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From market integration to security integration: Taking the next steps for European defence-industrial cooperation

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brief

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- *Russia's war of aggression constitutes a tectonic shift in European history.*

Versailles Declaration, European Council, March 2022

- *We will make a quantum leap to become a more assertive and decisive security provider, better prepared to tackle present and future threats and challenges.*

EU Strategic Compass for Security and Defence: For a European Union that protects its citizens, values and interests and contributes to international peace and security, March 2022.

- *The Union's geopolitical context has changed dramatically in light of the Russia's military aggression against Ukraine. The return of territorial conflict and high-intensity warfare on European soil requires Member States to rethink their defence plans and capacities.*

European Commission, Proposal on establishing the European defence industry Reinforcement through common Procurement Act, July 2022

Introduction

Crises tend to transform institutions and actors, and many argue that crises, as pivotal moments, 'have been catalysts for major breakthroughs and for advancements of the integration process' (Dinan et al., 2017: 9). And European Commission President Ursula von der Leyen argues that the war in Ukraine has created 'a watershed moment for our Union'; and that 'this crisis is changing Europe' (von der Leyen 2022). High Representative/Vice President Josep Borrell has similarly argued that the EU has broken several taboos and had a 'geopolitical awakening' (Borell 2022; see also Blockmans 2022; *Financial Times* 2023). This policy paper consequently discusses how the war in Ukraine has started to transform and strengthen the role of the European Commission in European Union security and defence policy, in particular in the defence-industrial domain. It also outlines the long-term ambitions of the EU and the European Commission in this area. Finally, it sets out some new ideas on EU defence cooperation.

These developments can be seen as part of a long-term ambition of the European Commission to become a stronger and more capable actor in the defence-industrial domain. The Commission has also moved over time from a logic of market integration to a stronger emphasis on security integration. To demonstrate this process, this paper examines 14 policy proposals made by the European Commission on defence-industrial policy since the mid-1990s. The paper also draws on interviews and informal discussions with officials and policymakers from the European Commission, the European External Action Service (EEAS), the European Defence Agency (EDA) and EU member states in the spring and autumn of 2022.

The paper first addresses long-term processes and argues that the Commission has shifted its focus and logic of integration. It then discusses the implications of the launch of the Commission's 2022 defence package, the adoption of the EU Strategic Compass, the May 2022 Commission and EDA gap-analysis and proposals, and the new proposal for European Defence Industry Reinforcement through a common

Procurement Act (EDIRPA), and outlines the need for more and enhanced cooperation at the EU level. Finally, it addresses the wider implications of these developments for Sweden.

Historical developments: from market to security integration

The European Commission has long held an ambition to be a stronger actor in European defence industrial cooperation; see for instance the discussions in Citi (2014); James (2018); Mawdsley (2018); Haroche (2020); Martins and Mawdsley (2021); Csernatoni (2021); and Håkansson (2021). This policy paper focuses on developments since the mid-1990s to discuss how the Commission has outlined the need to enhance or create a European defence market. While it is possible to identify that its approach has moved at least somewhat from stick (regulation) to carrot (financial contributions), some arguments have clearly remained consistent throughout.

As early as in its 1996 communication, the Commission was underlining problems with the 'fragmentation of the defence markets in Europe', and especially the problems of European defence industry competitiveness vis-à-vis US defence companies. Thus, it argued the need for a 'deepening of the European Union, to include a defence policy in the long term…' and that 'Close cooperation on armaments is a key factor in defence policy'. This should be achieved, among other things, by setting public procurement rules, facilitating intra-Community trade, and enhancing synergies between civilian and defence industries (European Commission 1996). The 1997 follow-up communication set a timeline to 'strengthen the competitiveness of the European defence industry' (European Commission 1997). However, implementation of these proposals was very limited. Consequently, the Commission in 2003 presented a new communication, 'Towards an EU Defence Equipment Policy,' on strengthening EU defence policy, which should be seen in the light of the then ongoing Convention on the Future of Europe. The 2003 communication contained proposals on intra-Community transfers and rules on defence procurement, among other things. It also outlined proposals for a 'preparatory action for advanced research in the field of global security' and supported work towards a European Defence Agency (European Commission 2003, see also Fiott 2015a; Håkansson 2021). The 2003 communication also discussed the importance of competition policy for the European defence market and underlined that 'Competition improves market efficiency and protects innovation' (European Commission 2003).

In 2004, the Commission published a Green Paper to advance the debate on defence industrial cooperation, with an ambition to 'open up' the European defence market (European Commission 2004). Following this and a 2005 paper on the results of the Green Paper consultation (European Commission 2005), the Commission in 2007 published a new communication on improving the state of defence-industrial cooperation in Europe. The 2007 communication presented proposals for new legislation on intra-EU transfers and defence procurement (European Commission 2007). Consequently, after more than a decade of trying, this culminated in the adoption of the so-called 2009 defence package and its two directives: on intra-EU transfers of defence products and on defence procurement. The Commission drew on 'court-driven integration' to adopt these directives (Blauberger and Weiss 2013). The 2009 defence package was an important stepping stone for the Commission in legitimising its role in defence in future initiatives. Nonetheless, the results of the 2009 defence package have thus far been limited (Ioannides 2020: Marrone and Nones 2020).

By 2013 there had been a further shift in focus, as the Commission's argumentation departed from the deteriorating security situation. The 2013 communication began by outlining the evolving and shifting geopolitical situation, and the various challenges and the complex threat environment facing Europe. The communication asserted that 'Europe must be able to assume its responsibilities for its own security and for international peace and stability in general'. The most notable initiatives were proposals on possible EU-owned dual-use capabilities and a proposal to launch a preparatory action on Common Security and Defence Policy (CSDP)-related research (European Commission 2013). While the proposal for EU-owned dual-use capabilities was scrapped by the European Council, the proposals on a preparatory action on CSDP research were adopted at the December 2013 European Council (Fiott 2015a). This preparatory action would later become important for other new initiatives such as the European Defence Fund (EDF) (Håkansson 2021).

The 2016 European Defence Action Plan (EDAP) was also a key development as it outlined the EDF. The EDAP followed the 2016 EU Global Strategy, which had provided new impetus to European defence cooperation. The Action Plan outlined a new ambition on the Commission's part and underlined the worsening security situation, arguing that Europe needed to take greater responsibility for its own security (European Commission 2016). It was therefore no surprise when the 2017 communication on the EDF proposal set out in its first sentence that 'the EU is facing increased instability and conflicts in its neighbourhood and new security threats are emerging' (European Commission 2017).

It is striking, however, how similar some arguments have remained over time, such as on the fragmentation of the market and the ambition to enhance civilian-military industrial synergies (see table 1). However, we also find a shift in the Commission's argumentation as communications since 2013 have focused on the deteriorating security situation to legitimise its role in EU security governance. Daniel Fiott, for instance, has identified this shift by the EU, and the Commission in particular, and how the 'purely economic rationale for defence-industrial cooperation is being reformulated to include questions of strategic relevance' (Fiott 2015b). Or as underlined in a recent study by Hoeffler (2023, 6), that 'the Commission's goal is no longer a well-functioning market only but also capacity-building. Regulation does not take the form of legal market rules but of tangible EU money'.

Table 1 Arguments for European Commission involvement in defence matters[1]

Arguments	**Communications**
Fragmentation of the European market	1996, 1997, 2003, 2004, 2005, 2007, 2013, 2016, 2017, 2022a, 2022b, 2022c, 2022d
Pressure from US competition	1996, 1997, 2003, 2007
Enhance competition/ competitiveness	1996, 1997, 2003, 2004, 2007, 2013, 2014, 2016, 2017, 2021, 2022a, 2022b,2022d
Worsening security situation	2013, 2016, 2017, 2022b, 2022c, 2022d
Enhance civilian-military industrial synergies	1996, 1997, 2003, 2007, 2013, 2014, 2016, 2017, 2021, 2022a, 2022b, 2022c
Underinvestment in defence	2004, 2007, 2013, 2016, 2017, 2022c, 2022d

Current and future developments

These policy developments could therefore be seen as in line with the long-term ambitions of the Commission in the defence field (see Håkansson, 2021; Martins and Mawdsley 2021; Csernatoni 2021). Nonetheless, establishment of the European Defence Fund (EDF) has been a game-changer for the EU and the European Commission. According to Csernatoni (2021: 16):

> [w]hat actually matters is the fact that the EDF truly represents a fundamental change in the European defense communitarization process. Namely, this financial instrument marks an important shift in the Commission's institutional role as an empowered, nontraditional defense actor [...] as well as a strong intervention on a sector that was the exclusive preserve of the intergovernmental method and member states.

Since the launch of the European Defence Fund, the Commission has further strengthened its role in European defence-industrial cooperation, not least with the creation of the DG Defence Industry and Space (DG DEFIS). In 2021, DG DEFIS initiated a spin-in communication to strengthen cooperation between civilian and defence- and space-related industries in Europe (European Commission 2021). Commission officials have also strongly argued for the need to reduce critical dependencies, something that is also very clear from its 2022 defence communication and the communication on critical defence technologies (European Commission 2022a; 2022b). The EU officials working on the packages emphasise how the Covid-19 crisis

[1] Full list of Communications can be found in the reference list.

has only made these dynamics stronger (Interviews, European Commission officials, EEAS official April 2022).

Moreover, there has in the past been scepticism in the US about EU defence-industrial developments (Fiott 2019; Bergmann et al. 2022). The early communications from the Commission also clearly outlined the pressure on the EU market from the US defence industry (on how the Commission has used the transatlantic spending and technology gap in its argumentation since the 1960s, see Martins and Mawdsley 2021). However, there have been positive signs of better cooperation between the US and the EU in the field. The 2021 Communication on the Action Plan on Synergies between Civil, Defence and Space Industries states that: 'in a broader geopolitical context, the EU has pledged to develop a common transatlantic approach to protecting critical technologies in light of global economic and security concerns and work together on technology, trade and standards' (European Commission 2021). Moreover, in 2022, the EU and the US launched a dedicated dialogue on security and defence that has helped to improve relations (US Department of State 2021; Interview, European Commission official, September 2022). This relationship has been further strengthened by a joint approach and cooperation in response to Russia's second invasion of and war in Ukraine (Interviews, European Commission officials, September 2022).

The February 2022 Commission defence communication, adopted just before the start of the war in Ukraine, had already outlined a new ambition on the EU side and the EU's Strategic Compass, adopted just after start of the war, can be seen as taking work even further forward. Among other things, the EU member states agreed in the latter, which led on from the Commission's defence communication, on the urgency of spending more and better together to mitigate strategic dependencies and to jointly develop strategic capabilities in critical and strategic military domains. The Compass also sets out new Commission proposals to further incentivise cooperation, through the possibility of a VAT waiver to support joint procurement, the creation of new financing solutions and a possible reinforced bonus system in the EDF. The member states also agreed that there should be an annual defence ministerial meeting on defence capability development and to create a Defence Innovation Hub within the EDA (EEAS 2022).

After the invasion, the EU responded in unprecedented ways. It launched the toughest sanctions packages ever, and funded and delivered weapons to Ukraine through the European Peace Facility. The invasion also led the member states to rethink and adapt their defence plans and capacities. The European Council Summit in Versailles in March 2022 could be seen as a key one, as the Heads of State and Government tasked the Commission and the EDA to analyse gaps in European defence and propose new solutions. The importance of the Versailles Summit is also underlined in the EU Strategic Compass. In line with this task, in May 2022 the Commission and the EDA published a communication on *Defence Investment Gaps Analysis and Way Forward* (European Commission 2022c), which outlined several new initiatives at the EU level. Most notable were a proposal on setting up a short-term instrument – the European Defence Industry Reinforcement through a common Procurement Act (EDIRPA), which will run from 2023 to 2024 – to provide €500 million to support joint procurement by the EU member states. While limited by the extent of overall EU budget expenses linked to Covid-19 and the effects of the war in Ukraine, this nonetheless broke the 'procurement-taboo' and could serve as an example for more ambitious future proposals. As Commission Vice President Margarethe Vestager argued when the proposal was presented: 'the proposal for the EDIRPA Regulation is a historic milestone in establishing the EU Defence Union, increasing the security of EU citizens and making the EU a stronger partner for our allies' (European Commission 2022e). The Commission will also present a proposal on a European Defence Investment Programme (EDIP) regulation in 2023 to create a vehicle for VAT exemption on collaborative procurement projects. It also envisages a new joint EU defence programming and procurement function, building on its earlier work on the EDF and the new short-term EDIRPA instrument (European Commission 2022c).

Furthermore, in the short term, and as preparatory work for the European Defence Industry Reinforcement through a common Procurement Act, the Commission (Secretariat-General and DG DEFIS), the EDA, the EEAS and the member states have set up a Defence Joint Procurement Task Force to support and coordinate the short-term procurement needs of the member states in the light of the new pressing security situation. This is also intended to reduce conflict over orders among member states and to avoid price spirals (European Commission 2022c; 2022d). The Task Force has consulted all the member states and 'engaged with those most interested to collect and aggregate their most critical and urgent procurement needs, and explore potential interest in future joint procurement projects, including under the future European Defence Industry Reinforcement through Common Procurement Act' (EDA 2022). As part of its 2023 work programme, the Commission has also outlined that:

> The cruel reality of war confirms the need to ramp up EU efforts in the area of security and defence. Following up on the EU Strategic Compass, in 2023 we will present the EU space strategy for security and defence as well as the updated EU maritime security strategy. We will also launch a dialogue with the European Defence Industries on how to bring about production increases to fill existing gaps in European armament stocks. (European Commission 2022f)

Moreover, in an unprecedented decision in March 2023, the EU decided to take a 3-track approach to support Ukraine with much-needed artillery ammunition. The plan includes spending €1 billion to reimburse member states for donated artillery ammunition, with the ambition of speeding up the overall delivery. Secondly, the EU (through the EDA or national processes) will jointly procure 155mm ammunition for Ukraine at a cost of €1 billion. Thirdly, the Commission in May 2023 put forward the Act in Support of Ammunition Production

(ASAP) to ramp up production capacity for defence equipment in Europe. The ambition is to deliver one million rounds of artillery ammunition to Ukraine this year, and diplomats have estimated that 250,000 rounds will be delivered before the end of May 2023 (Council of the European Union 2023; EDA 2023; *Politico* 2023; European Commission 2023).

New steps forward: time to take a leap for European defence

While these are promising steps, work must be taken even further forward. For too long, European countries have underinvested in their defence capabilities. While the defence budget has been rising in recent years and has been further strengthened since the launch of Russia's war in Ukraine, European countries still lack critical defence capabilities. Moreover, the European defence market is deeply fragmented and EU member states have not lived up to their earlier decisions and agreed benchmarks. For instance, the member states have failed to live up to their benchmark on collaborative spending (a commitment of 35%), which today accounts for only 18% of their total spending (European Commission 2022d; CARD 2022). Moreover, there is a risk that continued national spending on defence will only increase the fragmentation of the defence market in Europe. The EDIRPA proposal (European Commission 2022d) notes that choices made on short-term acquisitions will have longer-term impacts on the market strength of the European Defence Technological and Industrial Base and on opportunities in the coming decades. A further risk is that uncoordinated orders will drive up prices. This, together with an increasing rate of inflation, would reduce the impact of new defence spending in Europe (Fiott 2022; European Commission 2022d).

That said, the EU has clearly taken steps to improve European defence cooperation. To further improve the state of European defence, however, the EU and its member states will need to continue to move forward. First, the member states must start to live up to the commitments outlined in the EDA, and their obligations on Permanent Structured Cooperation (PESCO) and to NATO. Second, the member states must ensure that they fully utilise (and learn lessons from) initiatives such as PESCO, the EU's Coordinated Annual Review on Defence and the European Defence Fund and implement the new proposals in the 2021 synergies communication, the EU Strategic Compass and the Commission/EDA May 2022 communication. While all of these are promising initiatives, however, the most important aspects are political will and future ambition. Many PESCO projects, for instance, have made little or no progress and, if they cannot be moved forward, should be terminated. Moreover, member states clearly need to account for the new EU tools in their national planning processes. The importance of aligning national and European processes is something that is discussed in the Strategic Compass, which states that the member states should 'ensure that all EU defence initiatives and capability planning and development tools are embedded in national defence planning' (EEAS 2022).

Russia's war in Ukraine has also led to a strengthening of the Brussels-based actors. This could be seen as part of the

Commission's new geo-economic agenda (see also Helwig and Wigell 2022; Biscop et al. 2022; Olsen 2022; Helwig 2019). In line with this new geo-economic push, there will be a new initiative on a critical raw materials act, something that has been highlighted as important for the European defence industry (European Commission 2022c; 2022d; 2022f). The Commission is also looking into revising the EU's foreign direct investment (FDI) screening regulation and will 'examine whether additional tools are necessary in respect of outbound strategic investments controls' (European Commission 2022f; on discussions on FDI screening and outbound strategic investments controls, see also Lundborg Reglér 2022). Moreover, the content of the Strategic Compass has also empowered the Commission with regard to issues such as cyber, space and hybrid threats (Håkansson 2022; Interviews, EEAS officials, April and September 2022; European Commission officials, September 2022). These new dynamics should be acknowledged and embraced by the member states.

Nonetheless, new ambitions and initiatives are still required to meet the needs of the current security situation. The short-term European Defence Industry Reinforcement through a common Procurement Act instrument should lead to the establishment of a new strongly financed long-term initiative to facilitate joint procurement. The May communication raises the idea of a joint EU strategic defence programming and procurement function, which 'would ensure joint comprehensive multiannual programming – building on the EDF multiannual perspective, refinement of needs and specifications – and act as a central purchasing body for EU joint procurement and support Member States in their joint procurements, including downstream from the EDF-funded projects' (European Commission 2022c). This needs to have a substantial budget. Moreover, in the light of the pressing security situation, the budget for the European Defence Fund and the Military Mobility project should be strengthened in the mid-term review of the Mulitannual Financial Framework.

To further strengthen European defence and support for Ukraine, the European Union should draw on its experience with the Next Generation EU to borrow on the capital market to support collaborative European defence projects and procurement. Proceeds could also be used to buy new defence equipment to send to Ukraine (see the discussion in Bergmann and Haddad 2022; Bergmann et al. 2022). Ideas on new common borrowing for defence are already being discussed within the EU but nothing concrete has materialised yet (Interviews, European Commission officials, September 2022). Greater responsibility and wider support for Ukraine from the EU member states is also needed, given the strong support from the US (Shapiro 2022; Bayer 2022).

The EU should also continue to strengthen cooperation with NATO, and a new EU-NATO declaration was sign in January 2023. And an updated procedure for the progress report between NATO and the EU is also expected. In addition, the EU should make use of the EU-US defence dialogue and the US-EU Trade and Technology Council to further strengthen the transatlantic dialogue on defence and geo-economic developments.

Another issue that must be addressed is the production capacity of the European defence industry. Increasing defence budgets, new industrial orders and the need to replace defence material put strains on the industry and the war in Ukraine has shown how the 'massive consumption of equipment, vehicles and ammunition requires a large-scale industrial base for resupply' (Vershinin 2022). The increased dialogue between the Commission and the European defence industry on how to increase production is therefore both necessary and welcome. Hopefully, as Nick Witney (2022) underlines, 'the shock of the Ukraine war, rising national defence budgets, and a European Commission in the driving seat could finally bring about true European defence integration and consolidation'.

Implications and recommendations for Sweden

During the Swedish Presidency of the European Union in the spring of 2023, several new EU defence initiatives will be discussed and launched. First, the negotiations on the European Defence Industry Reinforcement through a common Procurement Act are set to be concluded under the Swedish EU presidency. Similarly, a proposal on the European Defence Investment Programme is also expected in 2023 (Lawrenson 2022).

In 2022 the Swedish Government received the results of an inquiry on a new equipment supply strategy for military defence (SOU 2022: 24). The inquiry identified several aspects that need to be addressed in the Swedish context, not least that European cooperation could be hampered by Sweden's strict export controls. Sweden should therefore seek discussions within the EU on export control rules (Lundborg Regér and Håkansson 2021). The EU Strategic Compass also states that the EU will 'bring forward ongoing work towards the streamlining and gradual further convergence of our arms export control practices for defence capabilities jointly developed, in particular in an EU framework' (EEAS 2022). The inquiry report states that the national Swedish process is not in line with the European process and that the Swedish Government 'should formulate a clear objective for what is to be achieved with Swedish participation in defence-related EU cooperation' (SOU 2022: 24). To increase participation in EU projects, Sweden should improve coordination and collaboration between the state and industry (for more proposals, see Lundborg Regér and Håkansson 2021; for an overview of the Swedish stance see Olsson et al. 2022).

There also needs to be close contact between the government and the national defence industry on the need and ability to scale-up production capability to meet the new security situation in both the short and the long term. Sweden should also investigate the possibility of increasing production of new defence material and equipment to send to Ukraine.

The new Swedish Government has expressed an interest in establishing a Centre of Excellence in Sweden focused on future technologies and communications (Mot. 2021/22:4039). Moreover, the need has been identified for a defence-industry strategy, a new national strategy on Swedish participation in EU defence-related projects and a defence-industry council to improve Swedish coordination and participation (Mot. 2021/22:3643). These could all be positive ideas, and there is a clear need to improve knowledge and expertise on EU development, and to strengthen competences in the Government offices, in national agencies and within the industry.

Sweden should also both strongly support politically and monitor implementation of the EU Strategic Compass. It is important that the Compass is fully implemented and that the EU becomes a stronger security actor.

Overall recommendations

- The short-term European Defence Industry Reinforcement through a common Procurement Act (EDIRPA) instrument should lead to the establishment of a new long-term substantially funded initiative to facilitate joint procurement at the European level.
- The production capacity of the European defence industry needs to be addressed and improved. The Act in Support of Ammunition Production (ASAP) is a good first step, but it should be further strengthened during the final legislative negotiation process.
- Member states and the EU institutions should have serious and open discussions about new forms of common borrowing/funds to spend in a collaborative way on European defence.
- The budgets for the EU Military Mobility project and the European Defence Fund should be increased in the mid-term review of the Multiannual Financial Framework in 2023.
- Member states must live up to the obligations and pledges entered into in the EDA and PESCO, and as part of NATO. National defence processes need to be updated to incorporate the new European tools and initiatives.
- In line with the new 2023 EU-NATO declaration the cooperation should be further strengthen between the two organisations.

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