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ECONOMIC GOVERNANCE

Defence financing and spending under the Economic Governance Framework

This paper covers possible defence financing and spending options under the European economic governance framework by reviewing the proposal for a ReArm Europe plan floated by the President of the Commission Ursula von der Leyen. The paper also analyses flexibilities under the EU budget, EIB and ESM financing while also assessing potential market challenges and public procurement. This paper has been updated with information from the European Commission's White Paper for European Defence Readiness 2030 and related documents published on 19 March 2025.

1. Introduction

On 19 March 2025, the European Commission presented a White Paper for [European Defence/Readiness 2030](#) as well as its overall ReArm Europe Plan/Readiness 2030. As stated by Commission President Ursula von der Leyen in a [letter](#) to EU leaders, ReArm Europe is intended to “significantly step up” EU spending on security and defence at a time that Europe “faces a clear and present danger on a scale that none of us have seen in our adult lifetime”.

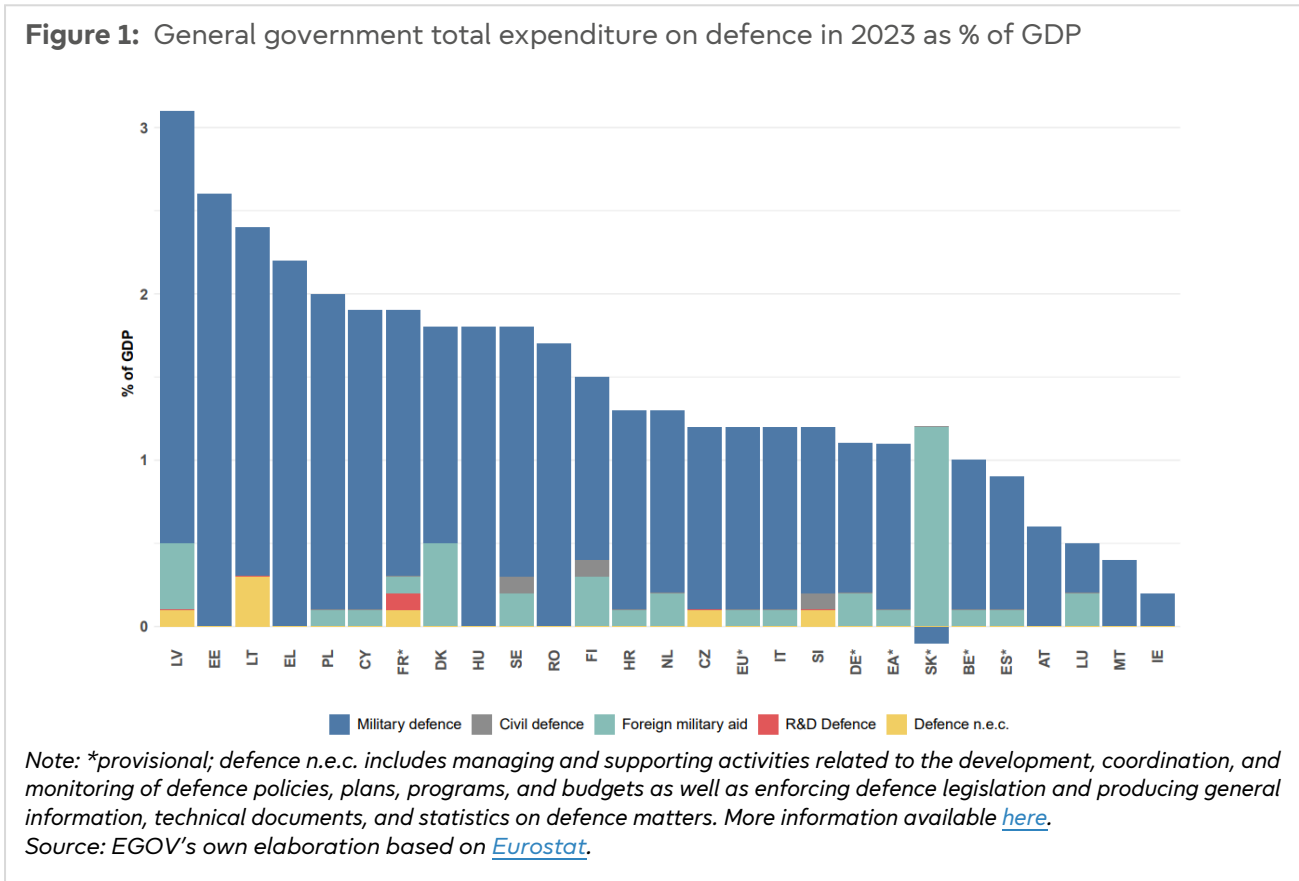
The [White Paper for European Defence Readiness 2030](#) identifies critical gaps in Europe's defence preparedness and proposes measures to enhance joint procurement, investment in cutting-edge military technologies, and interoperability among Member States. It stresses the need for greater coordination, faster response mechanisms, and a more resilient European Defence Technological and Industrial Base (EDTIB) to address evolving security challenges. It also outlines how Europe faces an acute and growing threat environment. It identifies Russia's continued aggression against Ukraine, China's military build-up, growing hybrid threats, and intensifying geopolitical competition as key challenges. A central focus is put on ensuring that Europe can act autonomously when needed, reinforcing its ability to defend itself while maintaining strong cooperation with NATO and other allies. The White Paper serves as a strategic roadmap to guide defence planning and investments toward 2030, aiming to bolster Europe's overall security and readiness in an increasingly complex geopolitical landscape.



Alongside the White Paper, the European Commission put forward the following initiatives as part of the ReArm Europe Plan, which it claims enables additional defence spending of up to 800 billion Euros:

- A new instrument called “Security Action for Europe” (SAFE) to provide up to EUR 150 billion in loans to Member States, backed by the EU budget.
- **Full use of the flexibility of the EU’s economic governance framework**, including through the activation of the so-called National Escape Clauses (NECs) of the Stability and Growth Pact as introduced in 2024.
- **Use of the EU budget to boost defence-related investments in Europe including by repurposing existing cohesion policy funds** under the 2021-2027 Multiannual Financial Framework (MFF) and expanding the scope of the Strategic Technologies for Europe Platform (STEP) to include defence.
- A more active role of the **European Investment Bank (EIB)** to unlock funding.
- **Private capital mobilisation** through the completion of the Capital Markets Union along the lines of the [Communication](#) on a Savings and Investments Union of 19 March.

Prior to the presentation of the plan, the European Parliament held a plenary debate on 11 March 2025 where Commission President Ursula von der Leyen [presented](#) some of ReArm Europe’s main characteristics.



Following the debate, the European Parliament first positioned itself in a [resolution](#) adopted on 12 March 2025 in which it welcomed the ReArm Europe and called “for a system of European defence bonds to be explored for financing large-scale military investments up front” as well as “the use of unused ‘coronabonds’ for defence instruments to be explored”, Members also supported the proposal to establish and investment guarantee programme based on the model of [InvestEU](#) with open architecture to trigger private sector investment. The European Investment Bank is also invited to urgently revise its lending policy to remove current restrictions on financing defence, and to investigate the possibility of issuing earmarked

debt for funding security and defence projects.

Figure 1 shows that Latvia, Estonia, and Lithuania had the highest government defence expenditure as a % of GDP in 2023, with Latvia exceeding 3%. Most countries allocated the majority of their defence spending to military defence, while a few, like Denmark and Slovakia, showed notable spending on foreign military aid. Overall, there is significant variation across EU countries in defence spending priorities and levels. In 2023, defence expenditure amounted to 1.3% of GDP for the EU and 1.2% of GDP for the euro area, with detailed data for all EU countries available in [Annex 3](#).

2. A new EU defence financing instrument

The new dedicated EU finance instrument for defence investment and spending has been officially named Security Action for Europe (SAFE) and would provide up to EUR 150 billion in loans. According to the Commission's proposal, the SAFE instrument established by a [Council regulation](#) would offer to Member States **loans with a maximum duration of 45 years**, including a 10-year grace period for principal repayments. The final approval for disbursements would need to take place by 31 December 2030. These loans would be dedicated to seven priority areas:

1. Air and missile defence
2. Artillery systems
3. Missiles and ammunition
4. Drones and anti-drone systems
5. Strategic enablers and critical infrastructure protection, including space-related aspects
6. Military mobility
7. Cybersecurity, artificial intelligence, and electronic warfare

According to the proposal, Member States seeking loans must submit a European Defence Industry Investment Plan to the Commission. This plan should outline the activities, expenditures, and measures for which funding is requested, specify the defence products to be procured, and, where applicable, detail Ukraine's involvement. Loan allocation will be demand-driven, without predetermined distribution quotas among Member States. However, the share of loans granted to the three Member States representing the largest share of the loans granted should not exceed 60% of the maximum amount of financial assistance under SAFE.

The loans will support joint procurement of defence products by at least two countries, one of which must be a Member State receiving SAFE financial assistance. The second partner may be another EU Member State, an EFTA state, an EEA member, or Ukraine. To ensure early financial support, up to 15% of the loan can be provided as pre-financing, with payments beginning in 2025.

SAFE will strengthen the European Defence Technological and Industrial Base (EDTIB) by ensuring that orders go to companies based in the EU, EEA EFTA states, or Ukraine. For war consumables (non-complex products), at least 65% of the end product's component costs must originate from these regions. For complex defence systems, the same rule applies, with an additional requirement that contractors retain full control over the equipment's design.

The legal basis for the new EU instrument will be provided for in [Article 122 of the Treaty on the Functioning of the EU](#). This article is part of the TFEU's chapter on economic policy. It allows the Council to adopt economic policy "measures" based on [qualified majority voting](#) in the Council and following a Commission proposal. Contrary to the ordinary legislative procedure, the European Parliament is merely informed. Likewise, possible Union financial assistance to Member States shall be granted by a decision adopted by the Council, acting by a qualified majority on a proposal from the Commission.

The application of Article 122 to the SAFE proposal raises several critical issues. In the explanatory memorandum of the SAFE legislative proposal, the Commission argues that it provides an **appropriate legal**

basis for addressing the pressing security needs of the EU in the face of increasing geopolitical tensions, particularly following Russia's aggression toward Ukraine. From this perspective, Article 122 can be viewed as a foundation for EU solidarity in addressing the collective defence challenges posed by external aggressions, which affect not just individual Member States but the security of the Union as a whole. The proposal aims to ensure that defence capabilities across the Union are strengthened in a coordinated manner, with emergency measures such as fiscal flexibility and financial assistance deemed necessary to achieve this goal. However, Article 122 has historically been used to respond to crises and provide emergency support to EU Member States facing severe difficulties, following events such as natural disasters, economic crises, or sudden disruptions. It has typically been invoked to address short-term, exceptional crises, rather than structural initiatives such as boosting defence spending across multiple Member States.

Another argument put forward by the Commission to justify the use of a legal basis that grants no role to Parliament is the [urgency to act](#). Past experience however demonstrates that the European Parliament has swiftly approved many urgent proposals using emergency or simplified procedures outlined in the Rules of Procedure. Questions arise therefore regarding **the democratic accountability of a process based on article 122**, especially in such a sensitive area as defence policy. In this regard, the powers of Parliament are limited to those explicitly defined in the Rule of Procedure. According to Rule 138, Parliament must invite the Commission President to explain the choice of legal basis and outline the main objectives and elements of the proposal. The Committee on Legal Affairs (JURI) shall verify the legal basis, and if it decides to question its appropriateness, it must report its conclusions to Parliament. Finally, and only in the case where JURI does not challenge the legal base, Parliament may request the initiation of the budgetary scrutiny procedure, as outlined in the joint declaration of the European Parliament, the Council, and the Commission from 16 December 2020.

Following the adoption of a regulation, the Commission can be expected to take the necessary steps to enable a quick and smooth use of it. These actions would comprise first of all the necessary budgetary adjustments, namely the creation of a budget line for the guarantee provided by the EU on Union loans raised for financial assistance under the new instrument, and a revision of the estimate of the available margin under the own resources ceiling. However, it should be noted that in normal circumstances, financial assistance under a loan-based instrument would not entail any budget expenditure unless a beneficiary Member State defaults on its obligations. While the loans are backed by the EU budget headroom, within the 1.4% EU GNI own resources ceiling as a first line of defence, the Commission may also need to confirm its capacity to raise funds on the financial markets. Currently bonds issued by European institutions are of the [highest credit quality](#) thanks to the backing of the EU budget and additional budgetary resources or guarantees that underpin the different EU programmes financed by bond issuance. In particular, according to Council Decision 2020/2053 the European Commission has the right to draw on Member States' resources to ensure that sufficient budget revenues are available at all times to cover all obligatory expenditures, including debt servicing. Moreover, Article 310 of the TFUE implies that Member States are collectively bound (joint and several liability) by law to ensure the balance of EU's budget, including the servicing of its debt.

The conditions for Member States to access funding will depend, among other things, on the **funding strategy** adopted by the Commission. In the past, a back-to-back approach was used, whereby the Commission issued bonds and transferred the proceeds directly to the beneficiary country on the same terms that it received (in terms of interest rate and maturity). However, while this method had successfully addressed small funding needs, it has reached its limits with the SURE programme where 19 Member States were being served by a single funding programme. Since [December 2022](#), similarly to what has already been applied since [April 2021](#) with Next Generation EU (NGEU), the Commission has therefore adopted a new [diversified funding strategy](#) that combines the use of [different funding instruments and funding techniques](#). The new funding strategy decouples the funding transactions from the programme's immediate funding needs, providing more flexibility in the execution of borrowing operation. This approach to managing maturities and repayments will also help the Commission to manage any underlying risks that these loans may represent for the EU budget and guarantee in such a way that these are kept within strict limits, in full

respect of sound financial management principles. The possibility of maturity transformation has a positive impact on lending conditions too. Indeed, it allows to offer long-term loans on more attractive terms to beneficiary Member States, whilst equal treatment among Member States that request a loan as they will receive loans with identical maturities and repayment conditions ensuring.

At the EU level, the success of the instrument would hinge on Member States' appetite for a credit line by the Commission and how well these extra financial means would be spend. As past experiences have shown, this appetite might be determined by a combination of factors such as conditionality, national borrowing conditions as well as political costs of borrowing. For instance, during the pandemic, no Member State drew on the ESM Pandemic Crisis Line whereas 19 Member State tapped into SURE and all requested the grants available under the Recovery and Resilience Facility, showing the critical importance of the design features of these programmes.

Given the considerable investments required, a loan-based instrument may also prove insufficient. Unlike grants, loans must eventually be repaid with interest, which could further exacerbate fiscal pressures on already-constrained Member State budgets. **This limitation might become problematic in combination with the temporary nature of the fiscal flexibility being offered through the national escape clause, potentially creating a "fiscal cliff" when both instruments expire.**

3. Defence spending flexibility under the Stability and Growth Pact

3.1 The National Escape Clause framework for defence expenditure

ReArm Europe Plan/Readiness 2030 pivots around making use of the flexibility provided by the revised economic governance framework, notably in the so-called [preventive arm](#) and [corrective arm](#) of the Stability and Growth Pact. In the Commission's view, this should provide sufficient leeway to Member States to ramp up their investments in defence without incurring in breaches of the EU's fiscal framework. In particular, the Commission sees the **activation of article 26 of the preventive arm - the so-called National Escape Clause (NEC)** - as a crucial instrument to foster defence expenditures in each Member States.

The European Commission has now published detailed guidance on "[Accommodating increased defence expenditure within the Stability and Growth Pact](#)" that provides a comprehensive framework for the application of flexibility under the EU fiscal framework. This Communication outlines how the NEC will operate to accommodate increased defence spending while maintaining overall fiscal sustainability.

The Commission has confirmed that Russia's war of aggression against Ukraine and its threat to European security constitute "*exceptional circumstances outside the control of Member States*," with a major impact on Member States' public finances through the related incurred and/or planned increase in defence expenditure. Given that all Member States are affected by this situation, the Commission is inviting all Member States to make use of the flexibility in a coordinated manner.

Key elements of the NEC flexibility framework include:

1. Scope of eligible defence expenditure:

- The flexibility would cover the increase of total defence expenditure, including both investment and current expenditure.
- The application will correspond to the entire statistical category of COFOG division 02 – Defence, which is a concept close to the aggregate used by NATO.
- Expenditure financed by SAFE loans will automatically benefit from this flexibility.

2. Maximum amount of flexibility:

- The flexibility under the NEC will be capped at 1.5% of GDP for each year of activation compared to the net expenditure path set out in the Member States' medium-term plans or to the corrective path under the Excessive Deficit Procedure.
- The cap will be applied on the net expenditure path net of the impact of the debt sustainability safeguard and the deficit resilience safeguard. This effectively provides greater fiscal space than if the cap were applied after safeguards, though the Commission notes this only affects a few countries where safeguards were binding (mainly Finland and possibly Germany).

3. Duration of the NEC activation:

- The flexibility would be available for a period of four years, starting from 2025 through 2028.
- Contrary to what might be inferred from the Communication, the reference year 2021 does not limit the maximum flexibility available to Member States. Countries that have already increased defence spending between 2021-2024 (such as Poland) will not be penalised as "frontrunners." These Member States will still have the full flexibility to increase defence spending by an additional 1.5% of GDP from their current levels, not just the difference between 1.5% and what they have already increased since 2021. This ensures that early adopters of increased defence spending are not disadvantaged compared to those who delayed their defence investments.
- For military equipment contracts signed during the period of NEC activation but delivered later, the flexibility will also apply to the related expenditure after the four-year period.

3.2. Procedure for activation:

- Member States are invited to submit their requests to activate the NEC by the end of April 2025.
- These requests could be coordinated by the Council to have joint requests from interested Member States.
- The Commission will assess the requests against three conditions: 1) the existence of exceptional circumstances outside Member States control; 2) a major impact on public finances; 3) no endangerment to medium-term fiscal sustainability.
- The Commission will adopt recommendations for Council, with adoption expected in July 2025.

Based on projections of gradual take-up, the Commission estimates that defence investment could reach at least EUR 800 billion over the next four years, including the expenditure financed by the EUR 150 billion from SAFE.

Box 1: Data collection on defence

The application of the NEC requires reliable and timely data collection. In its Communication, the Commission clarifies that, for this purpose, official data on defence expenditure must be anchored within the national accounting framework to ensure methodological consistency and comparability with other statistics used in the economic governance framework, as well as with national accounts data (e.g., GDP). **Accurately measuring defence expenditure based on fully harmonised definitions and methods in the context of the European System of National Accounts (ESA) is essential.**

The current European System of National Accounts ([ESA 2010](#)) classifies defence expenditure under COFOG Division 02 – Defence. Although this classification is similar to the one used by NATO, the two systems diverge on some important aspects due to their differing original objectives.

COFOG, developed by the United Nations and used by Eurostat under [ESA 2010 regulations](#), is designed to classify public expenditure according to various government functions, including defence. It focuses on expenditures directly incurred by national governments for armed forces, military research, civil protection for military purposes, and the procurement of military equipment. **Dual-use goods and services** (e.g., infrastructure serving both civil and military purposes) **are included only under specific conditions.**

NATO's classification, however, is broader and includes not only the expenditure categories recognised by COFOG but also additional items such as military personnel pensions, contributions to allies, and spending on paramilitary forces with defensive functions. Conversely, COFOG includes expenditures not covered by NATO's definition, such as civil defence, capital support for the defence industry, and military support abroad (e.g., to Ukraine).

Another important divergence is in the **timing of recording defence expenditures.** NATO records defence expenditures at the time of payment, while COFOG follows the accrual basis principle, meaning that the impact of military spending on public expenditure and on the deficit occurs when the goods are shipped, which generally marks the transfer of ownership. This principle aligns with the reporting requirements for public expenditure in the context of the European Semester, as established in Regulation (EU) No 549/2013 (ESA 2010). Although this difference is temporary and expected to balance out over time, the relevant time for comparing expenditures and deficits, especially for budget flexibility purposes, is determined only by COFOG.

These differences have tangible implications for the application of the NEC and for monitoring Member States' defence spending commitments within NATO. Since the Commission relies on COFOG to define defence expenditures eligible for fiscal flexibility, some expenditures recognised by NATO may not qualify under the EU fiscal framework. However, the Communication clarifies that NATO's definition should serve as a reference, and any discrepancies will be addressed in the reporting system. Additionally, to prevent a potential disincentive for military spending due to the classification differences, the Communication explicitly states that fiscal flexibility will extend beyond the NEC activation period to cover expenses related to contracts signed during the NEC period but delivered afterward.

Another critical issue concerns expenditures financed through loans obtained under the SAFE instrument. Since eligible expenditures may include items beyond those defined as military spending under COFOG, the Commission has explicitly stated that all such expenditures will automatically benefit from fiscal flexibility.

Finally, there is a **data transmission challenge.** Defence expenditures classified under COFOG Division 02 must be reported by national statistical authorities to Eurostat with an 11-month delay, whereas data on deficit, debt, and other key indicators for the European Semester cycle are reported with a 3-month delay, as part of the twice-yearly EDP national notifications. This discrepancy has already been identified as a challenge in the reform of European economic governance. It has so far been addressed through the voluntary early submission of defence data by Member States

3.3 Existing flexibility in the reformed Economic Governance Framework

Irrespective of the triggering of the use of the NEC, the EU's reformed economic governance framework, which entered into force in April 2024, already introduces significant provisions recognising defence investment as a strategic priority. Both the preventive and corrective arms of the framework provide flexibility for defence investments while maintaining overall fiscal sustainability objectives.

Under the preventive arm, for instance, Member States should outline when relevant **how the reforms and investments in their fiscal plans may contribute to the build-up of defence capabilities**. Additionally, Member States may **commit to undertake investments in defence and benefit from an extension of their fiscal adjustment period** to smoothen the consolidation efforts over a longer timeframe. The preventive arm also foresees escape clauses to allow for targeted derogations from the rules in exceptional circumstances (see [Annex 1](#) for more details).

Similarly, the **corrective arm clearly establishes a role for defence investments when assessing the launch of excessive deficit procedures**. For instance, defence spending is to be considered, under certain limits, as a **potential mitigating factor** in the process of assessing if corrective action is needed when deficit and debt exceed the thresholds (see [Annex 2](#) for more details).

3.4 Implementation scenarios and limitations

Member States have two main options for accommodating major defence investment programs:

3.4.1 Scenario A: Using standard flexibility provisions

In the context of the **preventive arm**, it is essential to include detailed defence investment plans within the medium-term fiscal-structural plan, as outlined in Article 13 of Regulation 2024/1263. Additionally, Member States may request an extension of the adjustment period (Article 14) if defence investments address the priorities of the European Union.

Regarding the **corrective arm**, if a Member State is subject to an EDP, it is crucial to ensure that defence investments are highlighted in the Commission's assessment, as specified in Article 2(3)(e) of Regulation 1467/1997. Moreover, these investments can be cited as a relevant factor in the deficit assessment, in accordance with Article 2(4). Finally, Recital 23 provides an additional flexibility buffer for the years 2025, 2026, and 2027, allowing the Commission to take into account increases in interest payments, provided that the concerned Member State explains how these expenditures contribute to addressing the Union's common priorities, including the build-up of defence capabilities.

3.4.2 Scenario B: Activating the national escape clause

The national escape clause represents the most significant flexibility mechanism available to Member States for defence spending.

The NEC offers several distinct advantages compared to the standard flexibility provisions. First, it provides a larger allowance for deviation—up to 1.5% of GDP—which significantly exceeds what would typically be available through regular channels. Second, it applies to both capital and current defence expenditure, whereas standard provisions primarily recognise capital investments. Third even Member States that have already increased defence spending since 2021 will still have the full flexibility to increase their defence spending by an additional 1.5% of GDP from their current levels. This ensures that early adopters of increased defence spending are not disadvantaged.

The expected (and desired?) impact from the activation of NECs would be a substantial increase in operational flexibility of defence budgets for Member States concerned. Observing deviations from the endorsed net expenditure paths the Commission would not recommend enforcement steps if these deviations were the result of additional defence spending and did not exceed 1.5% of GDP. For Member

States currently in, or at risk of entering, an excessive deficit procedure, this mechanism would indeed provide a critical buffer that could prevent or delay EDP initiation.

Unlike the previous activation of flexibility clauses, this approach is specifically tailored to defence and represents a targeted rather than a blanket exemption; it reflects the Commission's view that the current security situation constitutes a specific type of exceptional circumstance warranting a dedicated response within the fiscal framework.

3.4.3 Limitations and safeguards

Despite the flexibilities outlined above, important limitations apply to defence spending under the fiscal framework and the Commission Communication raises important questions:

The NEC does not establish a permanent "golden rule" for defence expenditure. Unlike proposals for other areas, such as green investments, defence spending is not permanently excluded from fiscal calculations. Its flexibility is temporary, with the expectation that Member States will eventually integrate higher defence spending into their regular fiscal frameworks. Once the NEC is deactivated after four years (unless extended), standard fiscal rules will fully apply again, potentially triggering excessive deficit procedures or requiring fiscal plan revisions.

Additionally, the control account mechanism grants only a temporary exemption. During NEC activation, permitted defence spending will not be debited (per Article 22(7) of Regulation (EU) 2024/1263) but will still be tracked as a memo item, reinforcing the temporary nature of flexibility while maintaining fiscal transparency. However, the Communication states that the control account will continue recording deviations unrelated to defence spending, contradicting the legal text, which specifies that recording stops entirely once the NEC is activated. **This inconsistency could weaken enforcement actions.**

Fiscal sustainability remains the primary concern of the framework. The preventive arm still requires debt to remain "on a plausibly downward path" (Article 6(a)), and the overall focus on debt sustainability is maintained (Article 16(2)). This creates a fundamental tension between increased defence expenditure and fiscal consolidation objectives, potentially forcing difficult trade-offs between defence and other policy priorities. Even with the NEC, the Commission must assess that deviations will not endanger fiscal sustainability over the medium term. Overall, there are inherent fiscal trade-offs over time. Increased defence spending today necessarily implies a postponement of fiscal consolidation efforts in the future. Member States must recognise that while immediate flexibility is available, the accumulated costs will eventually need to be addressed. The White Paper's emphasis on a massive increase in defence expenditure to "at least EUR 800 billion" over four years represents a substantial fiscal commitment that will likely necessitate adjustments in other spending areas or increased revenue generation in the long term. This could potentially lead to difficult trade-offs between different policy priorities.

Additional defence spending could potentially mitigate these limitations if it increases economic potential. To the extent that additional defence spending enhances the productive capacity of Member States – through technological spillovers, skills development, or industrial modernisation – it may help avoid future fiscal trade-offs by contributing to economic growth. The White Paper emphasises this potential for positive spillovers across the economy, but the actual economic impact will depend on the nature and efficiency of the defence investments made. **However, this optimistic perspective rests on implicit assumptions about fiscal multipliers that deserve scrutiny.** The Commission's estimate of EUR 650 billion in fiscal space appears to assume that defence spending will generate sufficient economic growth to partially offset its fiscal impact. Economic studies suggest that defence spending multipliers are often lower than

those for other public investments. Research by [Barro and Redlick \(2011\)](#)¹ estimated defence spending multipliers around 0.6–0.7 for the United States, while [Auerbach and Gorodnichenko \(2012\)](#)² found multipliers ranging from 0.5 in expansions to 1.0 in recessions. **These multipliers are typically lower than for other public investments like infrastructure or education**³. With multipliers potentially below 1.0, defence spending might not create additional fiscal space through growth effects alone. This means that the fiscal impact could be larger than anticipated, particularly for highly indebted countries. Notably, the **Commission has not published detailed calculations or assumptions** underlying these estimates, including their assumed multipliers, time profiles of spending, or country-specific impacts, making independent assessment of the fiscal projections difficult.

Defence spending is just one factor in a broader assessment. Under the corrective arm, defence investments are considered as potential mitigating factors in a "*balanced overall assessment*" (Article 2(4)), but they cannot alone exempt a Member State from an EDP. Furthermore, the consideration of mitigating factors remains rather limited when debt is above the 60% GDP threshold. This means the overall fiscal position of the country will still be evaluated comprehensively, with defence being just one consideration among many. It is also understood from the Communication that the exemption of defence expenditures under the NEC would not automatically translate into a shield from corrective actions triggered by an overshooting of the net expenditure path as measured by the control account due to non-defence related spending.

The scope of qualifying expenditure is subject to specific definitions. Under the corrective arm provisions, only capital expenditures clearly qualify as "*government investment in defence*" (Article 2(3)(da)), typically including procurement of military equipment, infrastructure, and R&D. Regular operational expenditures such as personnel costs, maintenance, and operational expenses generally do not receive the same favourable treatment. This significantly narrows the portion of defence budgets eligible for special consideration under the standard provisions, although the NEC framework now broadens this to include both investment and current expenditure.

In that vein, concerns about potential circumvention of fiscal rules cannot be excluded. The expanded definition of eligible defence expenditure under the NEC creates a risk that regular budget items could be recategorised as defence expenditures to circumvent existing fiscal rules. The Commission will need to carefully monitor implementation to ensure the integrity of the framework.

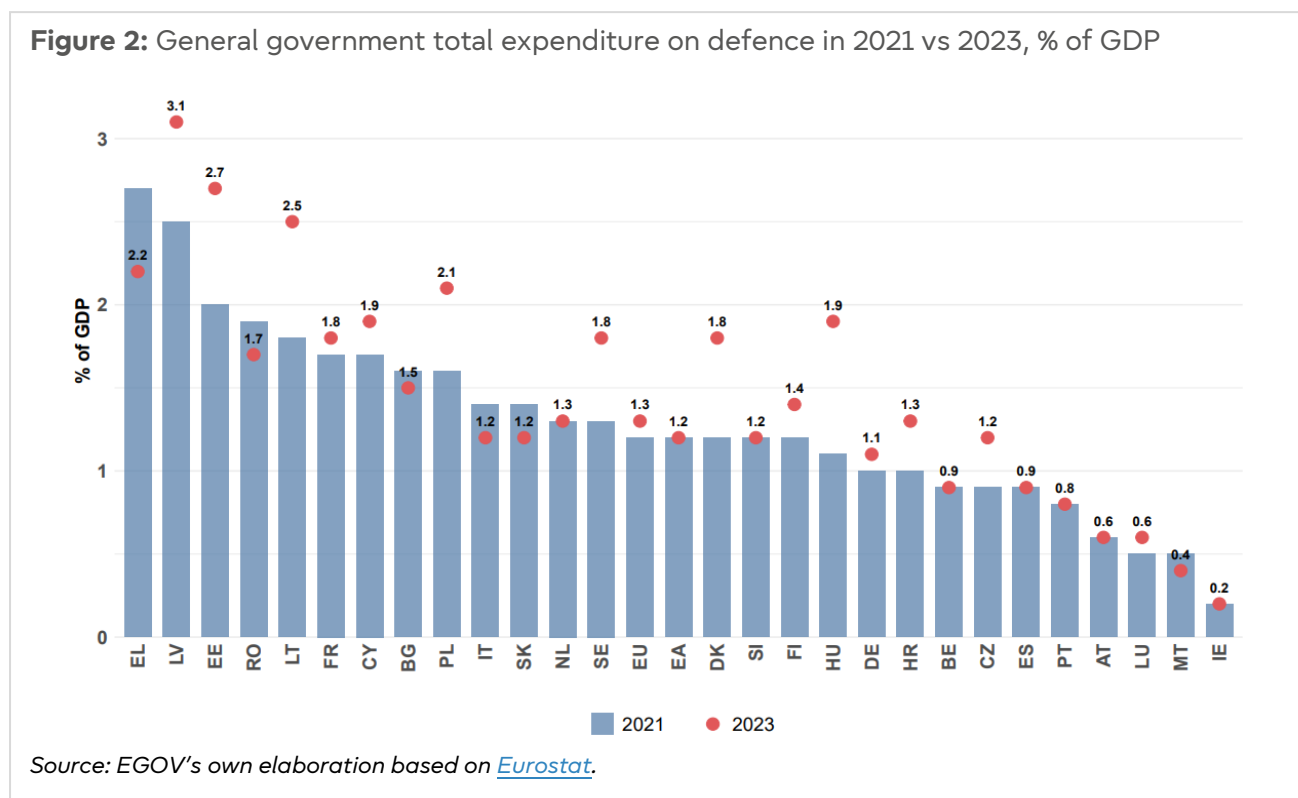
The Commission's clarification regarding the 2021 reference year addresses previous equity concerns but may raise new questions about fiscal impacts. By confirming that Member States that have already increased defence spending since 2021 will still have the full flexibility to increase their defence spending by an additional 1.5% of GDP from their current levels, the Commission has ensured that early adopters are not disadvantaged. However, this approach could potentially lead to significantly higher total defence spending increases than the headline 1.5% figure suggests. For instance, a Member State that has already increased defence spending by 1% of GDP since 2021 could now increase by another 1.5% of GDP, for a total increase of 2.5% of GDP from 2021 levels. This more generous interpretation will likely increase the overall fiscal impact of the initiative across the EU as a whole, which may have implications for debt sustainability in some

¹ Barro, R. J., & Redlick, C. J. (2011). Macroeconomic effects from government purchases and taxes. *The Quarterly Journal of Economics*, 126(1), 51-102.

² Auerbach, A. J., & Gorodnichenko, Y. (2012). Measuring the output responses to fiscal policy. *American Economic Journal: Economic Policy*, 4(2), 1-27.

³ Contrary to public investment in education or infrastructure, public defence spending typically has a multiplier effect below one because it involves specialised equipment with limited civilian applications, a significant portion of defence expenditure goes toward personnel costs and maintenance rather than new productive capacity, and suffers from market fragmentation that prevents economies of scale. Unlike investments in infrastructure or education, defence expenditures often do not generate the same level of productive capacity improvements that would stimulate broader economic growth.

Member States. See **Figure 2** for figures on defence spending in 2021 and 2023 (latest year for which data is available).



Finally, the NEC is normally intended for temporary, country-specific emergencies rather than long-term structural spending needs. Defence investment requires sustained, predictable funding over many years, while the NEC is time-limited by design. **This may create uncertainty about the fiscal framework after the NEC period ends.** Additionally, the activation of the NEC for four years, i.e. the lifetime of the majority medium-term fiscal-structural plans, risks creating inconsistencies and uncertainties on the fiscal consolidation path to be followed by those Member States who requested an extension of their plan to 7 years.

4. Other options to finance defence spending

4.1. EU budget tools

The ReArm Europe proposal calls for an increase of European defence investments financed through the EU budget, including by using of the mid-term review of cohesion policy as a way to re-direct more funding towards defence-related investments.

The possibility of using national co-financing of Union programmes to increase funding to defence under cohesion policy should in turn be read in conjunction with the preventive arm regulation of the Stability and Growth Pact (see previous section). Under [Article 2 of the preventive arm regulation](#), such national expenditure of co-financing would not be included by the net expenditure indicator used for monitoring compliance with the national fiscal consolidation trajectories. In other words, Member States would have further leeway to increase (dual use/indirect) defence spending without incurring the risk of being subject to an excessive deficit procedure due to overshooting their national net expenditure ceilings

by means of higher defence spending (or at least postponing the fiscal consolidation effort to a later stage in the future).

At this stage, it remains uncertain whether there will be any limits on the amount of cohesion funds that may be reoriented towards defence. What is clear is instead the notable delays in the absorption of cohesion programmes, as recently pointed out by the Commission in its 2024 country-specific recommendation where it urged virtually all Member States to accelerate roll-out. Current estimations is that approximately 5% of the EUR 526 billion available under cohesion policy have so far been spent.

Among the options floated to unleash the EU budget in support of defence-related spending, the letter of the Commission President mentions the use of the Strategic Technologies for Europe Platform (STEP), a platform established in the context of the mid-term review of the Multiannual Financial Framework to pool resources to invest in critical technologies, notably in the digital, clean and bio tech sectors. STEP is also closely linked to the RRF as the Commission encourages Member States *"to leverage step opportunities"* under the facility to reallocate resources for STEP projects by transferring up to 6% of their RRF envelope to their national compartment in InvestEU with a view of funding these projects.

Consequently, the Commission has called upon Member States to review the feasibility of the projects under the RRF set to be completed by the legal deadline of August 2026. If Member States were to expect delays, the Commission is encouraging revisions to the RRFs to shift committed resources towards STEP/InvestEU. Instead, Commission's officials have so far rejected the idea of repurposing the EUR 93 billion of RRF loans that were not taken up by the legal deadline.

At the ECOFIN meeting on 11 March, the Italian Minister of Economy Giancarlo Giorgetti presented an [initiative](#) aiming to mobilise private capital for strategic investments in European security and industrial innovation. The initiative aims to overcome the problems related to the issuance of new public debt, both by individual Member States and by the Union, and seeks to encourage the mobilisation of private capital in crucial sectors such as defence, security, aerospace, and dual-use technology. According to this proposal, a public guarantee totalling approximately 16.7 billion euros could leverage up to 200 billion euros of private investment over the next three to five years, achieving an estimated multiplier of around 12x. This ambitious mobilisation should be achieved by reshaping and enhancing the existing national compartment of [InvestEU programme](#) - on which the Commission has already put forward a [proposal for amendment](#) on 26 February - through the creation of a multi-tranche European guarantee structure that involves both the Member State and the EU budget.

The White Paper confirms that the Commission will propose changes to the European Regional Development Fund by the end of March 2025. Following the mid-term review of cohesion policies, national, regional, and local authorities will be able to voluntarily allocate funds within their current programmes towards emerging priorities including strengthening defence and security capabilities. **The co-legislators are invited to consider these changes with priority.**

The White Paper also calls for a coordinated approach from all stakeholders. It stresses that the EU budget can boost defence-related investments by making existing EU instruments more flexible and maximising the contribution of EU agencies. The White Paper is clear that the urgency of the situation requires all available EU instruments to be engaged to support defence spending.

4.2. European Investment Bank

The ReArm Europe plan identifies the European Investment Bank (EIB) as a relevant player to unlock sources of funding for investments in defence.

The EIB is also constrained by requirements to only finance dual use defence projects. However, in 2024, its Board of Directors [updated](#) its definition of dual-use goods and infrastructure with a view of facilitating financing of projects with a primary defence purpose. In this context, they removed a minimum threshold of 50% expected revenues from civilian application or share of civilian users to boost their firepower. Similarly, it also updated the rules to facilitate financing of small and medium-sized enterprises (SMEs) active in the field of security and defence.

The White Paper makes explicit calls for expanded EIB action on defence outlining several key initiatives to enhance its role in supporting Europe's security and defence sector. First, the EIB should plan to double its annual investment to €2 billion, directing funds toward critical projects such as drones, space, cybersecurity, quantum technologies, military infrastructure, and civil protection. Additionally, the EIB intends to refine its eligibility criteria, ensuring that excluded activities are more precisely defined and kept to a minimum. This adjustment aims to better align its investments with the EU's evolving policy priorities. Furthermore, the EIB should propose revising its operational framework by replacing the ad-hoc Strategic European Security Initiative with a dedicated, overarching public policy objective. This new approach will provide a stronger, more structured commitment to Europe's peace and security, backed by an ambitious financial and capital allocation. The White Paper also issues a direct call to the EIB's Board of Governors, urging them to "urgently step up support to the European defence industry, notably by further narrowing the list of excluded activities and increasing the volume of available funding.

While the Bank is so far still prohibited from investing in projects with purely military application, on [21 March](#), the EIB Board expanded the eligibility criteria for security and defence investments, minimising exclusions in line with EU leaders' proposals from 6 March. The €8 billion Strategic European Security Initiative (SESI) will now be part of a permanent public policy objective, with no fixed financing cap, and annual allocations will be set in the EIB Group Operational Plan. This change enables the EIB to support a wide range of defence-related projects, including military infrastructure, vehicles, drones, satellites, cybersecurity, border protection, and advanced technologies, while ensuring financial stability.

The expansion of the range of projects that would be eligible for EIB funding is raising questions on the implications on the rating of the bank. Today the EIB benefits from a triple AAA rating, yet it is uncertain whether a change in its mandate would affect its credit rating.

4.3. ESM loans

On 3 March, after attending an emergency summit on Ukraine in London, French President Emmanuel Macron [called](#) on Europeans to dramatically increase their yearly defence spending. To this purpose he suggested to give a mandate to the Commission to use innovative funding, such that common borrowing or the European Stability Mechanism (ESM). Although most of the financial instruments available in the [ESM toolbox](#) are crisis management tools to be used as last resort instruments when the situation of a Member State or its financial sector is already quite deteriorated, one of the instrument has indeed a preventive nature. Such financial assistance takes the form of a credit line that Member States may secure before they face major difficulties when raising funds in the capital markets. There are two types of [credit lines](#): the Precautionary Conditioned Credit Line (PCCL), for those Member States that comply with specific eligibility criteria, including compliance with the Stability and Growth Pact, and the Enhanced Conditions Credit Line (ECCL), for those Member States that do not comply with the eligibility criteria for PCCL. The granting of such precautionary credit line is not conditional to the launch of a full macro-adjustment programme, but to a lighter set of conditions enshrined in a Memorandum of Understanding (MoU) agreed with the Commission.

A precedent in this sense is represented by the [ESM Pandemic Crisis Support](#), proposed by the Eurogroup of [9 April 2020](#) and subsequently endorsed by the European Council on [23 April 2020](#), and based on the ECCL. The justification for this instrument were the difficulties created by the Covid-19 pandemic. The ESM

[could provide loans](#) amounting to 2% a country's GDP at very low interest rates to support domestic financing of direct and indirect healthcare, cure and prevention related costs. The Commission, in liaison with the ECB, and in collaboration with the ESM, provided for a [preliminary assessment](#) in respect to each ESM Member on the existence of a risk to the [financial stability](#) and [external sustainability](#) of the euro area, on whether the [public debt was sustainable](#), on the existence of [bank solvency problems](#) that would pose systemic threats to the stability of the euro area banking system, and on the actual and potential needs. Given the very specific and limited scope of that instrument, which was a one-off instrument of temporary nature, the Commission [recommended](#) - and the Eurogroup [endorsed](#) - a streamlined reporting and monitoring framework. Despite these simplifications and the limited conditionality, and although countries would pay a broadly similar interest rate for lending from [SURE](#) and [NGEU](#), not a single Member State tapped the ESM's support, while nineteen EU countries used the SURE program, and nine countries requested NGEU loans.

The White Paper notes that should demand by Member States for loan-based financing supported by the EU budget under SAFE outstrip supply, the Commission will continue to explore innovative instruments, "such as in relation to the European Stability Mechanism (ESM)." This indicates that the ESM option remains on the table as a potential future funding source for defence investments if the initial SAFE instrument proves insufficient to meet Member States' needs.

5. Market challenges and public procurement

5.1 Defence procurement complexities

A critical consideration is whether the focus should be on headline spending figures or on addressing the fragmentation and inefficiency of current defence expenditures.

Defence contracts fall into two types of modes of procurement, either between countries (one sovereign buying from another sovereign), or a government buying directly from market producers. According to publicly available information, the first type is quicker as a delivery mode, the second will typically involve a standard procurement procedure that can have long lead times in order to allow a sufficient number of offers to be sourced on the market and to find the economically most advantageous offer.

In this context the future European procurement of weapons could face the following challenges based on information discussed in public media. As outlined in the [Joint Communication](#) of 5 March 2024, 78% of the defence acquisitions by EU Member States between the start of Russia's war of aggression and June 2023 were made from outside the EU, with the US alone representing 63%. As explained by the president of the French Republic in his public address of 5 March, the only exception from this general pattern is France with a clearly identified national pipeline of procurement of weapons that encompasses all stages of the process from the identification of needs, the design of contracts, the award of contracts, the production, the use and ensuring the maintenance of availability of moving replaceable parts as well as the availability of munition throughout the life cycle of weapons products. The French president mentioned on 5 March also the successful launch of a military satellite by the new Ariane 6 as a step to start building European space based intelligence which is regarded as one of the major missing pieces for a future self-standing European defence.

Other than France, EU Member States have predominantly bought, or are in the process of buying, military assets from the U.S., in particular fighter jets (F35). Expensive U.S. produced weapons have indeed been a part of a dividend of the U.S. investment into European security and defence. Signed contract for F35 alone constitute many billions of euros in commitments and it is not clear if and how such contracts can be exited

and at which cost. These difficult questions are on the table now as U.S. equipment will always depend on U.S. support to be operational.

[On 5 March](#), President Macron explicitly mentioned those necessary changes in order to reduce the dependence on U.S. going forward: start buying European weapons; make the necessary changes to public procurement rules and systems to even allow such a switch to European products. One can to this the necessary changes to state aid and merger control framework enforced by the Commission, to allow a more coordinated procurement of arms from a future set of fewer and bigger producers. The European Commission's Directorate-General for Competition policy, DG COMP, has started work on such changes already in the context of the Competitiveness Compass (and the request was already in the mission letter to Executive VP Ribera), but the arms procurement dimension is certainly an additional focus of this broader horizontal work stream.

Anecdotal evidence⁴ is accumulating that EU based weapons producers can absorb some of the workforce that is set free by the scaling down of the automotive sector.⁵ However, one should not expect too much positive short-term impact for two simple reasons. First, the scale of the weapons industry is nowhere near the automotive sector that is going through a deep structural adjustment. Second, discussions around the [Special European Council summit on defence](#) of 6 March insisted on the fact that scaling up the EU military capabilities is a long-term endeavour with 5, 10, and 15 year horizons depending on the exact type of military capability. Munitions occupy the short term horizon, i.e., piling up stocks of munition is the most immediate measure that can be implemented. Ordering additional vehicles and air-based material as well as ships takes longer and requires the additional financing to be in place. Consolidating the types of weapons systems will be in a second step and may require product development. Entirely new systems and the finalisation of space-based military intelligence capability would then be the last step over such a 10-15 year horizon.

The March European Commission White Paper tries to address these procurement challenges directly.

It acknowledges that the European defence industrial sector has structural weaknesses and is currently unable to produce defence systems and equipment in the quantities and speed that Member States need.

The White Paper identifies several issues:

- The European defence industry remains too fragmented with dominant national players catering mostly to domestic markets
- It has suffered from under-investment and needs increased EU investment and sourcing
- Lack of collaboration has led to inefficiencies in capability development and imposed additional costs
- Low and fragmented defence spending on innovation negatively impacts emerging disruptive technologies vital for future capabilities

To address these issues, the White Paper outlines several initiatives:

1. *Defence Omnibus Simplification*: The Commission will present a dedicated Defence Omnibus Simplification proposal by June 2025 which will aim to:

- Increase cross-certification of defence products and facilitate mutual recognition of certification

⁴ In the context of recent plant closures or reduction of plant size by automotive producers (such as the Audi plant in Brussels) producers of weapons systems have declared to seek qualified personnel in the same area; however, the order of magnitude seems to be around 10% of the freed up workforce, i.e., these substitution impacts should not be overestimated in the short run (Sources: <https://www.autonews.com/manufacturing/suppliers/ane-suppliers-layoffs-benefit-defense-firms/>;

⁵ According to Financial Times on 31 January 2025, the European Association of Automotive Suppliers estimates that Europe's automotive sector has shed some 100,000 jobs in 2024 alone and the trend is still strong with more massive downscales announced for 2025 and beyond. In comparison, the anecdotal evidence of defence industry taking up some of the slack is typically in the hundreds of jobs for the time being. <https://www.ft.com/content/e990155b-29ac-4cf3-87cf-6924e1a24c8a> : "German defence groups turn to car supplier layoffs to meet soaring demand"

- Enable rapid grant of construction and environmental permits for defence industrial projects as a matter of public-interest priority
- Ensure timely availability and usability of all necessary materials in the EDTIB supply chain
- Remove obstacles to availability of military personnel and access to finance (including ESG investment)
- Facilitate exchange of confidential information under conditions ensuring both simplicity and security
- Streamline EU defence industrial programs to reduce delivery time and simplify management

2. *Strategic Dialogue with Industry*: The Commission will launch a Strategic Dialogue with the defence industry to discuss regulatory hurdles and industry challenges

3. *European Military Sales Mechanism*: The EU intends to launch a pilot to gradually set up a European Military Sales Mechanism to increase availability and delivery time for defence products from Europe

4. *Collaborative Procurement*: The White Paper proposes that Member States should reach a common target of 35% of total defence equipment procurement to be done collaboratively

5.2 Debt market implications

In contrast to this very structured and medium to long term developments, the financial impact of a structural shift away from the current model of a European lease of U.S. manufactured security can materialise much more quickly, not only because national resources need to be reorganised and rescheduled as of now to create space for the additional military expenditure, but also because debt markets immediately react to the expected future change in the volume of sovereign debt that will need to be issued (there seems to be a broad consensus that additional military spending should mostly be funded by issuance of new debt and not crowd out other important spending items or lead to an increase in the level of taxation; this consensus appears especially strong in the case of Germany, and the Commission's SAFE proposal not only embodies this consensus as well, but adds the notion that EU Member States with less fiscal space than Germany should not be excessively constrained by such lack of fiscal space).⁶

On 6 March, [FT reported](#) that Standard and Poor's expected global sovereign debt issuance in 2025 to reach USD 12.3 trillion, bringing the stock of global sovereign debt to USD 76.9 trillion. It is not clear how much of the 12.3 trillion is new debt and how much is due to rolling over existing debt. However, Germany alone has announced plans amounting to more than USD 1 trillion and China 2 trillion. On 20 March, the OECD warned in its [Global Debt Report](#) that debt service costs have now reached that highest level since the peak of the Great Financial Crisis in 2007 and stood at 3.3% of GDP in 2024 for the 38 OECD countries. This means that asking debt markets to absorb even more debt going forward as new defence related issuance would come on top of current funding needs will be challenging, and the OECD warns about the risk of crowding out other important funding needs.

Debt market priced in higher future issuance as well as higher economic activity. The implied return on the German Bund 10 year benchmark rose sharply in the wake of the announcement of German debt brake reform and the associated additional spending as market investors sold off debt and moved into higher yielding assets. While the cost of German debt remains comparatively low and Germany has a comparatively low level of debt, the cost of other EU Member States' debt tends to rise in parallel with the German

⁶ On 10 March 2025, the FT reports a survey of 28 economists where the consensus sees Germany able to raise its debt to GDP ratio from 63% to 86% of GDP (implying fiscal space of almost EUR 2 trillion) provided the additional spending is related to an increase in productive capacity and not simply in supporting final consumption. <https://www.ft.com/content/fd0cfe7e-3fc9-4218-9266-d19ad2954d4e>

benchmark. For highly indebted countries, the mere German announcement thus translated into immediate and non-negligible increase in the cost of funding the existing stock of debt.

The following examples can serve as an illustration.

An increase by 25 basis points of debt financing costs (roughly the increase between the announcement of new German spending on Tuesday, 4 March, and the start of the special summit in Brussels on Thursday, 6 March) translates into additional roughly 0.3 % of GDP in the case of Italy and France, and 0.4 % of GDP in the case of Greece. Of course this is a very rough high-level estimate, the actual additional cost depends on a wide range of factors including how refunding of existing debt plays out across the calendar, and also if there are significant changes to the maturity structure of the debt stock.

The White Paper acknowledges these debt market implications and emphasises the need for financial predictability. It states that *"the Commission will continue to explore additional funding sources for defence at EU level and further elements and options to substantially boost financing for European defence and to strengthen the EDTIB."* It specifically notes that *"Given the urgency and priority for Europe to rebuild its defence, underpinned by a competitive defence industrial base, the next MFF should provide a comprehensive and robust framework in support of EU defence."*

The White Paper also highlights the need to mobilise private capital through the Savings and Investment Union, which *"should help channel additional private investment towards EU priorities, including the defence sector."* It states this could *"attract hundreds of billions of additional investments per year in the European economy, boosting its competitiveness."*

Additionally, the White Paper addresses ESG investment concerns, noting that *"The EU's Sustainable Finance Disclosures Regulation (SFDR) does not prevent the financing of the defence sector. However, both the finance and defence sector may benefit from additional clarification on the application of the SFDR. The Commission will provide the necessary clarification in the context of the review of the SFDR, on the relationship of defence with the investment goals of the sustainability framework."*

6. Conclusion and outlook

The ReArm Europe initiative represents a significant evolution in European defence policy and financing, responding to an urgent security environment that requires substantial investment in defence capabilities. **However, the approach taken by the Commission raises important questions about both its effectiveness and its implications for the EU's broader fiscal and institutional framework.**

The Commission's strategy appears to prioritise expediency over systematic reform. By relying on the interpretation of (recently revised) existing rules – particularly the national escape clause and Article 122 TFEU – rather than pursuing targeted amendments to the fiscal rules or Treaty provisions, the Commission has created short-term fiscal space but potentially at the cost of long-term coherence and credibility. The interpretation of the national escape clause, originally designed for country-specific temporary emergencies rather than continent-wide structural defence needs, creates particular concerns about the integrity of the newly reformed economic governance framework.

The financing approach also presents limitations. The loan-based SAFE instrument may prove insufficient to address the scale of investment required, particularly for Member States with already high debt levels. Unlike grants, loans must be repaid with interest, potentially exacerbating fiscal pressures in the medium term. This creates a potential "fiscal cliff" when both the SAFE instrument and national escape clauses expire, leaving Member States to integrate substantially higher defence expenditure into regular budgets under normal fiscal rules.

The projected economic benefits warrant scrutiny. The Commission's projections for EUR 800 billion in defence investment rely on untested assumptions about fiscal multipliers, which economic research

suggests are typically lower for defence spending than for other public investments. With defence multipliers potentially below 1.0, the fiscal impact could be larger than anticipated, particularly for highly indebted countries, and may not generate the expected economic growth to offset increased debt burdens.

The legal foundations of the initiative also deserve scrutiny. The Commission's interpretation of Article 41(2) TEU—arguing that loans for military expenditure do not constitute "expenditure" in the Treaty sense—represents a narrow technical reading that may not align with the provision's intended purpose. **The lack of European Parliament involvement under Article 122 TFEU also raises democratic legitimacy concerns for such a significant policy initiative.**

Furthermore, the Commission's approach risks creating divergences between Member States. Countries with stronger fiscal positions can more easily increase defence spending without concerns about debt sustainability, while those with limited fiscal space face difficult trade-offs between security imperatives and economic stability. Without a more comprehensive burden-sharing mechanism, these divergences could undermine both defence readiness and economic cohesion.

Despite these concerns, the White Paper does provide a comprehensive framework for addressing critical capability gaps and strengthening the European defence industrial base. Its emphasis on collaborative procurement, supply chain resilience, and innovation addresses important structural weaknesses in European defence. The identification of seven priority capability areas creates clear focus for investment, and the proposed Defence Omnibus Simplification regulation could remove significant regulatory barriers.

The success of the ReArm Europe initiative will ultimately depend on several factors: the willingness of Member States to prioritise collaborative approaches over national ones; the ability to overcome procurement fragmentation and create genuine industrial integration; the willingness to create genuine industrial integration rather than merely increasing spending; the management of debt market responses to increased borrowing; the resolution of data collection challenges for consistent defence expenditure monitoring; and the development of a more sustainable long-term framework for defence financing that reconciles security imperatives with fiscal discipline.

The implementation of these plans will require close coordination between EU institutions and Member States, as well as substantial financial commitments in the years ahead.

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Annex 1 – Relevant preventive arm provisions

Recognition of defence as a Common EU Priority

- **Article 13(c)(iv)**: Requires Member States to "*explain how [they] will ensure the delivery of reforms and investments responding to... the following common priorities of the Union: (iv) where necessary, the build-up of defence capabilities*"
- **Recital 10**: Specifies that plans should include investments that address "*implementing the Strategic Compass for Security and Defence, or subsequent Union acts relevant for those priorities*"

Extension of Fiscal Adjustment Periods

- **Article 14(1)**: States that "Where a Member State commits to a relevant set of reforms and investments in accordance with the criteria set out in paragraph 2, the adjustment period may be extended by up to three years"
 - **Article 14(2)(c)**: Specifically requires that the set of reforms and investments "addresses the common priorities of the Union referred to in Article 13, point (c)" – which explicitly includes "where necessary, the build-up of defence capabilities" as established in Article 13(c)(iv)

Against this background, a Member State making significant defence investments can request an extension of their fiscal adjustment period (from 4 to up to 7 years) and therefore a more gradual fiscal adjustment timeline, providing Member States with additional fiscal space to build necessary defence capabilities, by demonstrating that these defence investments:

- Address the common Union priority of defence capabilities (Article 13(c)(iv))
- Are sufficiently detailed, time-bound and verifiable (Article 14(3))

National Medium-Term Fiscal-Structural Plans

- **Article 13(g)(v)**: Requires plans to contain information on "*public investment needs including those related to the common priorities of the Union referred to in point (c)*" (including defence)

Escape clauses

- **Article 26(1)**: Establishes that "*Following a request from a Member State and on a recommendation by the Commission based on its analysis, the Council may ... adopt a recommendation allowing a Member State to deviate from its net expenditure path... where exceptional circumstances outside the control of the Member State have a major impact on the public finances of the Member State concerned*"
- While not explicitly referencing defence, urgent security threats or major unforeseen defence procurement requirements could potentially qualify as "*exceptional circumstances*" if they have a "*major impact on public finances*". One of the main shortcomings may however be represented by the one-year time limit.
- **Article 26(2)**: Allows the Council to "*extend the period during which that Member State may deviate from the net expenditure path*" if exceptional circumstances persist.

Annex 2 – Relevant corrective arm provisions

The corrective arm establishes a clear procedural pathway for considering defence spending when assessing potential excessive deficits:

Step 1: Commission Report must consider defence investments

- **Article 2(3)(da)**: Requires the Commission's excessive deficit report to explicitly reflect "*the increase of government investment in defence, where applicable, considering also the time of recording of military equipment expenditure*"
- Against this background, when preparing reports under Article 126(3) TFEU on potential excessive deficits, the Commission must specifically analyse and document defence investment increases

Step 2: Assessment of defence spending as a relevant factor by the Commission

- **Article 2(4)**: When preparing its report, the Commission must "*give due and express consideration to any other factors*" relevant to assessing compliance with deficit and debt criteria
- The provision specifically requires "*particular consideration*" be given to "*financial contributions to fostering international solidarity and achieving the common priorities of the Union*" (which explicitly includes defence capabilities as per Article 13(c)(iv) of the preventive arm)
- **Recital 14a**: Provides clear justification by acknowledging "*the rising geopolitical tensions and security challenges and the corresponding need for Member States to build-up their capabilities*" and explicitly states that increases in defence investment "*should be considered as a relevant factor when assessing the existence of an excessive deficit*"

Step 3: Balanced overall assessment by Council and Commission and impact on decision making

- **Article 2(4)**: The Council and Commission must make a "*balanced overall assessment of all the relevant factors,*" evaluating whether they should be considered as "*aggravating or mitigating factors*"
- Defence investments can thus serve as mitigating factors when a Member State exceeds deficit or debt thresholds
- While defence spending alone cannot exempt a Member State from an EDP, the procedural requirements ensure that:
 - Defence investments must be documented in Commission reports
 - They must be explicitly considered as potential mitigating factors
 - They form part of the "*balanced overall assessment*" that informs the final decision
- This procedural framework creates a formal mechanism through which defence spending increases can be considered as mitigating factors when determining whether an excessive deficit exists and in setting correction timelines (**Articles 3(6) and 5(2)** – also allowing for revised EDP recommendations based on "exceptional circumstances").

Annex 3 – Government expenditure on defence in EU Member States

	Defence, in % of GDP					Military defence, in % of GDP				
	2019	2020	2021	2022	2023	2019	2020	2021	2022	2023
BE	0,8	0,9	0,9	1,0	0,9	0,8	0,9	0,8	0,9	0,9
DE	1,0	1,1	1,0	1,0	1,1	0,9	1,0	0,9	0,9	0,9
EE	2,1	2,4	2,0	2,2	2,7	2,0	2,3	2,0	2,0	2,6
IE	0,2	0,2	0,2	0,2	0,2	0,2	0,2	0,2	0,2	0,2
EL	2,0	2,5	2,7	2,6	2,2	2,0	2,5	2,7	2,6	2,2
ES	0,8	0,9	0,9	1,1	0,9	0,7	0,8	0,8	1,0	0,8
FR	1,7	1,9	1,7	1,8	1,8	1,5	1,6	1,5	1,6	1,6
HR	1,1	1,1	1,0	1,0	1,3	1,1	1,1	1,0	0,9	1,2
IT	1,3	1,4	1,4	1,2	1,2	1,2	1,3	1,3	1,1	1,1
CY	1,7	1,8	1,7	1,5	1,9	1,6	1,7	1,6	1,4	1,8
LV	2,0	2,5	2,5	2,4	3,1	1,9	2,5	2,4	1,8	2,6
LT	1,6	2,3	1,8	2,1	2,5	1,3	1,9	1,4	1,5	2,1
LU	0,4	0,7	0,5	0,5	0,6	0,3	0,6	0,4	0,4	0,3
MT	0,6	0,5	0,5	0,5	0,4	0,6	0,5	0,5	0,5	0,4
NL	1,2	1,3	1,3	1,3	1,3	1,1	1,2	1,2	1,1	1,1
AT	0,6	0,6	0,6	0,6	0,6	0,6	0,6	0,6	0,6	0,6
PT	0,8	0,8	0,8	0,8	0,8	0,7	0,7	0,7	0,7	0,7
SI	1,0	1,1	1,2	1,2	1,2	0,8	0,8	1,0	0,9	1,0
SK	1,1	1,2	1,4	1,0	1,2	1,1	1,1	1,2	0,8	-0,1
FI	1,2	1,4	1,2	1,2	1,4	1,1	1,2	1,1	1,1	1,1
EA	1,2	1,3	1,2	1,2	1,2	1,0	1,1	1,1	1,1	1,0
BG	1,2	1,5	1,6	1,6	1,5	1,1	1,4	1,5	1,5	1,4
CZ	0,9	1,0	0,9	1,0	1,2	0,8	0,9	0,8	0,9	1,1
DK	1,1	1,2	1,2	1,2	1,8	1,1	1,1	1,1	1,1	1,3
HU	1,0	1,1	1,1	1,4	1,9	1,0	1,1	1,1	1,4	1,8
PL	1,6	1,7	1,6	1,6	2,1	1,6	1,7	1,5	1,6	1,9
RO	1,7	2,3	1,9	1,8	1,7	1,6	2,3	1,9	1,8	1,7
SE	1,2	1,4	1,3	1,7	1,8	1,0	1,1	1,2	1,4	1,5
EU	1,2	1,3	1,2	1,3	1,3	1,1	1,2	1,1	1,1	1,1

Source: [Eurostat](#), data extracted on 26 March 2025