, some member states might see greater benefits in improving naval vessels while others might see the improvement of land capabilities as a greater priority¹²⁴.

Last but not least, the question has been raised what are the incentives for countries with relatively small DTIBs to steer funding towards the EU budget and collaborative projects if they're unlikely to industrially benefit much from it. If their DTIBs are mainly made out of SMEs, why should they contribute to an EDIP that will most of the time be used to finance large-scale defence projects where largest firms from big member states are likely to be the

¹¹⁹ Ibid, pp. 12.

¹²⁰ <https://www.eib.org/en/press/all/2024-174-eib-board-of-directors-steps-up-support-for-europe-s-security-and-defence-industry-and-approves-eur-4-5-billion-in-other-financing>

¹²¹ <https://www.eib.org/en/press/all/2024-174-eib-board-of-directors-steps-up-support-for-europe-s-security-and-defence-industry-and-approves-eur-4-5-billion-in-other-financing>

¹²² European Commission. (2024). *The European Commission and the European Investment Fund join forces to boost investment in defence innovation through the Defence Equity Facility*. Press release 12/01/2024, Brussels. European Commission.

¹²³ <https://www.euractiv.com/section/defence-and-security/news/explainer-how-to-make-sense-of-the-eus-defence-funds-and-programmes/>

¹²⁴ Fiott, D. (2022). *The Fog of War: Russia's War on Ukraine, European Defence Spending and Military Capabilities*. Intereconomics, ISSN 1613-964X, Springer, Heidelberg, Vol. 57, Iss. 3, pp. 154.

main beneficiaries?¹²⁵ In addition, if major partners invoke article 346 TFEU to abstain from being transparent and from issuing competitive biddings, this would give more power to large firms and would de facto exclude a lot of SMEs from supply chains and projects. It has been argued that the EU and mainly the large industrial states should make cooperative programmes attractive to Central and Eastern European countries through transfers of knowledge and of some segments of production¹²⁶. Considering the fact that this would notably entail cuts in their domestic profits, one can reasonably doubt the realistic nature of such scenario. In addition, participating in collaborative development and procurement processes stretching over long periods implies some rigidity associated to the necessary engagement of budgetary means towards and the involvement into these programmes. By contrast, buying off-the-shelf equipment provides budgetary flexibility, a factor worth considering when taking into account the questionable sustainability of current defence efforts and budget increases.

4.3 Foreign challenges

4.3.1 Foreign defence equipment acquisitions

The risk has long been identified that uncoordinated increases in defence budgets may lead to a deepening of the fragmentation and further duplications of efforts. Most member states – especially the ones geographically closer to Russia - prioritise the swift acquisition of capabilities and often resort to off-the-shelf purchases and imports from non-EU countries, in part due to capacities shortfalls in the EDTIB. In such case, urgent priorities prevail over the long-term objective of fostering a resilient and competitive EDTIB over the next years and decades. Besides, dependencies on foreign actors are either extended or created by such preference for rapid acquisitions. To give an idea of the magnitude of this challenge, 78% of EU member states' 2022-2023 commitments to acquisitions were contracted with non-EU suppliers. Out of this share, 63% were represented by the US alone¹²⁷. In this regard, the Foreign Military Sales (FMS) programme is a Government-to-Government setting

¹²⁵ Fiott, D. (2024). *In Whose Interests? Regulating Europe's Defence Industry and the Politics of Exemptions*. CSDS Policy Brief, 3/2024.

¹²⁶ Mölling, C., Helmonds, S. (2023). *Security, Industry, and the Lost European Vision How Russia's War in Ukraine Is Changing the European Defense Technological and Industrial Base*. German Council on Foreign Relations. DGAP Report, pp. 11.

¹²⁷ Maulny, J-P. (2023). *The impact of the war in Ukraine on the European Defence Market*. Ares Group, IRIS, Policy Paper 2023/09, pp. 17.

exonerating parties to the defence contract from the requirements of Directive 2009/81 (in particular article 13 of the Directive which, in specific instances, excludes some market rules when defence contracts take place between two governments). This programme is very effective and flexible, which leads EU member states to massively use it when purchasing defence equipment from US producers. Important also is the strategic dimension of purchasing from the US government through the FMS. Traditionally, recipient countries have developed closer ties with the US military, for instance under the form of joint training and exercises. An important consideration when envisaging further integration of European defence industries is that the European member states having developed industrial connections with the US are - to different degrees - influenced by these transatlantic links in their positions¹²⁸. It is worth mentioning that the EDIS hints at the creation of a European Military Sales Mechanism from 2028 onwards¹²⁹. However, the functions of this mechanism would be manifold and similarities with the US FMS are limited.

One outcome of the prioritisation of immediate off-the-shelf acquisitions is a reduced occurrence and appeal of European collaborative initiatives, thereby perpetuating the EDTIB's shortcomings. Indeed, this represents a missed opportunity to obtain virtuous benefits from collectively and coherently channeling investment towards the EDTIB. Regrettably, another outcome is a loss of market share for European defence companies. In addition, these foreign-made defence products will remain in European inventories and the willingness to achieve greater interoperability might induce other member states to procure the same foreign equipment. Furthermore, the surge in acquisitions from non-EU suppliers following the Russian invasion of Ukraine also increased existing foreign dependencies and generated some others.

Additionally, the production of foreign equipment on European soil is a growing phenomenon¹³⁰. For instance, Poland reaps benefits from procuring equipment from South Korean producers notably through manufacturing licenses granted to Polish companies. Objectively, there is a strong case to be made that this arrangement represents a fairly attractive opportunity for the development of the Polish DTIB. Another illustration comes

¹²⁸ Fiott, D. (2019). *The Poison pill: EU defence on US terms?* European Institute for Security Studies (EUISS), Brief 2019/7, pp. 4.

¹²⁹ European Commission and High Representative of the Union for Foreign Affairs and Security Policy (2024), JOIN 2024, 10 Final, *Joint communication to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the regions. A new European Defence Industrial Strategy : Achieving EU readiness through a responsive and resilient European Defence Industry*. European Commission. Pp. 13.

¹³⁰ Maulny, J-P. (2023). *The impact of the war in Ukraine on the European Defence Market*. Ares Group, IRIS, Policy Paper 2023/09, pp. 16.

from Lockheed-Martin (US) and Rheinmetall (Germany) that have announced in June 2023 their partnership in the manufacturing in Europe of the High-Mobility Artillery Rocket System or HIMARS¹³¹. In this latter case, there does not exist any EU-based equivalent to this specific piece of defence equipment.

Importantly, there is a misconception that European defence purchases from foreign contractors entirely fail to convey industrial benefits for the EDTIB. However, as previously mentioned, industrial participation requirements often go along with foreign defence procurement, under the form of offsets.

4.3.2 Transatlantic relations

The transatlantic relationship introduces various complexities that challenge the EU's effort towards greater defence Europeanisation. The risk of antagonising their most critical ally has often constrained European member states in their approaches. The fact that many European countries - especially those from Eastern Europe - heavily rely on American security guarantees grants the US significant influence over European defence decision-making. Indeed, countries that view US security guarantees as indispensable or that have developed privileged industrial ties with the US may be less inclined to support EU initiatives when these may be perceived as undermining the economic and geopolitical interests of the US¹³². Moreover, European defence industrial integration can sometimes be compromised by the significant presence – both through direct sales and subsidiaries – of American defence companies. As we have seen, this diverts funds away from European cohesive projects and lessens their appeal.

Furthermore, European states have divergent views on the objective and modalities of achieving European strategic autonomy. Some member states favor a strong and self-sufficient Europe while others are more moderate and rather prioritise NATO as the primary security framework, often aligning with US strategic directives, making sure that European defence initiatives complement NATO and ensuring American access to Europe's defence market¹³³. The outcome of such state of affairs is a long-established dependence on the US as regards military equipment. The US supports the reinforcement of European defence capabilities but provided that it enhances global security and NATO's overall strength and

¹³¹ <https://www.rheinmetall.com/en/products/tactical-wheeled-vehicles/wheeled-armoured-vehicles/gmars>

¹³² Bergmann, M., Morcos, P., Wall, C. Monaghan, S. (2022). *Transforming European Defense*. Center for Strategic and International Studies. CSIS briefs, pp. 4.

¹³³ *Ibid*, pp. 4.

does not go against American commercial interests. As the US military's attention is now geared towards the Indo-Pacific, a strong Europe able to defend itself and watch over its direct neighbourhood is also pivotal from an American perspective.

The 2024 European defence industrial strategy (EDIS) strongly emphasises the aim of reducing weapons imports, by bringing imports share below 50% of total European defence procurement by 2030¹³⁴. If this objective has merits from an industrial policy perspective (i.e. develop resilient European defence industries by fostering higher demand for domestic suppliers), it might also contribute to the deterioration of the transatlantic relations. In addition, given the increasing needs for military equipment, which in several instances outpace current European supply capacities, keeping imports alternatives open might prove essential to address Europe's defence requirements. This would hold especially true in case of a crisis scenario¹³⁵. On the other hand, security of supply can also be harmed by an excessive reliance on third countries' imports. Hence, a balance should be struck between the guarantee of external sources of supply and the reinforcement of the EU's ability to autonomously deliver the necessary capabilities.

All in all, the US represents at the same time an impediment to the European defence integration and a paramount security partner. Therefore, it can be argued that the reinforcement of Europe's strategic weight through a more resilient defence industrial base should be envisaged in a way that preserves the transatlantic alliance¹³⁶. Yet, the EDIS invites member states to give priority to EU-based defence producers over non-EU suppliers. In addition, the reproach has been made – notably by the AmCham which speaks for American business in Europe - that the EDIS fails to provide a vision of the future collaboration with important security partners such as Canada, the United Kingdom and the United States. The AmCham also warns against the risks of a European protectionist approach, such as loss of technology and intellectual property, as well as interoperability and interchangeability issues. The AmCham argues that the future regulation implementing the EDIS will need to also support “EU-based entities with third-country entity ownership from like-minded allies”¹³⁷. Other papers criticise the lack of references in the EDIS to the NATO framework and the

¹³⁴ Wolff, G. (2024) *The European defence industrial strategy: important, but raising many questions*. Bruegel analysis, pp. 2.

¹³⁵ Ibid, pp. 5.

¹³⁶ Ibid, pp. 5.

¹³⁷ AmCham EU. (2024). *The European Defence Industrial Strategy (EDIS) and the European Defence Industry Programme (EDIP). Our position*, pp. 4.

NATO-EU relation¹³⁸.

5 Conclusion

The integration of European defence industries presents both a significant challenge and an opportunity for the European Union (EU) as it seeks to enhance its strategic autonomy. This thesis has explored the complex dynamics shaping European defence industrial integration, emphasising both the potential benefits and the substantial obstacles that must be addressed to achieve a more unified and coherent European defence industry.

A central issue that emerges from this analysis is the tension between national interests and the old continent's collective security. The longstanding reluctance of EU member states to approach defence matters from an European perspective has resulted in a fragmented defence industrial landscape, where collaborative efforts are often undermined by conflicting priorities and national interests.

Looking ahead, Europe faces an imperative to reinforce its defence apparatus. Achieving this will necessarily imply reaching political convergence on a more European approach to defence challenges. External factors, such as the war in Ukraine and the potentiality of a more isolationist stance from Washington as of 2025, may provide additional political impetus for a cohesive European thrust. Yet, a multitude of challenging considerations remain and are likely to act as countertendencies to this European effort and significantly constrain and limit the extent of European defence industrial integration. Ultimately, the success of any future European defence industrial strategy hinges on the willingness of EU member states to deepen collaboration and invest more in joint equipment programmes. Securing the necessary political backing will require the strategy to successfully balance divergent interests and strategic visions while providing the financial incentives essential for gaining broad approval from member states. In addition, the strategy will need to tackle contentious issues, particularly regarding the inclusion or exclusion of partner countries' defence firms in EU programmes.

¹³⁸ Fiott, D. (2024). *Beyond Strategy? Industrial Strategy and the Future of European Defence*. Real Instituto Elcano. ARI 57/2024, pp. 8.

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