

Issue paper #2

Towards a European Defence Industrial Strategy: Investing better and together in defence capabilities and innovative technologies

The Commission, together with the European External Action Service in coordination with the European Defence Agency, has launched, based on a first overall consultation paper ('Issue paper #1'), a comprehensive stakeholder engagement process to inform the new European Defence Industrial Strategy. This second paper outlines key issues and questions for further discussion on defence investment.

The purpose of this second Issue paper is to support the informal discussions with the stakeholders. It does not constitute an official position of the Commission and does not pre-empt the content of the future Strategy.

Already in 2016, the European Defence Action Plan¹ recognised the insufficient level of the Member States' **defence investment and R&D**, the **fragmentation of the demand**, and the significant quantities of **equipment procured from non-EU players**, as key trends hampering the competitiveness of the European Defence Technological and Industrial base (EDTIB). Moreover, the **lack of defence cooperation** within the EU was also identified as having a **negative impact on the operational effectiveness of the armed forces** of the Member States, causing significant challenges in terms of interoperability. Several EU defence initiatives were launched to remedy these realities (CARD, EDF, PESCO – all in line with the CDP priorities).

The **return of high intensity warfare in Europe** has confirmed the urgency to address these concerns, reflected in the Strategic Compass, the Versailles Declaration, and the following Joint Communication on the Defence Investment Gaps Analysis and Way Forward². As a response, further initiatives have been launched.³

The limited impact of increased defence spending on EDTIB

Since the start of the Russia's full-scale and unjustified war of aggression against Ukraine, **Member States have increased their defence expenditure**⁴: there has been a 12% growth since 2022, with further plans to increase in 2024-2025⁵; moreover, 25% of the total defence expenditure allocated to defence investment in 2022 was used to accelerate the procurement of needed capabilities and the replenishment of stocks with predominantly off-the-shelf procurement in search of immediate solutions.

Against this backdrop and given the **past and recurrent under-investment**, the **European defence industry** is **undersized** and struggles to cope with the sudden and

¹ COM(2016) 950 final.

² JOIN(2022) 24 final.

³ Regulation (EU) 2023/2418 of 18 October 2023 establishing an instrument for the reinforcement of the European defence industry through common procurement (EDIRPA); Regulation (EU) 2023/1525 of 20 July 2023 on supporting ammunition production (ASAP); Defence Joint Procurement Task Force (DJTPF), Ammunition Initiative aimed at providing one million rounds of artillery ammunition for Ukraine in a joint effort in 12 months of 20 March 2023.

⁴ +40% from €171bn to €240bn between 2014 and 2022, as an average with high discrepancies between Member States (constant 2022 prices), including +6% between 2021 and 2022, EDA 2023 Defence Data Publication.

⁵ 2023 HR Annual Report on the Status of PESCO implementation.

considerable increase in equipment demand linked to massive transfer of equipment and supplies to Ukraine and the urgent need to replenish national stockpiles and inventories. A **lack of coordination** in Member States' procurement, particularly on some most urgent and critical defence needs (e.g. ammunition), has resulted in a **supply crisis characterised by price-spiralling and crowding-out effects** as Member States are competing with one another on the constrained European defence equipment market.

The EDTIB is deprived of predictability regarding Member States' demand and **cannot fully reap benefits of the internal market** to undertake sustained investments in production capacities that also have a longer-term impact.

Demand fragmentation

The **fragmentation of Member States' defence development and procurement** along national lines was identified as a major issue since 2004⁶. Collaborative defence equipment procurement remains significantly below the collective benchmark of 35% agreed in the EDA and PESCO-frameworks⁷. Obstacles to Member States' decisions to engage in coordinated planning and/or procurement are manifold, starting with a lack of fully embedding EU's defence tools and instruments in national planning and budgetary processes. This has impeded harmonised requirements, resulted in diverging prioritisations of investments, challenges in the synchronisation and pooling of national contributions, and differing industrial and acquisition strategies.

The insufficient purchase of EU products in defence procurement

The recent urgent acquisitions caused by the radically changed security environment were undertaken against the backdrop of an EDTIB constrained by, limited, "peace time" production capacity. New procurement efforts **benefited mostly non-EU industry, even when competitive European products were available, suggesting that potential limitations in terms of production capacity are not the sole driver**.⁸ Thus, the trend of favouring non-EU solutions has further intensified, increasing existing dependencies or generating new ones, thereby limiting the potential virtuous circle of increased investment resulting in a strengthening of the EDTIB. US Foreign Military Sales (FMS) in Europe has increased by 89% between 2021 and 2022⁹ emerging armament manufacturers from other third countries have penetrated the EU market.

From emergency responses to building-up EU defence industrial readiness

⁶ Initially in *The challenges facing the European defence-related industry, a contribution for action at European level* (COM(96) 10 dated 24 January 1996); and subsequent communications such as the *Green Paper* on Defence procurement (COM(2004) 608 dated 23 September 2004) or Towards a more competitive and efficient defence and security sector (COM(2013) 542 final dated 24 July 2013).

⁷ European collaborative defence equipment procurement accounted for 18% of defence equipment procurement expenditure in 2021, after 11% in 2020 (EDA, Defence data 2020-2021, key findings and analysis, December 2022).

⁸ According to a recent study (Maulny, ARES Group, 9/2023) from a total of EUR 75 billion spent by MS between June 2022 and June 2023, 78% is being procured from outside the EU, out of which 80% from the US, 13% from South Korea, 3% from the UK and Israel.

⁹ Based on CIP figures in the Security and Assistance Monitor: [Arm Sales \(securityassistance.org\)](https://securityassistance.org/)

As emphasized in the Strategic Compass and the Versailles Declaration, EU Member States have repeatedly agreed on the need to not only **spend more** but also **better**, by investing **together**.

The Joint Communication on Defence Investment Gap Analysis further stressed the need to “bolster European defence capabilities”. As an immediate short-term action, the Defence Joint Procurement Task Force (DJPTF) was set up in May 2022. The Task Force identified the urgent and critical needs of the Member States, which was instrumental for the implementation of EDIRPA (supporting Member States’ cooperation on common procurement of the most urgent and critical defence products) and ASAP (supporting the industrial ramp up of ammunitions' production).

It is now time to **move away from responding to urgencies towards achieving defence industrial readiness** and to develop a more **articulated, comprehensive and sustainable approach that supports Member States in coordinating their demand**. In that context also, strengthening the CARD becomes an imperative need.

This may encompass different solutions depending on the type of defence needs and shortfalls identified. In many respects, the joint procurement of off-the-shelf products (consumable such as ammunition, missiles) is different from that of more complex systems or platforms (such as ground vehicles, airplanes or warships). Moreover, cooperation on **strategic enablers** necessary for the protection of **contested areas** present a particularly strong case for cooperation, as some of the involved infrastructures required to develop and operate such enablers would be out of the reach of a single Member State. The acquisition and financing of such enablers could call for **more innovative solutions, going beyond joint procurement** and possibly envisaging the joint ownership and operational use of such strategic assets.

Three main issues must be addressed to unlock the EDTIB’s potential on a structural basis.

1. Identifying common needs at an early stage and ensuring transparency on demand

It is essential to **identify the most critical priorities at the earliest possible stage, fully using the 2023 EU Capability Development Priorities**¹⁰. This should result in their immediate translation into national defence planning and budget cycles. The first step in that direction was the Defence Joint Procurement Task Force (DJPTF), aggregating urgent joint procurement needs of interested Member States, and mapping the industrial capacity of related parts of the EDTIB. The work of the DJPTF enabled the fast identification of the production capacity of a given product across the supply chains within the Union. The Task Force has proven the need for greater transparency and more solidarity, evidencing the need to explore the set-up of a **more structured mechanism enabling the aggregation of demand and the mapping of the production capacity of the EDTIB** to deliver upon Member States’ needs.

Such effort could be pursued and amplified through a **Joint Programming and Procurement Function**, building on the existing DJPTF and lessons learnt in the context of the ammunition initiative, EDIRPA and ASAP, bringing together the Commission, EEAS (incl. EUMS), the EDA and the Member States. Its role could be to coordinate efforts of all stakeholders, to collect information on the demand side, and to propose consolidation and de-conflicting of the demand while ensuring security of supply, greater

¹⁰ The Capability Development Priorities serve as a central reference for the development of Member States’ defence capabilities for the coming years at EU level, as well as for ensuring coherence among EU defence initiatives.

efficiencies in public spending and the timely availability of defence products, notably those that are of the highest urgency and criticality, and whose production capacity in Member States may need to be further reinforced¹¹.

As far as the identification of **European Defence Industrial projects of common interest** is concerned, building a common understanding of Member States' future challenges and possible operational scenarios, as well as the anticipation of global technological trends¹² are goals to be pursued. This is particularly compelling in respect to the capabilities necessary to ensure **free and unfettered access to contested strategic domains** (cyber, space, air and maritime), which are beyond the reach of a Member State alone. In addition, projects of common interest also require continuous financing.

While the **European Defence Fund indicative multiannual perspective** (MAP) encourages such an approach at the level of R&D, its potential remains to be further developed, in particular for the development of complex European systems and platforms.

Finally, the crisis has also shown that most Member States, alone or together, lack sufficient awareness of industrial production capacity, which is indispensable to ascertain EU collective capacity. The absence of a shared mapping of manufacturing capacity casting light on the intricacies of cross-border supply chains results in a **systematic underestimation of the EDTIB's capacity** to deliver upon Member States' needs, as well as in an **inability to address bottlenecks in a timely manner**.

Questions:

- ⇒ *How to enhance and further support the identification of short-term to long-term defence product needs? How can we build upon the DJPTF's experience to aggregate demand and map production capacity to deliver upon it?*
- ⇒ *How can we identify, based notably on the CDP, which long-term priorities should and could realistically result in EU European Defence Industrial projects of common interest? What role do we see for current and possible future EU defence initiatives, such as the European Defence Investment Programme (EDIP)/European Defence Capability Consortium (EDCC)¹³(for more details see below), PESCO and/or EDF in this regard? How to ensure and secure the commitment of interested MS for these projects?*
- ⇒ *Could a consistent EU support for European Defence Industrial projects of common interest, starting with research through development up to joint procurement and potentially maintenance and upgrades, incentivise Member States to finally procure the final product?*

2. Coordinating defence spending and procurement plans, including the harmonisation of requirements

Once collectively identified at EU level, short and long-term priorities need to be translated into cooperative solutions. A successful outcome of collaborative programmes

¹¹ This work should be carried out in respect of the EU processes and instruments (CDP, CARD, ...) and fully take them into account.

¹² In this regard, the defence capabilities priorities commonly agreed by Member States at EU level and the EDA technology foresight activities and Overarching Strategic Research Agenda (OSRA) should be taken into account

¹³ As mentioned in section 5.3 of the [Joint Communication on the Defence Investment Gaps Analysis and Way Forward of 18 May 2022](#)

can be facilitated by the harmonization of requirements from the earliest possible stage and in a timely manner.

While the CARD provides greater visibility of collaborative opportunities for capability development, the **defence spending and procurement plans** of the Member States are still **not sufficiently coordinated**. Cooperation remains essentially perceived as complex, generating additional delays and costs. In spite of promising collaborative projects on the horizon, cooperation is not yet the norm but remains the exception.

When it comes to requirements:

- **Member States' Defence Forces and planners** often **tend to focus on specific national requirements** without taking the overall benefits of standardisation and interoperability fully into account. However, increased **standardisation** and **greater interoperability** of the defence products are prerequisites for efficient operational use. As a result, even standardized consumables, such as ammunition, are too often not interchangeable¹⁴.
- As regards **new capabilities**, the EDF can finance activities that aim to establish defence products standards. A special attention should also be given to **standardisation requirements** at the stage of the procurement decision to ensure the application of the most common standards and ensure interchangeability with existing weapon systems. In this respect, efforts to ensure the coherence of the output, including in respect of the relevant activities of NATO (e.g. as regards standardisation) need to be taken into account.
- **Limited possibilities to ringfence defence investment** benefitting genuine European defence priorities exist at Member State-level today. Despite recent defence budget increases, there is no certainty that Member States will be able or determined to sustain their current investment effort. Downturns in the economic cycle might lead again to budgetary cuts, which in the past have often negatively impacted collaborative projects. For collaborative projects running over several years - if not decades - there is a need to ringfence budgetary resources, as well as ensuring their synchronisation among partners.

The EU still critically lacks a mechanism or framework allowing Member States to pool resources and jointly finance, procure, maintain and upgrade defence products or technologies, including those that received support from the Union budget. While the European Peace Facility provides for a mechanism to finance military assistance to third countries, there is no solution at EU level to finance Member States' own critical defence product needs, e.g. the replenishment of stocks but also procurement of new capabilities¹⁵. Moreover, there may be room to explore measures to 'simplify' and streamline defence cooperation between the Member States.

¹⁴ As an example, due to vast amount of military assistance provided, Ukrainian armed forces cope with a fragmented and sometimes not interchangeable variety of defence products.

¹⁵ While EDIRPA provides EU funding, it does not co-fund the procurement of defence products but financially support the cooperation between Member States in the procurement phase of defence products.

Multinational armament projects and even cooperative R&D projects are confronted with delays or even termination when promised national contributions are withdrawn or when the budgetary contributions of partners, although potentially available, are not synchronised. This applies to a lesser extent to projects conducted jointly and in particular in the context of a **European programmes** (e.g. EDF) that benefit from higher **political and budgetary stability but for which co-funding is necessary**. The issue was identified in the EDA framework, leading to the elaboration of the Cooperative Financial Mechanism. However, the programme has not been used by Member States yet.

Questions:

- ⇒ *How to simplify the launch and successful completion of cooperative defence programmes?*
- ⇒ *How to strengthen interoperability and interchangeability of defence products developed and procured by Member States? How can current and possible future EU defence initiatives and instruments, such as the EDF and PESCO projects, EDIP/EDCC (see below) or other EU tools contribute to standardisation and help to achieve interchangeability of consumables?*
- ⇒ *How to improve synchronisation of national budgetary provisions for cooperative programmes? How to ring-fence budget allocated to cooperative programmes in the national setting? Would Member States be ready to consider pooling national contributions in a wider EU scheme?*

3. Aggregating demand through joint procurement

Once common priorities have been identified and funded, collaborative programmes launched and successfully conducted, there is a **need to ensure that Member States will procure, operate, and maintain jointly the defence products** resulting from that cooperation. The EU has put in place new tools and instruments to reverse the long-standing trends hampering the efficiency of Union's defence sector. But further ways to boost cooperation should be explored, while the most recent initiatives need to be made structural and long-term.

Supporting cooperation along the whole life cycle of defence capabilities

Multinational armament **cooperation** requires increased efforts in initiation and implementation (compared to national programmes), including highly skilled workforce and organisational stability. Several Member States lack the **administrative capacity to secure their participation in complex procurement** processes. EDA and OCCAR offer expertise in that regard, but their usage is still limited. Armament cooperation benefits can be maximised **in the long run**, in particular when Member States cooperate throughout the life cycle of the acquired defence product.

The Joint Communication on Defence Investment Gaps Analysis considered the possibility to establish dedicated and VAT-exempted **European Defence Capability Consortia (EDCC)** to jointly procure, for the use of participating Member States, defence capabilities developed in a collaborative way within the EU. Such EDCC would create a very strong cooperative element and bring additional benefits such as interoperability and efficiency gains over the life cycle, the harmonisation of procedures and training curricula for operation, maintenance, repair and overhaul, tapping economies of scale. Such a European legal framework could also facilitate a collaborative approach towards:

- Joint procurement of **off-the-shelf products**, including the joint stockpiling of inputs, such as raw materials/components, ammunition or spare parts;

- Joint procurement and maintenance of **more complex defence systems** (either off-the-shelf or as a result of EU defence research and development);
- Joint procurement, ownership and maintenance of **strategic assets for ensuring access to contested areas**. The joint operational use of these assets could also be considered and explored.

Those EDCCs would make use of existing provision to be exempted from Value Added Tax (VAT), which would also apply to operation, maintenance and decommissioning, which are a major cost over the lifecycle of defence equipment.

Simplifying and accelerating procurement processes

Complex next-generation systems require massive investments, offsetting partly the benefits of R&D cost sharing, whilst the resurgent threat of high intensity conflict and the ongoing war of attrition in Ukraine suggest giving priority to readily available solutions. At the same time, the well-established need for the rapid recovery from decades of underspending, combined with the ever-increasing pace of innovation, require an **acceleration of the development and acquisition processes**. Even for the same category of products or systems, **investment decisions happen too iteratively**, often in an uncoordinated way, leading to a proliferating number of tendering procedures having as their subject matter similar capability shortfalls, possibly resulting in further fragmentation and less interoperability.

This situation also de facto favours off-the-shelf procurement from third countries (e.g. through the US Foreign Military Sales Scheme (FMS))¹⁶ or leads to non-competitive national procurement. Comparatively, using a one-stop shop offering quick solutions for procuring off-the-shelf equipment is deemed much simpler than launching a parallel procurement process within the EU. Strengthening national administrative capacity (procurement skills and processes) and simplifying procurement procedures seems therefore essential to allow EDTIB to operate on a level playing field.

Some Member States have reported issues related to procurements (e.g. legal framework for joint procurement, possibility to modify an existing contract or framework agreement, etc.). Even though a call for evidence within the Expert Group on Defence Procurement did not enable to identify significant issues related to Directive 2009/81/EC, so far, further data on specific issues faced by Member States at procurement level might call for solutions at EU or national levels.

Questions:

- ⇒ *Is the complexity of defence procurement procedures an obstacle to the timely availability and supply of European made products? If so, to what extent and for which reasons, and how to reduce it? How to further facilitate the acceleration of defence procurement? What are the barriers to Member States' cooperation beyond common/joint procurement, e.g. in maintenance, procurement of spare parts and logistics?*
- ⇒ *Could a one-stop-shop further incentivise joint procurement, especially for Member States lacking the relevant administrative capacity? Could potential EDCCs contribute to the aggregation of defence demand supporting the EDTIB's competitiveness, and how?*
- ⇒ *Should the EDIRPA logic be extended to covering 2025 to 2027, including by providing financial incentives e.g. through EDCCs, for joint procurement and beyond?*

¹⁶ As an example, 95% of Member States' orders from the US since the beginning of the war have been made through US-FMS (Maulny, ARES, 2023), amounting to an expenditure above US\$ 60 billion.

⇒ *Should an EU equivalent of the US FMS-scheme be considered, building on government-to-government schemes, to support procurement from the EDTIB by EU Member States and support to partners, including Ukraine? If so, how should such a mechanism operate? How could it support the availability of defence equipment from the EDTIB?*