paper

4/2021

# Sweden, the European Defence Fund and Permanent Structured Cooperation: Challenges Ahead for Third Party Participation

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PUBLISHED BY THE SWEDISH INSTITUTE OF INTERNATIONAL AFFAIRS | UI.SE

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## Introduction

A deteriorating European security situation and calls to reduce foreign dependency have characterized the European defence realm in recent years. The EU has therefore sought to ensure its own security and strengthen its defence capabilities, part of what has been conceptualized as "strategic autonomy". Two of the biggest projects in pursuance of these ends are the European Defence Fund (EDF) and Permanent Structured Cooperation (PESCO). Following cuts partly linked to the COVID-19 pandemic, the former has used €7.95 billion from the EU budget to finance collective defence technology research and capability development,[1] while the latter seeks to promote joint capability projects and collaboration.[2]

Sweden has engaged extensively with the EU Common Foreign and Security Policy (CFSP) and the Common Security and Defence Policy (CSDP). However, it has historically been sceptical about or reluctant to pursue EU defence integration. This reluctance has begun to waver in recognition of the need to make adjustments post-Brexit and the various new policy initiatives coming out of Brussels.[3] Nonetheless, Sweden's industry is an outlier in being fully privatized and having high levels of foreign ownership in which non-EU countries such as Norway, the United States and the United Kingdom are strong partners, and this has guided the Swedish position.

This UI Paper explores the negotiations on third-party access to EU defence funding and initiatives, the Swedish position and its industry's perception of the way forward under the new conditions. Section 1 traces the development of the EDF and PESCO, with an emphasis on the negotiations on third state participation. Section 2 outlines and discusses the Swedish defence industrial base with regard to these initiatives. Section 3 presents and analyses the impact on the Swedish defence industry and discusses the impact on Sweden's biggest partners: the UK, Norway and the US. Section 4 asks what is ahead for third parties in the EDF and PESCO frameworks. The paper concludes with some policy recommendations for Sweden and discusses a number of remaining uncertainties.

## PESCO and EDF third state participation

Early Brexit negotiations acknowledged a mutual need for continuing defence collaboration with the EU and the 2018 political declaration pledged to make the

[1] European Commission (2020a). Commission welcomes the political agreement on the European Defence Fund.
[2] Béraud-Sudreau, L (2020). Integrated markets? Europe's defence industry after 20 years. In: Fiott, D (ed.) The CSDP in 2020 - The EU's legacy and ambition in security and defence. EUISS.
[3] Håkansson, C. (2021a). Finding its way in EU security and defence cooperation: A view from Sweden. *European View*.; Fägersten, B., Danielson, A. & Håkansson, C. (2018). Sweden and European defence cooperation: interests in search of a strategy. The Swedish Institute of International Affairs.

necessary arrangements. Much of this declaration was discarded during 2020, in a sign of the vacillation on future security and defence relations that took place throughout the Brexit negotiations. A lack of agreement on these issues would lead to the UK missing out on participation entirely, but the British lack of interest kept Brussels guessing.[4] Europe's reliance on the British defence industry, however, was a driver of more general discussions on third party participation in both PESCO and the EDF.[5]

In the PESCO negotiations, member states generally persisted with being protective of their national industries. This conservative line was driven not least by EU member states in competition with both British and American entities seeing participation conditions as a way to shut the door to the European market on their competitors.[6] In contrast, countries such as Poland had long opposed any limitations, especially on US participation.[7] Cyprus was outspoken about ensuring that no participation would be possible by Turkey.[8] Nonetheless, a balance had to be struck and countries or entities outside the EU could be allowed to contribute if this was essential to making a potential project financially viable.[9]

The original idea for an EDF came from the European Commission's DG GROW, supported by Michel Barnier who argued that it would have French support.[10] However, it was important that such an initiative would not just benefit the largest "defence states" in the EU.[11] Member states without major defence-related companies worried that this would push them and their small and medium-sized enterprises (SMEs) out, thereby consolidating an exclusive club of firms for the future. Nonetheless, the deteriorating international security environment and the high level of political support from the then European Commission President, Jean-Claude Juncker, and the HR/VP, Federica Mogherini, helped to increase support for the EDF. Moreover, the Commission's relatively high funding scheme, as well as the 10% extra bonus for SME participation and for PESCO *projects* within the EDF provided important incentives for the EU member states.[12]

While Sweden has been extensively engaged in both the CFSP and the CSDP, its EU membership was a "rational economic risk management strategy" rather than a strategic choice that sought to advance its security policy, particularly in the light of its history of neutrality and non-alignment.[13] This contradiction initially made Sweden a sceptical voice alongside the UK in the debates, hesitant about common institutional security and defence commitments. PESCO and the EDF were consequently viewed with caution.[14] However, this reluctance towards the EU's

[4] Banks, M (2019). Britain's defense ties to the EU are still up in the air post-Brexit. Defense News.
[5] Taylor, T (2020). Brexit's Implications for UK Defence Industrial Cooperation with Europe. RUSI.
[6] Biscop, S (2020). European Defence and PESCO: Don't Waste the Chance. EU IDEA policy papers (1).
[7] Engberg, K (2021). A European Defence Union by 2025? Work in progress. SIEPS.
[8] Ibid.
[9] Biscop, S (2020).
[10] Haroche, P (2018). The European defence fund: How the European commission is becoming a defence actor. IRSEM.
[11] Ibid.
[12] Håkansson, C. (2021b). The European Commission's new role in EU Security and Defence Cooperation: the case of the European Defence Fund. *European Security.*
[13] Fägersten, B., Danielson, A. & Håkansson, C. (2018).
[14] Ibid.

new "defence push" is slowly starting to change as Stockholm tries to adjust to the new political landscape since Brexit and the various new policy initiatives driven by Brussels.[15]

Central to non-European participants in the EDF, not least the US, was the issue of Intellectual Property Rights (IPR).[16] Béraud-Sudreau argues these are the "driver of shareholder value and a sovereignty concern". Lack of IPR from participation in projects limits the allure of the EDF for third parties.[17] Drawing on their safeguarding of national industries and the need for autonomy, most EU member states however agreed that third parties should not be eligible for funding from the EDF, even if this put non-EU entities in a less advantageous position.[18] Sweden disagreed and attempted to stretch these rules. Ultimately, it was decided that third party entities could participate, but that IPR would be restricted to the European subsidiary and could thus not be transferred to a parent company outside the EU.[19]

## The Swedish defence-industrial base

Unlike most other EU member states, which have partially or fully state-owned defence industrial bases, Sweden's defence industry is fully privatized and to a large extent owned by foreign entities as a result of a series of acquisitions that began in the early 2000s.[20] The Swedish government remains a customer and, in line with article 346 of the Treaty on the Functioning of the European Union (TFEU),[21] has excluded its industry's areas of excellence from public procurement rules on national security grounds. The purpose of singling out these areas of excellence is to sustain security policy freedom of action and avoid dependency in strategically important areas. Furthermore, the national development and production of defence materiel sought by other states allows Sweden access to foreign technology that ultimately strengthens the operational capacity of its Armed Forces. Thus, Swedish excellence makes Sweden an attractive trade partner, benefitting its national defence.[22] The end of the Cold War meant a down-scaling of capabilities and a move away from the policy of self-supply, and thus a decrease in orders for the defence industry. As national policy shifted towards international missions instead of national engagement, industry also shifted outwards to engage with new customers and partnerships.[23]

Signing first a bilateral Defence Trade and Security Initiative (DTSI) and then a

[15] Håkansson, C. (2021a).
[16] Friis, K (2020a). The European Defence Fund and Norway. NUPI.
[17] Béraud-Sudreau, L (2019). UK access to future European defence-research funds: another Brexit uncertainty?. International Institute for Strategic Studies.
[18] Besch, S. (2017). What future for the European defence fund? Center for European Reform.
[19] Engberg, K (2021).
[20] See for example Axelson, M., & Lundmark, M (2007). Försvarsindustri i Sverige: konsekvenser av internationaliserat ägande. Totalförsvarets forskningsinstitut (FOI).
[21] Béraud-Sudreau, L (2020).
[22] SOFF (2015). Varför finns det behov av en stark säkerhets- och försvarsindustri i Sverige?. Säkerhets- och försvarsföretagen (SOFF).
[23] Belin, J., Hartley, K., Lefeez, S., Linnenkamp, H., Lundmark, M., Masson, H., Maulny, J. & Ungaro, A. (2017). Defence industrial links between the EU and the US. French Institute for International and Strategic Affairs (IRIS).

Declaration of Principles (DoP[24]) with the United States in 2003 laid the groundwork between the two countries.[25] This eventually resulted in the US giving Sweden a general exemption from its Buy American Act (BAA), which provides significant comparative advantage for the Swedish defence industry,[26] but arguably also serves as an incentive for continued good relations. As for the UK, Sweden being chosen as the first partner in the British Tempest sixth-generation fighter programme serves as evidence of a good relationship.[27] Norway currently holds Swedish subsidiaries, which makes it a third important non-EU partner. Using a narrow definition of a third party that strictly limits their PESCO participation would therefore have distorted European competition to Sweden's disadvantage. Access to the EDF would also have been very limited.[28]

In a 2018 written opinion, the Swedish security and defence company association (Säkerhets- och försvarsföretagen, SOFF) argued that defence cooperation partners must be chosen based on competence rather than EU membership. To maximize utility and the benefits for industry, the Swedish government pursued an active role in negotiations on the EDF and PESCO early on. This would provide Sweden with a competitive advantage in obtaining both financial aid and guaranteed customers for their systems (given the required partners), technology and/or capabilities, and therefore a competitive advantage in shaping the future European defence market.[29]

Thus, the question of the participation of third party entities has been important for Sweden, which has pursued a consistent line in both PESCO and EDF processes to keep participation open.[30] The Swedish Defence Commission's 2019 report, "Värnkraft", emphasizes that strict third-party conditions would discriminate against or shut out its national industry and restrict Swedish cooperation with non-EU member states. The government was encouraged to "find ways" to support Swedish research institutions' and defence industry participation in the EDF.[31] The success of the Swedish line in achieving more liberal rules for third parties was mentioned by the defence minister at a seminar in late February 2021. The same statement however also contained the caveat that although European initiatives such as PESCO and the EDF are important, they are two of many components when it comes to national defence and procurement opportunities,[32] which distanced Sweden

[24] The Declaration of Principles for Enhanced Cooperation in Matters of Defense Equipment and Industry.
[25] Belin, J., Hartley, K., Lefeez, S., Linnenkamp, H., Lundmark, M., Masson, H., Maulny, J. & Ungaro, A (2017).
[26] SOFF (2021). Webinar "Förändringar och restriktioner i amerikanska försörjningskedjor – hur påverkas företagen?". 9 February 2021.
[27] Chuter, A (2019). Sweden to join British 'Tempest' next-gen fighter push. Defense News.
[28] Swedish MoD (2018). Faktapromemoria 2017/18:FPM153.
[29] SOFF (2018). SOFF:s remissvar på EU-kommissionens förslag till Europaparlamentets och rådets förordning om inrättande av europeiska försvarsfonden COM (2018) 476 med hänvisning till diarienummer Fö2018/01010/MFU. SOFF.
[30] Fägersten, B., Danielson, A. & Håkansson, C. (2018).
[31] Swedish Government (2019). Värnkraft – Inriktningen av av säkerhetspolitiken och utformningen av det militära försvaret 2021–2025 (Ds 2019:8).
[32] EU-kommissionen i Sverige (2021). Webinar "Sveriges roll i EU:s fördjupade försvars- och säkerhetssamarbete". 25 February 2021.

from dependence on such efforts and possibly indicates the strength of its non-European defence relations. This arguably became evident when Sweden chose to participate in the UK's Team Tempest instead of the Franco-German Future Combat Air System (FCAS) project.[33]

## The impact on the Swedish defence industry

The conditions for third-party participation in PESCO are as political as they are strategic. First, entities situated, or with ownership structures, in countries outside the EU must have a valid Security of Information Agreement with the EU and receive an invitation from a PESCO project member. Third state entities must then share the EU's founding values, such as democracy, freedom and respect for human rights, while also respecting "the principle of good neighbourly relations" with member states.[34] This essentially excludes (and targets) countries such as China, Russia and Turkey, while also partially being a result of the renewed emphasis on strategic autonomy.

Given Europe's dependence on a number of non-European entities, a further condition on the need to add "substantial value" gives these entities a good chance of being included.[35] Nonetheless, discussion of the need for European "strategic autonomy", which has resurfaced and broadened during the pandemic,[36] has seemingly left its mark on the conditions. Once the pandemic hit, strategic autonomy became the most important project for Brussels, according to an industry representative. Almost all the progress towards freer trade and recognition of the importance of open partnerships with non-European partners, on which Sweden had based its industrial model, was lost. The focus and discussions instead turned to re-shoring production and protecting value chains in a sudden move to reduce external dependency. While this might be seen as a logical shift from a political perspective to redistribute risks in combating the pandemic, it could be argued that it is not the ultimate direction of decisions on the defence industry.[37] As a consequence, the conditions stated participation must not restrict EU member states or make them more dependent on third parties. This restricts, for example, the export of final products.[38]

Ultimately, all these conditions place small obstacles in the way of the EU's most common partners. Countries such as Norway, Canada and the US share the EU's values and add the sought after substantial value – the latter indicated by their existing high level of cooperation with Europe. This also makes issuing the invitation required less of an obstacle. The partners nonetheless voiced disappointment over the problems

33 Schmidt-Felzmann, A (2019). PeSCo: The Swedish perspective. French Institute for International and Strategic Affairs (IRIS).
34 Council of the European Union (2020). COUNCIL DECISION establishing the general conditions under which third States could exceptionally be invited to participate in individual PESCO projects.
35 Ibid.
36 EEAS (2020). HR/VP blog: Why European strategic autonomy matters.
37 Interview, Industry representative (1), February 2021.
38 Council of the European Union (2020).

raised for them in connection with IPR. These conditions have excluded parties from countries that the EU is in political disagreement with, as well as rising geopolitical and economic competitors. They are however – at least in part – favourable for Sweden's three most central non-EU cooperation partners, although they also share the disappointment over IPR.

In 2019, the first call for the European Defence Industrial Development Programme (EDIDP) – the EDF's precursor – led to the Commission rolling out several projects with EU-based but third country-owned entities, in an effort to demonstrate the EU's openness to companies from "strategic partners". The Commission heavily emphasized that this demonstrated the ability "to involve EU-based subsidiaries controlled by third countries or third country entities provided they fulfil appropriate security-based guarantees approved by Member States" as was "the case with four participants controlled by entities from Canada, Japan and the United States".[39] However, while in theory both PESCO and the EDF are open to industries owned by entities outside the EU, as explained above, this could now be even more challenging. Swedish industrial and governmental agencies have emphasized that the increased administrative burden, enhanced financial risks for partners and complex regulations risk making Swedish industry unattractive partners in these processes. There are also further problems connected to the difficulties with IPR, the Swedish industries' ownership structures, and export control regulations, where differences between member states could hamper cooperation.[40]

## Processes for partners: the UK, Norway and the US

The UK has a significant defence industry that is heavily integrated into the European defence industry. This makes a special partnership on these issues likely eventually. Several European (including some Swedish) entities see themselves as part of the British Defence Technological Industrial Base following years of cooperation and building business sites on both sides of the channel. While some concerns have been raised that Brexit might endanger interconnected supply chains, the industry's main worry seems to be the lack of either British or European political will to enter into joint projects.[41] The UK government recently stated that its security and defence cooperation with the EU would be conducted "as independent partners, where this is in our interest".[42] With both industry and policymakers reportedly in disagreement over the advantages that the EDF and similar initiatives might bring, the

[39] European Commission (2020b). European Defence Fund: €205 million to boost the EU's strategic autonomy and industrial competitiveness, Press release 15 June 2020.
[40] Interviews, Industry representatives (3), February 2021; Interview, Government representative, February 2021; On IPR and export control, see also Article 10.2, 22.3 and 25.2 of the draft regulation establishing the European Defence Fund.
[41] Gen. Abrial, S., Sir Westmacott, P., Bel, OR., Besch, S., Starling, C.G., Wieslander, A. & Aronsson, L. (2021). Toward a Future EU-UK Relationship in Foreign Policy and Defense.
[42] UK Government (2021). Global Britain in a competitive age - The Integrated Review of Security, Defence, Development and Foreign Policy.

UK government currently feels no sense of urgency to join any of them.[43] An absence of expressed interest and partnership can thus be expected at least in the short term, with potential consequences for joint projects.

Drawing on its EEA membership, Norway participated in the Preparatory Action on Defence Research (PADR) between 2017 and 2019, but was not asked back for the subsequent EDIDP.[44] The uncertainty surrounding Brexit is argued to have left Norwegian participation as collateral damage, due to the central question of whether the UK would end up as part of the EEA. As negotiations on this dragged on, the Council "bracketed" a paragraph on EDF participation for "associated countries" such as those in the EEA.[45] Norwegian planning and preparation were hampered while awaiting a final decision. However, once the decision to grant participation came through, national momentum was lost as the national budget for 2021 did not contain any funding for the EDF. While arguing that its "active Europe policy" remained in place,[46] Norway now risked ending up in the scenario it had lobbied to avoid. Early in 2021, however, a new shift in policy occurred and Norway is now set to join the EDF in 2021 as an associated country.[47]

Throughout the negotiations, US representatives lobbied the European Parliament in particular to ensure an unchanged position regarding its access to the European defence market.[48] The US claim that lack of IPR would unfairly limit its access to the European market was swiftly rebuffed by Brussels, which noted that regulations in the other direction are much more limiting.[49] The US nevertheless seem to remain positive towards PESCO, having recently announced a request to join the "Military Mobility" project, in which all participating states aim to "simplify and standardize cross-border military transport procedures".[50] Requests to join the project also came from Canada and Norway.[51] This was met with a positive initial reaction from the European External Action Service, although nothing has been formally decided.[52] The Pentagon also confirmed that it was considering requesting to join other projects within the framework. HR/VP Josep Borrell and US Secretary of State Antony J. Blinken recently stated "that EU defense initiatives should enhance the European contribution to Transatlantic security and can offer concrete opportunities for cooperation between the EU and the United States. With this in mind, the principals supported the fullest possible involvement of the United States in EU defense initiatives and enhanced dialogue on these issues".[53]

[43] Gen. Abrial, S., Sir Westmacott, P., Bel, OR., Besch, S., Starling, C.G., Wieslander, A. & Aronsson, L. (2021).
[44] Friis, K (2020a).
[45] Ibid.
[46] Friis, K (2020b). Innlegg: Hvorfor sier regjeringen nei til forsvarsfondet? *Dagens Næringsliv*.
[47] The Norwegian Government (2021). Det europeiske forsvarsfondet - EDF- EØS-notat15.02.2021.
[48] Engberg, K (2021).
[49] Friis, K (2020a); Fiott, D (2019) The poison pill: EU defence on US terms?. EUISS.
[50] Sprenger, S. (2021a). Pentagon pushes to partake in EU military mobility planning.
[51] Reuters Staff (2021). US ready to help EU speed up troop movement to meet Russia challenge.
[52] Sprenger, S. (2021b). US-EU cooperation pitch on military mobility gets positive response.
[53] US Department of State (2021). Joint Statement by the Secretary of State of the United States of America and the EU High Representative for Foreign Affairs

The UK is still conspicuous by its absence, alluding back to the current disagreement among industry and policymakers.

## The future of EDF and PESCO third party participation

While formally third party participation in the EDF is feasible, one industry representative told how some companies in the industry – including some in Swedish industry – had been recommended not to include third state owned entities because of the increased administrative burden and financial risk.[54] Swedish companies owned by entities outside the EU had already been lukewarm about participating in the EDF precursors. Nevertheless, eight projects in the PADR and the EDIDP currently involve Swedish participation.[55] To prevent losing out in future European defence cooperation, Sweden has developed a national template agreement between the Swedish Defence Materiel Administration (FMV) and defence industry companies controlled by entities in third countries to try to enhance their participation. The application process that used the template for the first time was the 2020 call, for which the results have not yet been announced.[56]

The primary reason for the defence industry's reluctance, however, seems to be the difficulties with IPR. These are said by Swedish industry representatives to be the core or most essential target for the industry to get its hands on when participating in a joint project.[57] While this issue may be an important component in the struggle for strategic autonomy, it risks limiting the interest of those capable of bringing substantial value or making projects financially viable, including the US. An industry representative indicated that this cooperation would primarily be continued on a bilateral basis, and signalled that bilateral cooperation would be strengthened rather than weakened for the foreseeable future. The bilateral line applies to the UK partnership too, although both government and industry representatives are still awaiting a clear policy steer from London.[58] This step away from EU initiatives might not be popular in Brussels, and reduced incentives for contributors of substantial value could also hamper European joint capabilities in the longer term.

Returning to Norway's recent decision to participate, it arguably now needs national structures to do this well. It is nonetheless joining the group of Nordic states, which seems to still be figuring this out despite its longer membership. Group members are yet to attain national synchronization with a shared strategy and coordination.[59] Tasks and responsibilities are currently divided between several agencies and government

and Security Policy/ Vice President of the European Commission.

54 Interview, Industry representative (1), February 2021.

55 Six of which are connected to SAAB, which is a Swedish owned company. On the outcome of the PADR and the EDIDP see La Fondation pour la recherche stratégique (FRS).

56 Interview, Government representative, February 2021.

57 Interview, Industry representative (1), February 2021.

58 Interview, Industry representative (1), February 2021; interview, Government representative, February 2021.

59 Interview, Industry representative (2), February 2021.

departments, something not seen in other countries with a competitive defence industry.[60] A Swedish government representative states that this is a result of a top-down approach to relevant decision making, where there has been an insufficient level of dialogue between the agencies concerned. In addition, the national processes with elements such as capability requests from the Armed Forces and subsequent funding decisions, are yet to be synchronized with the Brussels process in terms of project proposals and funding periods for both the EDF and PESCO. This means, for example, that funding decisions have already been taken when it is time to commit to projects in Brussels.[61] In Sweden, this fragmentation also means a lack of dialogue between industry and government. In member states where the state is a partial or full owner of a company, this element would arguably be more natural and therefore less of an issue.[62] This lack of dialogue has been identified as hampering development by both sides, but it seems that structures for this are yet to be devised.

The relatively low degree of national coherence or coordination across the Nordic states, however, provides opportunities for cooperation. Within the framework of the Nordic defence cooperation (NORDEFCO), a dialogue has begun to coordinate EDF/EDIDP efforts both at the national level and between states.[63] Although participating under different conditions, the Nordic countries should seek to put in joint proposals, not least given their shared threat perceptions and already close cooperation on security and defence. Combined, the Nordic countries and their industries also amount to one of the largest industrial players in Europe. Enhanced and increased Nordic cooperation in this format could thus be highly beneficial, especially as Norway, through its associated country status, is to participate in the EDF in 2021–2027.[64] While it should be noted that Nordic defence-industrial cooperation has had its troubles in the past,[65] the framework should be used to learn lessons from each other and improve best practices. For instance, Swedish officials have been impressed by Denmark's approach to and strategy on the EDF.[66] Finally, the Nordic defence industries also need to be closely involved in and consulted on these processes.

A "whole of government" approach appears to be missing from the Swedish side with regard to these processes. The FMV has a national coordination office for the EDF that has been operational since 1 January 2020. Despite this, the process of handling the EDF and PESCO is split between the Ministry of Defence, the Armed Forces, the FMV and in part the Ministry for Foreign Affairs. There is a need to improve coordination between these different actors in the Swedish system. Furthermore, industry needs to be closely involved in this process to be able to plan and develop projects. There are also plans in the

60 Interview, Government representative, February 2021.
61 Ibid.
62 Interview, Industry representative (2), February 2021.
63 Interview, Government representative, February 2021.
64 Friis, K (2020a); The Norweigan Government (2021).
65 See e.g. Garberg Bredesen, M. & Friis, K (2019). Governance Entrepreneurs as Spoilers in Nordic Defence Cooperation. Journal of Regional Security, 14:2, 77–100..
66 Interview, Government representative, February 2021.

Swedish Government to establish an inquiry into how to improve national planning and coordination of the EDF, but this inquiry is yet to be established.

At the same time the Swedish Government has launched a larger inquiry on a new equipment supply strategy for military defence, which will conclude in 2022.[67] A new equipment supply strategy is clearly needed as the current guidelines are from the late 2000s and emphasize the importance of cost efficiency (e.g. by buying off the shelf). The security, political and industrial landscapes have changed since then, and this needs to be taken into account. This inquiry will, among other things, look at the effect of the EDF on the Swedish defence market.

While other countries have been able to create synergies and strategic planning between PESCO and the EDF (and before that the PADR and EDIDP), Sweden, at least initially, took a strict view on the difference between the two formats. Although PESCO formally lies within the intergovernmental decision-making structures, it has clear links to the EDF programme through the "bonus system" in the Fund. Hence, the planning and development synergies between PESCO and the EDF need to be more coherent and joined up in future Swedish planning, especially since a new round of PESCO projects should be established in 2021.[68]

The EDF has two distinct "windows": one aimed at research and one aimed at development. The "development window" requires co-financing by the member states. The Swedish Armed Forces and the FMV have therefore developed a new co-financing mechanism to improve the possibility of financing Swedish EDF projects. However, this new mechanism is yet to be entirely aligned with the European process, which creates difficulties. In the spring of 2021, the Swedish Armed Forces will provide an account of its experience of the co-financing mechanism with regard to the EDIDP process in order to drive improvements. Moreover, Sweden and other EU member states should make full use of the Capability Development Plan (CDP) and the Coordinated Annual Review on Defence (CARD) to streamline national and European defence planning processes. This will be one of the larger challenges, but also an opportunity for Sweden and other EU member states.

However, one potential risk within the EDF is that projects with lower technology readiness levels (TRL) will be pushed into the development window as €2.65 billion will be allocated to research and a larger amount, €5.3 billion, will be allocated to the development phase.[69] Furthermore, while defence spending has increased in Europe, there is still a significant lag in European R&D investment as well as decreasing levels of collaborative spending.[70]

Following a year of the COVID-19 pandemic, its long-term effects on the defence industry must be closely monitored. There are risks

67 Swedish Government (2020). Kommittédirektiv - En materielförsörjningsstrategi för det militära försvaret.
68 Lazarou, E and Lațici, T (2020). PESCO: Ahead of the strategic review. European Parliamentary Research Service
69 On TRL, see e.g. Mauro, F., and Thoma, K (2016). The future of EU defence research. European Parliament, p.13.
70 EDA (2021). European defence spending hit new high in 2019. 28 January 2021.

that member states' various support measures for the defence industries could affect or distort market competition in Europe.[71] Several European countries see the defence sector as important to economic recovery after the pandemic and could focus on providing support through the EU recovery fund.

Moreover, the pandemic has challenged the Swedish approach to the concept of EU strategic autonomy. Sweden has traditionally been rather sceptical about the concept and has often actively sought to nuance the language and use of the phrase in EU Council conclusions.[72] Defence Minister Peter Hultqvist has previously noted that with regard to the security and defence policy field, Sweden "opposes European Strategic Autonomy in industrial terms".[73] The Swedish defence industry has tried to influence these discussions in a similar way. However, the concept of strategic autonomy now has a broader meaning that affects the overall policy direction of the EU.[74] This is something that will be important to engage with in an attempt to influence the overall policy direction of the EU.

Finally, in 2021 the EU will develop a new so-called Strategic Compass on security and defence.[75] The process will address capability development, among other things, and should focus on how coherence between the EDF and PESCO can be maintained. At the same time, Sweden will also update its National Security Strategy and should focus on how the Strategic Compass process and national planning could mutually reinforce each other. The new Swedish security strategy should also address security threats to Sweden in-depth, with regard to economic and technological aspects as well as critical infrastructure.[76]

## Policy recommendations for Sweden

- Sweden needs to work more proactively towards EU defence initiatives such as PESCO and the EDF.
- Sweden should establish an inquiry on how to improve national planning and coordination for the EDF. This should result in a new Swedish EDF strategy.
- An integrated public-private partnership must be developed to have the Swedish defence industry included early on and in a more structured way in these processes.

[71] Béraud-Sudreau, L (2021). COVID-19 As An Opportunity For European Armament Cooperation? Institut de Recherche Stratégique de l'Ecole Militaire (IRSEM), pp. 5-6.
[72] Interviews, Swedish MFA and the Prime minister's office, January 2021.
[73] Swedish Riksdag (2019). Committee on EU Affairs, 14 June 2019.
[74] Helwig, N (2020). EU Strategic Autonomy: A Reality Check For Europe's Global Agenda. The Finnish Institute of International Affairs.
[75] For an overview of the Strategic compass process, see e.g. Nováky, N (2020). The Strategic Compass: Charting a New Course for the EU's Security and Defence Policy. Wilfried Martens Centre for European Studies; Koenig, N (2020). The EU's strategic compass for security and defence: Just another paper? Hertie School Jacques Delors Centre; Fiott, D (2020). Uncharted Territory? Towards a common threat analysis and a Strategic Compass for EU security and defence. EUISS, Brief No.16; Mölling, C., and Schütz, T (2020). The EU's Strategic Compass and Its Four Baskets. German Council on Foreign Relations.
[76] See e.g. Fägersten, B. 5G-affären visar behovet av en ny säkerhetsstrategi. *Dagens Industri*, 17 February 2021.

 

Sweden could also work with companies or products outside the traditional defence sphere. It could seek to involve non-traditional products or industries in the EDF framework, such as its large IT, telecommunications and technology industries.

- The Swedish Armed Forces and the FMV should work on improving the national co-financing mechanism for the EDF during 2021.
- The dialogue between government agencies and departments should be strengthened to synchronize national efforts and seek harmonization of Swedish and EU processes.
- Collaboration in the NORDEFCO framework should be promoted to find possible Nordic projects in the EDF and PESCO. Similarly, this format should also be used to exchange best practices and lessons learned from the EU processes.
- Sweden should initiate discussion on export control issues. These must be discussed in the long run, given that differences between EU member states could hamper cooperation.
- Sweden should engage actively and constructively in the EU's Strategic Compass process. This should also feed into the national process for developing the Swedish Security Strategy.
- Sweden should continue to second personnel to the European Commission's new Directorate-General on Defence Industry and Space (DG DEFIS).
- The results of the PADR and EDIDP should be followed up closely by government and industry, in order to learn lessons from these processes.

## Concluding remarks

This UI Paper has explored the negotiations on third-party access to PESCO and the EDF, the Swedish position in these negotiations and the defence industry's perceptions of the way forward under the new conditions. While Sweden's quest for conditions on third-party access that benefit its industry might be deemed a success given the final outcomes, its defence industry does not appear convinced. Unlike many European defence industries, the Swedish industry is self-reliant and must consequently secure reliable sources of investment. It already has strong bonds to non-EU countries in terms of both ownership and market access. Nonetheless, industry representatives have been active in seeking to influence the conditions in which both the EDF and PESCO operate, thereby indicating their interest in participation.

Engaging fully with these European initiatives would offer opportunities to assert influence over, and ensure a place in, the future of the European defence industry market. It constitutes a platform for projects that are guaranteed to secure dividends several years ahead, as well as for forming new partnerships. While some of the inherent obstacles are formally beyond the defence industry's control, its engagement could strengthen public-private sector dialogue and serve as an incentive to improve both governmental interagency dialogue and the national process for facilitating participation in PESCO and the EDF. Industry commitment may therefore be required if national actors are to obtain an appropriate level of facilitation. If the European line is pursued, it poses a dilemma regarding how it can be achieved in parallel with the development of existing connections to non-European partners and markets.

A balancing act of active engagement in both markets is probably not sustainable in the long term, which means that the defence industry could eventually arrive at a crossroads and have to choose between the EU and the non-EU sphere. The benefits of each will have to be compared. For the choice to fall on the first, third party regulations on both the EDF and PESCO would arguably have to become more generous. If developed along these lines, and participation in both initiatives were to be extended to a number of third-party entities in several projects, this might augment incentives for the Swedish defence industry.

For the choice to fall on the latter, some effort could still be made initially to participate in the European initiatives. The conclusion might eventually be drawn, however, that non-European partnerships are more profitable and thus better serve the Swedish industry's need for self-reliance. This line of action would mean that the industry's influence and place in the future EU defence market and industrial base would be limited, as other entities implement the projects and secure the available funding. Turning away would therefore seem to be a fairly permanent decision with far-reaching consequences.

Finally, while a reluctance to engage with the EU in the short term appears obvious on the British side, informal opportunities could be used in the meantime to prepare for the medium term, which is likely to see cooperation similar to other close partners. The idea of a European Security Council could be a useful suggestion in these discussions. Returning to the need for new post-Brexit partners, NORDEFCO could produce significant Nordic benefits if used as a frame for collaboration and joint application. If it can overcome its past difficulties, it could position itself as a strong player in European defence, which would be beneficial for both government and industry. Moreover, if the national template agreement for third countries turns out to be a success, it could serve as a key for SMEs and non-traditional companies, such as those with dual-use technologies, to be included in the EDF in addition to traditional entities. These processes will hopefully be taken into consideration in the development of the Strategic Compass, and remain relevant for Sweden's forthcoming equipment supply strategy and for the Military Defence and National Security Strategy, as well as the possible EDF inquiry. This would arguably serve the interests of both the government and the defence industry, while also benefiting Nordic cooperation. Given the advantages of such an effort, it could be argued this should have been pursued at an earlier stage.

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