



European Defense Trends 2012: Budgets, Regulatory Frameworks and the Industrial Base

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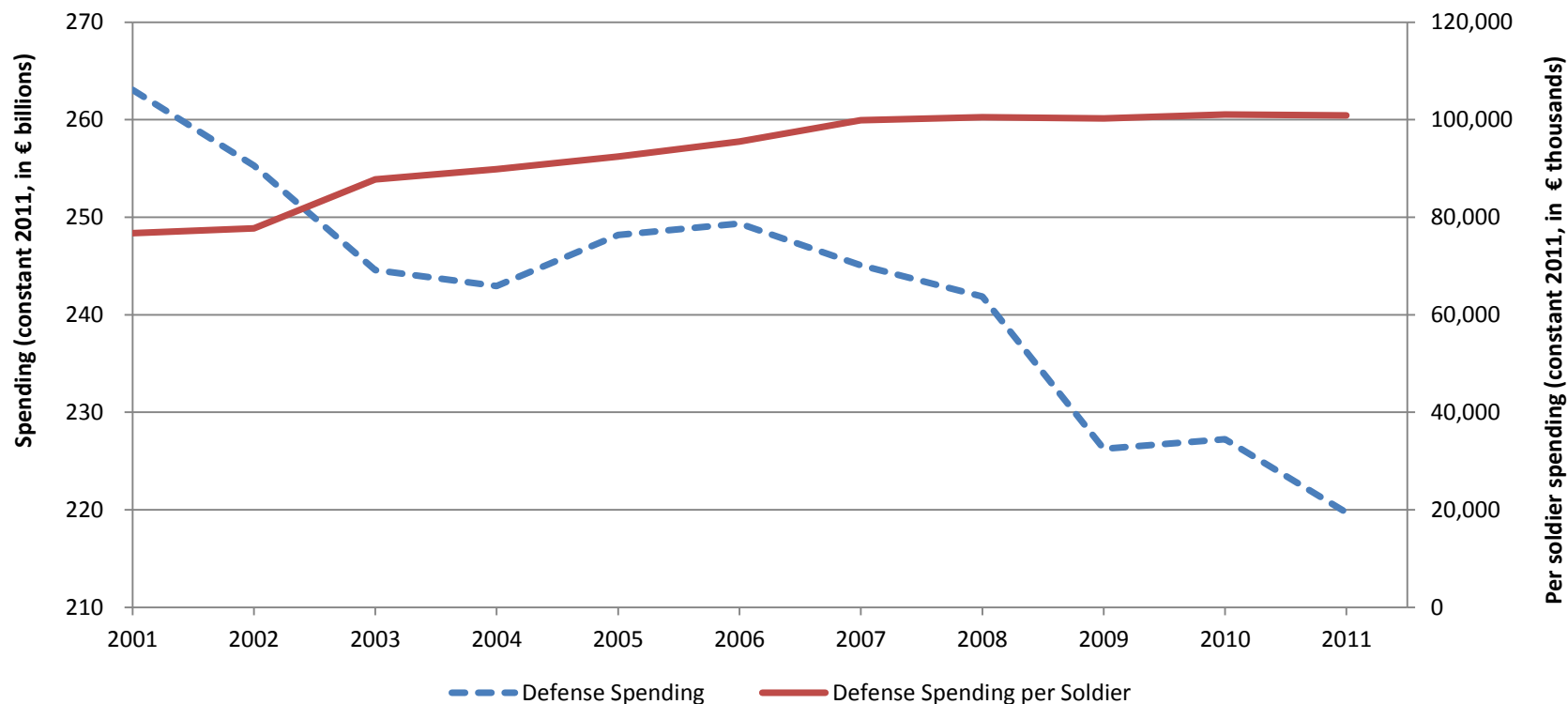
Outline

- **Methodology**
- **Demand side**
- **Regulatory frameworks**
- **European defense and security industrial base**
- **Trend analysis**
- **Future spending trajectories**
- **Options for reversing the course**
- **Areas for further research**

Methodology

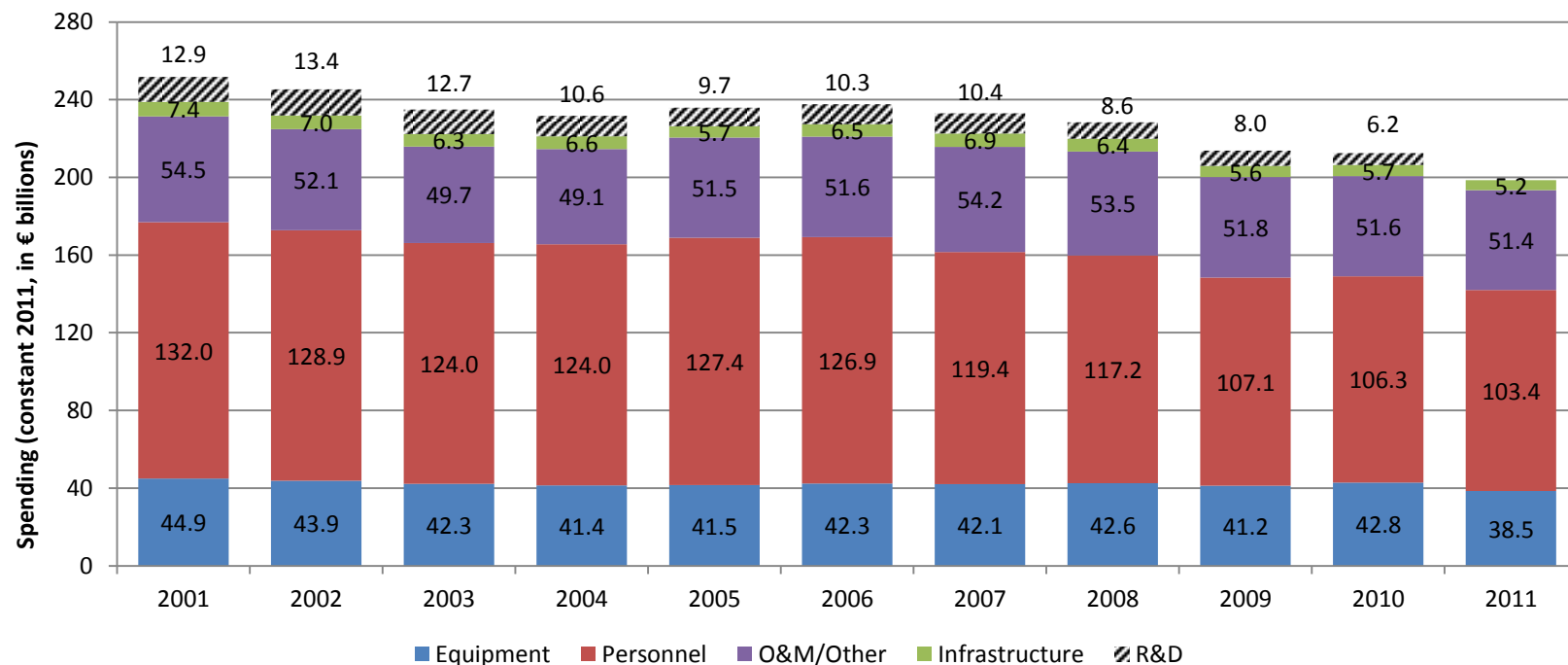
- **Scope**
- **Data sources**
- **Data analysis**
- **Defense spending categories**
- **CSIS ESDS Index**

Total European Defense Spending and Defense Spending per Soldier



Source: NATO Defense Expenditures; SIPRI Military Expenditure Database; IISS Military Balance; analysis by CSIS Defense-Industrial Initiatives Group.

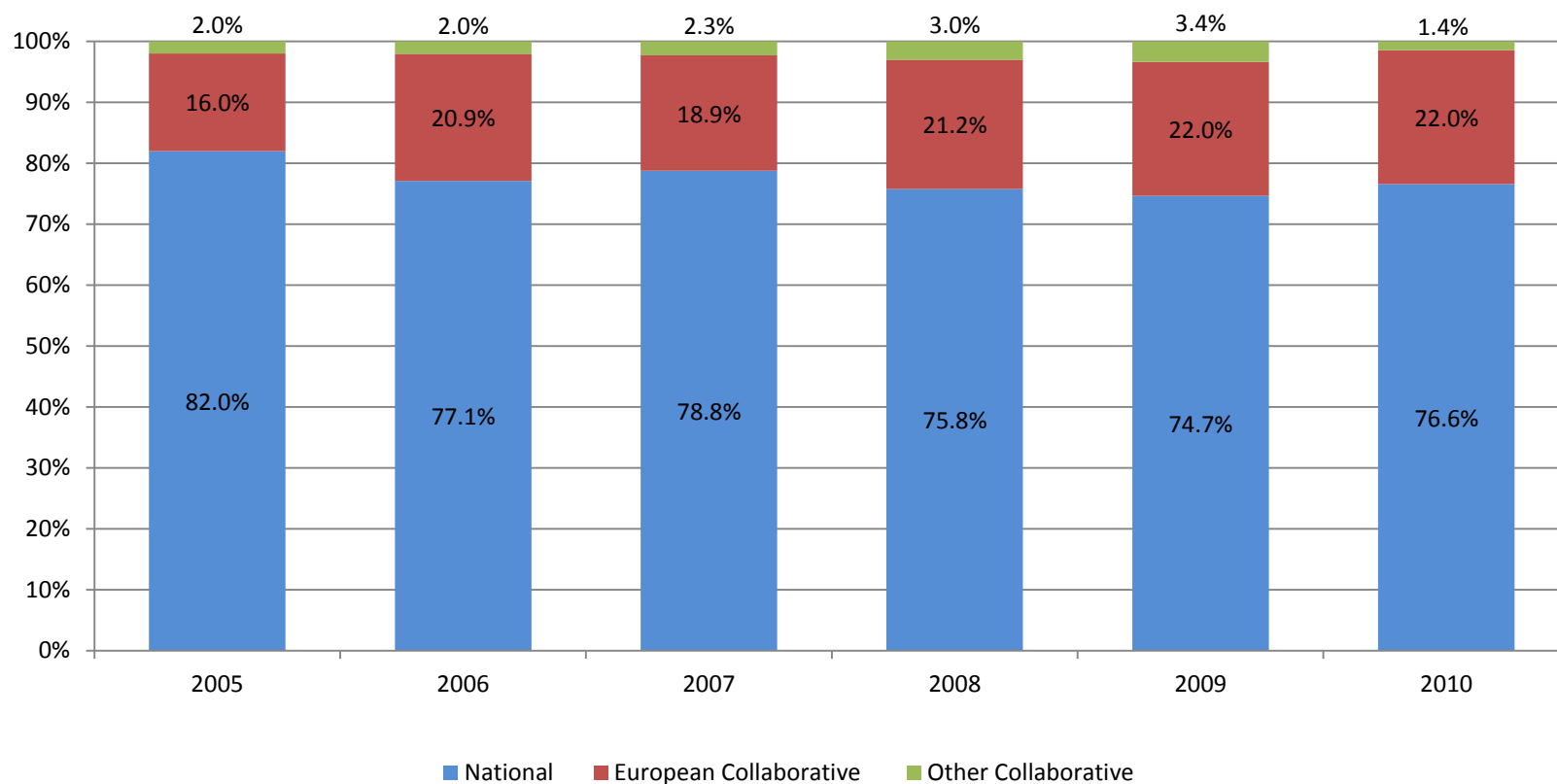
Total European Spending by Defense Spending Categories



Note: NATO budget sources do not provide a separate breakdown for R&D spending. They instead subsume the research portion of R&D in the O&M/Other category and the development portion of R&D in the Equipment category. To provide a separate breakdown for R&D spending, CSIS added OECD data on defense R&D. R&D spending is therefore accounted for twice in this chart, once directly in the R&D category and once combined in the Equipment and the O&M/Other categories. In addition, the combined category aggregates do not match the aggregate values displayed in Chart 1 as complete functional spending breakdowns are not available for all 37 countries. Only countries with complete time series data are included in the aggregates of the respective categories.

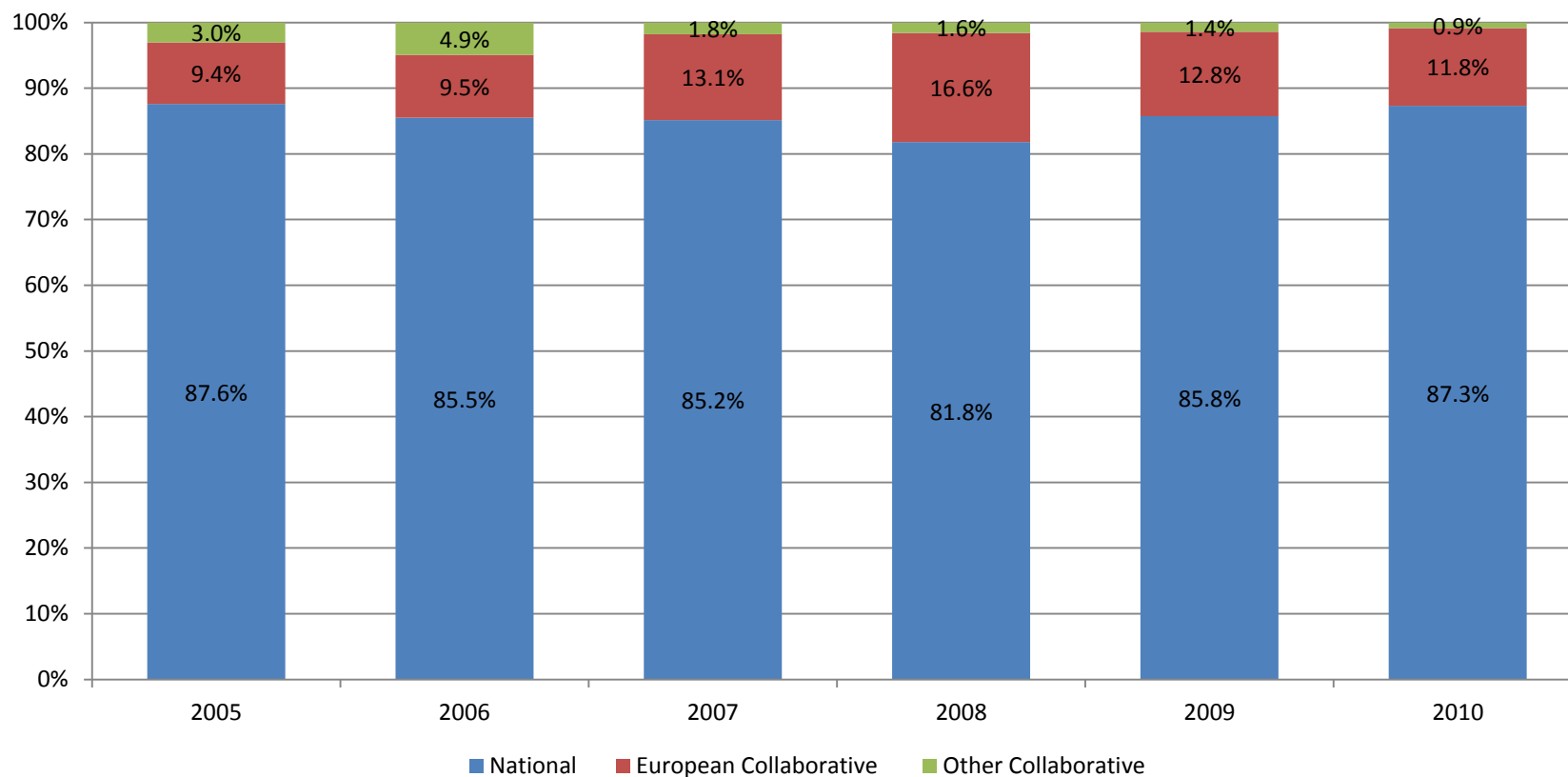
Source: NATO Defense Expenditures; OECD Main Science and Technology Indicators; analysis by CSIS Defense-Industrial Initiatives Group.

Defense Equipment Spending for EDA Member States



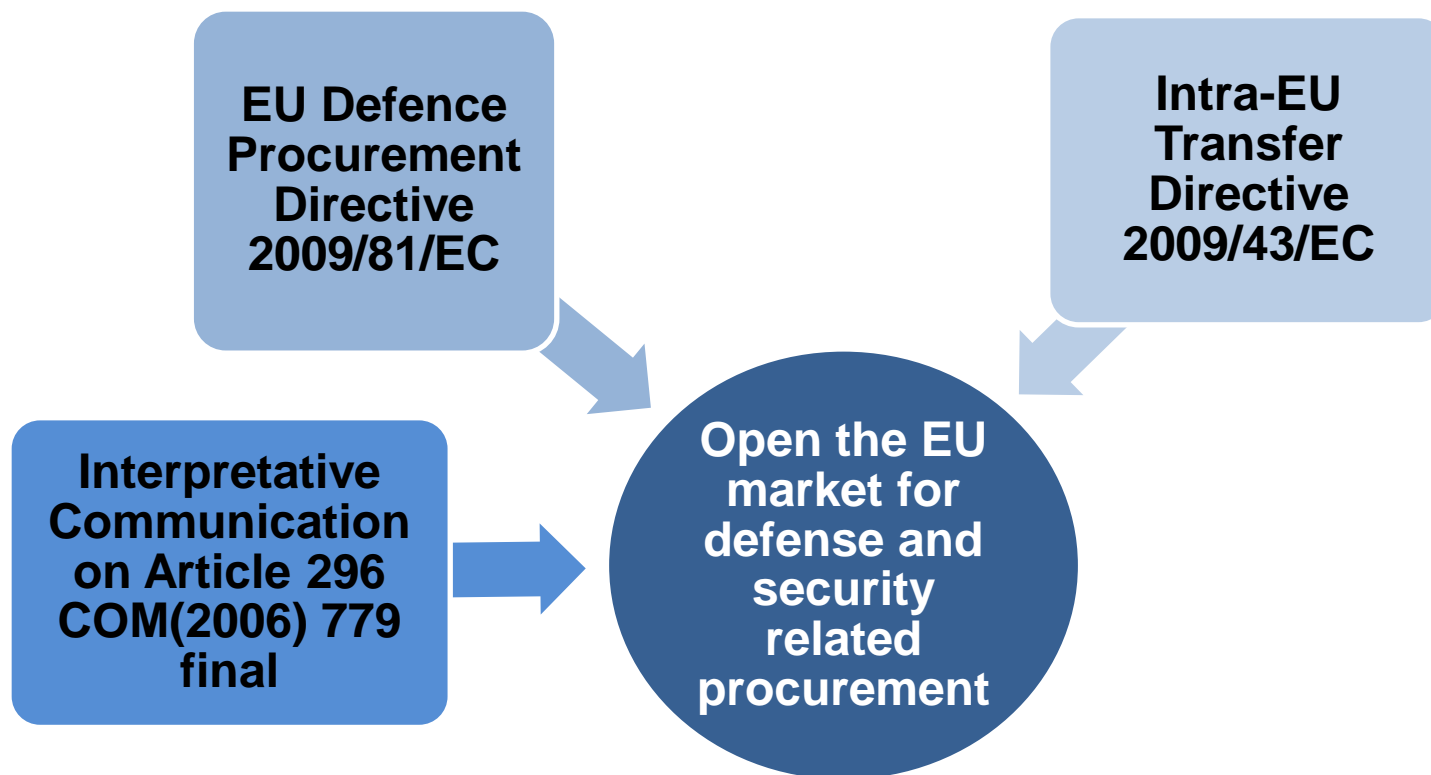
Sources: EDA Defense Data; analysis by CSIS Defense-Industrial Group.

Defense R&T Spending for EDA Member States



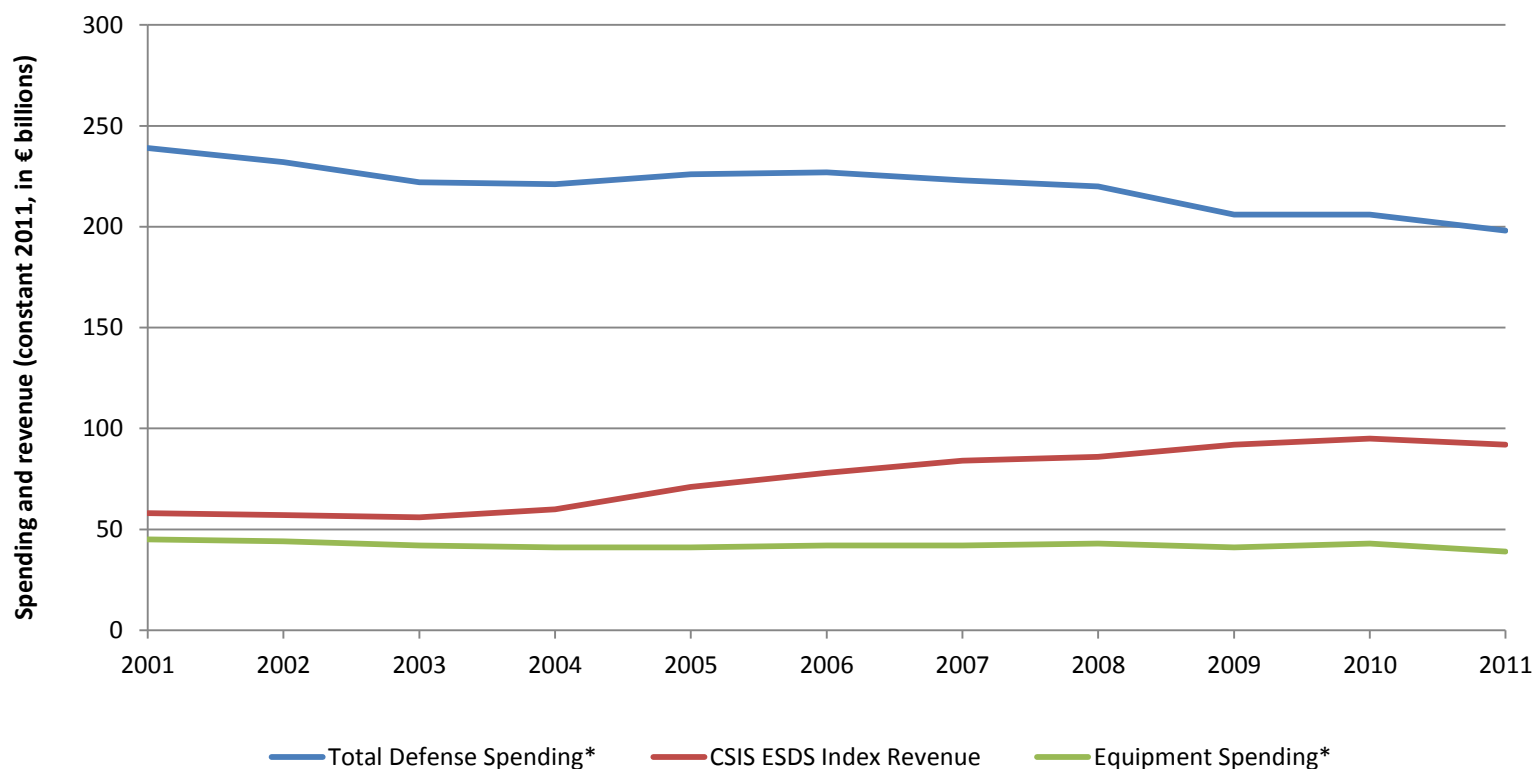
Sources: EDA Defense Data; analysis by CSIS Defense-Industrial Group.

Key European Commission Regulatory Reform Efforts



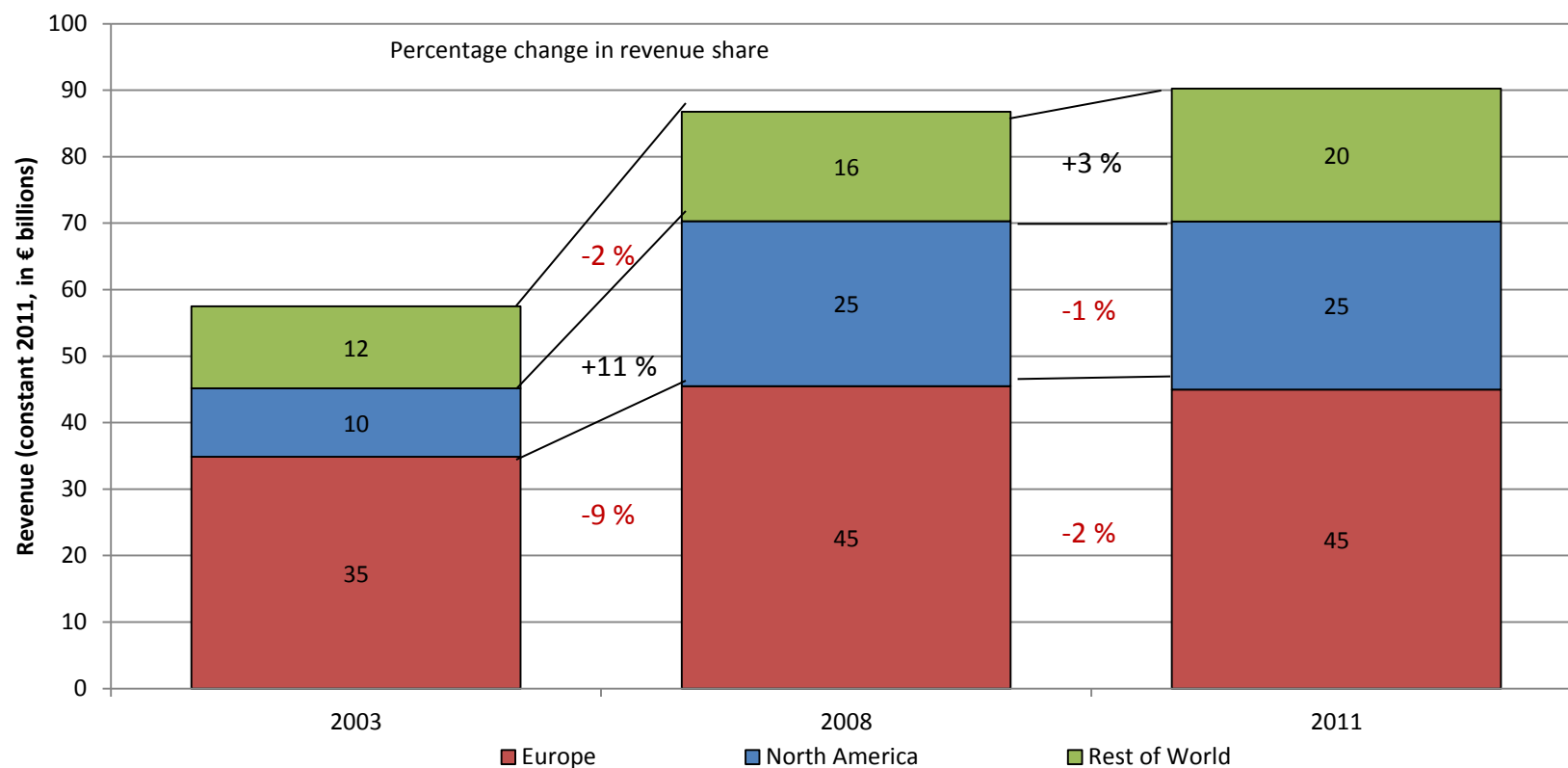
Source: Analysis by CSIS Defense-Industrial Initiatives Group.

CSIS ESDS Index Revenue, Total and Equipment Defense Spending



* Note: Only countries with a complete time series for total defense spending and Equipment spending are included.
Source: Bloomberg; NATO Defense Expenditures; analysis by CSIS Defense-Industrial Initiatives Group.

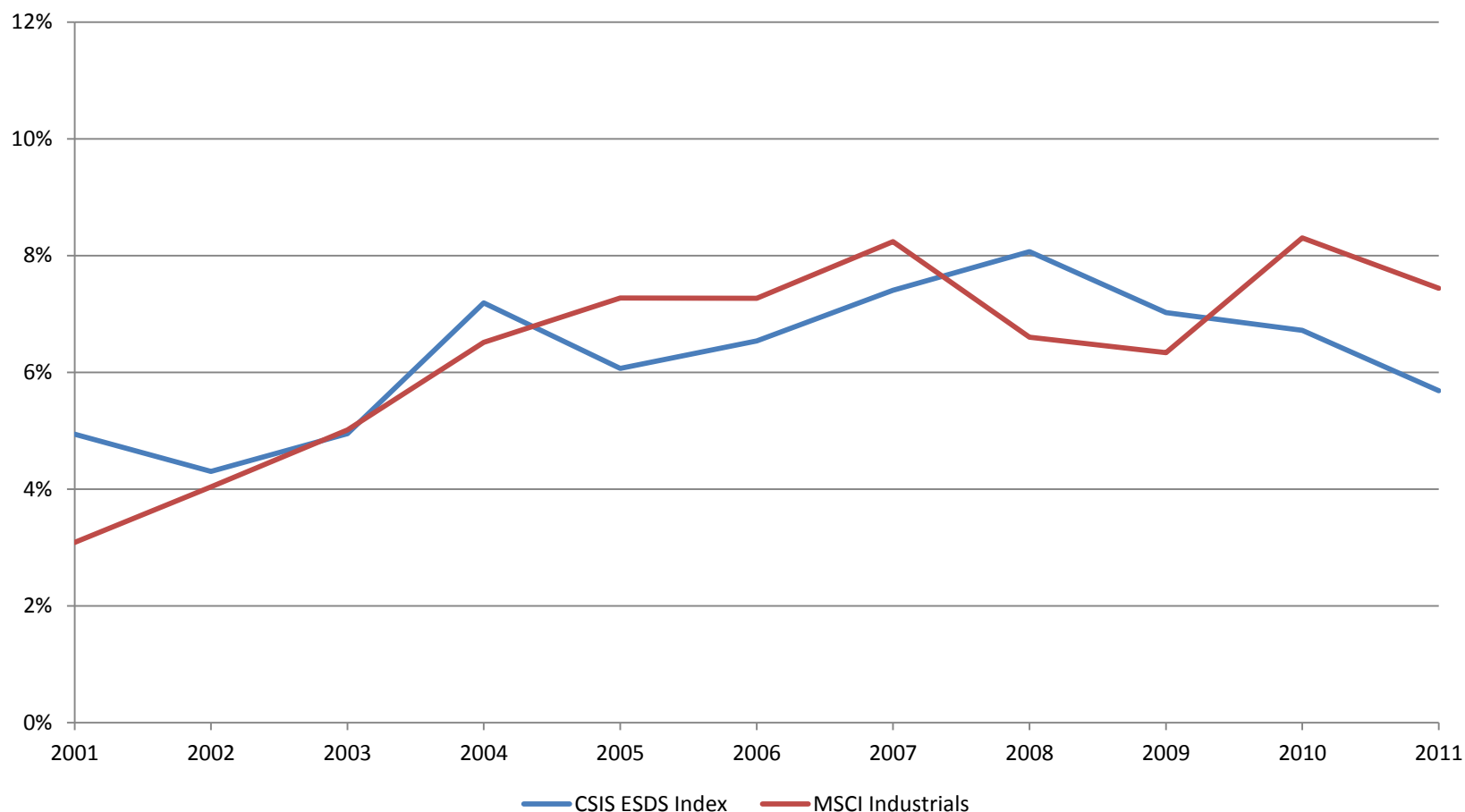
CSIS ESDS Index: Revenue by Geographic Origin



Note: Excludes the following companies due to lack of data in 2003: Comrod Communication, ZKT Lubawa, Simrad Optronics, Cohort, and Aselsan.

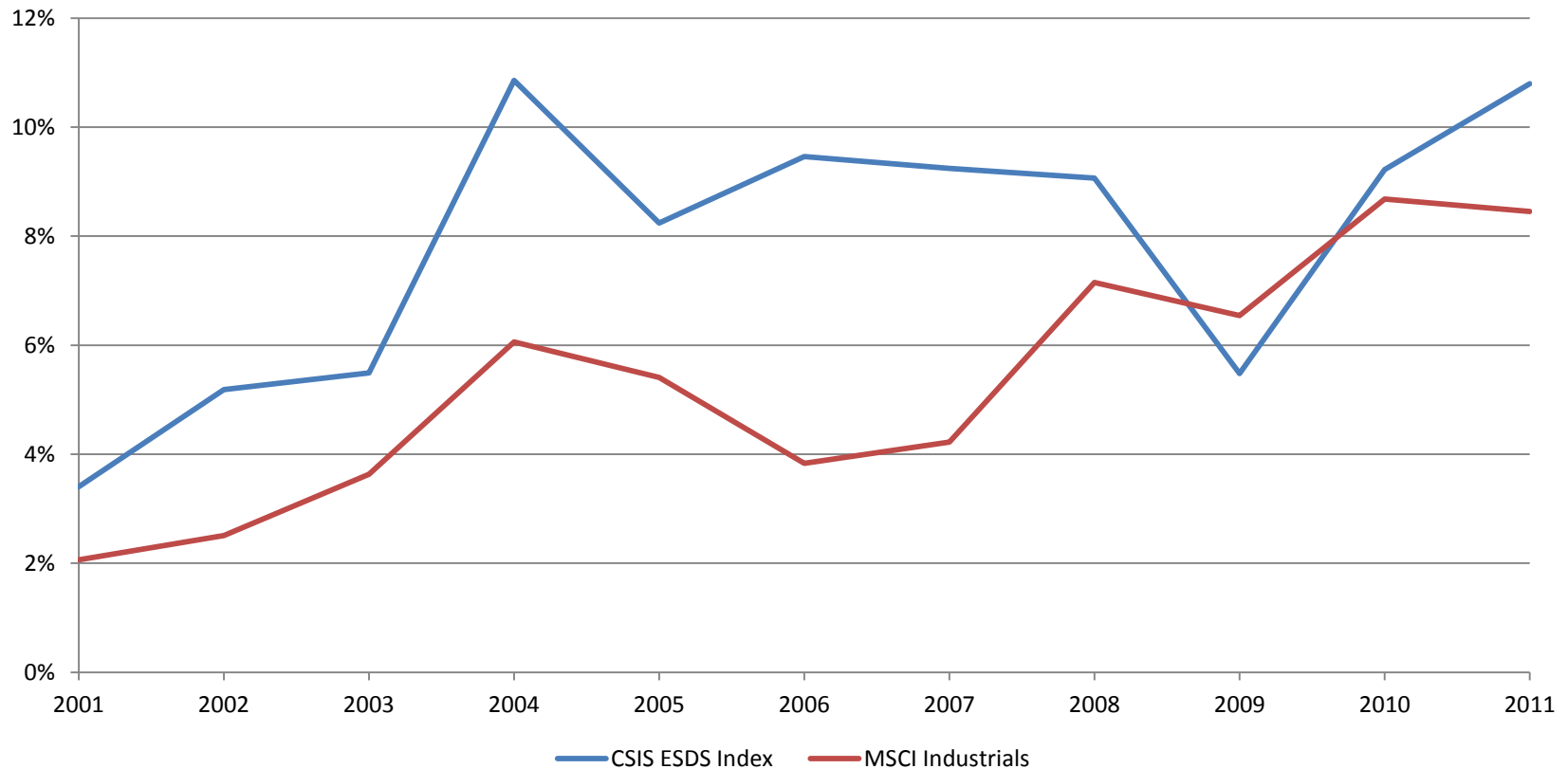
Source: Bloomberg, company financial reports; analysis by CSIS Defense-Industrial Initiatives Group.

Operating Profit Margin, Revenue Weighted



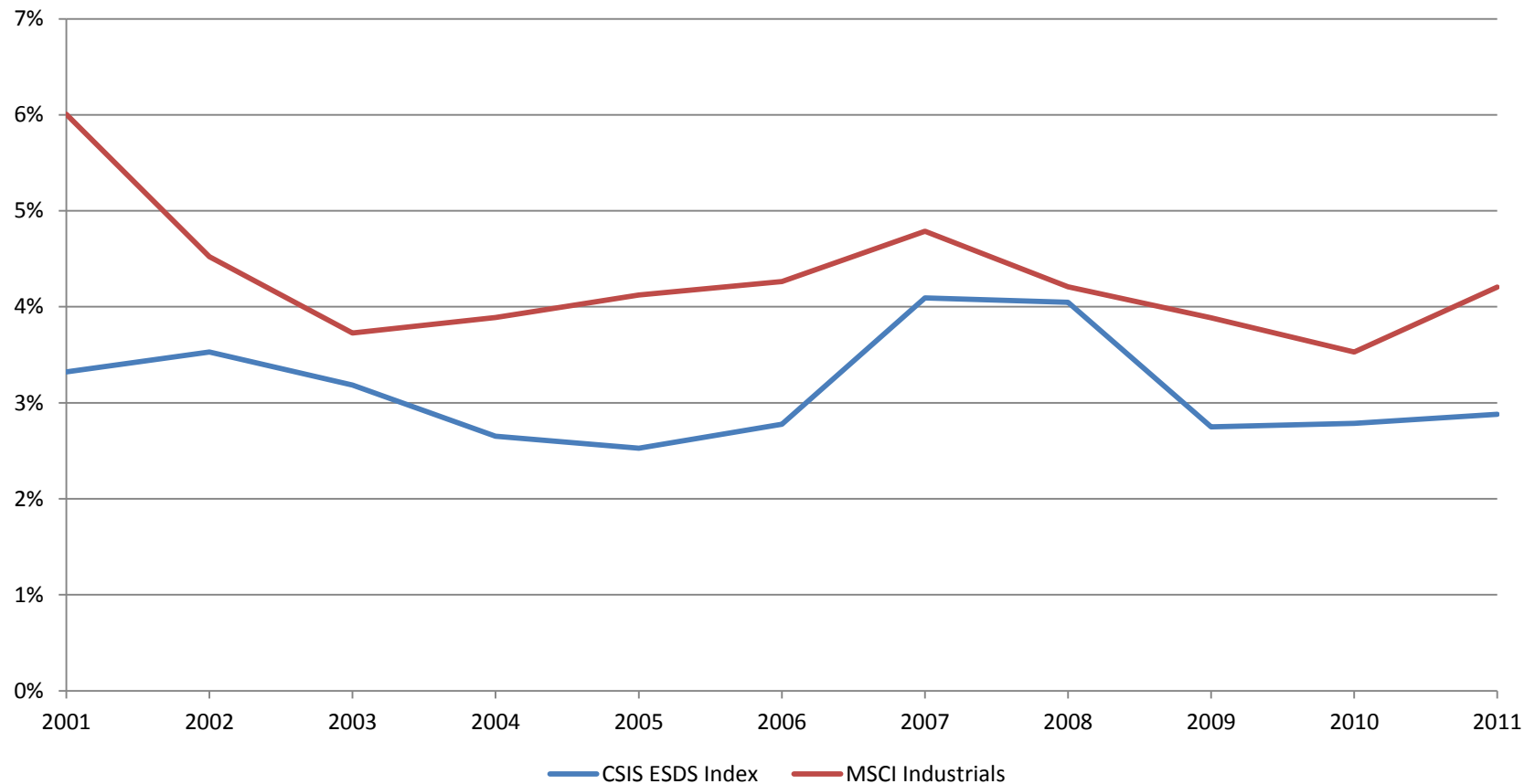
Source: Bloomberg; analysis by CSIS Defense-Industrial Initiatives Group.

Return on Invested Capital (ROIC), Revenue Weighted



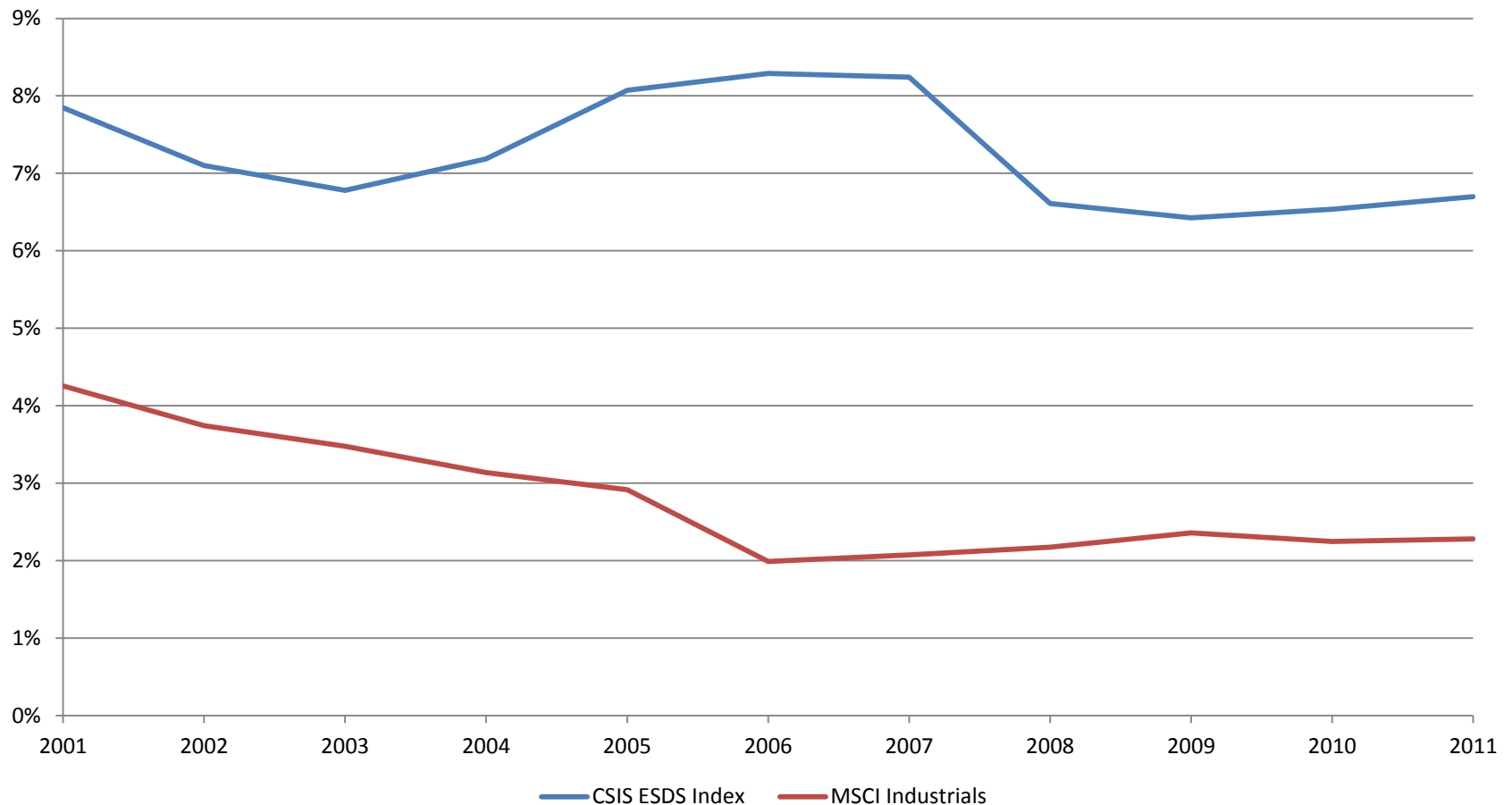
Source: Bloomberg; analysis by CSIS Defense-Industrial Initiatives Group.

Capital Expenditure, Revenue Weighted



Source: Bloomberg; analysis by CSIS Defense-Industrial Initiatives Group.

Research and Development Investment, Revenue Weighted



Key Trends

- **Force Structure Reductions Will No Longer Offset Budget Declines**
- **The Regulatory Environment Leads Drive for Market Defragmentation**
- **Future European Industrial Capabilities Depend on the Global Defense Market**

CSIS Total and Per-Soldier Spending Trajectories

CSIS Spending Scenarios

Total spending declines slowly (continues 2001-2011 CAGR of -1.8 percent)

Total troop numbers continue at the 2008-2011 CAGR of -3.3 percent

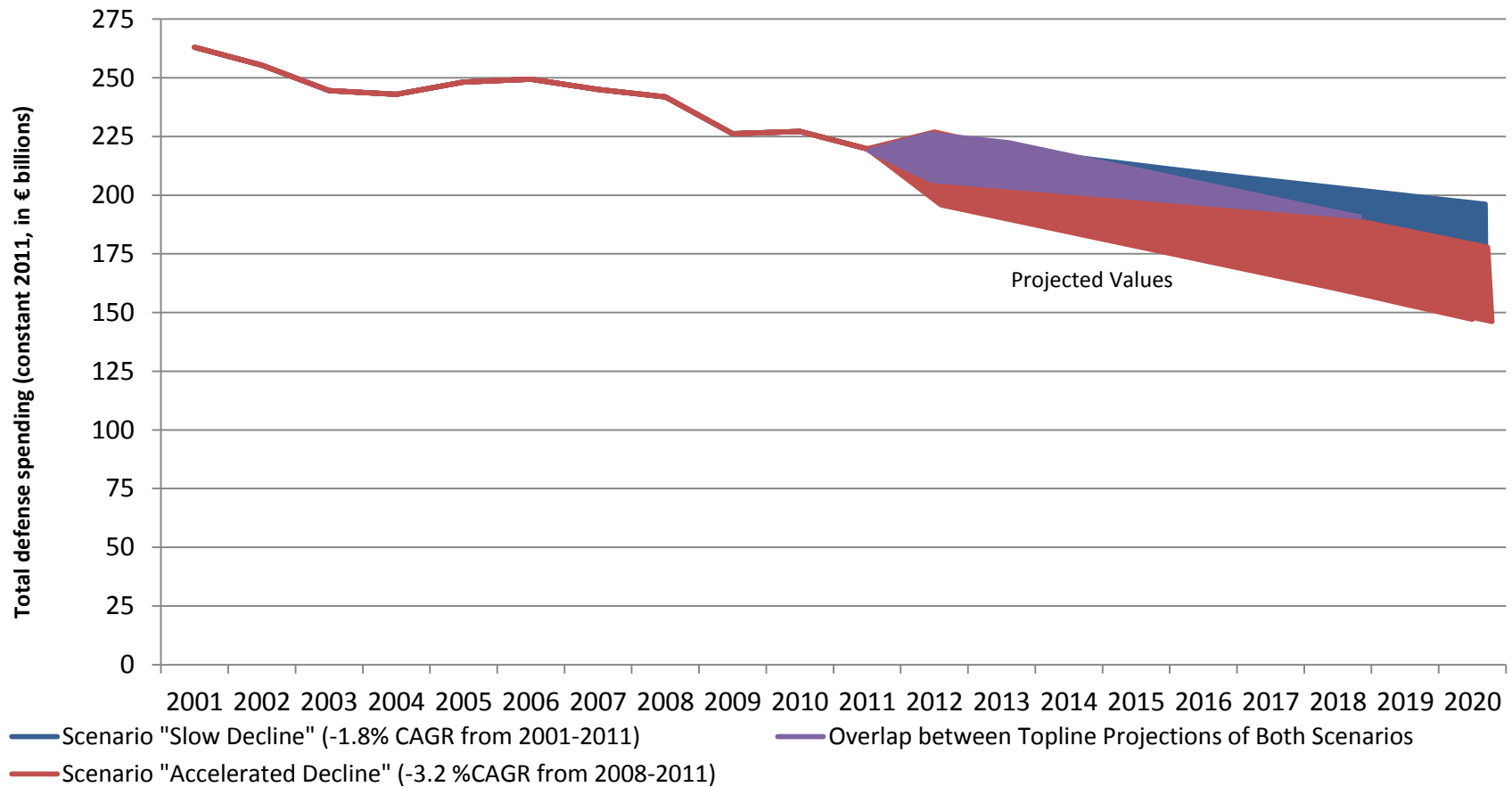
Aggregate 2011 European troop numbers hold steady through 2020

Total spending declines quickly (continues 2008-2011 CAGR of -3.2 percent)

Total troop numbers continue at the 2008-2011 CAGR of -3.3 percent

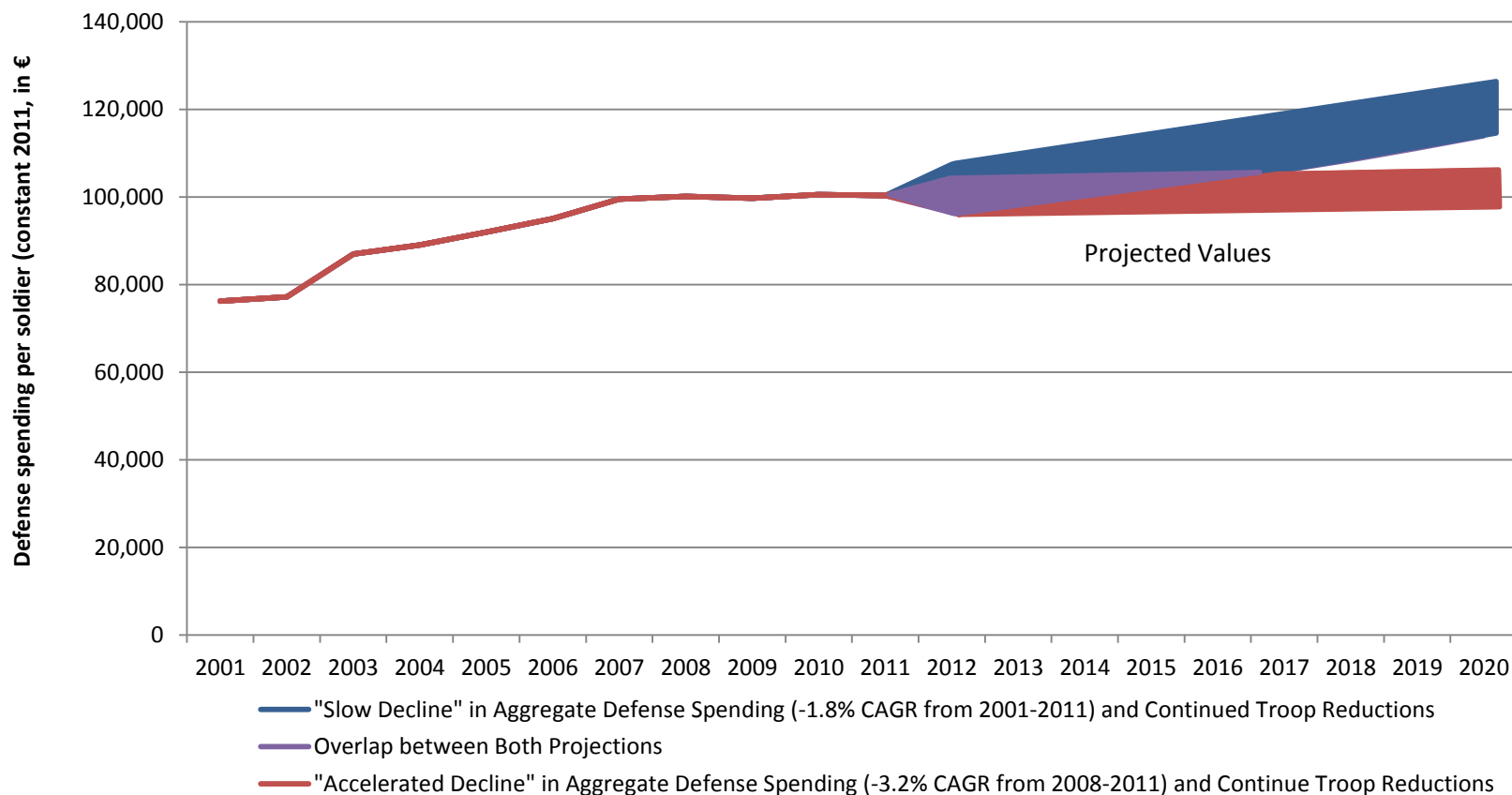
Aggregate 2011 European troop numbers hold steady through 2020

Total European Defense Spending Projections



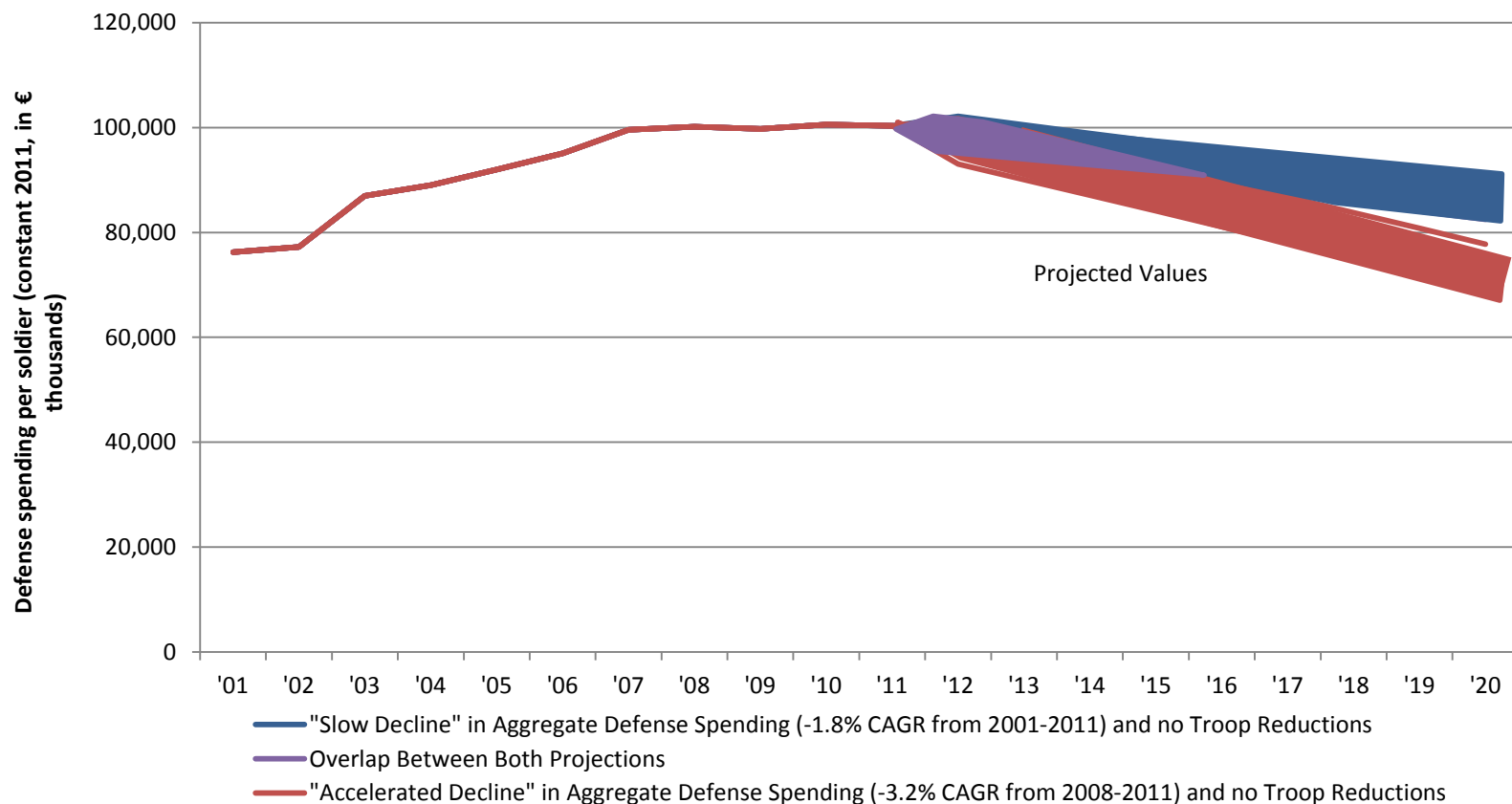
Source: NATO Defense Expenditures; SIPRI Military Expenditure Database; analysis by CSIS Defense-Industrial Initiatives Group.

Per-Soldier European Defense Spending Projections with Troop Reductions



Source: NATO Defense Expenditures; SIPRI Military Expenditure Database; analysis by CSIS Defense-Industrial Initiatives Group.

Per-Soldier European Defense Spending Projections without Troop Reductions



Source: NATO Defense Expenditures; SIPRI Military Expenditure Database; analysis by CSIS Defense-Industrial Initiatives Group.

Problem Statement

Decline in available resources

- Unlikely to change

Inefficient resource utilization due to:

- Market barriers along country borders
- Ineffective collaboration
- Inefficient acquisition processes
- Public sector over-involvement on the supply side
- Lack of strategic direction

Demand Side

- **Further troop reductions**
- **More coordinated capability trade-off decisions**
- **More effective and systematic forms of collaboration and cooperation**
- **Utilize more innovative business models**
- **Become a more business savvy customer**
- **Better leveraging of competition**

Regulatory Environment

- **Finalize implementation of regulatory reforms**
- **Monitor and enforce their application**

Supply Side

- **Limit public sector involvement on the supply side**
- **Support exports more systematically and create more efficient and predictable frameworks**

Areas for Further Research

- **Import and export patterns**
- **Industrial analysis beyond publicly traded companies**
- **Metrics for European defense spending efficiency and effectiveness**

Questions or Comments?

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