



# Defence Spending in Europe in Light of the Economic Crisis

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## Abstract

The economic crisis has impacted deeply on defence spending in Europe. It has led to uncoordinated cuts to defence budgets at national level, but has also revived interest in bilateral and multilateral cooperation. Both the EU and NATO have made an effort to involve European countries in cooperative projects, under the banners of “Pooling and Sharing” and “Smart Defence” respectively, with limited results. At the same time, the European Commission has adopted two directives regarding defence spending, and the European Defence Agency has been strengthened. While defence spending remains predominantly a national prerogative, European countries will soon face the choice of pooling certain capabilities at international level or losing them because of insufficient spending. In this light, Italy is rationalizing its defence budget, while preserving its commitments to international cooperation.

**Keywords:** *European Union / NATO / European countries / Italy / Economic crisis / Defence budget / Military procurement / Defence cooperation / European Defence Agency (EDA) / Smart defence / Pooling and sharing*

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## Defence Spending in Europe in Light of the Economic Crisis

by Alessandro Marrone\*

### Introduction

The financial and economic crisis is shaking the foundations of the European Union (EU). At the same time, problems affecting European defence spending remain unsolved despite the military shortfalls epitomized by the recent operations in Libya and Afghanistan. This paper analyses the impact of the crisis that began in 2009 on the defence spending of European Union Member States (MS). In particular, the focus is on defence procurement at national, multilateral and EU/NATO level. A specific section is dedicated to Italy, whose role is often under-analysed despite the fact that the country has the fourth largest defence budget in Europe and is one of the main contributors to both EU and NATO crisis management operations.

The paper will look first at the situation before the economic crisis by underlining structural elements of defence spending and assessing the multilateral frameworks in which part of defence spending takes place. Then it will evaluate the impact of the economic crisis at national and EU levels, and the renewed interest of member states in defence cooperation aimed at cost-saving. In this context, the paper outlines how Italy has undertaken a process of rationalization of its defence spending.

### 1. The situation before the European economic crisis

#### 1.1. Three structural elements of defence spending in the pre-crisis period

Defence procurement is aimed at acquiring the whole range of military capabilities used by armed forces. Procurement traditionally involves either purchasing equipment “off-the-shelf” or funding the Research & Development (R&D) and production programmes needed to acquire a certain military capability.

The defence spending of European countries was heavily influenced by the strategic context of the Cold War and post-Cold War periods. While analysis of such contexts is beyond the scope of this paper, suffice it to say here that three structural elements characterized the *status quo* that preceded the current economic crisis. These three elements have influenced Western Europe since the 1950s, and Eastern European countries since their integration into NATO and the EU. They remain relevant today, although the crisis has affected their specific meanings.

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First, defence spending remained firmly within the competences of EU MS despite the European integration process. The acquisition of defence capabilities was exempted from EU single market rules, and up until the economic crisis no international or supranational EU institution had regulatory or political powers in this field.

Second, particularly since the 1980s, European countries have undertaken a number of multilateral procurement programmes aimed at jointly acquiring complex, expensive and high-tech military capabilities, considered unaffordable on a national basis. These programmes have usually featured the participation of few European countries willing and able to acquire a certain military asset. Through such bilateral or multilateral initiatives and despite frequent delays and increases in costs, important European military capabilities were acquired, like the Tornado and Eurofighter fighter aircraft.<sup>1</sup> At times they involved only two countries, such as in the case of the FREMM frigate, produced jointly by France and Italy in recent years.

A third element that marked European defence procurement in the pre-crisis period is the strong reliance on US supplies, through off-the-shelf acquisitions, under licensed production of American products, or transatlantic procurement programmes such as the ongoing one aimed at delivering the 5<sup>th</sup> generation F-35 fighter aircraft. Transatlantic procurement programmes allowed for the economies of scale needed to obtain certain capabilities, despite rising costs and delays.<sup>2</sup>

### *1.2. Multilateral, EU and NATO frameworks for defence spending*

Since the 1990s, a number of European multilateral frameworks outside the EU governance system have been set up to increase cooperation among MS in the defence domain. For example, the Organization conjointe de coopération en matière d'armement (OCCAR) was established by Belgium, France, Germany, Italy, Spain and the UK in 1996 to manage joint procurement programmes agreed by participating members.<sup>3</sup> In 1998, the Letter of Intent/Framework Agreement (LOI/FA) forum was established by France, Germany, Italy, Spain, Sweden and the UK to create the necessary political and legal framework to facilitate industrial restructuring, also through the harmonization of military requirements in the six countries. However, up until 2009, these initiatives did not have a significant impact on the way MS managed defence procurement. The harmonization of military requirements did not make significant progress despite the LOI/FA's efforts, and the amount of defence procurement funds managed by OCCAR remained very low in comparison to those managed at the national level.

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<sup>1</sup> Both capabilities were jointly acquired by Germany, Italy, Spain and the UK.

<sup>2</sup> The F-35 procurement programme envisages the participation of Denmark, Italy, Netherlands, Norway and the UK alongside Australia, Canada, the US and Turkey. Michele Nones, Giovanni Gasparini, Alessandro Marrone, "Europe and the F-35 Joint Strike Fighter (JSF) Program", in *IAI Quaderni English series*, No. 16 (July 2009), <http://www.iai.it/content.asp?langid=2&contentid=143>.

<sup>3</sup> Currently, also Finland, Luxembourg, the Netherlands, Poland, Sweden and Turkey participate in one or more OCCAR Programmes.

The EU as such only began to play a minor role in defence spending in the 2000s.<sup>4</sup> The need for European cooperation on defence spending was affirmed by the “Headline Goal Process” initiated with the 1999 Helsinki Headline Goals and re-launched with the Declaration on Strengthening Capabilities issued by the European Council in 2008. In 2004, a Joint Action of the European Council established the European Defence Agency (EDA) to work on four aspects of the acquisition of military capabilities: research and technology, industry and market, armaments cooperation, and capabilities. At the same time, the European Commission’s Seventh Framework Programme (FP7) started funding research related to internal security, for example with regard to the protection against Nuclear, Biological, Chemical and Radiological (NBCR) attacks or incidents. In these fields, technologies are often dual-use: the same system or technology can be used for civilian and military purposes regardless of its original design.

The EU, through the Commission and in cooperation with the European Space Agency (ESA), has also funded the acquisition of space capabilities such as Galileo and the Global Monitoring for Environment and Security (GMES). In particular, the Commission, through the FP7, has financed research on downstream space applications and services to be derived from Galileo and GMES, while the ESA has managed the development and production of assets (such as satellites, sensors and ground stations) through national contributions by its members.<sup>5</sup> The intrinsic dual-use feature of space technologies allows civil and military uses of space assets, for instance in the field of satellite communications, Earth observation and navigation.

As a whole however, EU influence on defence spending was very limited until 2009, as it did not affect the bulk of European defence budgets, either in terms of regulations or in terms of investments.

Unlike the EU, NATO has traditionally been the cornerstone of European defence since the onset of the Cold War and throughout its aftermath. It has proved to be a significant engine of harmonization with regard to military doctrine, tactics and procedures, as well military standards through over 1,300 NATO Standardization Agreements (STANAGs). Since the 1990s, the Atlantic Alliance has conducted a number of military operations involving substantial European contributions. In this sense, NATO has provided an indirect contribution to the standardization and convergence of European military capabilities. NATO has also provided a direct contribution by managing few trans-national procurement programmes: the Airborne Early Warning and Control Programme, established in 1978 and currently involving 17 NATO members<sup>6</sup>; the acquisition of the NH90 multi-role helicopter by ten European countries<sup>7</sup> through the NATO Helicopter Management Agency (NAHEMA), and the Medium Extended Air

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<sup>4</sup> EU efforts in the field of foreign and security policy, including military and civilian operations outside EU territory, are beyond the scope of this paper.

<sup>5</sup> ESA has a different membership with respect to the EU, as it also includes, for example, Canada and Switzerland.

<sup>6</sup> Belgium, Canada, Czech Republic, Denmark, Germany, Greece, Hungary, Italy, Luxembourg, The Netherlands, Norway, Poland, Portugal, Romania, Spain, Turkey, and the United States.

<sup>7</sup> NH90 is being acquired by nine MS: Belgium, Finland, France, Germany, Greece, Italy, the Netherlands, Spain and Sweden. Norway has also bought the NH90.

Defence System (MEADS). Notwithstanding these three examples, and as with the EU, NATO has not had an important role in the defence spending field.

Until 2009, European defence spending thus remained predominantly a prerogative of the member states. As one observer aptly pointed out, despite the fact that Europeans have jointly conducted large military operations over the last two decades, in peace time they have continued to equip their militaries in a national, “insular”, manner.<sup>8</sup> This situation has caused an inefficient use of resources through the duplication of efforts among MS and the low interoperability of European military equipment. Moreover, it is one of the main reasons for the 27 MS’ inability to deploy more than 10 percent of their armed forces abroad, which together amount to 1.7 million soldiers.

## 2. The impact of the economic crisis

The global financial crisis and the ensuing Eurozone crisis have had discernible impacts on defence spending at national, EU and multilateral levels.

### 2.1. The national level: uncoordinated cuts and limited cooperation

At the national level, the economic crisis has led to substantial cuts in defence budgets particularly in 2010-2011. The extent of the cuts is different across Europe, with the German defence budget remaining relatively stable, while deeper cuts have been made in France and Spain.<sup>9</sup> The UK in 2010 planned to reduce its defence budget by 7.5 percent over four years, but in reality the cuts may have been deeper.<sup>10</sup> Most other MS have reduced their defence budgets by 10-30 percent.<sup>11</sup> As a whole, almost all MS - with the significant exception of Poland - have reduced, to different degrees, the share of the state budget devoted to defence, and this trend is likely to continue in the years ahead. This has implied, among other things, reduced investments in defence procurement, for example by decreasing the number of assets to be acquired or by postponing their acquisition. Some procurement plans have been completely cancelled. Not only have cuts been planned and implemented on a national basis, but there has been little information sharing among MS on their respective budgetary decisions and no effective coordination has taken place to prevent the cancellation of a particular military capability in the EU. The risk is that the EU as a whole may lose certain military capabilities as a result of uncoordinated decision-making.<sup>12</sup>

<sup>8</sup> Tomas Valasek, *Surviving austerity. The case for a new approach to EU military collaboration*, London, Centre for European Reform, April 2011, <http://www.cer.org.uk/publications/archive/report/2011/surviving-austerity-case-new-approach-eu-military-collaboration>.

<sup>9</sup> Alessandro Marrone, “La crisi abbatte i bilanci della difesa”, in *AffarInternazionali*, 26 July 2012, <http://www.affarinternazionali.it/articolo.asp?ID=2095>.

<sup>10</sup> Clara Marina O'Donnell (ed.), *The Implications of Military Spending Cuts for NATO's Largest Members*, Washington, Brookings Institution, July 2012 (Analysis Paper), <http://www.brookings.edu/research/papers/2012/07/military-spending-nato-odonnell>.

<sup>11</sup> House of Lords European Union Committee, *European Defence Capabilities: lessons from the past, signposts for the future*, London, The Stationery Office Limited, May 2012 (HL Paper 292), <http://www.publications.parliament.uk/pa/ld201012/ldselect/lducom/292/292.pdf>.

<sup>12</sup> Christian Mölling and Sophie-Charlotte Brune, *The Impact of the Financial Crisis on European Defence*, Brussels, European Parliament, May 2011 (Policy Department External Policies Study), <http://www.europarl.europa.eu/committees/en/studiesdownload.html?languageDocument=EN&file=40671>.

The cuts in defence budgets are one of the main reasons for the recent revival of bilateral and multilateral agreements outside the EU institutional framework. The most important example in this regard is the agreement signed by France and the UK in November 2010. This envisaged a package of joint defence procurement initiatives, including R&D investments in new military capabilities such as Unmanned Aerial Systems (UAS), as well as studies on missiles, submarines and satellites communications.<sup>13</sup> Germany and Italy also signed a joint letter of intent in November 2011 on defence procurement cooperation in fields such as UAS, submarine development, long-range precision munitions and pilot training. Following this agreement, Italian and German defence industry associations signed a cooperation agreement in December 2011 covering UAS, unmanned ground vehicles, guided munitions, satellites and missiles.<sup>14</sup>

Other recent initiatives to foster defence cooperation among small groups of like-minded MS include the Weimar Triangle composed of France, Germany and Poland, whose political role resurfaced after 2009 to seek opportunities for cooperation and savings; the Nordic Group encompassing the Scandinavian countries; the Visegrad Four including the Czech Republic, Hungary, Poland and Slovakia; and the Benelux Group made up of Belgium, Luxembourg and Netherlands. Such mini-lateral frameworks have achieved some concrete results with respect to logistics and training related to existing military capabilities. For example, the Netherlands and Belgium have completely pooled the maintenance of their navies' vessels and the training of crews, while keeping the actual fleets under separate national ownership.<sup>15</sup>

However, as a whole these bilateral or mini-lateral frameworks have delivered mixed and limited results so far,<sup>16</sup> without substantially improving the effectiveness and/or the efficiency of European defence spending.

## 2.2. The EU level: EDA developments and Commission directives

At EU level, the economic crisis has not directly influenced the current Commission's FP7 and ESA activities, since they are based on predefined, long-term budgetary cycles. However, EU and ESA budgetary constraints have fuelled a reflection on future investment plans in space capabilities and related funds. Indeed, a review could take place with regard to "Horizon 2020", the FP7's successor to finance EU-wide research from 2014 to 2020. In both cases, investments in dual-use capabilities relevant for European security and defence may be reduced.

<sup>13</sup> Stefano Silvestri e Alessandro Marrone, "La pax franco-britannica non basterà", in *Risk*, a. 11., n. 59 = 15 (novembre-dicembre 2010), p. 25-27, [http://issuu.com/risk\\_rivista/docs/risk\\_59](http://issuu.com/risk_rivista/docs/risk_59).

<sup>14</sup> Tom Kington and Albrecht Müller, "Italy, Germany Make Their Own Pacts", in *DefenseNews*, 19 December 2011, <http://www.defensenews.com/article/20111219/DEFFEAT04/112190321>.

<sup>15</sup> Tomas Valasek, *Governments need incentives to pool and share militaries*, London, Centre for European Reform, 1 November 2011, <http://www.cer.org.uk/insights/governments-need-incentives-pool-and-share-militaries>.

<sup>16</sup> Mart Laar, "How austerity is deepening Europe's defence crisis", in *Europe's World*, No. 21 (Summer 2012), p. 30-35, [http://www.europesworld.org/NewEnglish/Home\\_old/Article/tabid/191/ArticleType/articleview/ArticleID/21999/language/en-US/Default.aspx](http://www.europesworld.org/NewEnglish/Home_old/Article/tabid/191/ArticleType/articleview/ArticleID/21999/language/en-US/Default.aspx).

The economic recession and in particular the European sovereign debt crisis have sparked substantial changes in EU economic governance over the last two years. So far, this process has not materialised in the defence domain. However, two important developments at EU level have occurred since 2009: the strengthening of the EDA and the new Commission regulations regarding defence procurement.

The EDA developments spurred by the Lisbon Treaty have enhanced the Agency's role by providing a legal basis for its activities, as with other full-fledged EU institutions, thus paving the way for its further enhancement. The EDA subsequently capitalized on this development in two ways. First, in July 2012 a new Agency Statute was approved by the European Council. According to the new Statute, the institution's primary mission is to support the efforts of the Council and MS to enhance EU crisis management capabilities and to sustain the EU's Common Security and Defence Policy (CSDP). The EDA was also tasked with identifying the operational requirements of European armed forces and promoting actions to satisfy such requirements; identifying and implementing any measure to strengthen the defence industrial base; contributing to the definition of an EU policy on defence capability and armaments; and supporting the Council in the evaluation of military capabilities.<sup>17</sup> As a whole, the new Statute clarified the EDA's tasks with regard to defence procurement cooperation, and strengthened its role by linking the Agency more closely to the EU. A second important step forward for the EDA was the signing of a series of agreements with other relevant European actors to increase coordination and cooperation. In 2010, the Commission, the EDA and ESA launched a European Framework Cooperation scheme aimed to synchronize and complement research activities in the three frameworks, and to allow for mutual use of results. In 2011, EDA and ESA signed an Administrative Agreement on Cooperation, establishing a structured relationship between the two agencies through the coordination of their activities, especially regarding space assets and the development of European capabilities for crisis management and CSDP. In July 2012, EDA signed an agreement with OCCAR allowing the latter to manage defence procurement programmes agreed by MS within the EDA framework and envisaging information sharing between the two institutions.

At the EU level, in 2009 the Commission intervened for the first time in the field of defence spending with two new directives affecting the way MS manage defence procurement - the so-called "defence package". The first directive on defence procurement limits the exemptions to the EU single market's rules set out in Art. 296 of the Treaty of the Functioning of the European Union,<sup>18</sup> in order to increase the standardization of defence procurement and the competitiveness of the European defence market. The second directive facilitates the intra-EU transfer of defence products, technologies and services by reducing and easing the bureaucratic controls previously put in place by national authorities.<sup>19</sup> The two directives have an important,

<sup>17</sup> Alessandro Marrone and Stefano Felician, *Observatory on European Defence*, July-August 2011, <http://www.iai.it/content.asp?langid=2&contentid=669>.

<sup>18</sup> Michele Nones, "Un mercato della difesa più europeo", in *Affari Internazionali*, 15 January 2009, <http://www.affarinternazionali.it/articolo.asp?ID=1040>.

<sup>19</sup> Michele Nones, "L'Ue verso un mercato unico della difesa", in *Affari Internazionali*, 19 December 2008, <http://www.affarinternazionali.it/articolo.asp?ID=1028>.

long-term effect on defence cooperation because they improve the integration of the European defence market and could lead to a change in how defence procurement operates. However, the directive's impact will depend on the implementation by the MS and their translation into national legislation. Moreover, European governments retain a strong role in defence procurement and old habits are likely to die hard: the majority of MS still try to maintain as many military capabilities as possible on a national basis; most purchases take place nationally; and where possible preference is given to national suppliers.<sup>20</sup>

### 2.3. Member State interest in saving money through cooperation

As mentioned above, developments within the EDA and the Commission directives have not been driven primarily by the crisis. This said, the defence budget cuts triggered by the crisis have slightly increased member states' interest in saving money through European cooperation on defence procurement.

This renewed interest has been directed mainly towards opportunities for Pooling & Sharing existing capabilities or those planned to be acquired. In December 2010, the adoption at EU level of the so-called "Ghent Framework" provided a political umbrella for European Pooling & Sharing initiatives.<sup>21</sup> Within the EU framework, the EDA has made a number of proposals for small, cost-effective initiatives in areas which are less sensitive to national interest considerations. An example is the development of systems to counter the threat to European militaries deployed in Afghanistan of Improvised Explosive Devices (IED). In December 2011, this process also led to the identification by the European Council of 11 "specific concrete" projects, including on air-to-air refuelling, precision guided munitions, intelligence, surveillance and reconnaissance including space situational awareness, and satellite communications. While there has been some progress in the last two years, notably on air-to-air refuelling, the fundamental challenge is still to achieve a critical mass of MS participating in each of these projects.<sup>22</sup> As a whole, European Pooling & Sharing is not yet living up to its potential.<sup>23</sup>

In parallel, NATO has launched the Smart Defence initiative, aimed at making allies' defence expenditures more efficient and effective through greater cooperation and coordination. The initiative was strongly supported by Secretary General Anders Fogh Rasmussen in 2011-2012, and gained momentum prior to the Summit of Heads of States and Government held in Chicago in May 2012. Yet the Chicago Summit somehow downplayed expectations regarding implementation: the Smart Defence

<sup>20</sup> Daniel Calleja-Crespo and Pierre Delsaux, "Defending European defence: the Commission's role", in *BEPA monthly brief*, No. 54 (March 2012), p. 6-7, [http://ec.europa.eu/bepa/publications/index\\_en.htm](http://ec.europa.eu/bepa/publications/index_en.htm).

<sup>21</sup> Giovanni Faleg and Alessandro Giovannini, "The EU between Pooling & Sharing and Smart Defence. Making a virtue of necessity?" in *CEPS Special Reports*, No. 61 (May 2012), <http://www.ceps.eu/node/6956>.

<sup>22</sup> Sven Biscop and Jo Coelmont, "Military Capabilities: From Pooling & Sharing to a Permanent and Structured Approach", in *Security Policy Briefs*, No. 37 (September 2012), <http://www.egmontinstitute.be/papers/12/sec-gov/SPB37.pdf>.

<sup>23</sup> Christian Mölling, "Pooling and Sharing in the EU and NATO", in *SPW Comments*, No. 2012/C 18 (June 2012), [http://www.swp-berlin.org/fileadmin/contents/products/comments/2012C18\\_mlg.pdf](http://www.swp-berlin.org/fileadmin/contents/products/comments/2012C18_mlg.pdf).



Concept laid out at the time was little more than a starting point for the process.<sup>24</sup> The path and pace of progress is unclear, and NATO's attention seems mainly devoted to the transition in Afghanistan. The most relevant examples of Smart Defence are the procurement programme managed by NATO to acquire an Alliance Ground Surveillance system, joined by 13 participating nations,<sup>25</sup> and the build-up of a NATO-wide interim missile defence capability. Other twenty small, specific Smart Defence projects were endorsed by the Summit.

EU Pooling & Sharing and NATO's Smart Defence partly overlap because they largely address the same set of European defence budgets, insofar as US defence procurement is so large that it does not need to be coordinated and/or pooled and shared with European counterparts. With regard to both, ongoing initiatives may eventually make some progress in the coming years, but so far there has not been a step change in European defence spending. In 2010, only 23 percent of European investment in defence procurement was spent through multinational programmes,<sup>26</sup> and this percentage has not increased substantially to date.

In this context, FA/LOI and OCCAR have not seized the opportunity provided by the economic crisis to launch new initiatives or to renew their role. However, the signing of the aforementioned agreement between OCCAR and EDA paves the way for important synergies, whereby the EDA can act as the forum in which agreements on multinational procurement programmes between interested MS can take place and subsequently be managed by OCCAR.

#### *2.4. Defence procurement and the economic crisis: looking ahead*

The cuts in defence budgets as a result of the economic crisis will likely lead to more substantial changes in defence spending over the next years. In fact, the reductions in defence budgets that have occurred in the last three years are expected to remain in place over the next decade. This means that MS ministries of defence will soon reach the threshold beyond which they will no longer be able to maintain the military capabilities needed to perform expeditionary missions such as those carried out in the last two decades. For example, NATO's air operations in Libya in 2011 revealed the inability of MS to establish and implement a no-fly zone without substantial US support in terms of military capabilities. This means either that MS will have to bolster their military strength through closer cooperation and partial integration or that they will no longer have adequate forces to intervene in situations where key European interests are at stake.<sup>27</sup> This inability affects not only the eventual conduct of expeditionary operations, but also the capabilities for territorial defence, which would be undermined in the medium term in several MS.<sup>28</sup> As a result, there is a growing awareness in

<sup>24</sup> Julian Hale, "NATO Considers Process To Harmonize Defense Procurement", in *DefenseNews*, 25 May 2012, <http://www.defensenews.com/article/20120525/DEFREG01/305250006>.

<sup>25</sup> Bulgaria, Czech Republic, Estonia, Germany, Italy, Latvia, Lithuania, Luxembourg, Norway, Romania, Slovak Republic, Slovenia and US.

<sup>26</sup> European Defence Agency, *Defence Data: EDA Participating Member States in 2010*, Brussels, EDA, 7 March 2012, [http://www.eda.europa.eu/publications/12-03-07/National\\_Defence\\_Data\\_2010](http://www.eda.europa.eu/publications/12-03-07/National_Defence_Data_2010).

<sup>27</sup> Tomas Valasek, *Surviving austerity*, cit.

<sup>28</sup> Thorvald Stoltenberg, *Nordic cooperation on foreign and security policy*, Oslo, 9 February 2009, [http://www.mfa.is/media/Frettatilkygning/Nordic\\_report.pdf](http://www.mfa.is/media/Frettatilkygning/Nordic_report.pdf).

Europe that the choice is no longer between acquiring a military capability on a national basis or through multinational cooperation: the choice is between acquiring it through multinational cooperation or not acquiring it at all.

This growing awareness will undoubtedly increase European governments' readiness to negotiate multinational procurement programmes with other like-minded MS for certain capabilities recognized as indispensable for national defence policy. Such a multinational approach may take place through bilateral, mini-lateral, EDA or NATO frameworks. It will continue to face strong obstacles, for example in terms of operational sovereignty or diverging industrial policies in MS, but it is unlikely to reverse. In the meanwhile, it is likely that the need for expeditionary operations will continue in the near future,<sup>29</sup> thus maintaining external pressure to preserve effective European military capabilities.

### 3. The economic crisis and Italy

The economic recession and the sovereign debt crisis had a particular impact on Italian defence expenditure. In the Italian case, an important parameter of defence spending is the "Defence Function", which includes all expenditures needed to perform the specific tasks assigned to the Army, the Navy, the Air Force and joint components, as well as to the technical and administrative personnel of Ministry of Defence (MoD). The costs of the Carabinieri operating on Italian territory, which formally falls under the MoD budget, is not included in the Defence Function insofar as the Carabinieri fulfil internal security and not defence tasks.

The economic crisis did not lead immediately to a reduction in the Italian budget devoted to the Defence Function, which remained relatively stable between 2005 and 2011 at around 0.9% of GDP.<sup>30</sup> However, a first significant cut - 5,5% - was envisaged for 2012. More importantly, what is changing is the way these funds will be used. In early 2012, the government led by Mario Monti, and particularly Minister of Defence Giampaolo Di Paola, undertook a rationalization of defence expenditures aimed at cutting costs that are not essential to maintaining operational capacities.<sup>31</sup> The reform currently debated by the Italian Parliament envisages: a cut within ten years of 20,000 military - particularly high- and mid-level officials - and 13,000 civilians serving in the MoD, with a first cut of 21,000 personnel to be completed by 2017;<sup>32</sup> the merger and/or cut of redundant structures for logistics and training; the postponement of some procurement programmes and/or a reduction in the number of assets to be acquired,

<sup>29</sup> Bastian Giegerich and Alexander Nicoll, "The Struggle for Value in European Defence", in *Survival*, Vol. 54, No. 1 (February-March 2012), p. 53-82.

<sup>30</sup> Alessandro Marrone and Francesca Capano, *Defence Economics and Industry: Tables and Graphs*, updated July 2012, [http://www.iai.it/pdf/Economia\\_difesa/Tabelle-grafici-EN.pdf](http://www.iai.it/pdf/Economia_difesa/Tabelle-grafici-EN.pdf).

<sup>31</sup> Vincenzo Camporini, "Una riforma necessaria", in *Affari Internazionali*, 20 February 2012, <http://www.affarinternazionali.it/articolo.asp?ID=1975>.

<sup>32</sup> Antonella Baccaro, "Di Paola: i supercaccia non si toccano", in *Corriere della Sera*, 18 July 2012, [http://archiviostorico.corriere.it/2012/luglio/18/Paola\\_supercaccia\\_non\\_toccano\\_Tuteliamo\\_co\\_9\\_120718029.shtml](http://archiviostorico.corriere.it/2012/luglio/18/Paola_supercaccia_non_toccano_Tuteliamo_co_9_120718029.shtml).

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including the downsizing of the acquisition of F-35s from 131 to 90 aircraft,<sup>33</sup> and the closure of some Cold War era military infrastructures for territorial defence. While these decisions were influenced by many political factors, the Italian Defence Minister, among others, acknowledged that the economic crisis was one of the main factors driving this change in defence spending at the national level.<sup>34</sup>

While the rationalization of defence spending is likely to affect MoD personnel and assets heavily, so far it has not weakened Italy's role in multilateral and European procurement programmes and defence activities. In the EU framework, Italy remains the third European contributor to ESA's activities behind France and Germany, while Italian participation in EDA and Commission initiatives has remained stable. Italy has supported the Ghent Initiative, and generally speaking is keen to seek multilateral approaches to defence issues. In addition, Italy, Poland, Spain and Sweden have initiated a process to stimulate an EU-wide debate on a European Global Strategy (EGS), which will likely also address defence-related issues.

At the multilateral level, Italian participation in major multinational procurement programmes - including but not limited to Eurofighter, NH90 and FREMM - has not been significantly reviewed because of the economic crisis. The only significant reduction has been with regard to the F-35 acquisition, making Italy still the second largest EU partner in the transatlantic programme after the UK.

Finally, as mentioned above, at the bilateral level, the Italian government has signed a Letter of Intent with its German counterpart on the procurement of defence capabilities such as UAS, submarine development, long-range precision munitions and pilot training, followed by an agreement between Italian and German defence industries.

On the whole, the economic crisis has had an important impact on Italy because it has triggered a process of rationalization of the defence budget with significant envisaged cuts affecting MoD personnel and facilities. Interestingly, the Monti government has tried to maintain international cooperation in the defence field at bilateral, European and transatlantic levels intact so far. This is partly due to the dominant view amongst policy-makers that the Italian armed forces can serve Italian security interests best within multilateral frameworks.

The immediate impact of the economic crisis at national level has been a series of cuts in defence capabilities without significant European coordination. At the multilateral and EU levels, the crisis has encouraged bilateral cooperation agreements on defence spending and has increased MS' interest in the EDA and NATO's initiatives. However, the most important effects of the persisting austerity affecting European defence budgets are only likely to emerge to the full in the years ahead, when European governments will face the hard choice between pooling military capabilities at multilateral level or losing them altogether.

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<sup>33</sup> Eugenio Lilli, "Come cambiano le forze armate", in *AffarInternazionali*, 17 February 2012, <http://www.affarinternazionali.it/articolo.asp?ID=1972>.

<sup>34</sup> Antonella Baccaro, "Di Paola: i supercaccia non si toccano", cit.

A cleavage may emerge between a few MS willing and able to maintain a certain amount of effective - and thus expensive - defence capabilities to contribute to a range of crisis management operations, and a majority of MS whose armed forces will not be able to do so. In this scenario, the first group of countries will still have to find ways to cooperate on defence spending, and current trends point towards a flexible mix of cooperation at various levels - bilateral, mini-lateral and within the EU/NATO frameworks. Such a flexible mix could ease national concerns over operational sovereignty, for example by differentiating approaches towards less sensitive issues - such as logistics and training - and more sensitive ones. It could also accommodate different requirements among military services, for example with respect to air or land capabilities. The process towards increased international cooperation will not be easy, regular or fast. However, the alternative scenario of a Europe unable to maintain sufficient capability as a result of reduced defence spending - coupled with a number of external factors including the US' relative shift towards Asia and the EU's unstable neighbourhood - will likely be a strong incentive to go down the hard path of international defence cooperation.

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