Defense: Growth Opportunities for European Companies

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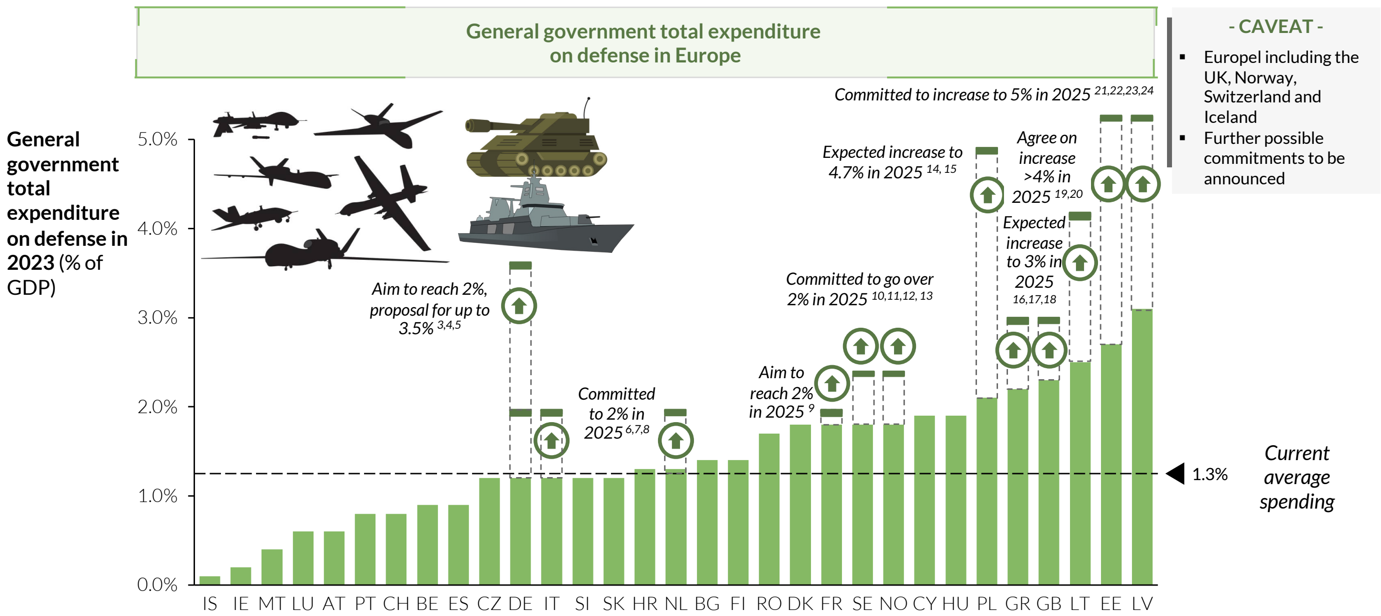
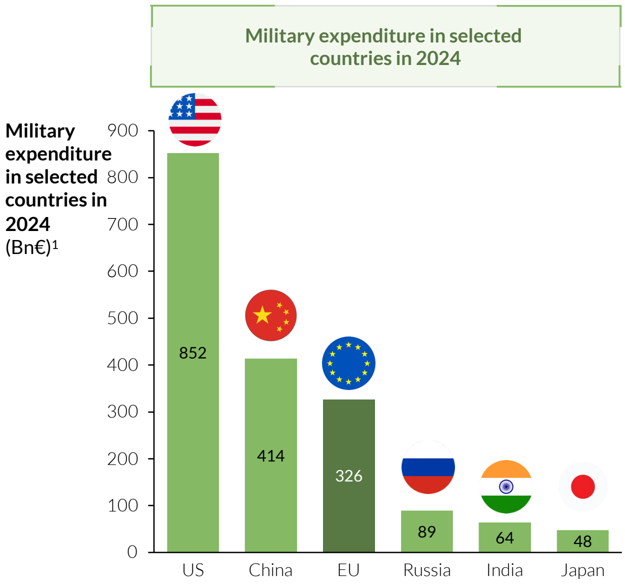
There is a growing consensus that, following several relatively peaceful decades, Europe will need to increase its defense budget and production of military equipment – and do so rapidly.

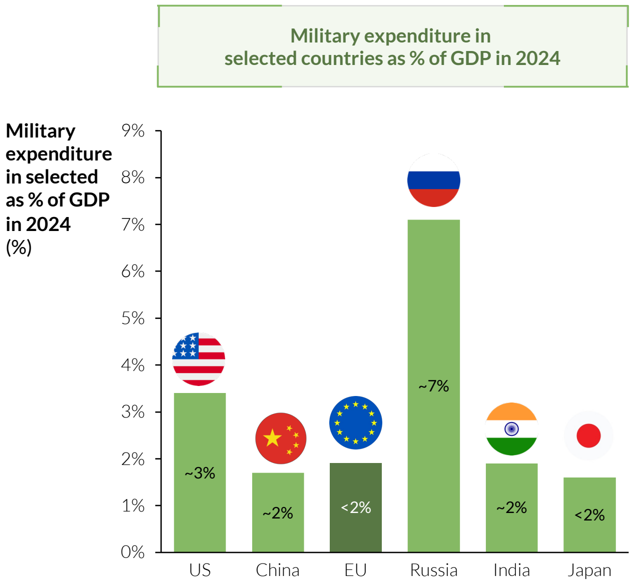
This need is largely independent from the outcome of the war in Ukraine, as well as from the recent changes in US government policy, which have simply amplified the degree of urgency and level of required budget increases. There seems to be an increasing conviction in Europe that in the mid- to long-term, Europe will have to assure its defense largely on its own, with the US shifting its focus towards the Asia-Pacific region.

If we assume an increase in budget from today's average of 1.3% of GDP in 2023 (1.9% in 2024 and 1.6% on average over the last decade) among European countries to the targeted NATO level of 2% and a more extreme scenario of 5%, this signifies defense budgets rising from 326 bn EUR in 2024[1] (279 bn EUR in 2023[2]) to ~860 bn EUR.



Note: Specific sources for each citation are Bibliography
Sources: Eurostat; GOV.UK; BBC; NATO; Euronews; Reuters; Government websites; Le Monde; Politico; Euractiv; Strategia Partners





1) Using the exchange rate as of 24 April 2025
Sources: SIPRI; International Institute for Strategic Studies; Carnegie Endowments for International Peace; Reuters; Euractiv; European Defence Agency; Consilium; TNSR: Stimson Center; Indiabudget.gov; Kyodo News; Nippon; Strategia Partners

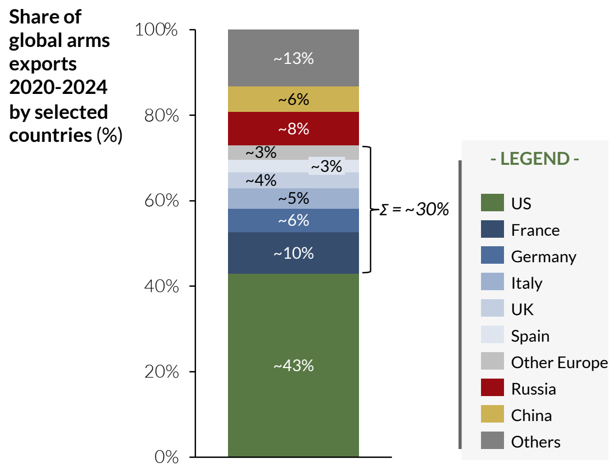
It is not the objective of this publication to determine the appropriate level of spending, to justify it, or to assess the feasibility to achieve it over a short time period and specify where to best invest. Rather, this article aims to demonstrate that such changes in budget spending will represent opportunities for companies and entrepreneurs to participate in a growing part of the economy while other parts of publicly financed sectors risk encountering shrinking budgets, as the mature European markets are not likely to accelerate growth.

Growth Opportunities in Defense

Focusing on the opportunities raised by this major reallocation of resources, the good news is that Europe has an established and competitive defense industry, and, if supported by politics, will strongly benefit from these budget shifts. Also, according to the European Commission, the share of military procurement within the EU is projected to increase to 50% by 2030 and 65% by 2035 – from the current level of about 20% only [25, 26].

The European defense industry is among the largest exporters of military equipment globally [27].

Share of global arms exports by selected countries



Sources: SIPRI Arms Transfers Database; Strategia Partners

Key insights

- **European countries collectively represented about 30% of global arms exports in 2020–24**
- **France emerged as the second-largest exporter, with a ~10% share, overtaking Russia for the first time (for the period)**
- **The European arms industry, while fragmented across several countries, collectively forms a significant block in the global market**
  - France and Germany in particular have strong defense industries that produce sophisticated weapons systems for both domestic use and export
- **The Russia-Ukraine conflict has fundamentally reshaped both export and import patterns, with Ukraine becoming the world's largest arms importer and Europe significantly increasing its share of both imports and exports**
- **Russia's position in the global arms market has been challenged in recent years by several factors, including Western sanctions following its invasion of Ukraine, competition from China, and issues with production capacity and technological innovation**

From a technological point of view, Europe has areas of competence that are at least on par with other large exporters, particularly in submarine, tanks, aerospace, mid-range missile systems, air defense, artillery systems, robotized infantry, etc.[28, 29, 30]

The EU is considering softening its deficit rules for the special purpose of defense spending and to increase national debt levels while establishing specific defense expenditure programs at the EU level. Financing constraints aside, the European defense industry's main challenges in fulfilling strong budget increases lie rather in the limited production capacities (at different levels of the supply chain), numerous insular systems (i.e. each major country has its own artillery system) leading to small volumes and limited scale effects, high costs and over-engineered designs, limited share of civil content in the designs (there can be a trade-off between reliability and speed of production), etc.

The real challenge lies not in a lack of budgets or commitment, but in establishing meaningful and effective production capabilities [31, 32]. In calling for a "wartime mindset," NATO Secretary General Mark Rutte highlighted a fundamental challenge: even as more funds are allocated to defense, significant obstacles remain in rapidly acquiring essential military equipment and scaling up production [33, 34].

Such shortcomings in the supply chain facing the requirement to essentially multiply output also present opportunities for new suppliers or for extending the presence of existing ones in defense. This is thanks to value chains that in some cases are opening up and in others are being integrated, thus presenting opportunities to dispose assets present in defense under attractive conditions.

Furthermore, in some cases, entry barriers are disappearing due to quickly shifting forms of warfare. Drones for example have been playing a major role in the war between Russia and Ukraine. Tactics are rapidly changing and a technology used currently might be obsolete within few months, as opponents innovate to improve their equipment. This leads to a massive acceleration in innovation, for which classical supply chains in defense systems are not adapted. Both Russia and Ukraine are relying on alternative, atelier style, flexible supply structures to keep up with the pace of innovation and rapidly evolving designs.

European defense must closely observe this development and must partially rethink their supply structures in order to be able to compete in the future. Traditional supply structures, with lengthy development cycles, approval and certification cycles that then produce defense equipment that is already obsolete upon delivery, simply won't work.

European enterprises should consider enhancing their presence in defense or to enter the market given their existing competencies in goods and services for which entry barriers are not too high.

This is especially true since, in many cases, criteria from shareholders and lenders have been weakened, and for defense-oriented military goods and services, an increase in the sector's revenue share appears feasible in the future. The European Investment Bank (EIB), the lending arm of the European Union, proposed in March 2025 to allow unlimited loans to the defense industry, including investments in non-lethal defense products and potentially expanding to projects dedicated for military use. This marks a major shift from its previous policy, which only allowed dual-use investments, and aims to put defense financing on par with other public policy goals, signaling to commercial banks that lending to arms manufacturers is now accepted [35, 36]. Overall, German financial associations, including the German fund industry association (BVI), the German Structured Securities Association (BSW), and the German Banking Industry Committee, have relaxed exclusion criteria for Defense investments. They scrapped the rule that excluded investments in companies with more than 10% of revenue from Defense, making it easier for funds, securities, and bonds to invest sustainably in the sector [37, 38]. Specifically, Deutsche Bank's investment arm (DWS) announced in April 2025 that it is removing restrictions that previously prevented many of its funds from holding defense assets. This change, enabled by updated German investment guidelines, could unlock "hundreds of billions" of euros for defense investments across Germany's asset management industry [39].

There are other reasons to believe that Europe will have to drastically and rapidly scale up its defense production. Reliance on the US has become an uncertain strategy in light of:

(1) Political acceptance of relying on US military technology. As recently demonstrated, the US government has the ability to switch off key software components of already delivered equipment (i.e. the LINK system in F-16 fighter jets, HIMARS systems or the denying of critical software updates [40, 41, 42]); and in light of this, European governments will be much more cautious and critical about purchasing US military technology in the future;

(2) Availability of US military technology. The waiting time for some goods and systems is already extremely long (i.e. patriot defense systems) and given own

capacity constraints, the US will prioritize its own needs even more in the future, rather than fulfilling orders from Europe.

For example, after signing a contract with the United States in 2022 for 250 M1A2 SEPv3 Abrams tanks, Poland faced significant delivery delays, waiting nearly three years for the first batch of just 28 tanks to arrive, with full delivery not expected until 2026 [43, 44, 45, 46]. Confronted with these slow timelines and the apparent inability or unwillingness of the US to deliver the required number of tanks quickly, Poland turned to South Korea, ordering hundreds of K2 Black Panther tanks in a series of multi-billion-dollar deals [47, 48, 49].

Nevertheless, entry barriers are not negligible and are of a various nature:

(1) Technological barriers: increased requirements for military equipment, with for example higher IP protection levels, NEMP protection, failure rate and reliability requirements, specific certifications for suppliers, security clearance for key personnel, etc.;
(2) Commercial barriers: significant share of tender processes in purchasing lead to advantages for incumbents with long list of references, expertise in specific tender processes and access to defense networks [50, 51];
(3) Long development cycles: necessity to position early on in co-development of solutions, with a prolonged duration of prototyping and testing phases at the absence of significant revenue volumes (unless they are financed with upfront payments or subsidized by national programs). On the other hand, product life cycles are long as well benefiting existing supplier structures [52, 53, 54];
(4) Customer concentration: by nature, the defense industry has a limited number of end clients, (with high entry barriers) and also a limited number of Tier 1 suppliers for subsystems [55, 56]

To overcome these entry barriers, companies have identified various strategies to participate in the attractive defense market, given its strong growth potential as well as its attractive margins.

Leaders are preparing their moves in Defense

In Germany, some industrial leaders have started to diversify or to intensify their presence in defense:

- *Volkswagen* (revenue of 325 bn EUR in 2024) announced in March 2025 that it is considering entering the defense sector by producing military equipment for the German armed forces, as confirmed by CEO Oliver Blume [57, 58, 59, 60]
- *Lufthansa Technik* (revenue of 7 bn EUR in 2024) has significantly expanded its defense activities in 2024 and 2025, establishing a dedicated "defense" business unit, committing to invest over 1 bn EUR globally as part of its Ambition 2030 strategy, with significant projects in Europe, the Americas, and Asia-Pacific [61, 62]
    - o Lufthansa Technik is focusing on the maintenance, repair, and conversion of military aircraft—including support for NATO, the German armed forces, and programs like the P-8A Poseidon, CH-47 Chinook, F-35, and

the PEGASUS SIGINT aircraft—while also developing new capabilities in avionics and power systems repair [63, 64, 65, 66]
  - The company began construction on a 25,000-square-foot expansion of its component workshop at Tulsa International Airport in the US, set for completion by the end of 2025, which will house new administrative and avionics facilities and create 90 new workstations to be used also in the defense industry [67, 68, 69]
- *OHB* (revenue of 1 bn EUR in 2024) launched a new UK subsidiary in March 2025 at the Bristol & Bath Science Park, aiming to develop advanced satellite and space systems for both national and European markets [70, 71, 72, 73]
  - This move is part of OHB's broader strategy to strengthen its presence in security-related and defense space programs, enhance Europe's technological sovereignty, and deepen partnerships within the European Space Agency (ESA) ecosystem [74]
  - OHB expects ~30% of its order intake between 2025 and 2027 to come from the Defense sector, and the new Bristol operation will focus on system-level capabilities across all major space domains, including satellites, spacecraft, and security-focused space technologies [74]
- *Schaeffler* (revenue of 18 bn EUR in 2024), a major German automotive supplier traditionally focused on bearings and motion technology, is actively seeking to diversify into the defense sector in response to slowing automotive sales and surging global military spending (Schaeffler's CEO Klaus Rosenfeld publicly emphasized the company's intent to expand its defense-related operations and highlighted existing connections to the defense industry) [75, 76, 77]
- *Trumpf* (revenue of 5 bn EUR in 2024), a global leader in industrial laser and machine tool technology, is exploring the development of laser systems for defense applications, particularly in counter-drone and air defense roles [78]
  - Trumpf has not yet formally announced a dedicated defense product line, but industry reports and company statements confirm ongoing R&D and interest in supplying advanced laser systems for directed-energy weapons and counter-UAV applications, which are in high demand due to the proliferation of drones on modern battlefields
  - Trumpf's recent investments, such as its new demo factory in Hungary, also support the development and demonstration of digitally networked manufacturing and laser solutions, which could be leveraged for Defense sector growth [79]

For many companies who are seeking a higher share of activities in Defense industry, this step has the characteristic of diversification linked to some risks when not planned in an appropriate way.

Strategia Partners approach and assistance

To this end, Strategia Partners has developed a methodology and tools specifically designed to support its clients as they consider this step.

In brief, our support includes:

- (1) Recording, structuring and mapping of a company's current competencies (technological, product and service offer, commercial, processes, etc.);
- (2) Determination of particular competencies to be useful in the defense sector (i.e. goods and services with dual-use potential);
- (3) Identification and structuring of potential target segments in the defense sector, plotting large number of applications and options;
- (4) Filtering of options, based on a set of pre-defined criteria for prioritization (i.e. market size, growth expectations, structural margins, entry barriers, consolidation of supplier structure, competencies of company & potential for differentiation, …);
- (5) Detailed analysis of selected growth options (commercial and technical feasibility, value-chain analysis, potential partnership with established players, etc.);
- (6) Go-to market strategy;
- (7) Business and action plan.

Strategia Partners methodology integrates strategic analysis and expertise in diversification strategies combined with our network of experts in the defense industry.

Strategia Partners is ready to provide you additional insights in its methodology, approaches and expertise. Do not hesitate to get in touch with us for a non-committal and confidential consultation.

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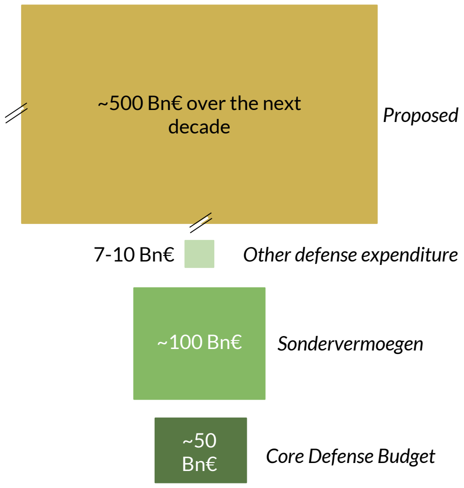
- Appendix -

Germany's military spending 2025
(Bn€)



Key insights on existing projects

- **The Core Defense Budget is the regular annual budget for the Bundeswehr (Ministry of Defence) which is ~50 bn€ for 2024–2025**
- **The 100 bn€ Sondervermögen (Special Fund) was established in 2022 for rapid modernization and procurement and is being spent in 2027, with most already committed to contracts for equipment like F-35s, helicopters and air defense**
- **Other defense expenditure relates to additional amounts spent via other ministries (e.g., interior, civil protection, intelligence and Ukraine support)**

Germany's current military funding is a combination of core annual defense budget, Sondervermögen and extra allocations

New extra fund proposal

- **In March 2025, Germany's new coalition (CDU and SPD) agreed to a new proposal of up to €1 trillion in new spending for defense and infrastructure over the next decade**
- **This includes the existing €100 billion Sondervermögen and a new extra-budgetary special fund of €500 billion for infrastructure, which will also support defense production and logistics**
- **The plan proposes exempting all defense spending above 1% of GDP from Germany's constitutional "debt brake," effectively allowing unlimited borrowing for defense expenditures**

This would give the government carte blanche to invest in the armed forces and infrastructure

Sources: CNN; Euractiv; Strategia Partners

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