

STRATEGIC REVIEW

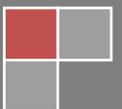
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EUROPEAN DEFENCE- INDUSTRIAL CONSOLIDATION AND THE TRANSATLANTIC RELATIONSHIP

□ Antonio Calcara

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Antonio Calcara is a Ph.D. Candidate at the LUISS Guido Carli in Rome. He is currently Adjunct Professor at the Vesalius College in Brussels and Visiting Lecturer at SciencesPo in Paris.



European Defence-Industrial Consolidation and the Transatlantic Relationship

Antonio Calcara

Ph.D. Candidate at the LUISS Guido Carli in Rome, Adjunct Professor at the Vesalius College in Brussels and Visiting Lecturer at SciencesPo in Paris

Email: acalcara@luiss.it

Introduction

Defence-industrial cooperation has gained central stage in the current European debate. In the wake of Brexit and security instability on the European southern and eastern borders, the relaunching of the Permanent Structured Cooperation (PeSCo) on defence and the new European Defence Fund (EDF) have been considered as “proofs” of a revived interest in defence cooperation. The coordination of these initiatives have the potential to increase EU countries' defence spending and to consolidate the long-term objective of a competitive European defence equipment market. In turn, developing a solid European technological and industrial base is an essential condition to ensure the so-called “European Strategic Autonomy”.

Therefore, the recent EU defence efforts should, ideally, have been appreciated by the United States (US) ally, given that the US administration has constantly emphasized the negative effects of EU countries' limited defence spending, especially within the NATO context. However, the latest European defence initiatives have received a sceptical reaction from some figures of the US administration. For instance, the American Ambassador to NATO, Kay Bailey Hutchinson, warned that Washington did not want PeSCo or a new EDF “to be a protectionist vehicle for EU”. According to the US administration, the recent EU defence initiatives would actually aim to introduce a “buy European preference” in defence procurement which could marginalize US companies from the European market.

This article aims to assess transatlantic relationship through the lens of defence-industrial issues. Specifically, I analyse the US concerns in this field and the possible implications for the transatlantic relationship. Moreover, I argue that it is inappropriate to consider the EU as a monolithic actor in this sector, given that European countries have different preferences regarding the consolidation of a European technological and industrial base. In this regard, I briefly consider Italy, Sweden and Poland's preferences towards the latest EU defence initiatives.

The New EU Defence Initiatives and the Spectre of a Fortress Europe

The “EU defence momentum” started in June 2015 when the European Council tasked the High Representative of the Union for Foreign Affairs and Security to draw up a Global Strategy on Foreign and Security Policy for the EU. In order to implement the priorities of the new Global Strategy on defence, EU institutions and member states have developed new important initiatives in this sector.

On 11 December 2017, the European Council reached an agreement to establish PeSCo in the defence sector. Unlike previous intergovernmental initiatives, PeSCo is a cooperative framework based on binding commitments to increase defence budgets and stimulate the joint development of military capabilities. Besides the periodic evaluation of these binding commitments, PeSCo will also house a series of projects aimed at supporting the development of European industrial capabilities. The other main initiative promoted in this sector is the EDF, a proposal presented in June 2017 by the European Commission and approved by the European Council and the European Parliament in February 2019. The EDF will consist in a research and in a capability window. The EDF research window will fund Research and Development (R&D) of defence-related products, while the capability window will help member states to jointly purchase military equipment and generate common investments for military procurement. The contributions for these instruments come mainly from the member states, but the programme itself will co-finance part of the development costs. In the next budget cycle, the EDF will be endowed with 13 billion euros: 4.1 billion will be allocated to research, while 8.9 billion will be assigned to co-finance capability development activities. The PeSCo and the EDF initiatives are also closely linked to the Coordinated Annual Review on Defence (CARD), which intends to institutionalize a systematic exchange among member states to help identify and fill gaps in military resources.

Some European countries have also decided to exploit this favourable climate to launch big-scale joint military projects. In this regard, French President Emmanuel Macron and German Chancellor Angela Merkel have already announced plans to develop a next-generation European fighter jet. Under the Franco-German political agreement, Airbus and France's Dassault Aviation have agreed to join forces for the development of a Europe's Future Combat Air System (FCAS), which is slated to replace current generation of Eurofighter and Rafale between 2035 and 2040. As highlighted by the CEO of Dassault Aviation:

“[O]ur joint roadmap will include proposals to develop demonstrators for the FCAS programme as of 2025. I am convinced that European sovereignty and strategic autonomy can and will only be ensured through independent European solutions. The vision that France and Germany have set forth with FCAS is a bold one and it's an important signal in, and for, Europe”.

In July 2017, Macron and Merkel also announced joint initiatives to develop major land combat, artillery and maritime patrol systems, while confirming their support for the Eurodrone programme, and launching structured cooperation between their cybercommands. Recently, Airbus and Dassault have revealed the first full-scale model of an envisioned European drone at

the Berlin Air Show, upping the visibility of a project meant to epitomize the continent's growing military profile. France and Germany awarded their industrial players, Airbus and Dassault, a first contract for a concept study worth €65 million (U.S. \$73 million), while Safran Aircraft Engines and MTU Aero Engines announced a partnership to supply engine propulsion.

The US Scepticism

As briefly pointed out in the introduction, the US reaction to the recent EU defence initiatives was sceptical. Katie Wheelberger, the US principal deputy assistant secretary for international security affairs, declared “we are supportive of it (referring to the EDF), as long as it is complementary to and not distracting from NATO's activities and requirements”. These comments were echoed by the NATO Secretary General, Jens Stoltenberg, who declared “it is important for European to state again and again that is not competition for NATO or an alternative to NATO (...) Some doubts remain”. A diplomatic cable, sent from Washington to Brussels, underscored US' worries that the EDF could duplicate NATO efforts and possibly marginalize US arms companies from future European contracts. For instance, one of the sources told to Reuters: “The two main concerns are that there is no duplication with NATO and that non-EU allies are not cut out of competitions for future weapons (...) if in the EU countries are joining forces to make acquisitions that are ultimately going to be used in the NATO context, there should be fair and open competition”. One of the main concerns of the US government and industries is to be excluded from the future EU investments. Indeed, according to the regulation, only EU member states can access the fund, while for other countries there is the possibility of participating in the cooperative activities, but only under certain conditions and without receiving funds. For what concerns the companies established in the EU, but controlled by non-European entities, in order to benefit from the EDF funding scheme, they need to provide guarantees to the European Commission regarding the governance structure and the transfer of sensitive information and technology.

Here is where Washington's economic concerns enter the picture. Indeed, the US firms have made huge investments in the European territory and their subsidiaries may not be able to fully benefit from the EDF, thus risking to be excluded from the upcoming collaborative projects. According to a recent report, the US presence in Europe has increased in recent years in a context of more open competition in the defence-industrial market. The report highlights that US subsidiaries in France, Germany, Italy, Sweden and the UK represent a 13% share.

Besides the US industries' concerns over its potential future penetration into the EU market, in recent years there has also been a growing market competition between the US and the EU firms. In 2017, the US accounts for the 34% of global arms transfer, confirming itself as the first arms exporter in the world. The five largest European suppliers – France, Germany, the UK, Spain and Italy – together account for 23% of global arms transfer in 2013-2017. However, the trend seems positive for European firms. France's arms export rose by 27% between 2008-2012 and 2013-2017. Several major deals were signed in 2013-2017, including 36 combat aircraft each for India and Qatar, and 12 submarines for Australia. Egypt was by far the largest recipient of French arms during that period. This was due to the French government's aggressive arms sales policy.

Indeed, when the US placed real restrictions on arms transfer to Egypt, Paris quickly attempted to fill this gap. As one French policy-maker cynically noted, “Obama was the (French fighter jet) Rafale's best salesperson”. For Germany, the combined arms sales of the three major German defence companies (Rheinmetall, ThyssenKrupp, Krauss-Maffei Wegmann) rose by 6.6 %.

The gap between the US and EU has been also exacerbated by the more recent US defence-industrial initiatives. On 15 November 2014, the US Department of Defence (DoD) adopted the Defence Innovation Initiative (DII), in order to maintain its military technology edge. Given the Europeans low spending on defence-related Research & Development and the significant barriers for technology transfer between US and Europe, the so-called “Third Offset strategy” raised important questions for European countries. For instance, it is not a case that France has developed similar initiatives. The former French defence minister Yves Le Drian announced a spending of \$750 million in defence innovation. On April 19, 2018, the US administration has also issued a new Conventional Arms Transfer (CAT) policy, which relaxed regulations of arms sales. The Trump administration has already moved forward on several controversial arms sales. Those include a push for \$7 billion in precision-guide munitions to Saudi-Arabia and the unblocking of \$3 billion in arms to Bahrein. This initiative is also linked to the Trump's administration new drone export policies, which is designed to make it easier for US companies to export armed drones.

European Countries' Preferences Towards Defence-Industrial Cooperation

Despite the numerous EU defence initiatives developed in the last few years, Washington's fears of a “Europe fortress” in defence procurement seem somewhat exaggerated. This is because the US establishment tends often to consider the EU as a monolith and not what it really is, namely a union of sovereign states with different economic and political structures and divergent preferences in the EU defence-industrial field.

In the wake of Brexit, France and Germany have been the main policy entrepreneurs in the European defence sector. For instance, the initiative to launch PeSCo came not from Brussels, but from France and Germany. However, other major European countries such as Italy, Sweden and Poland have consistently expressed concerns towards the new EU defence initiatives.

The Italian political and industrial establishment has raised several problematic aspects of the new EU defence-industrial initiatives. Italy tried to counter the "effective control" criteria in the EDF, promoted by the Franco-German establishment and which provided that the program could only be accessed by companies with over 50% of the ownership and effective control by Member States or their citizens. This poses fundamental problems for the Italian position, which supports the need to make it possible to access the Fund also to European companies controlled by non-European owners. Italy has also promoted an open approach to the participation of third countries or companies based in third territory, but obtaining a partial result: these subjects can participate in the programs but with some restrictions, and the cost of these activities will not be eligible for EU funding. This point is crucial especially with regard to the relations of the Italian “national champion”, Leonardo, with the British and the US markets.

A similar situation can be envisaged for the Swedish case. In September 2016, the Prime Minister, Stefan Löfven, greeted with great scepticism the French-German non-paper on European defence cooperation that was presented at the informal European Council meeting in Bratislava. At the time, the Swedish political debate revolved around the fear that the Franco-German proposal could result in the creation of a "European Army", a vision that is strongly rejected in Stockholm. Sweden has also shown very little interest to be involved in PeSCo. Stockholm is participating to only 6 out of 25 programmes. Furthermore, Sweden is mostly involved in very generic and inclusive projects, such as the European Medical Command, Military Mobility and the European Union Training Mission Competence Center. As noted in a recent report on the topic: "The Swedish government is deeply concerned that the restrictive approach to fostering European defence industrial partnerships promoted by France and Germany is creating unequal opportunities for Swedish industry as it might severely hamper Swedish access to the European Defence Fund".

Polish leaders have also been quite sceptical towards the new EU defence efforts. After months of criticising the launch of PeSCo, Warsaw became one of the last Member States to join the initiative. Similarly to the Italian and Swedish cases, the Polish political and industrial establishment is concerned that the new EU defence initiatives could disproportionately favour the biggest European industrial players. In this regard, it is interesting to note that the pattern of defence industrial cooperation split across central and eastern Europe. The Visegrad group is divided as regards PeSCo and the steady progress of EU defence cooperation. While Poland and Hungary are skeptical, Slovakia and Czech Republic have been proactive and also "early adopters of PeSCo projects". However, the group is also aware that the new EU defence-industrial initiatives could primarily favour first-tier states, which drives them either to relative isolation or to find partners to collaborate on projects. Therefore, the Visegrad countries are among the strongest proponents of making the UK and the US as involved as possible in defence issues. This reflects a relatively similar approach to transatlantic security and the perception of London and Washington as a necessary counterbalance to the industrial interests of Paris and Berlin.

Conclusions

In the wake of Russian's assertiveness on the Eastern Flank, Brexit and the election of Trump, there has been a significant activism to strengthen European defence cooperation. Many of the new initiatives developed in this sector focus on developing a European defence technological and industrial base and consolidating a European market for defence equipment. In this regard, some members of the US administration have raised concerns regarding the possible duplication with assets within NATO and the potential European protectionist posture in defence procurement that these initiatives may entail. This would have negative implications for the penetration of US military companies in the European market and, as a consequence, a potential negative impact on transatlantic relationship.

However, as emphasized in this article, the US' fears of being gradually excluded from the European defence market seem somewhat exaggerated. As shown in this brief analysis, Italy,

Sweden and Poland (among others) are constantly lobbying to involve the US in European armaments policy, in order to mitigate the perceived Franco-German bloc preponderance in this sector. Given these considerations, at least as far as military procurement is concerned, I expect a substantial continuity in the ability of US companies to penetrate the European market through bilateral agreements with local industries. Moreover, this analysis sheds light on some aspects that are often overlooked in the debate about European defence. Indeed, on European defence there is a wide discussion about systemic incentives that are pushing for greater cooperation in this field. However, systemic incentives clearly do not constitute sufficient conditions for more defence-industrial cooperation. As shown in this article, given the strategic nature of this sector and the EU Member States' different preferences towards European defence industry consolidation, it is difficult to implement a continental “one size fits all” approach.

*This article is based on a broader more theoretically grounded research project on which the author is currently working on.