CHAPTER 3: MILITARY SPENDING AND THE MISSING INDUSTRIALIZATION STRATEGY

The positive prospects for the world heralded by globalization have proven to be unfounded. Frictions between states have grown to unprecedented levels, and Europe's position in the global context is declining in terms of innovation, industrial power and growth. In this context the EU appears as a collection of nations without a shared strategy, or rather, as a collection of nations whose only shared strategy is rearmament (Pflüger, 2025). National governments are supported in this approach by the European Commission, which has relaxed fiscal constraints, introducing the possibility of accessing the national safeguard clause in the presence of 'necessary' military expenditures. Those countries respecting the government deficit threshold of the Stability and Growth Pact may access the national escape clause, which allows increased spending up to 1.5% of GDP in the event of exceptional circumstances outside the country's control with a major impact on its public finances, provided that it does not endanger fiscal sustainability over the medium term (Art. 25, Reg. (EU) 2024/1263). It follows that in subsequent years military expenditure will become an additional burden on the public budget, to be paid by European citizens either directly - through taxes - or indirectly - through cuts to social expenditure (Frangakis, 2025).

Europe is undergoing a substantial shift towards militarisation, with the EU reorienting its policy priorities and, as a result, its budgetary allocations. In recent years, military expenditure has not merely reached record levels but has also become deeply embedded in the Union's investment and industrial policy landscape.

The outcome is a complex array of programmes and agencies that, after years of fragmentation and inefficiency, are finding a new cohesive force: military security. The EU's mechanisms for defence investment - ranging from the European Defence Fund (EDF) to agencies such as the European Defence Agency (EDA) and initiatives like the European Defence Industrial Strategy (EDIS) and European Defence Industry Programme (EDIP) - are increasingly consolidated under the banner of security and military readiness.

3.1 The EU's pursuit of security and military preparedness

The new strategic direction is enshrined in the Omnibus Package for Defence Readiness (or 'Defence Readiness 2030', successor to RearmEU), which explicitly advocates rapid enhancement of military capabilities - even at the expense of transferring budgetary resources from social welfare, public health, and pension schemes. The Commission has assumed the central role in European rearmament, directly financing programmes and overseeing the European Peace Facility - a so-called 'off-budget' fund used primarily to supply arms to Ukraine.

In 2021, with the European Defence Fund, the multiannual budget for 2021–2027 for the first time included a 'Security and Defence' line, amounting to 1.2% of the EU budget. Between 2022 and 2023, funds allocated to military programmes rose sharply, reaching €8.2 billion. In March 2024, the European Defence Industrial Strategy (EDIS) was launched: a framework for the European military-industrial sector aiming to coordinate investments and anticipate the conversion of civilian production to military use in times of crisis. Its associated programme, the EDIP (European Defence Industry Programme), has a budget of €1.5 billion for 2025–2027.

Overall, defence spending by the 27 EU Member States reached €343 billion in 2024, marking a 19% year-on-year increase, while the total defence expenditure figure is projected to reach €381 billion in 2025, about 2.1% of EU GDP (EDA, 2025).[1] EU-level 'security and defence' instruments (e.g. European Defence Fund, European Peace Facility) total around €25–40 billion for 2021–2027 and are separate from national spending.

Yet resources remain insufficient. The option of joint EU debt, as seen with Next Generation EU, is under consideration, whilst the Commission has begun reallocating funds from other budget chapters or raising funds from common borrowing that ultimately will bear on the shoulders of national budgets[2]. The mid-term review of the 2021–2027 Multiannual Financial Framework introduced changes to structural funds, shifting the priorities of EU financial instruments:

- The Regional Development Fund (ERDF), Just Transition Fund (JTF), and Cohesion Funds have been adapted to finance 'dual use' projects - civilian and defence infrastructure - and military mobility;
- The European Social Fund (ESF+) may now finance defence-related training and skill development.

Separately, the European Council is urging modifications to five key programmes - Digital Europe, Horizon, EDF, Connecting Europe Facility, and STEP (Platform for Strategic Technologies for Europe) - to promote investments in the defence sector.

[1] More data on EU defence expenditures can be found in European Council (2026).
[2] For example the 90 billion loan to Ukraine raised through common borrowing is unlikely to be repaid.

3.2 Multiannual Financial Framework 2028-2034

Looking to the 2028–2034 budget, ambitions are even greater: defence and security are poised to become strategic foundations of a 'stronger and more autonomous' Europe. The defence industry is calling for €100 billion, and the Commission plans to merge 19 funds under a new overarching framework - the European Competitiveness Fund.

Militarisation has likewise reached the European Investment Bank (EIB). Previously prohibited from funding defence, the EIB launched the SESI (Strategic European Security Initiative) in 2022, now valued at about €8 billion. In 2024, the Defence Equity Facility (DEF) was introduced, with an initial investment of €175 million: within months, the restriction of financing only civilian projects was lifted. In summer 2024, the European Investment Fund (EIF) signed an agreement with NATO's Innovation Fund, pooling resources to support the European defence industry.

More recently, InvestEU - launched in 2021 to aid post-COVID recovery and the green and digital transition - has accelerated its pivot to defence investment. In September 2025, it offered a guarantee for the first time to a private credit fund, Sienna Hephaistos Private Investments, which supports arms manufacturers. The public guarantee attracted additional capital from institutional investors, including pension funds.

The decisive shift came with a delegated act from the Commission, altering guidelines that previously limited InvestEU's defence and security investments. InvestEU may now finance any product or technology predominantly for military use and, crucially, may support defence companies - and their suppliers - even in 'associated' countries, a vague definition that could include any nation with EU-cooperation agreements. If not tied to an associated country, a company may still access financing with a Member State's special guarantee, thus enabling non-EU companies to benefit from EU funds without transparency, via private intermediaries.

What emerges is a hybrid funding model – grounded in what Gabor (2021) framed as Wall Street Consensus– that uses public resources as collateral for financial markets: EU taxpayer money increasingly de-risks private investment in defence, creating a protected, profit-guaranteed market for global asset managers and pension funds. The Commission's latest White Paper (European Commission, 2025b) unapologetically signals an intention to attract global finance to defence spending, raising questions about ultimate beneficiaries and the risk of a defence-driven financial bubble. This is crystallising a new ‘bubble’ in military-industrial investment, reminiscent of pandemic-era risk-sharing benefitting pharmaceutical industries but now centred on arms production. Large asset managers, such as BlackRock, are now identifying European militarisation as a lucrative opportunity. Unsurprisingly, the Stoxx Europe aerospace and defence index has more than tripled since Russia’s invasion of Ukraine, with over half the increase occurring in 2025.

As part of the Defence Readiness Omnibus, the Commission also seeks to boost defence spending by relaxing various regulations, including the EU’s framework for sustainable finance, which sets criteria and benchmarks for environmental and social investment. Recent proposals seek to weaken the exclusion criteria for controversial weapons from EU sustainability indexes, advancing a narrow definition of ‘prohibited weapons’ that omits highly controversial arms like nuclear, incendiary, depleted uranium, and lethal autonomous weapons. Consequently, companies manufacturing such weapons may become eligible for investments labelled as sustainable and aligned with the Paris Agreement’s objectives.

Looking ahead to the 2028–2034 cycle, the Commission aims to further elevate defence as a pillar of EU power and autonomy, with industry leaders calling for a €100 billion minimum as well as consolidation under the Competitiveness Fund (Soler, 2025).

In November 2025, as part of the Defence Industry Transformation roadmap, the Commission proposed upskilling and reskilling 600,000 workers by 2030 to meet defence production needs. This involves converting and restructuring manufacturing branches, especially the automotive industry and its supply chain, for defence production.

3.3 Risks and alternatives

Europe’s pivot towards militarisation is systemic and the pace and scale of budgetary, legislative, and industrial reforms is striking. Policymakers should critically assess the risks of opaque fund flows, off-budget guarantees, and the growing network of military-industrial linkages beyond the EU. Serious consideration is also needed regarding the resulting economic model - the lower employment multiplier of defence spending compared to social and green investments (Stamegna et al., 2024; Elveren et al., 2025; Krebs & Kaczymarczyk, 2025). The immense profits accruing to arms firms like Rheinmetall, Thales Group, and Leonardo, the role of global financiers, and the hard fact that, in this ‘era of European defence’, as defined by the EU High Representative for Foreign Affairs and Security Policy Kaja Kallas, weapons must be used or sold to keep production and the associated financial bubble alive. Notably, European aerospace and defence stocks drop sharply whenever geopolitical developments, such as US-led pushes for peace in Ukraine, threaten the war's continuation (EU Defence Spending/Eunews, 2025).

Participation in wars is supposed to build economic strength in the midst of global chaos (Canale & Cozza, 2025), but it promises catastrophic consequences, not only on human lives, but above all on the continent's ability to sustain growth on a socially sustainable basis (healthcare, education, etc.).

In the absence of an industrial policy strategy capable of supporting and driving businesses in the processes of innovation, digitalization, and ecological transformation, European countries, although supported in the short term by increased spending on weapons, will find themselves unprepared and marginalized in the long run with respect to the challenges of digital and ecological transformation. The only effective result will be the growth of short-term profits of the defence industry and of the financial institutions investing in the militarization of the economy.

A common response to the real threat of Europe's industrial decline would require a quantum leap in common political institutions, which currently doesn't seem to be on the horizon. But pressure from below can make the difference (Clua Losada, 2025).

The one thing we can all certainly agree on, today is that the economic system does not function solely according to market mechanisms but is the result of policy choices destined to shape Europe's future for years to come. And the future will depend on the shape current choices will give to Europe.