



## From Community to bilateral: an opportunity for European Defence industries?

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**Budget cuts in the European defence sector are reaching a critical threshold both in the armed forces and in the defence industries. European integration, traditionally regarded as a means of pushing back the frontiers set by declining resources of member States, has in turn broken down. Pro-European views have faded away behind the supremacy of national logic. With this in mind, the London agreements drawn up between France and the United Kingdom - and the subsequent signature of bilateral agreements - seem to offer an ideal opportunity to revive or prolong the industrial bridge-building policies of the 1990s. More than ever, the existence of transnational groups is in fact proving to be a guarantee of the existence of a solid, efficient defence industry in Europe.**

Europe is becoming further and further embedded in an economic and political crisis, whilst national isolation, budget cuts and even staff cutbacks in the civil service seem to be the order of the day. Defence budgets and military strength are following the same pattern. Yet if we compare the changes in defence expenditure around the world, Europe is clearly lagging behind. European industries may well be amongst the most efficient in the world at the moment, but the gap between Europe and its new competitors is narrowing and as a result of the budget situation in European countries, they can no longer carry out major programs solely on a national basis. The issues at stake for each country and for Europeans in general are just as significant as the efforts that need to be made. An efficient defence industry is not only an instrument of sovereignty in an uncertain world, but also a creator of wealth and of employment and a stimulant for establishing centres of excellence.

## Budget cuts and critical threshold

Most defence budgets in Europe are suffering major reductions. In France, there is talk of a decrease of 3.6 billion over three years. The UK defence budget, which stood at 44.5 billion Euros excluding expenditure connected with external operations in Afghanistan and Iraq, is about to be cut by 8%, instead of the 10 to 20% initially requested by the Chancellor of the Exchequer. In Germany, the net defence budget is expected to be reduced from 31 billion Euros in 2010 to 30 billion in 2011 and 27 billion in 2014. Only a few countries are so far escaping the general trend. Finland for instance is planning an annual increase of 2% in defence expenditure between 2011 and 2015, and the Polish Defence Minister requested an increase of 7.1% in Poland's defence budget for 2011, to bring it to around 6.7 billion Euros (1).

The consequences of such budget cuts are even more alarming than the actual sums. In France, future cuts in military strength are likely to call into question certain aspects of the 2008 White Paper. In the same way, budget cuts delay the deployment of military equipment and the armed forces may even suffer a reduction in their capabilities. On 19<sup>th</sup> October 2010, when British Prime Minister David Cameron announced that HMS *Ark Royal*, the *Royal Navy's* aircraft carrier and flagship was to be dismantled, he deprived his country of the ability for fighter aircraft to take off from aircraft carriers until 2019 or even 2020 and beyond, since the first of two orders for new aircraft carriers has been put on hold. The idea of a "strategic break" may make sense in terms of budget and politics, but as Colonel Michel Goya reminds us, a "strategic break" is only conceivable if it goes hand in hand with a rational policy for the preparation and rapid mobilisation of national resources. However, such a policy would no doubt end up being rather expensive, and appears difficult to reconcile with a willingness to take action abroad." (2) And, we may well add, it would also be difficult to reconcile with the requirements of modern conflict and the constraints of equipment production.

Faced with operating expenditure and cost overruns produced by external operations, research budgets represent an inevitable adjustment variable. Over the last three years, R&T in the United Kingdom has dropped by 20%. According to figures provided by the European Defence Agency (EDA), the sums allocated to R&T by European countries have dropped by 8% within the last year. R&D – which integrates R&T – is no better off, standing at 9.7 billion Euros in 2006 and 8.4 billion in 2009 (3). And yet research is a guarantee of excellence, ensuring the efficiency of future equipment and, when faced with a drop in domestic orders, industrialists are more and more reticent about using their capital to develop products with little or no prospects. Land robotics in France is characteristic of the situation: the State invests in studies every year – albeit sparingly – but given the lack of commercial prospects and sales, industrialists are more and more reluctant to carry on work without a return on their investment, and several European countries are therefore turning to the Israelis.

The next few years look just as bleak. The only remaining certainty is of budget austerity and the necessity to seek new export opportunities or niche markets, within a context of increasing competition in the form of new arrivals such as the South Koreans. "There is a simple alternative", as we were reminded last October on the subject of naval operations by Laurent Collet-Billon, French General Delegate for armament. Either European industrialists identify sufficient points of common interest to join forces and strengthen their positions, [...] or they decide to go it alone and face the market and the competition." The inevitable consequence of which would be that industrialists in emerging countries would catch up with their European counterparts.

## The failure of European integration

European integration is traditionally regarded as a means of pushing back the frontiers of natural resources by pooling purchasing procedures and capacities. However, one cannot fail to notice that despite the Lisbon treaty and the success of agencies such as FRONTEX, which is in charge of coordinating operational co-operation between European Union Member States in the field of border security, the hopes raised were not followed by the results envisaged by its advocates.

Permanent structured co-operation, which was previously an object of debate, seems to have reached a dead-end (4). Indeed, its powerlessness is not specific to defence issues. In a state of crisis, both

economic and political, it is as if the very idea of Europe has broken down and been diluted within a structure lacking any geopolitical coherence and unable to do any more than dress the most serious wounds. Europeans are reacting on a case by case basis, but are unable to tackle the roots of the problem or implement any major reforms. Europe lacks a leader who could end the deadlock and move things forward. The Franco-German couple has lost its shine, but the Anglo-French couple cannot hope to replace it on account of United Kingdom's ambivalence towards the European Union – which is not ambivalence at all from a British point of view. Spain had requested a study on permanent structured co-operation prior to its Presidency of the European Union, but has since put the subject on hold in order to concentrate on the economic and financial crisis which is threatening the community's structure. Lastly, Europe sometimes appears to have become the scene of power games in which it is inadvisable to become isolated from the other players, coupled with the problem of inadequate *leadership*.

The situation is no better as far as industry is concerned. Despite the creation of EADS and MBDA and the signature of an agreement designed to create the political and legal framework required to facilitate the restructuration of the European defence industry by six European nations in July 2000, little or no progress has been made. Contrary to what was announced, i.e. recognition of an interdependency in supplying defence equipment, each country has taken care of reorganising its industries on a national scale to create national champions, no matter how fragile. In Sweden, Saab (aeronautics) is having trouble surviving with no civil activity and no programs, and Kockums (naval) is virtually bankrupt. In Spain and Italy, as well as in Switzerland and other countries, American companies have bought out their European competitors (5). Two figures illustrate the extent of the fragmentation: Europe has seventeen military shipyards, the United States only four, and seventeen armoured vehicle programs are currently in progress in Europe.

From this point of view, the economic crisis has merely revealed some deeper-seated logic. Rather than talking of Europe, we should talk of Europeans. It is all very well for industrialists to call upon Europe to become more committed, just like Patrick Boissier and Antoine Bouvier, Managing Directors of DCNS and MBDA respectively, at the most recent *Euronaval* fair. But the EDA, without a budget of its own or any basic skills, like the ESA in the case of space programs, has become an orphan of its age, unable to influence the community's destiny on account of its lack of power.

## Bilateral logic: a lesser evil

The Anglo-French agreement signed on 2<sup>nd</sup> November 2010 sanctions the failure – albeit temporary – of a certain idea of European defence, or in any case the type of defence that the British and French aspired to and set up in Saint Malo in 1998. Whereas the Saint Malo agreement was designed to be *avant-garde*, a precursor that would be open to other European countries, the "London agreements" aimed to exclude other European nations, focussing on bilateral projects. This was in fact one of the conditions set by the British before signing the agreement, or so it seems.

Although it is regrettable that European defence has made so little progress, bilateral agreements remain a means of continuing the process of integration whilst sidestepping national preferences. Opening up the markets within a community framework, with every European country contributing to research expenditure according to their individual resources, would be the ideal solution. But in the current circumstances, even this seems utopian. Given the fragmented industrial fabric and the appetite of industrialists on the other side of the Atlantic, it would be dangerous to completely open up the markets with no European preference, regardless of political considerations which are nonetheless applied by every country in the world with a defence industry. The American desire to take control of European manufacturers was emphasised by economist Jean-Paul Hébert in 2003 (6). As for the idea of joint financing for a European industry, not even NATO is coming forward. The authors of the report led by Madeleine Albright on the future of NATO pointed out that only six of the twenty-eight countries belonging to the Atlantic Treaty Organisation were meeting their commitment to devote at least 2% of their GDP to defence.

From a European point of view, the London agreements seem a lesser evil. They represent a chance to move forward under a more flexible model of integration whilst avoiding community inertia and the persistence of national preferences, and may help create a driving force within Europe. However, there is a risk of isolating the two signatories from the remaining European countries. With the exception of the nuclear industry and the problem of international maritime powers, most aspects of the London agreements would probably be of interest to other European partners. If France and Britain turn their backs on other countries, they could actually damage Europe, as the political climate within the European Union would inevitably be impaired, especially as there is little chance of an Anglo-French couple emerging to replace the Franco-German couple on account of British ambivalence towards the European Union. Even if the London agreements are not opened up to include additional countries, the Anglo-French rapprochement could still represent a model for all those in Europe who wish to make an effort in terms of capacity and attempt to pool the available resources, especially Germany which, like France, has the ability to form the basis of an integrated, competitive industry, particularly on land. Berlin's announcement of budget cuts in European multilateral programs and the difference in military culture between the two countries bordering the Rhine leave little hope of the two neighbours moving forwards together.

When it comes down to it, the establishment of co-operation in the defence industry is what is really at stake behind the bilateral logic of the London agreements, with a view to promoting joint industrial politics between European countries. Given the failure to progress on a community scale, these agreements mark the rehabilitation of a Europe of nations, as well as providing an opportunity to re-establish a European industry based on bilateral defence agreements, whilst acknowledging the persistence of national preferences and the dead-ends they lead to.

## Re-establishment of transnational groups

Budget restrictions, market fragmentation and an increase in the cost of the acquisition and maintenance of military equipment are jeopardising the future of national industries already dependent on aid. Domestic markets are no longer sufficient. In the absence of an industrial policy shared by European nations, the combined effects of budget pressure and scale factors will defeat the most fragile industrial players, initially affecting small and medium sized companies, no matter how essential a role they play in innovation. In this respect, re-establishing a European industry following the example set in the 1990s, in line with an *ad hoc* approach, seems to be the *sine qua non* condition of maintaining European skills and abilities.

We can see from the process initiated in the 1990s that integration has never occurred without a multilateral program to instigate it and above all to maintain it. The Anglo-French cruise missile program is what christened MBDA, and the Tiger and NH90 are what made Eurocopter. Projects continue, such as the drones or heavy helicopter programs. However, such potentially structure-building projects are rare and do not promote integration with a view to pooling project management. As far as the naval industry is concerned, the German company TKMS has just completed four Type 212A submarines for the German navy, and will be supplying one last vessel in 2013, but any further orders will probably have to wait until existing ships need to be replaced, i.e. over twenty years. There is a similar problem in Italy, where there will probably be no more national orders for fifteen years or so once two Type 212As have been commissioned in 2015 and 2016.

And yet solutions do exist. Co-operation programs can be based on export objectives. Another answer is to envisage partnerships involving maintaining equipment in operational condition. But many challenges remain. The danger of co-operation programs is that one of the two partners might stop playing the game if there are no clear rules or firm political commitment, as shown by the recent announcement of a split between DCNS and the Spanish company Navantia, who had been working together on the construction of Scorpene submarines since the 1990s. Similarly, arbitration will be required in future budgets in order to break with the trend of reducing the funding granted to co-operation programs of less political impact than national programs. Lastly, we need to take heightened national sentiments into account, not forgetting that the efforts made in the 1990s ended up being regarded as a French attempt to conserve its industries. France has a major part to play in

the process in federating other countries, increasing awareness and offering reassurance. France's allies must acknowledge that France's interests are also those of the European Union. France can help Europe become an independent player on the international scene equipped with high-tech industries, and make it a stakeholder within a solid, well-balanced transatlantic unit, with competitive, complementary industries that are on no account subservient.

Individual countries are of course on the front line. They can support the industrialists who emerged from the re-organisations of the 1990s and promote the re-establishment of partnerships between national players. But without the involvement of industrial players, all their attempts would be doomed to failure. Consequently, it is up to the latter to establish ambitious projects and to support the process initiated by pragmatic policies, without copying past errors on co-operation programs.

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(1) Figures quoted by Olivier Jehin, *L'économie européenne de défense malade de la crise*, IFRI, 4<sup>th</sup> November 2010, available on <http://www.ifri.org/downloads/ojeconomiedeladefense04112010.pdf>. More recent sources indicate figures for Germany of 31.9 billion in 2010 and 31.5 billion in 2011.

(2) Colonel Michel Goya, *Res Militaris. De l'emploi des forces armées au XXI<sup>e</sup> siècle*, Paris, Économica, 2010, p. 45.

(3) European Defence Agency, *Additional Defence Data 2009*, 11<sup>th</sup> January 2011, available on <http://www.eda.europa.eu/WebUtils/downloadfile.aspx?fileid=1262>

(4) Permanent structured co-operation is a system designed to enable Member States that meet certain criteria in terms of military capacity and have agreed to strict commitments on the subject to share common aims and desires. It is a unique, permanent system established according to a decision made by a qualified majority of the Council which requires no minimum number of Member States. This type of co-operation was regarded as one of the cornerstones of strengthening European defence given the differences between the budgets and capacities of Member States. On the same subject, see *Europe of Defence one year after the Lisbon Treaty: review and future prospects* (Thomas More Institute, October 2010, available on [http://institut-thomas-more.org/pdf/457\\_fr\\_NoteBenchmark5-ITM-Oct2010-Fr.pdf](http://institut-thomas-more.org/pdf/457_fr_NoteBenchmark5-ITM-Oct2010-Fr.pdf)). At the time, the debate regarding permanent structured co-operation in fact seemed to be ongoing...

(5) Gregoire Montory (pseudonym), *Pour une industrie de défense européenne. En finir avec les replis nationaux*, terra nova, 20<sup>th</sup> September 2010, available on <http://tnova.typhon.net/images/stories/publications/notes/100920%20-%20pour%20une%20industrie%20de%20defense%20commune%20europeenne%20-%20grgoire%20montory.pdf>

(6) Jean-Paul Hébert, *Le débat stratégique 1992-2005*, Paris, EHESS-CIRPES, pp. 181-184. Jean-Paul Hébert found that following industrial Europeanization in 1999 and 2000, American players started developing a bypass strategy to take control of the most fragile companies.

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