Opinion of the European Economic and Social Committee on 'Proposal for a regulation of the European Parliament and of the Council establishing the European Defence Fund'

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1. **Conclusions and recommendations**

1.1. In the EESC's view, it is imperative that the EU Global Strategy and the Implementation Plan on Security and Defence be implemented consistently and in accordance with the provisions of the Joint Declaration of the EU and NATO of July 2016, as well as the United Nations principle of collective security.

1.2. Since 2017, the EESC has advocated the creation of a European Defence Union (EDU) and has supported the European Defence Action Plan, including the establishment of a common European Defence Fund. We believe that such strengthening of European defence is not intended to weaken but rather to reinforce NATO and transatlantic relations.

1.3. The EESC strongly supports the proposal for a Regulation establishing the European Defence Fund under the 2021-2027 MFF published by the Commission on 13 June 2018.

1.4. The EESC is calling for significant qualitative progress on European defence cooperation. Indeed, limited cooperation between Member States on defence generates duplications and results in a defence industry that remains highly fragmented. The lack of integration on the demand side of the market does not stimulate transnational cooperation between undertakings and further integration of the industry. This causes inefficient allocation of resources, overlapping industrial capabilities, technological gaps and a lack of new programmes, especially collaborative programmes.

1.5. The EESC supports the objective of strategic autonomy, with the development of key technologies in critical areas and strategic capabilities. This objective is strictly related to the need for sound assessment and coordination to ensure that those technologies can be mastered, retained and produced at European level, enabling the EU to take decisions and act autonomously if necessary.

1.6. The EESC believes that a *sine qua non* for the development of common defence capabilities is to strengthen the industrial and technological base of European defence.

1.7. The EESC emphasises that the European Union needs to work on maintaining, renewing and developing a highly skilled workforce and to secure workers with such skills.

1.8. The EESC proposes that the European Union step up its efforts to harmonise export rules within the Union.

1.9. The EESC strongly supports giving special attention to SMEs, also start-ups, including in the area of research and development for defence purposes.

1.10. The EESC would argue that the EU budget in support of defence activities should not replace or be a substitute for national defence spending, but rather boost and accelerate more and better defence cooperation. In the same vein, the EU budget for defence research should not be allocated at the expense of civil research in other sectors. Even if decisions on defence investment and defence development programmes remain the prerogative of Member States, the EDF could bring the EU added value by incentivising joint research on, and development of, products and technologies in the area of defence.

1.11. The EESC strongly believes that a more harmonised and streamlined European defence policy might bring efficiency gains by increasing the market share of the European defence industrial and technological base and by better distributing the products between states, regions and companies.

1.12. The European defence fund will only make a difference if it supports activities that really matter. Its work programmes should therefore be established on the basis of a robust European defence planning process that identifies the key capability priorities for Europe.

1.13. The EESC supports a policy of cooperation which will promote the involvement of SMEs as well as countries which are not signatories of the Letter of Intent, without, however, forgetting the skills they can add to the industrial and technological base of the defence industry.

1.14. The EESC supports the proposal to limit the benefit of European funds in the case of European companies controlled by the same entity, and to require guarantees where a third country participates in developments supported by the European Defence Fund.

1.15. The EESC supports the idea that European funds should be managed by the European Commission, but thinks that the European Defence Agency can usefully intervene in the definition of defence equipment needs and the Organisation for Joint Armament Cooperation (OCCAR), taking advantage of what have not always been happy experiences, and play its part in the management of programmes, as the duplication of skills in the field would be detrimental to the effectiveness of the system.

1.16. The EESC supports the idea that research and development must be submitted to an ethics committee. Ethical conditions must be spelled out clearly and assessed already in the evaluation of the proposal to ensure legal certainty and clarity.

1.17. The EESC is concerned about the future of cooperation with the UK after Brexit, and argues for strong security and defence which includes the UK's association with the EDF.

1.18. The EESC believes that our ageing continent feels threatened, displaying a tendency to blame and sometimes confuse problems like terrorism and migratory movements and lacking sufficient solidarity both within and between Member States, with a resurgence of nationalism and authoritarian regimes all around the European Union putting our democracy under pressure. An industrial policy tool as interesting as the European Defence Fund will not dispense us from further reflection on European defence policy.

2. **Presentation of the proposal**

2.1. The geopolitical context has become unstable over the past decade: we face a complex and challenging environment in which new threats such as hybrid threats and cyber-attacks are emerging and more conventional challenges are returning.

2.2. In the Joint Declaration of 25 March 2017 in Rome, leaders of 27 Member States and the European Council, the European Parliament and the European Commission stated that the Union would strengthen its common security and defence and foster a more competitive and integrated defence industry.

2.3. European defence faces significant market inefficiencies linked to untapped economies of scale (fragmentation of national markets with a single buyer) and duplication of resources at European level.

2.4. Demand comes almost exclusively from Member States, but their defence budgets, in particular for research and development (R & D), have seen substantial budget cuts in the past 10 years.

2.5. In 2015, only 16 % of defence equipment was procured through European collaborative procurement, which is a long way from the collective benchmark of 35 % agreed through the European Defence Agency.

2.6. The defence sector is highly fragmented across national borders, with substantial duplication and resulting inefficiencies in terms of failure to capture economies of scale and learning.

2.7. The existing situation is not sustainable and the development of major next-generation defence systems is increasingly beyond the reach of individual Member States.

2.8. The lack of cooperation between Member States further weakens the ability of the EU defence industry to sustain the industrial and technological capabilities necessary to preserve the EU's strategic autonomy and meet its current and future security needs.

2.9. On 7 June 2017 the Commission adopted a Communication launching the European Defence Fund, consisting of 'windows' for research and capability, accompanied by a legislative proposal for a Regulation establishing the European Defence Industrial Development Programme under the capability window.

2.10. The proposal for a Regulation establishing the European Defence Fund under the 2021-2027 MFF was published by the Commission on 13 June 2018.

2.11. The European Defence Fund is intended as an instrument to foster the competitiveness and innovativeness of the EU defence technological and industrial base, thereby contributing to the strategic autonomy of the EU. The instrument is designed to trigger cooperative programmes that would not happen without an EU contribution and to provide the necessary incentives to boost cooperation at each stage of the industrial cycle.

2.12. Collaborative projects with significant cross-border participation of small and medium-sized enterprises will be particularly encouraged. This will ensure that the EDF remains open to recipients from all Member States, regardless of their size and location.

2.13. The proposal provides for a date of application of 1 January 2021 and is presented for a union of 27 Member States.

2.14. While defence research falls under the scope of the Research and Innovation Framework Programme (*Horizon Europe*), the corresponding specific provisions for defence research — such as objectives, rules of participation and delivery mechanisms — are specified in this proposal.

2.15. The proposal seeks to ensure synergies with other EU initiatives in the field of civil R & D, such as security and cyber security, border control, coastguard, maritime transport and space.

2.16. There will be close links between the Fund and projects implemented in the framework of permanent structured cooperation in defence (PESCO).

2.17. The Fund will take account of the EU capability development plan (CDP), identifying the defence capability priorities, and the EU coordinated annual review on defence (CARD).

2.18. In this context, account may also be taken of relevant activities carried out by the North Atlantic Treaty Organisation (NATO) and other partners where they serve the Union's security and defence interests.

2.19. The Fund also takes into account defence activities implemented through the European Peace Facility, an off-budget instrument proposed outside the MFF.

2.20. The present proposal provides for the possibility of blending support under the Fund with financing backed by Invest EU.

2.21. The Fund should be used to address market failures or sub-optimal investment situations, in a proportionate manner and without duplicating or crowding out private financing, and should have clear European added value.

2.22. The Union will need to take greater responsibility for protecting its interests, values and the European way of life, in complementarity and cooperation with NATO.

2.23. To be ready to face tomorrow's threats and to protect its citizens, the Union needs to enhance its strategic autonomy. This requires the development of key technologies in critical areas and strategic capabilities to ensure technological leadership.

2.24. Decisions on defence investments and defence development programmes remain the prerogative and the responsibility of Member States.

2.25. The proposed policy approach is proportionate to the scale and gravity of the problems that have been identified. The initiative is limited to goals that Member States cannot achieve satisfactorily on their own and where the Union can be expected to do better.

2.26. The preparatory action on defence research was launched in April 2017 with a total budget of EUR 90 million over three years. It has started to bring initial concrete results, with the first grant agreements signed in 2018, but all projects are still ongoing.

2.27. The proposed European Defence Industrial Programme Regulation for 2019-2020 will have a budget of EUR 500 million and should be operational from 1 January 2019.

2.28. An open public consultation on EDF for all stakeholders was carried out from 13 January to 9 March 2018. Some criticism was expressed from an ethical perspective, but the directly affected stakeholders support the initiative. The rules on Intellectual Property Rights need to be adapted for defence.

2.29. The proposed budget allocation for 2021-2027 is EUR 13 billion (in current prices), of which EUR 4,1 billion is for research actions and EUR 8,9 billion for development actions.

2.30. Subject to confirmation of cost efficiency through a cost-benefit analysis, the Fund may be managed by an Executive Agency of the Commission.

2.31. A monitoring scheme is proposed to support performance reporting and evaluation. Results will become available progressively.

2.32. The Commission proposal for the 2021-2027 MFF set a more ambitious goal for climate mainstreaming across all EU programmes, with an overall target of 25 % of EU expenditure contributing to climate objectives. The contribution of EDF to the achievement off this overall target will be tracked through an EU climate marker system at an appropriate level of disaggregation, including the use of more precise methodologies where these are available.

2.33. The proposal provides for a date of application of 1 January 2021.

3. **General comments**

3.1. The EESC points to the requests already set out in opinions CCMI/149 (2017), CCMI/116 (2013) and CCMI/100 (2012). The EU Global Strategy and the Implementation Plan on Security and Defence also provide for important approaches to that end. In the EESC's view, it is imperative that these initiatives be implemented consistently and in accordance with the provisions of the Joint Declaration of the EU and NATO of July 2016 as well as the United Nations principle of collective security.

3.2. In view of the actual geostrategic circumstances and security developments, Europe must strengthen its security and defence capabilities. It is essential to have a clear understanding of the Union's common strategic objectives: this is still missing and urgently needs to be developed. It is a prerequisite for identifying the necessary defence capabilities that need to be underpinned by a sustainable European defence technological and industrial base.

3.3. The US withdrawal from the nuclear agreement signed with Iran in 2015, the crisis in Ukraine, Russia's worrying displays at the borders of the Baltic States and eastern EU border, the conflagration of the Libya-Iraq-Syria arc, the constant instability in the Sahel, the potential political and military confrontation between a US-Israel-Saudi axis and an Iran-Syria-Russia axis, all against a backdrop of cyber threats, a rise in authoritarianism in Europe, and the heightened unpredictability of US diplomacy: the EU's strategic balancing has rarely ever been so complex and worrying.

3.4. Security matters both within and around the EU are among the predominant concerns of citizens and heads of state alike.

3.5. At least four challenges need to be addressed by the EU, in the most consensual way possible: autonomy in decision-making, crisis anticipation, political influence, and the coherence between our interests and our democratic principles.

3.6. In 2017 the EESC advocated the creation of a European Defence Union (EDU) and supported the European Defence Action Plan, including the establishment of a common European Defence Fund.

3.7. The EESC has called for significant qualitative progress on European defence cooperation. Indeed, limited cooperation between Member States on defence generates duplications and results in a defence industry that remains highly fragmented. The lack of integration on the demand side of the market does not stimulate transnational collaboration between undertakings and further integration of the industry. This causes inefficient allocation of resources, overlapping industrial capabilities, technological gaps and a lack of new programmes, especially collaborative programmes.

3.8. The EESC supports the objective of strategic autonomy in identified critical capability and technology areas. This objective is strictly related to the need for sound assessment and coordination to ensure that those technologies can be mastered, retained and produced at European level, enabling the EU to take decisions and act autonomously if necessary.

3.9. The EESC endorses the choice to support the defence sector as a demand-driven industrial policy.

3.10. The EESC agrees that greater efficiency in national budgets should make it possible to achieve cover of entire European needs for defence equipment.

3.11. The EESC agrees that coherence between the programmes at European level should make it possible to increase the size of the European market served by the European defence industry.

3.12. The EESC has stated that a *sine qua non* for the development of common defence capabilities is to strengthen the European defence industrial and technological base.

3.13. The EESC emphasises that the European Union needs to work on developing a highly skilled workforce and to secure the workers with such skills.

3.14. The EESC proposes that the European Union step up its efforts to harmonise export rules within the Union.

3.15. The EESC strongly supports paying special attention to SMEs, including in the area of research and development for defence purposes.

3.16. The EESC has rejected opening up for defence purposes existing funds that serve economic or social objectives.

3.17. The EESC has rejected a special provision for national budgetary resources allocated for defence under the Stability and Growth Pact. Defence expenditure should not destabilise public finances.

3.18. The EESC has supported the creation of a Defence Fund with two windows covering both research and the development of capabilities. This could support the design of an integrated planning process for investments across the whole technology cycle. Procurement decisions remain in the hands of the Member States. A form of joint procurement, however, can enhance the efficiency of the demand side and contribute to the competitiveness and efficiency of the European defence industry. The EU budget in support of defence activities should not replace or be a substitute for national defence spending, but rather boost and accelerate more and better defence cooperation. In the same vein, the EU budget for defence research should not be allocated at the expense of civil research in other sectors. The aim of the EDF is to trigger cooperative programmes and, by supporting research and development activities, to provide the necessary incentives to boost cooperation at each stage of the industrial cycle. Even if decisions on defence investments and defence development programmes remain the prerogative of Member States, the EDF could bring EU added value by incentivising joint research on, and development of, products and technologies in the area of defence.

3.19. The defence industrial sector is not only of strategic importance for the security and defence of European citizens, but it is also a major contributor to the European economy and welfare with a total turnover of about EUR 100 bn/year and around 500 000 highly skilled people directly and indirectly employed. This sector is the source of cutting edge products, services and technologies where innovation and Research & Development (R & D) efforts are key to competitiveness.

3.20. The European defence industry as well as R & D spending are quite concentrated in the six Letter of Intent (LoI) countries (France, Germany, Italy, Spain, Sweden and the UK), accounting for 95 % of the investments, the bulk of SMEs and mid-caps as well as top companies. A more harmonised and streamlined European defence policy might bring efficiency gains through further specialisation of countries, regions or companies in certain technologies.

3.21. LoI countries dominate the European defence market in terms of the number of active companies and their arms sales. For example, in the UK, *BAE Systems* is the largest defence company. *SAAB* is the main Swedish aerospace and defence company, while the largest in France are *Dassault Aviation, Naval Group, Safran* and *Thales*. In Germany, Rheinmetall, ThyssenKrupp Marine Systems and Diehl are important companies. In Italy, *Leonardo* and *Fincantieri* represent the two main companies. *Airbus*, a trans-European company, ranks second in Europe after *BAE Systems*. Another relevant transnational company is MBDA, a joint venture of the three European leaders in aerospace and defence (*Airbus, BAE Systems* and *Leonardo*) active in missile and missile system manufacturing. And *KNDS*, owner of Nexter and KMW, is also becoming a trans-European company. Note that some of these companies are not exclusively operating in the defence market, which explains the varying ratios of sales to employees.

Looking at smaller companies, a recent IHS study identified almost 1 600 SMEs active in the defence sector in Europe and estimated the total number of SMEs in defence supply chains at 2 000-2 500. A number of these companies are dual-use in nature, engaged in both the civil and defence domains. In any case, SMEs play an important role in the defence industry and are a key enabler for competitiveness.

3.22. The European defence industry is not evenly spread across the EU. This suggests that increased military spending by EU Member States may not flow equally to all the Member States. If higher spending in one country flows to firms in other countries, this could result in new trade flows.

4. **Specific comments**

4.1. The European defence fund will only make a difference if it supports activities that really matter. Its work programmes should therefore be established on the basis of a robust European defence planning process that identifies the key capability priorities for Europe.

4.2. The EESC supports a policy of cooperation which will promote cross-border cooperation — the involvement of SMEs, also from states that are not members of the LoI, without, however, going back to the right-of-return policies that sometimes reinforced the duplication of skills.

4.3. The EESC supports the proposal to limit the benefit of European funds to European companies controlled by European interests and to require guarantees where a third country participates in developments supported by the European Defence Fund.

4.4. The EESC supports the idea that the granting of European credits should be managed by the European Commission, but thinks that the European Defence Agency can usefully intervene in the definition of defence equipment needs and the OCCAR, taking advantage of what have not always been happy experiences, and play its part in the management of programmes, as the duplication of skills in the field would be detrimental to the effectiveness of the system.

4.5. The EESC supports the idea that research and development must be submitted to an ethics committee. Ethical conditions must be spelled out clearly and assessed already in the evaluation of the proposal to ensure legal certainty and clarity.

4.6. The EESC supports the idea of European industrial sovereignty in Europe but still questions its political translation, as most of the European Union Member States see themselves as part of the Atlantic alliance, while many states remain attached to a national concept of sovereignty.

4.7. The EESC is concerned about the future of cooperation with the UK after Brexit, and argues for a strong security and partnership which includes the UK's association with the EDF.

4.8. Hit by globalisation, which is disruptive in many ways, Europeans are already aware of some of their mistakes and their illusions. Their biggest mistake is their inaction. The policy of strategic abstinence, which allowed us to focus on the economy and brought so much wealth for us during the Cold War and up to the turn of the century, has now become the main European stumbling block.

4.9. Europe has for a long time imposed its will on the world, first on its own and later with the USA. In a world where global warming and authoritarian regimes are growing stronger, the inequalities of development between countries but also within countries are becoming unbearable. Our ageing continent feels threatened, displaying a tendency to blame and sometimes confuse problems like terrorism and migratory movements, and is lacking sufficient solidarity both within and between Member States, in a context of resurgence of nationalism and authoritarianism putting pressure on European democracies. An industrial policy tool as interesting as the European Defence Fund will not dispense the European Union from political reflection on what we want to defend and how we want to defend it.

4.10. European defence is not solely about strategic threats, external interventions, military capacity, technological innovation and industrial excellence. As the greatest threat that Europeans face today is the challenge to European democracy itself, the common defence policy can no longer ignore this political dimension.

Brussels, 12 December 2018.

The President
of the European Economic and Social Committee
Luca JAHIER