

Soft Law and the Single Market

Measuring the Impact of the EDA's Code of Conduct on
Marketizing Defence Procurement in the European Union

Abstract

After several decades of collaborative arms procurement conducted on *juste retour* principles the Member States of the European Union are moving towards market based solutions in their attempts to maintain a competitive and sustainable defence technological and industrial base on the continent. This paper seeks to conduct a baseline study on the impact of the European Defence Agency's 2005/6 Code of Conduct on Defence Procurement, the first explicitly market based measures enacted. The research design employs mixed methods in the following manner: A) a preliminary statistical study into the volume of intra-European trade in conventional weapons from 1994-2011, and B) a series of semi-structured interviews with policy makers, as well as policy practitioners from both the supply and demand side of the defence procurement equation. Results indicate that at best the measures have had a small impact on marketization. Although the initial results of the preliminary statistical study are decisive, equifinality in causation is ultimately difficult to attribute to the Code of Conduct as many complex dynamics ultimately affect the trends observed.

Key words: Defence Procurement, Marketization, EU, European Defence Equipment Market, European Defence Agency, Code of Conduct on Defence Procurement

Words: 19,233

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Abbreviations

CFSP	Common Foreign and Security Policy
CNAD	Conference of National Armaments Directors
CoC	Code of Conduct on Defence Procurement
CoJ	Court of Justice
CSDP	Common Security and Defence Policy
DG ENTR	Directorate General for Enterprise and Industry
DG MARKT	Directorate General for the Single Market
DTIB	Defence technological and industrial base
EADS	European Aeronautic, Defence and Space Company
EBB	European Bulletin Board
ECSC	European Coal and Steel Community
EDA	European Defence Agency
EDEM	European defence equipment market
EU	European Union
FDI	Foreign direct investment
GDP	Gross domestic product
GPS	Global Positioning System
IEPG	Independent European Programme Group
ISAF	International Security Assistance Force
ITAR	International Traffic in Arms Regulations
JSF	Joint Strike Fighter
M&A	Mergers and acquisitions
NATO	North Atlantic Treaty Organisation
OCCAR	Organisation Conjointe de Coopération en matière d'Armement
R&D	Research and development
SIPRI	Stockholm International Peace Research Institute
SME	Small and medium enterprise
TEU	Treaty on the European Union
TFEU	Treaty on the Functioning of the European Union
TIV	Trade Indicator Value
UK	United Kingdom
US	United States
WEAG	Western European Armaments Group

1 Introduction

The production and procurement of defence and security materials in Europe is largely fragmented and divided into several individual markets. This set-up is perpetuated by Article 346 which enables Member States to derogate internal market rules when procuring defence and security related products. In the post Cold War era this status quo has become ever more unsustainable as the manner in which arms are produced globally has undergone significant shifts. Broadly speaking, the cost of the most technologically advanced systems continues to rise in real terms meaning that the high-value end of the sector is become ever more capital intensive.¹ Furthermore, on a global scale the industry has undergone a process of internationalisation and companies are now feeling the heat of competition². The United States (US) reacted early to these pressures and through the efficiency gains of decisive restructuring and consolidation have come close to monopolising the global market for international arms sales³.

Although aware of these pressures and the threat they pose to their own collective defence technological and industrial base (DTIB), European states initially reacted slowly and largely pursued collaborative projects to counteract the problems of small production runs and duplicated research and development costs. This strategy however, did not sufficiently address the issues of duplication and over-capacity. Thus recent efforts to promote cross-border trade and mergers & acquisitions (M&A's) have been focused on market based solutions. Here the logic employed by the institutions that promote defence procurement marketization, such as the European Defence Agency (EDA) and the European Commission, is that Article 346 has been wildly misinterpreted by Member States. In their view, most defence material should fall under Single Market rules and Article 346 should be used under special circumstances only and not used as blanket sector wide exemption as Member States have persistently done.

This paper will focus on assessing the impact of the first such market based approach made, namely; the EDA's Code of Conduct on Defence Procurement (CoC). As a soft law instrument, expectations of its ability to regulate a market are somewhat low; however, no impact is not equal to low impact. Ultimately any progress in a field that is such a closely guarded prerogative of Member States can, depending on your predisposition, be seen as a success. The overall research question can be summed up as:

¹Economist, The, *Defence spending in a time of austerity* (2010)

² Camus, Philippe CEO EADS, Hertrich, Rainer CEO EADS, Ranque, Denis Chairman & CEO Thales & Turner Mike CEO BAE Systems, *The new European Defence Agency: Getting above the Clouds*, June 24th 2004

³ Jones, Seth G., *The Rise of European Security Cooperation* (Cambridge University Press:2007) p.169

Has the EDA's CoC been successful in promoting the marketization of defence procurement in the European Union?

Measuring success of the CoC in bringing about marketization will be conducted by utilizing a multi strategy research design in which the two methodological approaches employed seek to answer two distinct yet complimentary aspects of the overall research question.

The preliminary quantitative study will treat cross-border trade as a proxy of marketization; i.e. if Member States commit to the pledges made in the CoC to conduct defence procurement in a cost-competitive manner without prejudice to firms based in other Member States then we would expect a rise in the cross-border trade of defence and security materials. Data from the international arms transfers database of the Stockholm International Peace Research Institute (SIPRI) will be utilized to enable a longitudinal study spanning 18 years from 1994-2011. This will permit the trend mapping and comparison of the six years since the CoC came into effect with the previous six years, as well as the six before it to enable the wider contextualization of any trends seen between the immediate pre and post CoC eras. The aim of this part of the study is to confirm whether there has been a rise in the intra-EU trade in conventional weapons since 2006, as existing literature refers to increasing collaborative projects but has not confirmed what is happening to cross-border transfers.

The second part of the study is comprised of a series of semi structured interviews with policy makers and practitioners from both the supply and demand side of defence procurement. Here the aim is to gain an insight into how experts engaged in defence procurement have actually perceived the CoC and see if they can provide more nuanced explanations and motivations for why the measure has functioned or failed. More significantly, the CoC is far from the only factor which may have played a role in influencing where and how Member States decide to do their defence material shopping. Thus this part of the study aims to shed some light on whether the CoC can be seen as having a significant impact on European defence marketization among other competing explanations for the trends observed in the statistical part of this paper.

2 Motivation

Throughout the past 60 years of its existence the European Union (EU) has brought ever more economic integration to the continent. Starting as the six member European Coal and Steel Community (ECSC) in 1952 the bloc has evolved and expanded to become the 27 Member State Single Market, which regulates 500 million consumers and discounting internal transactions accounts for approximately 20% of all global trade.⁴ Single Market rules have expanded to liberalise markets traditionally close to Member States' national prerogative such as telecommunications and energy supply.⁵ However, the defence sector in Europe has until recently remained largely exempt from any such liberalisation and remains largely fragmented in a multitude of nationally protected markets and industries. It is estimated that a single European Defence Equipment Market (EDEM) could yield cost savings of up to 20 percent once economies of scale and comparative advantage have had their impact⁶. Aside from the burgeoning pressure of recession induced austerity the urgency for reform is compounded by continuous rises in the cost of defence equipment. Augustine's law displays the exponential rise in the cost of procuring cutting-edge defence equipment as real costs more or less double from generation to generation⁷, while another study estimates yearly costs rises of approximately 5-10% per year.⁸ Ultimately, the citizens of Europe are the de facto end consumers of the security that is provided by this equipment and should there for have a thorough interest in how to reduce costs

2.1 The case for European capabilities

2.1.1 Sovereignty, the security dilemma and arms production

⁴ Bomberg, E., Peterson, J. & Stubb, A. *The European Union: How Does it Work?* (Oxford University Press: 2008) p.7

⁵ Bache, Ian & George Stephen. *Politics in the European Union* (Oxford University Press: 2006) p.420

⁶ Hartley, K., *Collaboration and European Defence Industrial Policy*, *Defence and Peace Economics*, 19:4, 303-315 (2008) p.307

⁷ The Economist, *Defence spending in a time of austerity*. (August 26th 2010)

⁸ Giegerich, B., *Budget Crunch: Implications for European Defence*, *Survival: Global Politics and Strategy*, 52:4 (2010) p.87

That the defence sector in the EU has largely remained exempt from Single Market rules comes as little surprise as the production of defence and security materials is inextricably linked to the very core notions of state sovereignty⁹ and would thus logically be one of the latter policy areas over which Member States would be willing to cede control to Brussels.

Max Webers work in *Politik als Beruf* stipulated that one of the unique tenets of sovereign states is their monopoly over the use of violence within their territory.¹⁰ Ideally this monopoly of violence is used to ensure the rule of law internally as well as thwart any would be external aggressors who threaten the territorial integrity of the state.¹¹ Thus the monopoly of violence exercised through police and military forces aims to provide security against existential threats both domestic and international.

In order to make its security credible the state must ensure its forces have supremacy over would be adversaries. In the domestic sphere the state can regulate its supremacy i.e. police forces may have the exclusive or partially exclusive right to bear arms, have the power monitor persons or groups, and can arrest and imprison would be threats. The threat from the international sphere however provides the state with a somewhat larger headache. Potential adversaries are wide ranging, numerous and subject to change over time. In order to guarantee its security and indeed survival in this sphere the state aims to insure its defensive forces are at least at parity with, if not better than, any plausible aggressors. This leaves states with necessity of maintaining a standing army that paradoxically leads them to fear one another even more. In his 1795 work *Toward Perpetual Peace*¹² Emmanuel Kant highlighted this predicament as a justification to remove standing armies if real lasting peace was ever to materialise. In 1951 Herz more broadly defined the existential threat faced by states as the ‘Security Dilemma’¹³ whereby states in an anarchic world system are in a perpetual arms race of sorts in which one states’ action to improve its security provokes a reaction by others in order to counterbalance, which in turn has knock on effect and so on and so forth.¹⁴ Of course forms of international cooperation, including the EU itself, can mitigate the full effects of the security dilemma, however as long as states continue to competitively invest in new arms technologies and upgrade their militaries we can assume that the Security Dilemma continues to be an occurring phenomenon.

⁹Hoeffler, C., *European armament co-operation and the renewal of industrial policy motives*, Journal of European Public Policy, 19:3 (2012) pp.435-451

¹⁰Hague, R. & Harrop, M., *Comparative Government and Politics 7th ed.* (Palgrave MacMillan, Basingstoke: 2007) pp.13

¹¹ Ibid . p.16

¹² Kant, Immanuel , *Zum ewigen Frieden* (Reklam, Stuttgart: 2005) p.5

¹³ Herz, John H., *Political Realism and Political Idealism: A Study in Theories and Realities* (University of Chicago Press, Chigaco: 1951)

¹⁴ Brauch, H. G, *From a Security Dilemma Towards a Survival Dilemma* Chapter in *Globalization and Environmental Challenges: Reconceptualizing Security in the 21st Century* , Hexagon Series on Environmental Security and Peace. Vol 3 (2008) p.540

By extension where states procure their defence and security materials is also a central tenet of the Security Dilemma. Security of supply is vital to complete an overall credible security, which explains why traditionally States owned their arms producing industries and to this day major powers typically procure defence materials within their national borders.

2.1.2 Europe's need for capabilities

What are Europe's capabilities needs? The EU is often painted as a civic or soft power¹⁵ preferring the use of its trade power and access to its Single Market as a means to influence around the world. This view of course holds water when contrasting the EU with the United States of America (US) with its colossal defence budget and its preponderance for the use of military force. However a closer look at the EU shows that it too needs investment in new capabilities due to operational requirements.

First and foremost the EU Member States like any other state must guarantee the security of its citizens and its continuing existence in the face of the security dilemma outlined above. Thus the EU must maintain a credible parity with its big regional neighbours such as Russia who has recently been flexing her muscles along the EU's outer borders.¹⁶ The 1990's gave Europe a so called 'peace dividend' as the Cold War threat had disintegrated yet the US presence on the continent remained strong with approximately 100,000 troops continuously deployed throughout the decade.¹⁷ However this free ride will be coming to an end as the US announced a strategic pivot towards the Pacific region. Although the full details of this shift are yet to be fully understood, the US Ambassador to the North Atlantic Treaty Organisation (NATO) remarked;

*“if there ever was a time in which the United States could be counted on to fill the gaps that may emerge in European defense that time is rapidly coming to an end.”*¹⁸

Secondly, Europe needs better capabilities for intervention in its immediate neighbourhood. When war broke out in the post-Soviet fragmenting Balkans in 1992 the Luxembourgian Deputy Prime Minister and Minister for foreign affairs, proclaimed “this is the hour of Europe; it is not the hour of the Americans”¹⁹ Fortunately, at that moment of its utterance no one could comprehend the ridicule

¹⁵Hix, S., *The Political System of the European Union* 2nd Ed. (Palgrave Macmillan, Basingstoke: 2005) p.404-405

¹⁶ Economist, *The Rethink the Reset: NATO should not give in to Russian aggression* (May 19th 2012)

¹⁷ Kane, T. *Global U.S. Troop Deployment, 1950-2003* Center for Data Analysis #04-11 (2004)

¹⁸ Barry, J., *Historic shift in U.S. Defence Strategy will have a Major Impact on Europe* in *European Affairs* (April 2012)

¹⁹ New York Times, *Conflict in Yugoslavia; Europeans Send High-Level Team* (June 29th 1991)

this statement would later attain.²⁰ Despite spending collectively \$230bn²¹ on defence Europe was not capable of putting an end to the conflict. By 1995 NATO initiated Operation Deliberate Force and acted again in 1999 under Operation Allied Force. The relative success of these campaigns was however due to US participation. In the latter campaign the US provided 95% of all NATO's intelligence needs,²² 90% of Air to Air refuelling capabilities²³ and delivered 83% of all ordnance.²⁴ Only the US was able to deploy all weather strike capabilities utilising precision munitions. European strike aircraft were grounded in the early stages of the campaign due to the persisting bad weather.²⁵ Considering that Brussels is approximately no farther from Belgrade than Madrid, Operation Deliberate Force displayed the inability of Europeans to conduct a military campaign within their own continent never mind beyond it.²⁶

The failure of the nineties did not go unheeded and by way of the St. Malo Declaration and the commitment to the Helsinki Headline Goal the EU eventually developed what is today's Common Foreign and Security Policy (CFSP). Since its initial deployment in 2003 the EU has embarked on 8 military operations and 19 civil security operations outside its borders.²⁷ Furthermore many Member States have had active deployments in Afghanistan and Iraq. More recently the Arab Spring has provided new security challenges to the EU. Several Member States intervened to create a no fly zone over Libya and while the Europeans did fare better than in the Balkan wars of the 1990's the operation still had heavy US participation in the early stages. After just a few months of operations the EU countries were already running low on much needed precision munitions that had to be hastily purchased at extra cost from the US.²⁸

Ultimately, forecasting the exact Capabilities needs of the EU and its Member States is a difficult task. Does the EU need trans-oceanic force projection capabilities? Probably not, but there are some unavoidable certainties; The Security Dilemma and the need for better intervention capabilities are both problems that will not go away and with the US retreating from Europe's overall security equation the onus is on the EU and its Member States to pick up the slack. To meet these needs in the future the EU will need to continue to act decisively to make its production and procurement of defence and security

²⁰ Howorth, J., *Security and Defence Policy in the European Union* (Palgrave Macmillan, Basingstoke: 2007) p.55

²¹ Ibid p.55

²² Yost David S. in *Defending Europe: the EU, NATO and the quest for European autonomy*, Edited by Joylon Howorth & John Keeler (Palgrave Macmillan, Basingstoke:2004) p.89

²³ Ibid

²⁴ Lambeth, B., *NATO's Air War for Kosovo* (Rand, Pittsburgh:2001) p.66

²⁵ Yost David S. in *Defending Europe: the EU, NATO and the quest for European autonomy*, Edited by Joylon Howorth & John Keeler (Palgrave Macmillan: 2004) p.88

²⁶ One can argue that Europeans could have resolved the conflict using a lower tech approach utilizing mainly land forces. However many European nations could not politically commit to the risk of losses involved with such an approach. See Arkin, W., *War Over Kosovo Politics and Strategy in a Global Age*, edited by Andrew Bacevich and Eliot Cohen (Columbia Univ. Press, New York: 2001)

²⁷ Council of the European Union, *Operations to date* (2012)

²⁸ Erlanger, S. *Libya's Dark Lesson for NATO* (New York Times : September 3rd 2011)

materials more efficient. What further compounds the problem is that the high-value high-tech end of defence production:

“is an industry which must operate in a long-term perspective of 20 to 30 years. Accordingly, the policy framework which is established today and the resources which are allocated now will determine the perspectives and performance of the industry for decades to come.”²⁹

Thus it is imperative that the EU acts swiftly so that future security is not compromised as a result of present day inaction.

2.2 The case for a European Defence Technological & Industrial Base

Theoretically EU Member States could pack in their defence industries and buy of the shelf on the international market. Indeed many Member States that lack the industrial capacity to build cutting-edge high-value weapons systems already do this. However, there are several motivations both security related and economic why this is not a viable long term strategy.

2.2.1 Maintaining security of supply & operational sovereignty

The primary motivation behind an indigenous defence industry for any state is the security of supply. When shopping for defence materials within its own borders the state has a guarantee of supply, as well as unquestionable access to parts, maintenance and upgrades regardless of the changes to its diplomatic relations or shifts in the international order. By buying off the shelf the state will effectively become dependent on the goodwill and continuing alliance with the firm and/or government which supplied the goods or service. Should alliances shift and relations sour the state faces a real threat of their supply being restricted.

A prominent example of the precariousness of this policy is provided by the Falklands conflict of 1982. The Argentine air force had been supplied with French aircraft and state of the art beyond-visual-range fire-and-forget *Exocet* anti ship missiles. These missiles proved deadly to the approaching British Royal Navy task force and after some diplomatic work the French Government announced an embargo on further arms sales to Argentina and supplied the United Kingdom (UK) with technical details of both the missiles and the aircraft.³⁰ If Argentina had

²⁹European Commission, *Strategic Aerospace Review for the 21st Century* (July 2002) p.38

³⁰ BBC, *How France helped both sides in the Falklands War* (5th March 2012)

had unrestricted access to more Exocet missiles the very outcome of the War may have been altered. Another prominent example is provided by the EU's global positional satellite programme. The very *raison d'être* of the program is to secure the supply of an accurate and unhampered positioning signal.³¹ This was deemed necessary as Europe had become wary of US' tendency to manipulate its Global Positioning System (GPS) for its own purposes.³²

Closely linked to the issue of security of supply is the concept of operational sovereignty. Here the issue is not about whether further supply is need, but rather whether the purchaser has full control and access to the technology that they have bought.

An example of this problem has been fermenting now for some time in the multilateral Joint Strike Fighter (JSF) Programme. The UK despite being a so called 'Tier 1' partner in the project and having invested \$2billion³³ in Research and Development (R&D) has still not guaranteed operational sovereignty as the US remains reluctant to transfer the source code of the aircrafts complex avionics software suite.³⁴ Unsurprisingly the tier two European nations participating in the project namely Denmark, Italy, The Netherlands, and Norway have no hope in acquiring this information should they proceed with purchasing the aircraft.³⁵ Procuring defence hardware without operational sovereignty comes with considerable risks. The UK learnt this the hard way when it procured Chinook helicopters from the US in 1995. Despite having been urgently needed in the war in Afghanistan they remained sealed in dry storage for over 10 years due to Boeings refusal to supply the avionics updates that would make them airworthy in adverse conditions.³⁶

Although procuring from within the EU does not guarantee the security of supply nor operational sovereignty it would be from partners that share common institutions, a Single Market and a Common Security and Defence Policy (CSDP). Furthermore, the chances of asymmetrical procurement relationships as found with US in the JSF programme would be less likely as the clout of the partners involved would likely be more balanced.

2.2.2 The economic argument

Discounting the security necessities of maintaining a European Defence Technological and Industrial Base (DTIB) there are direct and indirect economic

³¹ European GNSS Supervisory Authority. *Why Galileo?* <http://www.gsa.europa.eu/go/galileo/why-galileo>

³² Jones, Seth G., *The Rise of European Security Cooperation* (Cambridge University Press:2007)p.163-164

³³ Defence Industry Daily, *F-35 Lightning: The Joint Strike Fighter Programme* (2012)

³⁴ Financial Times, 'UK denied waiver on US arms technology' (November 22nd 2005) &

Reuters UK, 'U.S: to withhold F-35 software code' (November 25th 2009)

³⁵ Ibid.

³⁶ Times, The. *£500m 'wasted' on Chinooks that have never flown* (June 4th 2008)

benefits that make it an imperative for Europe to maintain a competitive industry in this sector.

Firstly, and perhaps most obviously there is the overall economic weight of the sector which provides many high skilled manufacturing as well as research and development jobs. As a collective whole the European DTIB has in recent years employed over 300,000 persons directly and seen annual profits of €55bn.³⁷ If one considers the jobs maintained indirectly through the supply chain it is estimated that the sector supports the employment of over 1.6 million people across the EU.³⁸

Secondly, the defence sector is highly innovative and is viewed by industrial policy makers as a direct way to boost a nation's technological capabilities.³⁹ Indeed, some go as far as to say it is "an important mechanism for driving a country's overall economic development and industrialisation"⁴⁰ This has become increasingly pertinent as the high technology gains from the defence sector can have huge commercial value once they 'spill-over' into products aimed for civilian markets. Such dual-use technology is also important for maintaining economic growth and can give a leading edge to other high-tech areas of the economy such as electronics, transport, information and communications technologies, biotechnology and nanotechnology.⁴¹ Furthermore, this technological spill-over is seen as a vital constituent of the EU's Lisbon Strategy to create economic growth and jobs on the medium term.⁴² With approximately 25 million⁴³ EU citizens without work in mid 2012 there is surely an imperative to leverage the gains of this strategy as best possible.

2.3 Europe's defence industry dilemma

As the global arms industry has undergone a process of internationalisation European firms have faced immense competitive pressure from the goliath prime contractors across the Atlantic.⁴⁴ This, when combined with declining defence budgets and hang over of excess production capacity⁴⁵ from the Cold War era has

³⁷European Commission, *A strategy for a stronger and more competitive European defence industry* (2007) p.2

³⁸Eurostrategies, *A comprehensive analysis of emerging competences and skill needs for optimal preparation and management of change in the EU defence industry* (2009)

³⁹Taylor, T., In, *The European Union and National Defence Policy*, Edited by Jolyon Howorth and Anand Menon (Routledge, London:1997) p.135

⁴⁰Bitzinger, Richard A., *Towards a Brave New Arms Industry?*, Adelphi Paper, 356, International Institute for Strategic Studies (2003) p.13

⁴¹European Commission, *A strategy for a stronger and more competitive European defence industry* (2007) p.2

⁴² Ibid.

⁴³ Eurostat, *European Unemployment* (2012)

⁴⁴ Camus, Philippe CEO EADS, Hertrich, Rainer CEO EADS, Ranque, Denis Chairman & CEO Thales & Turner Mike CEO BAE Systems, *The new European Defence Agency: Getting above the Clouds* (June 2004)

⁴⁵ Bitzinger, Richard, *Towards a Brave New Arms Industry?*, Adelphi Paper, 356, Institute for International Institute for Strategic Studies (2003) p.5

led to the present scenario where Europe's fragmented and nationally protected defence industries cannot expect to survive without reform. Indeed political and industrial elites have perceived this fragmentation competitiveness problem as an existential threat to the DTIB in Europe⁴⁶ as R&D spending in US Aerospace and Defence companies yield nearly twice the financial return than that of European ones.⁴⁷

2.3.1 Fragmentation & duplication

Realising the new budgetary environment of the post Cold War period the US consolidated its defence aerospace sector from 25 individual companies to just four global behemoths in the eight years to 1998.⁴⁸ Further expounding the competitive pressure was that these four companies had more or less exclusive access to the largest single market and budget for defence equipment. The European's response, even if aware of the pending competitive pressure and that autarky in arms production was becoming anachronistic and unsustainable, was continued protection of national suppliers.⁴⁹ Consolidation if it occurred happened within Member States in what was presumably a scramble to create a national champion or two that might survive any eventual restructuring and consolidation at the European level. While this has no doubt helped and along the way led to the creation of some big European primes such as EADS, BAE Systems, Thales, Finmeccanica and Saab it still falls short of the reform needed.

Fragmentation is still rife across Europe. After supply side consolidation in the nineties Europe still had ten armoured vehicle manufacturers, ten helicopter producers, eleven missile companies and fourteen Shipyards; in each of these categories the US had 5 or less.⁵⁰ The demand side also remains fragmented as, aside from the odd collaboration, national procurement agencies act as 27 autonomous entities spending on average 85% of their procurement budget within their own national borders.⁵¹

Why is this fragmentation so destructive? Essentially it means that across Europe many weapons programmes are duplicated, sometimes several times. Duplication can happen at the R&D stage, in production facilities, in certification and leads ultimately to shorter inefficient production runs vis-a-vis the economies of scale reached in the US defence industry. This in effect results in European resources being spread much wider and thinner than comparative projects in the

⁴⁶ Jones, Seth G., *The Rise of European Security Cooperation* (Cambridge University Press:2007)p.169

⁴⁷ Ben-Ari, G. & Zlatnik, M., *Aerospace & Defence: Inventing and Selling the Next Generation*, Center for Strategic & International Studies (May 12th 2009) p.1

⁴⁸ Aviation Week & Space Technology (March 16 1998) p. 25

⁴⁹ Salmon, Trevor C. & Shephard, Alistair J. K., *Toward a European Army: A military power in the Making?* (Lynne Rienner Publishers, Boulder:2003) p.193

⁵⁰ Dodd, T., *European defence industrial and armaments cooperation*. House of Commons library research paper no 97/15 (February 4th 1997)

⁵¹ European Commission, *A strategy for a stronger and more competitive European defence industry* (2007) p.4

US. For example, in Europe there are currently 89 unique major weapons platforms under development while in the US there are 27.⁵² Keeping in mind that the US defence budget is more than double than that of Europe's fragmented total and that it outspends Europe by 3 to 1⁵³ on procurement and by 6 to 1⁵⁴ on defence R&D, it should come as little surprise that the EU DTIB is under competitive pressure. This is critical as the financial viability of many European defence programmes hang on the success of lucrative export sales.⁵⁵ Consolidation in demand and supply must take place or European companies and defence programmes will lack the scale and capital needed to develop systems that can compete both technologically and on cost with those from the US or indeed other rising powers.

2.3.2 Escaping the dilemma

How does Europe move forward to strengthen its DTIB and enable it to supply cutting edge equipment to Member State armed forces at a viable and sustainable cost? As argued earlier in this chapter, dependency on non-EU suppliers is not a viable solution from either a security or economic perspective; this leaves EU Member States with no other option than to collaborate a view wide held among European policy makers.⁵⁶

Yet collaboration has its different forms; traditionally EU Member States have come together on joint multinational procurement programmes in an attempt to pool demand and benefit from the associated economies of scale. Although this strategy has yielded some successes in terms of technologically competitive products, it has ultimately failed to deliver a sustainable long term solution. Thus the new approach has been to integrate the until recently exempt defence procurement ever more into the Single Market.

The past half century is dotted with institutions set up to manage joint procurement efforts such as the Conference of National Armaments Directors (CNAD), the Independent European Programme Group (IEPG), Western European Armaments Group (WEAG), Organisation Conjointe de Coopération en matière d'Armement (OCCAR). Ultimately all these institutions failed to deliver meaningful restructuring in the defence industry as they did not attempt or did not effectively succeed in eliminating the principle of *juste retour* which has hampered most collaborative procurements programmes to date.⁵⁷ Under this

⁵² European Commission, *A strategy for a stronger and more competitive European defence industry* (2007) p.4

⁵³ European Defence Agency. *European - United States defence expenditure 2008*, (December 2009) p.9

⁵⁴ European Commission, *A strategy for a stronger and more competitive European defence industry* (2007) p.4

⁵⁵ Struys, W., 'Y'a-t-il encore un rôle pour les petits et moyens pays dans le cadre de la construction de l'Europe d'armement?', *Arms* 21/53 (2004), pp. 27-8.

⁵⁶ Witney Nick, *The EDA's Goals: Strengthening Europe's Capabilities and Defence Industrial Base*, speech at the European Institute's Transatlantic Roundtable on Defence and Security, Washington (February 14th 2007)

⁵⁷ Hoeffler, C., *European armament co-operation and the renewal of industrial policy motives*, *Journal of European Public Policy*, 19:3, 435-451 (2012) p.441

principle each participating Member State receives, at every stage of the project, a corresponding amount of jobs and contracts (based on man hours and value) to its overall investment.⁵⁸ Thereby suppliers are seldom selected for their expertise or price but rather because a given Member State in a multinational collaborative project needs its allotted share of the work. In many cases final production lines are built in each participating state⁵⁹ and even sub components are developed and produced by multilateral participating nation consortia.⁶⁰ Add to this international logistics and multilateral international management costs⁶¹ and many cost savings from pooled R&D spending and long production runs will most likely have evaporated. Ultimately the level of national protectionism sustained throughout many of the collaborative procurement projects means they have had a negligible effect on restructuring and consolidation in the European DTIB and have arguably served to perpetuate the status quo of its fragmented structure rather than bringing any wholesale change through cross-border mergers and acquisitions.

Post-millennium the focus on collaboration efforts shifted towards the objective of creating a single European Defence Equipment Market (EDEM). The logic was to integrate the hereto exempt defence sector more comprehensively into EU single market rules thereby obliging procurement agencies to provide fair and transparent tendering procedures. As countless researchers in this field such as Guay & Callum⁶²; Hartley⁶³; Jones⁶⁴; Mörth & Britz⁶⁵; and Hoeffler⁶⁶ have noted, the root and persisting cause of Europe's fragmented defence markets and industries can be linked unequivocally to Articles 346 TFEU (ex 296 TEC). Part 1 (a) States that;

*“no Member State shall be obliged to supply information the disclosure of which it considers contrary to the essential interests of its security”*⁶⁷

With part (b) adding that

⁵⁸ Taylor, Trevor, *The European Union and National Defence Policy*, Edited by Jolyon Howorth and Anand Menon (Routledge, London:1997) p.126

⁵⁹ Taylor, Trevor, *The European Union and National Defence Policy*, Edited by Jolyon Howorth and Anand Menon (Routledge, London:1997) p.126

⁶⁰ Taylor, Trevor, *The European Union and National Defence Policy*, Edited by Jolyon Howorth and Anand Menon (Routledge, London:1997) p.126

⁶¹ Ibid.

⁶² Guay, T., & Callum, R. *The transformation and future prospects of Europe's defence industry*, International Affairs, 78, 757-776. (2002)

⁶³ Hartley, K., *Defence industrial policy in a military alliance*. Journal of Peace Research, 43, 473-489 (2006)

⁶⁴ Jones, Seth G., *The Rise of European Security Cooperation* (Cambridge University Press:2007) Chapt. 5

⁶⁵ Mörth, U. & Britz, M., *European integration as organizing: The case of armaments*. Journal of Common Market Studies, 42, 957-973 (2004)

⁶⁶ Hoeffler, C., *European armament co-operation and the renewal of industrial policy motives*, Journal of European Public Policy, 19:3, 435-451 (2012)

⁶⁷ European Union, *Consolidated Treaties & Charter of Fundamental Rights* (EU Publications Office, Brussels 2010) p.194

“any Member State may take such measures as it considers necessary for the protection of the essential interests of its security which are connected with the production of or trade in arms, munitions and war material; such measures shall not adversely affect the conditions of competition in the common market regarding products which are not intended for specifically military purposes.”

Part (b) refers to an extensive list of defence equipment dating back to 1958 to which Article 346 TFEU is applicable. In principle, Article 346 should not be a wide-ranging, industry-encompassing automatic exemption. Rather, each defence procurement contract should, in theory, be assessed on a case-by-case basis judging its sensitivity to the given Member States national security concerns if an exemption is sought.⁶⁸ However, this is far from the reality in which Member States have taken a very liberal definition of “*essential security interests*” and blanket derogation has been the rule rather than the exception.⁶⁹

In order to establish a Europe wide ‘single market’ for defence equipment it has thus been imperative to try and limit the excessive use of Article 346. Hoeffler observes that it has been the target of European Commission initiatives on five separate occasions⁷⁰ or six if one includes the most recent Defence Procurement Directive 2009/81/EC. Alongside the Commission’s efforts the EDA was set up in 2004 in part with one of its central objectives being the establishment of an EDEM.⁷¹ This finally brought the field of defence industry policy into the EU framework, and thereby codified the process begun back in the 1990’s.⁷² By late 2005 the EDA had launched its Code of Conduct on defence procurement that sought by way of a voluntary soft law commitment to open up defence procurement and limit Article 346 use as a first step towards establishing a true EDEM. It is this CoC along with its complimentary European Bulletin Board (EBB) of contracts that this paper shall seek to assess.

2.4 Ambition & scope of the study

Considerable research has been conducted on the changing structure, as well as the fragmentation, deficiencies, and challenges facing the European DTIB. Others have focused on the Europeanization of the policy area, while yet another group have sought to assess the merits of European collaborative projects. However, little has been done to evaluate more recent efforts towards the marketization of defence procurement at the EU level.

⁶⁸ European Commission, Green paper, *Defence procurement*, (September 23rd 2004) p.6

⁶⁹ European Commission, *A Strategy for a Stronger and More Competitive European Defence Industry (2007)*

⁷⁰ Hoeffler, C., *European armament co-operation and the renewal of industrial policy motives*, *Journal of European Public Policy*, 19:3, 435-451 p.444 (2012)

⁷¹ Britz, M., *The Role of Marketization in the Europeanization of Defense Industry Policy*, *Bulletin of Science Technology & Society* 2010 30: 176 (2010) p.178

⁷² *Ibid.* p.178

For example, Guay & Callum⁷³, Hayward⁷⁴, Meijer⁷⁵ and Vlachos-Dengler⁷⁶ have all explored causal pressures behind European defence industry consolidation of the 1990's that saw the emergence of a quad global players; namely EADS, BAE Systems, Finmeccanica and Thales.⁷⁷ While others such as Schmitt⁷⁸, Barrinha⁷⁹ and Giegerich⁸⁰ have focused on the European DTIB 'existential threat' discourse which has driven European efforts to move beyond the consolidation of the 1990's and create a true EDEM. There has also been considerable investigation into the Europeanization of defence industrial policy by the likes of Hoefler⁸¹, Britz & Eriksson⁸², and Mawdsley⁸³. This is the process whereby national systems including institutions, policies and even the polity itself orientate themselves towards the EU level, while helping to shape the emerging field in the process.⁸⁴ A more recent paper by Britz⁸⁵ has explored, specifically, the role of marketisation in the process of defence industrial policy Europeanization. This is a very timely contribution as EDA and Commission efforts have converged on liberalising defence procurement across Europe with the eventual aim of creating a true single EDEM.⁸⁶

What is notable about the research in this field is the lack of any quantitative assessment of how this policy of 'marketizing' towards an EDEM is faring. Past studies such as those by Hartley⁸⁷ and Donaldson⁸⁸ investigated the merits of European multinational collaborative projects of the type that have dominated

⁷³ Guay, T. & Callum, R., "The transformation and future prospects of Europe's defence industry", *International Affairs*, 78-4 (2002) pp. 757-776.

⁷⁴ Hayward, K., *The globalisation of defence industries*. *Survival*, 42 (2000) pp.115-132

⁷⁵ Meijer, H., *Post-Cold War Trends in the European Defence Industry: Implications for Transatlantic Industrial Relations*, *Journal of Contemporary European Studies*, 18:1, (2010) pp.63-77

⁷⁶ Vlachos-Dengler, K. *From National Champions to European Heavyweights. The Development of European Defense Industrial Capabilities Across Market Segments*, Briefing, RAND, Santa Mónica: 2002)

⁷⁷ SIPRI, *Top 100 arms-producing and military services companies* (2010)

⁷⁸ Schmitt, B., *Defence Procurement in the European Union: The Current Debate* (EUISS, Paris: 2005)

⁷⁹ Barrinha, A., *Moving towards a European Defence Industry? The Political Discourse on a Changing Reality and its Implications for the Future of the European Union*, *Global Society*, 24:4, (2010) 467-485

⁸⁰ Giegerich, B., *Budget Crunch: Implications for European Defence*, *Survival: Global Politics and Strategy*, 52:4, (2010) pp.87-98

⁸¹ Hoefler, C., *European armament co-operation and the renewal of industrial policy motives*, *Journal of European Public Policy*, 19:3, (2012) pp.435-451

⁸² Britz, M. & Eriksson, A. (2000) 'British, German, and French defence industrial policy in the 1990s', Swedish Defence Research Establishment, User report.

⁸³ Mawdsley, J., 'The changing face of European armaments co-operation: continuity and change in British, French, and German armaments policy, 1990-2000', Ph.D. dissertation, Department of Politics, University of Newcastle upon Tyne (2000)

⁸⁴ Bomberg, E., Peterson, J. & Stubb, A. *The European Union: How Does it Work?* (Oxford University Press: 2008) p.72

⁸⁵ Britz, M., *The Role of Marketization in the Europeanization of Defense Industry Policy*, *Bulletin of Science Technology & Society* 30: 176 (2010)

⁸⁶ Mawdsley, J. (2008): *European Union Armaments Policy: Options for Small States?*, *European Security*, 17:2-3, (2008) p.367

⁸⁷ Hartley, K., *Collaboration and European Defence Industrial Policy*, *Defence and Peace Economics*, 19:4, 303-315 (2008)

⁸⁸ Donaldson, P., *Major European Defence Programmes*, *Military Technology* Vol 35, Issue 9 (2011) p.63

cooperation since the end of Cold War and Jones⁸⁹ has shown that intra European collaboration has taken preponderance over collaboration with other regions, however his figures do not inform us on developments after 2000. Indeed, Hartley has noted that finding quantitative data for the defence sector is a tough challenge in itself.⁹⁰ Defence companies and procurement agencies are not necessarily the most transparent actors in the economy and it is often difficult to separate a large conglomerate's civil sales from its defence ones. This paper naturally faces the same constraints as others with regards to sourcing viable quantitative data and is therefore utilising an open source database maintained by the Stockholm International Peace Research Institute which aims to track all international arms transfers.⁹¹ Although as an open source database it can never be perfect, it should be safe to say that among the 27 EU Member States in the post cold war period it is not likely to have omitted many cases of transfers.

The primary aim of this paper is to conduct a baseline study policy evaluation of the EDA's 2005 CoC on Defence Procurement and the corresponding EBB set up to facilitate its objectives. Broadly speaking the question sought to be answered will be;

Has the EDA's CoC had any success in promoting marketization in the field of defence procurement?

The analysis will focus on whether the measures have been successful in promoting intra-European trade in defence goods. This cross-border trade will be the key indicator of marketization and treated as a proxy of whether governments and their procurement agencies have adopted policies of 'fair and equal' treatment of suppliers as pledged in the CoC.⁹² The study will involve two parts: a quantitative trade analysis and a series of qualitative interviews.

The first part of the study will involve mapping quantitative trade data to display the levels of intra-EU arms transfers pre and post 2006 in search of discrepancies. This type of baseline comparative analysis is not dissimilar in principle to the approach used by the European Commission to measure the impact of its new Directives on the single market.⁹³ This part of the study will broadly seek to answer the question;

Have levels of cross-border trade in defence equipment increased among the 27 Member States of the EU?

In addition to this quantitative approach this study will also seek to gather qualitative data by way of expert interviews. This addition is necessary in order to

⁸⁹ Jones, Seth G., *The Rise of European Security Cooperation* (Cambridge University Press: 2007) chapt. 5

⁹⁰ Hartley, K., *Collaboration and European Defence Industrial Policy*, *Defence and Peace Economics*, 19:4, 303-315 (2008) p.314

⁹¹ SIPRI, *Arms Transfers Database* (2012) : <http://www.sipri.org/databases/armstransfers>

⁹² European Defence Agency. *The Code of Conduct on Defence Procurement* (November 21st 2005) p.2

⁹³ Interview 10: Legal Officer, DG MARKT, European Commission

clarify any questions of equifinality that may arise should the result of the quantitative enquiry display a noticeable rise in cross border trade. This is to say; in the myriad of collaborative procurement efforts, an interpretative communication, and Court of Justice case law, how can one be sure that a rise in cross-border trade can be attributable to the EDA's CoC? Indeed, with the quantitative method alone it cannot be. Thus the objective of the interviews is to gain an insight, from economic actors on both the supply and demand side of the sector as well as from policy practitioners on the National and EU level, as to whether the pledges of the CoC have been successful in bringing about a change in behaviour. Broadly speaking, this part of the study shall seek to answer the question;

Has the EDA's CoC led to a change in the protectionist defence procurement preferences of Member States?

This study therefore aims to answer two unique questions that are to my best knowledge yet to be investigated in the sphere of academia. Furthermore, it seeks to provide a quantitative insight in field that has thus far, and for good reason, been somewhat lacking in this regard.

Finally, many Europeans both pro-EU and Eurosceptic are often hesitant about even discussing matters related to defence and the dirty word 'superstate' or visions of an imperial 'European army' are suddenly part of the discussion. Thus for those who equate the quest for an EDEM as a move toward a centralised supranational army, Giegerich provides a terse response;

*"Greater collaboration among European governments is not about creating a European army. The motivation should not be ideological, but hard-nosed pragmatism: cooperation is about delivering usable capabilities at better value for money to ensure that the inevitable period of constrained resources does not lead to the downgrading of European defence capabilities."*⁹⁴

Indeed the motivation should be penny pinching. Although an unfortunate necessity, the production of defence equipment is not as beneficial to society as the tangible gains of schools or hospitals. Therefore efforts should therefore be made to make it as efficient and cost effective as possible.

⁹⁴Giegerich, B., *Budget Crunch: Implications for European Defence*, *Survival: Global Politics and Strategy*, 52:4, 87-98 (2010) p.97

3 Methodology

3.1 A multi-strategy research design

As mentioned in the previous chapter, in order to answer the research problem fully and with any degree of certainty, it was necessary to utilize more than one method. Thus a *Multi-Strategy* or *Mixed Methodology* research design was employed. The two methods being: 1. the use of exploratory data analysis and descriptive statistics to determine whether there has been an increase in the cross border trade of conventional weapons in the EU, and 2. A series of semi-structured expert interviews to determine whether the expected rise in trade can be attributed with any certainty to the actions of the EDA. To further define this research design it is worth considering the differing classifications of multi-strategy research put forward by Hammersley in 1996⁹⁵ and Morgan in 1998⁹⁶.

Hammersley suggests there are three broad approaches towards multi-strategy research dubbed: *Facilitation*, *Complementarity*, and *Triangulation*. Facilitation is rather loosely defined as “employing one research strategy in order to aid research using the other strategy”⁹⁷ whereas Complementarity “occurs when the two research strategies are employed in order that different aspect of an investigation can be dovetailed”⁹⁸. Finally, and probably of most use in highlighting the approach used in this study, there is Triangulation. It is defined as the “use of quantitative research to corroborate qualitative research findings or vice versa”⁹⁹. This study is indeed representative of the ‘vice versa’ in that the primary purpose of the qualitative semi-structured expert interviews is to determine equifinality in the findings provided by the quantitative investigation.

Morgan’s classification system of approaches to multi-strategy research design has four delineations. In his approach he determines which of the methods, qualitative or quantitative, is principle and which is complimentary as well as which one is preliminary and which one is follow-up.¹⁰⁰ This double categorisation of how the qualitative and quantitative methods are placed and

⁹⁵ Hammersley, M. *The Relationship between Qualitative and Quantitative Research: Paradigm Loyalty versus Methodological Eclecticism*, in Richardson, J (eds.) *Handbook of Research Methods for Psychology and the Social Sciences* (BPS Books, Leicester: 1996)

⁹⁶ Morgan, D. L., *Practical Strategies for Combining Qualitative and Quantitative Methods: Applications for Health Research*, *Qualitative Health Research*, 8: 362-76 (1998)

⁹⁷ Bryman, A. *Social Research Methods* 2nd Edition (Oxford University Press, Oxford: 2004) p.455

⁹⁸ Ibid.

⁹⁹ Ibid.

¹⁰⁰ Morgan, D. L., *Practical Strategies for Combining Qualitative and Quantitative Methods: Applications for Health Research*, *Qualitative Health Research*, 8: 362-76 (1998) p.368

interact with one another in the overall research design, in terms of *Priority* and *Sequence*, provides a rather neat matrix that describes the four possible outcomes. See Fig 1.¹⁰¹ below.

		Priority Decision	
		Principal Method: <i>Quantitative</i>	Principal Method: <i>Qualitative</i>
Sequence Decision	Complementary Method: <i>Preliminary</i>	<p>1. Qualitative Preliminary qual → QUANT</p> <p>Purposes: Smaller qualitative study helps guide the data collection in a principally quantitative study.</p> <ul style="list-style-type: none"> • Can generate hypotheses, develop content for questionnaires and interventions, etc. <p>Example: Focus groups help to develop culturally sensitive versions of a new health promotion campaign.</p>	<p>2. Quantitative Preliminary quant → QUAL</p> <p>Purposes: Smaller quantitative study helps guide the data collection in a principally qualitative study.</p> <ul style="list-style-type: none"> • Can guide purposive sampling, establish preliminary results to pursue in depth, etc. <p>Example: A survey of different units in a hospital locates sites for more extensive ethnographic data collection.</p>
	Complementary Method: <i>Follow-Up</i>	<p>3. Qualitative Follow-up QUANT → qual</p> <p>Purposes: Smaller qualitative study helps evaluate and interpret results from a principally quantitative study.</p> <ul style="list-style-type: none"> • Can provide interpretations for poorly understood results, help explain outliers, etc. <p>Example: In-depth interviews help to explain why one clinic generates higher levels of patient satisfaction.</p>	<p>4. Quantitative Follow-up QUAL → quant</p> <p>Purposes: Smaller quantitative study helps evaluate and interpret results from a principally qualitative study.</p> <ul style="list-style-type: none"> • Can generalize results to different samples, test elements of emergent theories, etc. <p>Example: A statewide survey of a school-based health program pursues earlier results from a case study.</p>

According to Morgan's classification this study would be defined as method number three in the matrix. That is to say, if we consider the *priority decision*, the quantitative investigation into the levels of cross border trade in conventional weapons represents the *principle method* and the semi-structured expert interviews represent the *complementary method*. Turning to the *sequence decision*: the quantitative study will be *preliminary* and the qualitative study will

¹⁰¹ Morgan, D. L., *Practical Strategies for Combining Qualitative and Quantitative Methods: Applications for Health Research*, Qualitative Health Research, 8: 362-76 (1998) p.368

be the *follow-up*. Bryman 2004 actually advises that the *priority decision* should be governed by which ever method is the principle data collection tool.¹⁰² Admittedly, using this advice alone it would be difficult to determine which part of this study was the *principle*. However, a closer look at Morgan's explanations for the purpose of the different methods provides clarification. He states that when using method number three the qualitative study is used as a follow up to evaluate and interpret the results found in proceeding quantitative study as well as explain poorly understood results or outliers.¹⁰³ This describes, more or less, the exact role that the quantitative and the qualitative methods will play in this multi-strategy research design. Thus this study would be representative or Type 3 in Morgan's grid.

3.1.1 Critiques of multi-strategy research

Despite growing popularity within the field of social sciences multi-strategy or mixed methods research is not without its detractors. Bryman 2004 identifies two main camps that challenge the mixing of qualitative and quantitative methods. Firstly, the *embedded methods* argument stipulates that the researchers choice of method and therewith their approach to data collection leads to a firm commitment to an epistemological position which will be irreconcilable with the differing position committed to by the 'other' method used.¹⁰⁴ Secondly, and closely linked is the *paradigm* argument. Here the qualitative & quantitative research fields each occupy a paradigm sphere in which they have their own incompatible methods, values and epistemological assumptions.¹⁰⁵ The end result is that mixed method research is essentially only taking place in one of these paradigms and on a superficial level. Bryman notes that there are rather central flaws to both these accusation. For the former there is little evidence to prove that methods are inextricably locked to certain epistemological positions and for the latter there is doubt as to whether the qualitative and quantitative research camps in fact constitute paradigms.¹⁰⁶ Pearce adds that "proponents of the metaphysical paradigm often assert that the two paradigms create incompatible kinds of knowledge, but this argument fails on multiple levels and disregards the practical considerations and many successes of actual research"¹⁰⁷. Indeed it seems that mixed methods research has become much more popular, or 'acceptable', in recent years and while their merits have been shown Bryman

¹⁰² Bryman, A. *Social Research Methods* 2nd Edition (Oxford University Press, Oxford: 2004) p.455

¹⁰³ Morgan, D. L., *Practical Strategies for Combining Qualitative and Quantitative Methods: Applications for Health Research*, *Qualitative Health Research*, 8: 362-76 (1998) p.368

¹⁰⁴ Bryman, A. *Social Research Methods* 2nd Edition (Oxford University Press, Oxford: 2004) p.452-3

¹⁰⁵ Ibid p.453

¹⁰⁶ Ibid.

¹⁰⁷ Pearce, L. (2012) *Mixed Methods Inquiry in Sociology*

warns against it being perceived as a universally applicable panacea. He warns that more methods and more data are poor substitutes for a good research design and that mixed methods should not imply any sort of superiority over a well conducted mono-method approach.¹⁰⁸ For this study the motivation for the use of the mixed methods approach is largely very straightforward. It was not possible to answer the research problem fully without using more than one method. Revisiting the problem: *Has the EDA's CoC had any success in promoting marketization in the field of defence procurement? (using cross-border trade as a key indicator)*

Clearly, the quantitative method deployed can determine whether there has been a significant change in the intra-EU conventional weapons trade, however, it sheds little light on what has been the cause of this rise as there are several complex dynamics that might affect this level of trade. The Qualitative method by contrast cannot provide any meaningful empirical evidence on the rise or fall in trade between 27 different countries yet should provide an insight into whether the EDA's CoC can be attributed as a leading causal instrument in any changes in behaviour observed. Thus the two methods employed in this study are complimentary but also wholly necessary if one is to attempt to answer the research problem.

3.1.2 What kind of output?

When embarking on this study considerable thought was expended on whether it is ultimately deductive or inductive. That is to say, is the ambition of the study to confirm or reject a held or developed hypothesis within a deductive and wholly positivist framework? Or is the ambition, by way of induction, to develop a theory from the observations in the data collected?¹⁰⁹ Unfortunately, the answer is not straightforward as it effectively comprises elements of both.

For example, if we look at the quantitative part of the study first: its primary purpose to test the hypothesis that the EDA's CoC has led to a rise in the level of intra EU trade in conventional weapons. This represents largely a text book approach to deductive study. Turning to the qualitative semi-structured expert interviews: the primary ambition is to help interpret any rise in trade observed in the first part of the study and determine whether this change can be attributed to the impact of the EDA's CoC. Here the approach is slightly different as there may be various explanations as to why there has been a rise in trade levels, should indeed a rise be the trend observed. Again the primary objective will be deductive in the sense that it will seek to verify, yay or nay, whether the CoC had an effective impact on any rise in trade levels. However, should the CoC not be deemed the instrumental cause behind such a rise in trade then there will arise an inductive element to this study. Data from the qualitative study may

¹⁰⁸ Bryman, A., *Social Research Methods* 2nd Edition (Oxford University Press, Oxford: 2004) p.464

¹⁰⁹ *ibid.* pp.8-10

present insights which go some way to help in the formulation of a new theory for the hypothesised rise in trade levels of conventional weapons. In addition to answering the basic yes or no, as to whether there has been a significant rise in trade levels, the quantitative study will involve Exploratory Data Analysis that is fundamentally inductive in nature as it seeks to find patterns in data without a predefined hypothesis.¹¹⁰

3.2 Quantitative – confirmatory & exploratory data analysis

This part of the study will conduct secondary analysis, both confirmatory and exploratory, on a dataset derived from the arms transfers’ database maintained by the SIPRI. Although a necessity, given the limited available sources of statistical data on arms transfers not to mention the scope of this paper, secondary analysis provides distinct advantages. Firstly, it provides high quality data versus little cost or time invested.¹¹¹ This is crucial as it enables the second part of this study to focus on the time consuming activity of conducting expert interviews. Secondly, it enables the possibility for longitudinal analysis. This is crucial for this study as it permits the mapping of intra-EU trade arms trade levels in time periods leading up to the EDA’s CoC and can thus act as a control when comparing to the period after.

As stated previously, the primary aim of the quantitative part of this study will be to determine whether or not there has been a rise in the intra-EU trade in conventional weapons since 2006 as a proxy for the occurrence of marketization. This can be deemed as run of the mill confirmatory data analysis. Once the data has been collected and transformed this test ought to be relatively straightforward. The secondary aim will be to conduct a form of exploratory data analysis on the dataset in order to search for interesting trends. While some have defined exploratory data analysis as involving prescribed statistical or computational tools for the preliminary analysis of one’s data¹¹², this will not be the definition employed here. Rather this study will utilize the definition provided by its founding father John Tukey who insisted that “Exploratory Data Analysis is an attitude, flexibility, and a reliance on display, NOT a bundle of techniques, and should be so taught.”¹¹³ Tukey was concerned that social science and even the natural sciences seldom begin with a tidy straightforward question. He emphasises

¹¹⁰ Behrens, T. *Principles and Procedures of Exploratory Data Analysis*, Psychological Methods, Vol. 2, No. 2, 131-160 (1997)

¹¹¹ Bryman, A., *Social Research Methods* 2nd Edition (Oxford University Press, Oxford: 2004) p.202

¹¹² Ibid.

¹¹³ Tukey, J. (1980) *We Need Both Exploratory and Confirmatory*, American Statistician Vol. 34. No.1 (February) pp.23-25. (1980) p.23

that most questions or hypothesis are derived from what he calls ‘quasi-theoretical’ insights that are most often based on the ‘best available’ past data. There are two main reasons for this approach to be applied in this study. Firstly, it may be possible to discover trends that help to deal with questions of equifinality that may arise, should the qualitative study provide an equivocal answer. Secondly, once the data set has been compiled and transformed, it would seem a terrible waste to only confirm or reject the initial hypothesis. Thus it is expected that such exploration might throw up trends that are inherently interesting and if not a direct aid to this study may be found useful in further studies.

3.2.1 Data - sourcing and limitations

Possibly the most daunting task when embarking on the quantitative part of this study was where to find the data. Although improving through outlets such as the EU Annual Report on Arms Exports, access to hard economic data on the defence sector can be less than straightforward to find.¹¹⁴ National government statistics may provide this sort of data but trying to patch such statistics together into a coherent dataset would be well beyond the task of this paper and more the scope of a doctoral study. National records would undoubtedly be uneven or patchy in their completeness as well as different in scope and method. Thus it became clear that a single source database or some form of collated statistics would be necessary.

In terms of compiled import-export data on the trade of arms between all EU Member States there are few sources to be found. For this study only two potential sources were found. One was the EU Annual Report on Arms Exports and the other was the SIPRI Trade Indicator Value (TIV) database of international arms transfers. Despite the EU Annual Report providing accurate official statistics several other factors made the open source SIPRI database a more suitable choice for this study.

The first has to do with the longitudinal investigation that will be part of this study. That is to say this study aims to cast its eye back to 1994 when looking at intra-EU arms transfers. As the EU Annual Report was only first published in 1999 this limits its use considerably. The SIPRI database by contrast has yearly statistics dating back to 1950.¹¹⁵ Secondly, it was not until the fourth EU Annual Report in 2002¹¹⁶ that exports were broken down on a country by country basis, a feature that the SIPRI database has from the start. For this study it is critical to know where the exports are going and not just the total sum of exports from any given EU country. Thirdly, the SIPRI database has all values regardless of year or currency represented in 1990’s US\$ prices. This permits the easy observation of

¹¹⁴ Hartley, K., Collaboration and European Defence Industrial Policy, *Defence and Peace Economics*, 19:4, 303-315 (2008) p.314

¹¹⁵ SIPRI, *Arms Transfers Database* <http://www.sipri.org/research/armaments/transfers/databases/armstransfers>

¹¹⁶ Council of the European Union, *Fourth annual report according to Operative Provision 8 of the European Code of Conduct on Conventional Arms Exports*. Brussels 11th November 2002.

trends in arms flows over time without being concerned with inflation or in what currency the trade was made in.¹¹⁷ While the EU Annual Reports does show values in Euros they have no such price adjustment and are often riddled with omissions of what the final export value actually was for a given transfer. Considering these factors, it is apparent that the SIPRI database provides the best statistics for the purposes of this study.

While the SIPRI database enables this study to reach far beyond what would be conceivable was the author to collect his own data on 18 years of arms transfers between 27 nations it also has its limitations. Firstly, the values it contains are not the actual transactions of the arms transfers; rather they are nominal values assigned using SIPRI's own unique algorithm that assigns values to certain types of armaments based on a combination of known unit production costs of a core set of weapons plus inputs for age and performance.¹¹⁸ While this is highly useful for exploring changing trends over time it does not permit for any comparison to actual economic values such as GDP figures, defence expenditure, or even national statistics on weapons exports. Furthermore the TIV can never be perfectly exact, as final sale costs may deviate from SIPRI calculations. Secondly, as it is open source there is of course a risk of omissions in the data, however, one would expect this to be low or non-existent among EU Member States, where the trade in defence goods is *relatively* transparent. However, provided error rates in valuation and omissions are to a certain degree constant across the data set then this should not void its trend generating capacity. Ultimately one has to try and work with the best data one can find. In this case, and despite the flaws listed, the SIPRI TIV database still provides the most suitable data for this study.

3.2.2 Transformation & operationalisation

Once the data had been sourced it was necessary to transform it into a form from which overall trends could be observed. The SIPRI TIV database can generate an import or export list to or from any one given country. For example, one can select imports to the UK, then select the preferred time span and the database will generate an excel table listing the value of imports, classified by country of origin and year they were imported. An example of such an import TIV table can be seen in Annex 1. One of these TIV import tables was generated for each of the current 27 EU Member States dating back to 1994¹¹⁹. The next step was to compile a yearly EU import sum for each Member States by adding all the EU originated imports for a given year into a single total. Once this had been executed, all Member State yearly totals for EU originated imports were compiled

¹¹⁷SIPRI, *Explanation of TIV Tables* (2012)

¹¹⁸ *ibid*

¹¹⁹ The implications of Enlargement will be considered in the Discussion.

into a single table, visible in Annex 2. From this table it is now possible to calculate the sum of all EU originating imports to all 27 Member States or in other words: the annual TIV sum of all cross-border trade in conventional weapons among the EU 27 from 1994 to 2011. From this dataset the quantitative part of our problem/hypothesis can now be tested.

To investigate the eighteen year period from 1994 to 2011 represented in the table it was segmented into six year periods and totals for each period were calculated. This helps to even out any anomaly/outlier years and permits the direct comparison of the pre and post EDA CoC era. Our hypothesis predicts that a rise in intra-EU trade levels will be observable in the six years after the CoC (2006-2011) in comparison to the previous six years before it (2000-2005). This expectation is based on the Ricardian theory of comparative advantage whereby, when markets are open suppliers will be chosen based on how cost effectively they can produce a given good relative to the other suppliers in the market.¹²⁰ In other words: procurement will flow cross-border to the supplier that can produce that item at the best value. Thus tanks might be predominantly supplied by the Germans, helicopters by the Italians and electronics by the French. In addition it is also necessary to compare the 2000-2005 period with the six years preceding it (1994-1999). This can be useful as it will help contextualise any rise observed after 2006 with the wider historical trajectory; i.e. is the rise extraordinary due to the EDA's CoC or has the intra-EU arms trade been rising steadily at the same rate since the end of the Cold War as suggested by Jones 2007¹²¹. The three periods of investigation will henceforth be referred to as P1 (1994-1999), P2 (2000-2005) and P3 (2006-2011).

In addition exploratory data analysis was undertaken. This had no wholly predetermined plan, but rather involved the drawing of various other tables and graphical representations of the data to generate among other things, which EU member is the biggest arms supplier to other EU Member States and which is the biggest importer. Furthermore as a by product of transforming the data it was also relatively easy to include EU import tables from third party states in order to observe how this trend has developed alongside intra-EU trading.

3.3 Qualitative - semi-structured expert interviews

This part of the study aimed to determine if the EDA's CoC played a significant role in any rise in intra-EU arms transfers observed in the first part of the study. Furthermore, should the EDA's CoC be deemed superfluous as an explanatory factor then the follow on aim is to forage for other causal explanations. Although the data from the quantitative study may indicate a cause and effect link between the CoC and a rise in trade by way of timing this link will be at best tenuous as the

¹²⁰ Library of Economics and Liberty, *Comparative Advantage* (2012)

¹²¹ Jones, Seth G., *The Rise of European Security Cooperation* (Cambridge University Press:2007) Chapt. 5

CoC is far from the only factor that may have had an impact. Hence the explanatory power of the quantitative study has reached its limits and it is necessary to speak those who are knowledgeable in this field. Given that the business of arms production and purchase is somewhat of a niche activity when viewed alongside civilian markets it was clear from the start that only expert interviews would be useful in trying to address the research problem; i.e. a general representative from a trade ministry or chamber of commerce might be able to comment on the level of trade in the defence sector but is highly unlikely to have the intricate knowledge necessary to tackle the questions of this study. However, provided relevant ones can be found, experts can provide insights into processes and effects that are not necessarily observable to those, who are so to speak, *on the outside*. They may have spent years or even decades working in the field and will have aggregated considerable specific knowledge that is unavailable elsewhere. Furthermore, provided one manages to find and connect with experts relevant to ones enquiry chances are that the interview process will yield high results; you and your interviewee will most likely share a common scientific background and mutual understanding of the systems that you intend to discuss.¹²² In the case of this study this final point was particularly noticeable in all interviews conducted.

Why semi-structured interviews? This method was chosen as it provides the flexibility and freedom for the interviewer to seek clarification and elaboration on answers given, as well as probe beyond the more rigid script of a questionnaire or structured interview should the respondent bring up issues of interest that are unexpected.¹²³ This is a particularly valuable asset when the expert interviewed may possess a considerable knowledge advantage over the interviewer and can provide answers to the research problem that the interviewer might have missed. Whereas questionnaires and structured interviews are aimed towards collecting standardized answers that can be quickly coded and processed, the objective in semi-structured interviews is much more to listen to the respondent's point of view¹²⁴. This is particularly pertinent as the issues to be discussed are complex in nature and are therefore unlikely to have simple or concise codifiable answers. Additionally, as the respondents in this study came from varied backgrounds there was no standardised questioning; rather each interview guide was to a certain degree tailored to the position and expected knowledge specialisation of the expert.

¹²² Bognor, A., Littig, B, Menz, W., *Interviewing Experts* (Palgrave MacMillan, Basingstoke: 2009) p.2

¹²³ May, T., *Social Research: Issues, Methods and Process* 3rd ed. (Open University Press, Maidenhead: 2001) p.123

¹²⁴ Bryman, A., *Social Research Methods* 2nd Edition (Oxford University Press, Oxford: 2004) pp.319-320

3.3.1 Data – sampling & collection

By targeting experts for their knowledge sampling was decidedly purposive rather than randomized, stratified or convenience based. That is to say, the experts were sampled for their direct relevance and perceived ability to provide answers relevant to the research question.¹²⁵ In order to gain insights from as wide a spectrum as possible (within the defence field of defence procurement) it was decided to attempt to achieve a broad sample. The resulting entities were targeted for interviews:

- **Those on the policy making side:** namely, the EDA who produced the CoC and the European Commission who have long eyed the defence sector their prerogative as part of the single market and have after repeated initiatives finally wrestled the policy area away from Member States.

- **Those economic actors on who the policy has effect:**
 - **Demand side:** such as ministries of defence and procurement agencies who are obliged to act accordingly with the pledges made in the CoC and are if you like the ‘targets’ of the measures.
 - **Supply side:** suppliers of defence and security materials, national level industry associations, and defence orientated export agencies.

In the end, interview requests were sent to 40 entities across ten different countries between June and July of 2012. With an effective response rate of 27.5% eleven interviews were secured. Three were with policy makers (one EDA and two at the European Commission); three were national level defence industry associations; two were with defence contractors (one prime, one medium sized); two were with defence related export agencies; and finally, one with a procurement agency.

Although the final response rate is respectable, there were considerable difficulties making inroads with defence contractors. Whereas public servants or policy makers may feel obliged to respond to academic requests¹²⁶, there seems to be little such culture among most defence contractors. Some already ward off the potential researcher blanket warning that they “do not respond to academic requests”. With others contact was made but then cancelled as the information would be considered classified. To get a picture of how difficult this was: of the 40 requests, 26 were actually sent to contractors yet these yielded only two interviews. Thus the isolated response rate for defence contractors alone was a much more meagre 7.7%.

The interviews were conducted by telephone between July and October 2012. They averaged 35 minutes in length with the shortest lasting 26 minutes and the longest 48. All in all, the knowledge of those interviewed exceeded

¹²⁵ Bryman, A., *Social Research Methods* 2nd Edition (Oxford University Press, Oxford: 2004) p.332

¹²⁶ Bogner, A., Littig, B, Menz, W., *Interviewing Experts* (Palgrave MacMillan, Basingstoke: 2009) p.2

expectations considerably. Although it was expected that the policy makers would have intricate knowledge of the issues surrounding the research problem of this study, it was less expected from the other respondents. Or let's say it was far less expected to be able to find connect to the person with that exact knowledge in the other organisations contacted. This may be in part attributable to the request mail which succinctly outlined the aims of the research in as clear a manner as possible. Additionally, a few of the organisations responded first in order to ask further questions upon which they then proceeded to search for the appropriate respondent within their organisation. Although preparations had been made to record the interview through the use of voice over IP (VOIP) calling in combination with recording software, this ultimately did not happen. The interviews had been agreed on the basis of anonymity and after the request to record was made and rejected in the agreement and planning of the first four interviews it was abandoned and no longer pursued. This was proved to be a disappointment as the benefits of recording are numerous¹²⁷. Two factors most likely played into this preference to remain unrecorded. Firstly, the nature of the field remains sensitive and secondly, having arranged everything by email and having never met in person it is understandable that respondents had qualms about being recorded. Notes, notes and more notes were made during the interviews and typed up immediately after. This set up was far from desirable as questions from the interview guides were routinely deviated from and tangents were embarked on during the interview process. However, this was the reality faced and every effort was made to type up the notes as immediately and accurately as possible.

3.3.2 Operationalisation

What sorts of questions were asked to determine if the EDA's CoC has had a significant impact on increasing the intra-EU trade of conventional weapons? This largely depended on the profile of the respondent. However, some of the general questions asked of most respondents were:

Have you heard of the EDA's CoC and corresponding EBB of defence contracts?

Do you believe the EDA's CoC has led to a decrease in the use of Article 346?

Has the CoC led to a change in behaviour on the part of Governments, i.e. have suppliers been treated in a fair and equal manner?

Do you feel all Member States have implemented the pledges of the CoC to the same extent?

¹²⁷ Bryman, A., *Social Research Methods* 2nd Edition (Oxford University Press, Oxford: 2004) p.330

When interviewing the defence contractors or national industry associations there was also more scope for asking indirect questions to which the answer may be indicative in itself, such as:

Have you seen a rise in exports to the EU over the past 5-6 years?

Have you lost contracts in other EU Member States in which you feel your company clearly had the better offer but was subject to national bias in the final outcome?

Has your company won contracts on the EBB?

When interviewing the policy makers, the questioning focused more on how they have measured the outcome of their own work and whether they think it has been effective, whereas with ministries or procurement agencies the questioning sought to determine which steps they had taken to implement the CoC in their modus operandi.

In all cases the primary focus was on whether or not the EDA's CoC had played a significant role, however, in expectation of competing explanations the secondary focus of the interviews was to determine if the respondents believed any other factor could explain the trends observed. These questions varied from the specific in order to assess the role of the Court of Justice cases in this field:

Has your company pursued legal action to challenge the unjust loss of a contract in another Member State?

Has there been a rise in COJ cases related to defence procurement in recent years?

To the most general:

Can you provide any explanation for the rise of intra-EU trade in conventional weapons?

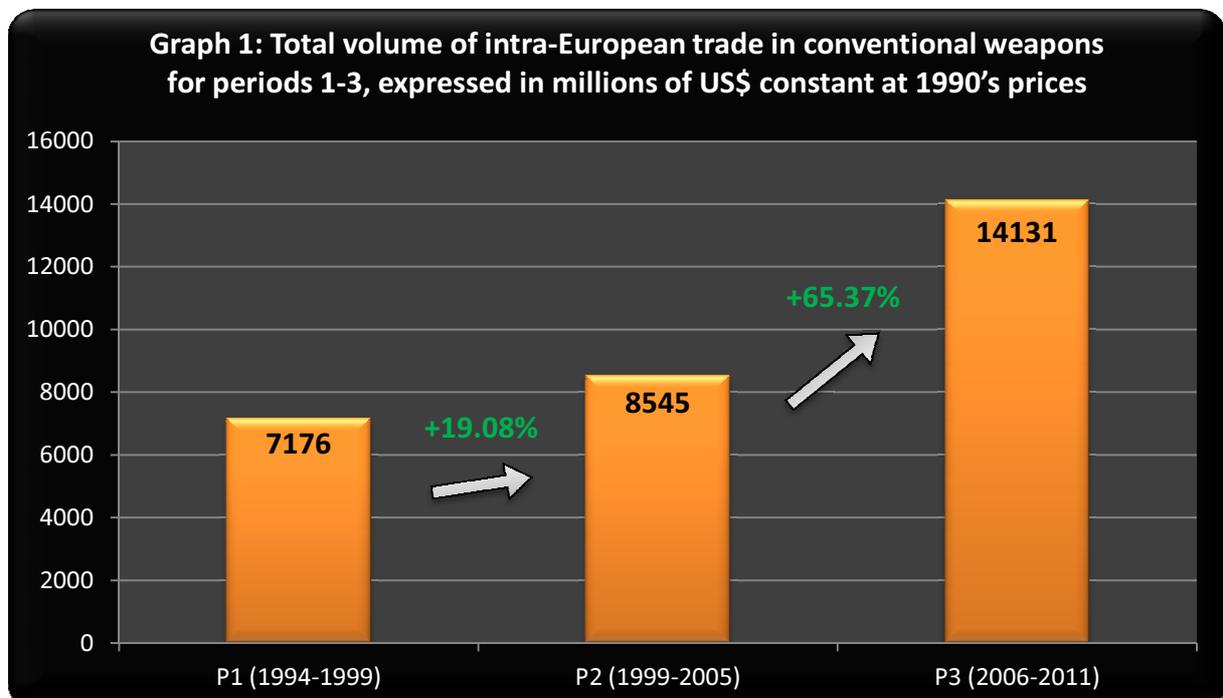
Typically the interviews guides consisted of between 8 and 12 questions, yet inevitably on some interviews these were extended upon considerably as dialogue developed. Once all the interviews were conducted and notes typed up the data was re-read to determine if there was a decisive conclusion on how the CoC has been perceived and whether it can be judged to have had an impact or not.

4 A definitive increase: but why?

The initial results from the statistical study show a substantial increase in the trade of conventional weapons among the 27 Member States of the EU. However, the feedback from the qualitative inquiry expresses little faith in the proposition that the CoC had much to do with this rise. Due to this response and in order to assist with the formulation a sounder theory to explain causation for the rise in trade levels my dataset statistics will be revisited in search of further clues.

4.1 Statistical results: growth in cross-border trade

The numbers speak decisively. Among the EU 27 there has been a notable rise in the trade of conventional weapons. If we compare the total trade volumes of the pre and post CoC era, i.e. the 2nd and 3rd periods, a **65.37% increase** is observable, see **graph 1**. Although starting from a relatively low base this rise is still significant and suggests that the trade in conventional weapons is opening up among the EU 27 as progressively more conventional weapons are being imported from other Member States.



Also noteworthy for the purposes of this study is that the 65.37% increase observed between periods 2 and 3 is considerably more than the 19.08% rise between periods 1 and 2. Thus we can speak of **accelerating growth** in the volume of intra-EU trade in conventional weapons. What is clear is that more trade is going cross-border among EU states. This indicates that marketization, as defined by Hoeffler¹²⁸, of some form is occurring; i.e. the preference of cost-effective procurement and an open attitude towards defence markets is leading to more cross-border trade as protectionism becomes less rife across the sector. Yet this does not necessarily mean that the CoC is responsible for the acceleration; indeed, growing trust among Member States may have a reinforcing effect, which over time leads to more and more trade with one another in the defence sector.

4.1.1 Discounting the eastern enlargement

After the millennium the EU undertook its so called big bang or Eastern enlargement. The union expanded, welcoming ten new Member States in 2004 and adding a further two in 2007. Intuitively one might come to the conclusion that it was this expansion of the union which led to the rises observed as 120 million+ new citizens¹²⁹ with their 12 militaries joined the Single Market. This however is not the case and is clearly demonstrable by comparing stats of the EU-15 and Eastern enlargement 12. There are two figures which can help explain this.

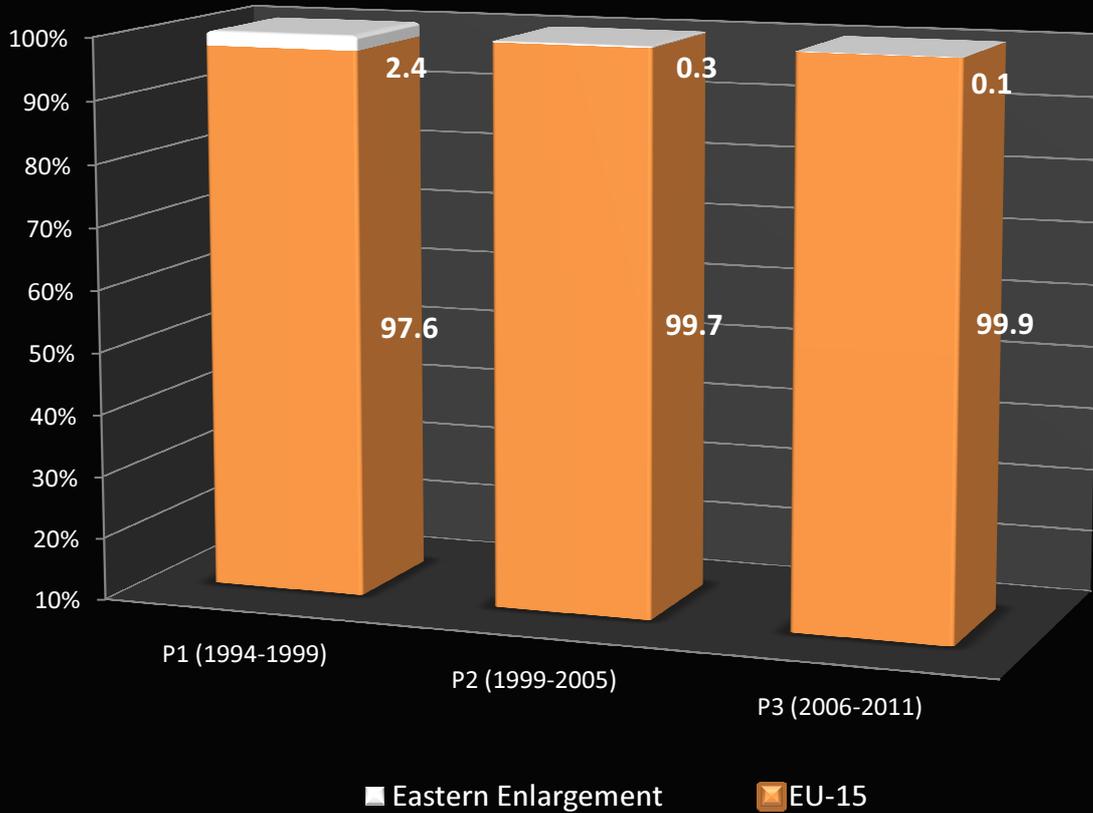
Firstly, looking at the Eastern enlargement states' share of exports in the entire intra-EU trade of conventional weapons one thing is strikingly clear: it is negligible. Across the three periods as a whole Eastern enlargement countries exports made up just 0.7% of all intra-EU transfers, see **graph 2**. Not only this, but it appears that exports from the Eastern enlargement countries to the EU-27 have actually declined across the three periods meaning that in the post CoC 3rd period from 2006-2011 exports fell to just 0.1% of the intra-EU total. This collapse in exports may be in part explained by the competitive pressures faced by the formerly state monopolized defence sectors that remained in many of the enlargement countries as a legacy of the Soviet era. Indeed, during one of the interviews with a specialist from a national-level defence industry association of a medium sized Eastern enlargement country, the respondent noted that defence industrial capacity had fallen to about 10% of its 1990 level in his country.¹³⁰ Although many states both west and east European reduced defence industrial capacity after the cold war, this contraction is particularly stark.

¹²⁸ Hoeffler, C., *European armament co-operation and the renewal of industrial policy motives*, Journal of European Public Policy, 19:3, 435-451(2012) p.437

¹²⁹ Economist, The, *A survey of the EU enlargement: In the nick of time*. (May 29th 2008)

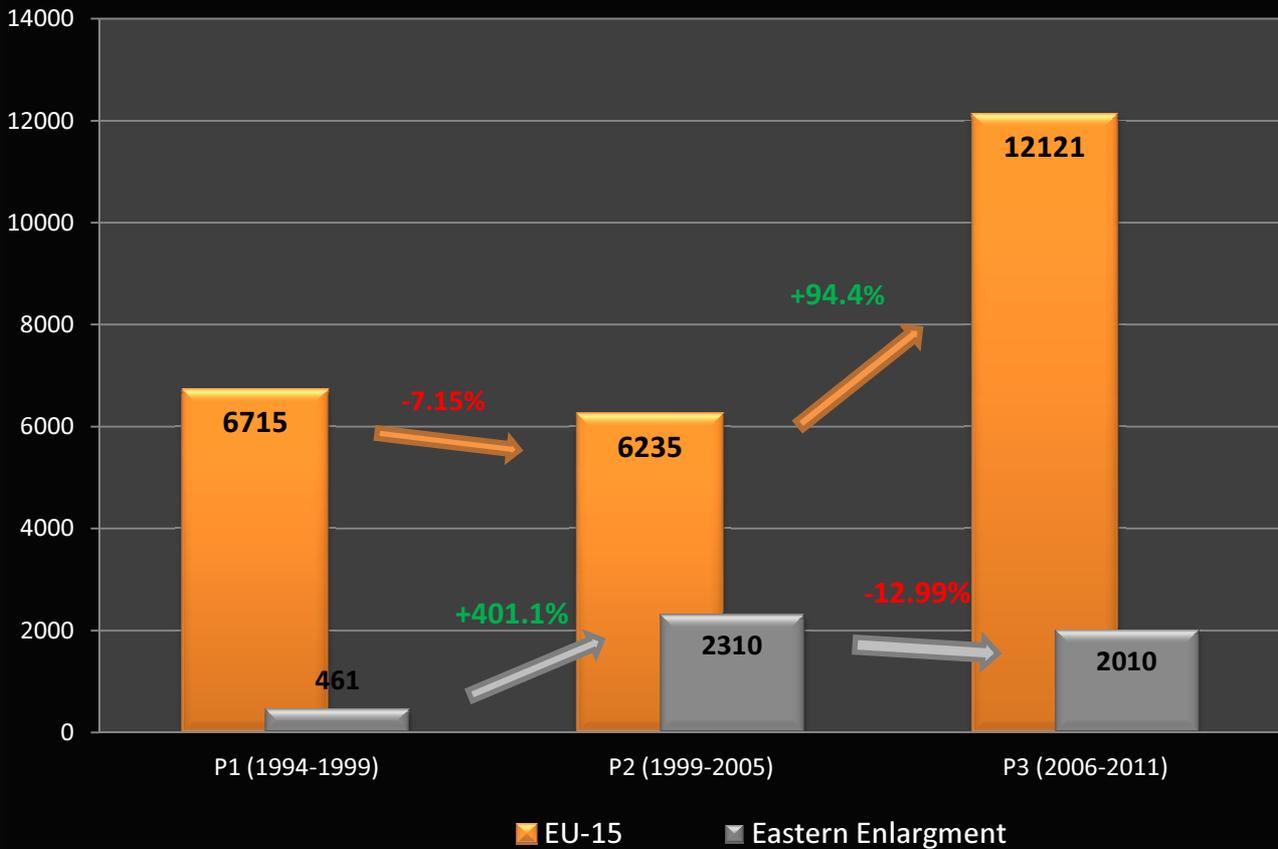
¹³⁰ Interview 04: Exports director, defence industry association, medium sized Member State

Graph 2: Eastern Enlargement Countries & EU-15 share of total intra-EU exports, expressed in percent



Secondly, it might be expected that upon joining the EU the new Member States became happy customers for the West European purveyors of modern defence equipment as their ties to Russia were actively severed. This is certainly the case and is very useful if we try to explain the rise in trade levels of 19.08% among the EU-27 between periods 1 and 2. Looking at **graph 3** we can see that intra-EU imports to the twelve new Member States rose by 401.1% whereas imports to the EU-15 were actually down -7.5% between periods 1 and 2. Thus the new Member States were actually responsible for the entire growth in the intra-EU trade of conventional weapons observed between these two periods. Thus one might speculate that without enlargement there would have actually been a subtle decline in trade levels among the EU Member States between periods 1 and 2.

Graph 3: Eastern Enlargement Countries & EU-15 share of total intra-EU imports, expressed in millions of US\$ constant at 1990's prices



However, the demand provided by the new Member States is less useful in explaining the much larger 65.37% rise in intra-EU trade levels observed among the EU27 between periods 2 and 3. If we turn again to **graph 3** one can observe that after the meteoric rise in import to the Eastern enlargement countries between periods 1 and 2 they actually decrease -12.99% between periods 2 and 3. The overall increase among the EU27 between periods 2 and 3 can be explained by the near doubling or 94.40% rise in imports to the EU-15 Member States.

Why did this occur? The rise between periods 1 and 2 is clearly attributable to the accession of the new Member States and can be explained by these states pivoting away from their former oppressor and principle arms supplier Russia. This sent them in search of new suppliers and with their membership of the EU becoming a reality it was perhaps in their interest to spend procurement budgets in the states which would be determining their accession prospects. But more importantly, why did trading among the EU-15 that had more or less plateaued between periods 1 and 2 rise so significantly between periods 2 and 3? So far it seems that the statistical study supports the hypothesis that the EDA's CoC has led to a rise in the intra-EU trade of conventional weapons.

4.2 Qualitative results: explaining causality?

Despite the rather remarkable changes in trade levels witnessed between the pre and post-COC periods the experts consulted expressed little confidence in the tentative theory that this soft law instrument could have had such a marked effect. Although some conceded that it may have had a very limited impact, pessimism that national governments could change their protectionist behaviour seemed to be the prevailing view and ultimately no resoundingly positive perceptions of the CoC were put forward by respondents.

4.2.1 Views from the policy makers

The policy makers from the European Commission and the EDA noted that it is indeed very difficult to measure the impact of the CoC in terms of its impact on cross-border trade and conceded that they had not attempted to do this.¹³¹ The first attempt to measure progress in the process of marketizing the European defence sector by reviewing trade levels has in fact only been recently outsourced by the Commission for assessing the impact of its own 2009/81/EC defence procurement directive.¹³²

Notably, when asked in general terms what impact they perceive the CoC has had the respondents did not cite cross border trade as a success factor. Rather they focused on how the CoC promoted transparency and openness to the process of defence procurement.¹³³ A legal officer from DG MARKT at the European Commission noted that “*it promoted transparency*” and “*helped pave the way for other initiatives*”¹³⁴, while the markets specialist from the EDA highlighted that it was unique as the first attempt at a genuinely market based solution opposed to the collaborative efforts seen so far and argued that this made it a “*a first real step in the right direction from a historical point of view*”¹³⁵.

However, when pressed more specifically on whether the CoC had led to an increase in cross-border trade or whether it had led to a reduction in the use of Article 346 the overall picture painted was one of little progress. The EDA did observe increasing cross-border awards on the EBB¹³⁶, however, without knowing what number of contracts went cross-border before the CoC & EBB started this doesn't necessarily indicate more than the fact that Member States are using the EBB as their primary advertising space. It also doesn't factor in how many contracts went cross-border outside the EBB. When asked if it had a real impact

¹³¹ Interview 10: Legal officer DG MARKT, European Commission

¹³² Interview 01: Principle markets specialist, European Defence Agency

¹³³ Interview 01: Principle markets specialist, European Defence Agency & Interview 10: Legal officer DG MARKT, European Commission

¹³⁴ Interview 10: Legal officer DG MARKT, European Commission

¹³⁵ Interview 01: Principle markets specialist, European Defence Agency

¹³⁶ *ibid*

on Intra-EU arms transfers the EDA markets specialist said “*no... the volume of cross-border trade in the defence sector remains very limited*”¹³⁷. This view was echoed by the respondent from DG Enterprise and Industry who argued that clearly the 2009/81/EC was a reaction to the inadequacies of the CoC.¹³⁸ Unfortunately, the EDA did not monitor the implementation of CoC principles in Member State behaviour so there is little insight to whether or not efforts were made to change procurement policy or not.¹³⁹

In terms of trying to explain the lack of progress the EDA respondent noted that sovereignty and security of supply issues still divide EU Member States and that there is a need to develop a mutual trust “*there has been centuries of national states producing their own arms, this doesn’t just change overnight with a law*”. Furthermore, there remain huge barriers in terms of language and local procuring specificities that make it both costly and risky for companies to compete in cross border tenders where the odds are stacked against them and outcome is either decisive win or a total loss, but little in between.¹⁴⁰ The Commission respondents by contrast believed that the CoC had little chance as a soft law instrument noting that non-binding and intergovernmental methods are not usually very effective in securing compliance. The respondent from DG MARKT answered quite bluntly that “*50 years of single market experience has shown that the community method with binding law is how we build markets*”.¹⁴¹ This interpretation likens the problem of creating a common market to the collective action problems posed by the prisoner’s dilemma.¹⁴² Or in other terms: there is a big free rider risk. Member States are aware that their defence production capacity is too large and costly to maintain¹⁴³, yet action will require them to specialise and cede market share of one type of defence material to another Member State. As defence procurement is not as regular as grocery shopping exchanges in goods and concessions of market share may have to be diffuse and to some degree asymmetrical. This is where the risk lies for the Member States; i.e. if Member State A agrees to buy exceptionally good tanks from Member State B at the cost of their own uncompetitive national tank producer going bust what guarantee will they have that state B will buy state A’s unquestionably superior jets in 7 years time? Without a hard law legal remedy and a court to appeal to, there is precisely very little guarantee.

4.2.2 Views from supply side practitioners

The response from the defence industry, comprising of contractors, national level industry associations and export support agencies, was largely similar to that of

¹³⁷ Interview 01: Principle markets specialist, European Defence Agency

¹³⁸ Interview 05: Policy officer DG ENTR, European Commission

¹³⁹ Interview 01: Principle markets specialist, European Defence Agency

¹⁴⁰ Interview 01: Principle markets specialist, European Defence Agency

¹⁴¹ Interview 10: Legal officer DG MARKT, European Commission

¹⁴² Library of Economics and Liberty *Prisoners Dilemma* (2012)

¹⁴³ Interview 05: Policy officer DG ENTR, European Commission

the policy makers. Muted references to the CoC making the process of defence procurement more ‘transparent’ and ‘open’ where again the more favourable points made. In particular, praise was given to the fact that the voluntary reporting system under which subscribing Member States notified all Article 346 contract notices worth over €1 million actually functioned exceptionally well and helped to build mutual trust.¹⁴⁴ Additionally, in terms of success, some of those interviewed noted that the access to the supply chains of prime contractors in other Member States had improved. One director of exports at a national industry association in a large Member State reported that our “*small and medium enterprises have actually been quite successful in selling high value sub-components and specialised pieces to European prime contractors*”¹⁴⁵ while another respondent noted that markets for “*sub-systems and prime contractor supply chain are more accessible...*”¹⁴⁶ than for finished systems.

Despite these few positive comments the prevailing opinion was again one of pessimism and respondents concluded that the CoC has had no impact on either the overall level of cross-border trade or in reducing the use of Article 346.

When asked about their success in exporting to other EU Member States and whether it had improved over the past five to six years there were no positive responses. The Vice President of European Affairs at one prime contractor glumly stated “*we cannot say we have seen positive results*”¹⁴⁷. Others noted that their strategic orientation for exports was now largely outside the EU as the chances of winning contracts in Europe’s protected markets were a waste of resources. Several cited the combination of mature, or saturated, markets as well as weak budgetary outlook for this re-orientation.¹⁴⁸ One respondent from an industry association noted that many of his members had somewhat given up on Europe, citing past bad experiences where despite supposedly open and welcoming tendering procedures the final contract award was seen as a ‘stitch-up’ and that and that most had now focused their efforts on extra-EU exports as they are “*so to speak, lower hanging fruit*”¹⁴⁹. Another respondent noted that his members look outside Europe for their future growth as the lingering over-capacity in Europe has led to a “*crowded market in which there are many wolves*”¹⁵⁰ fighting over flat demand.

Regarding the impact on the use of Article 346 respondents were unconvinced that the CoC could have had an effect in reducing its use.¹⁵¹ They cited the

¹⁴⁴ Interview 04: Exports director, defence industry association , medium sized Member State

¹⁴⁵ Interview 02: Exports & overseas director, defence industry association, large Member State

¹⁴⁶ Interview 04: Exports director, defence industry association , medium sized Member State

¹⁴⁷ Interview 11: Vice-President of European affairs, large prime contractor, medium sized Member State

¹⁴⁸ Interview 06: Director of international affairs, defence industry association, USA , Interview 02: Exports & overseas director, defence industry association, large Member State & Interview 04: Exports director, defence industry association , medium sized Member State

¹⁴⁹ Interview 02: Exports & overseas director, defence industry association, large Member State

¹⁵⁰ Interview 04: Exports director, defence industry association , medium sized Member State

¹⁵¹ Interview 02: Exports & overseas director, defence industry association, large Member State, Interview 04: Exports director, defence industry association, medium sized Member State & Interview 11: Vice-President of European affairs, large prime contractor, medium sized Member State

difficulty of challenging such a contentious issue in general and that it would be implausible to curb Member States' persistent and wide-ranging application of Article 346 using a soft law instrument. This view is unsurprising as the CoC essentially challenges the prevailing interpretation of the Article 346 which, whether right or wrong, is set squarely within the binding hard law of the EU treaties. The jury of the legal profession is largely out¹⁵² on what value soft law has in regulatory application. Some argue it provides a viable way forward when Member States wish to collaborate but there is no political will for EU level binding legislation¹⁵³ however, others have noted that it lacks the certainty and precision to form a reliable basis for taking legal action¹⁵⁴. Under this latter interpretation it is highly unlikely that a soft law instrument will change actor behaviour as actors in the market will still have no functioning legal remedy to challenge any perceived or actual 'infringements'.

Regarding the EBB, views were mixed. Some welcomed its conception inasmuch as it created a centralised "*shopping list for all EU Member States ministries of defence*"¹⁵⁵, while others confirmed that they definitely use it¹⁵⁶. However, this was not the full picture; one respondent's company was apparently unaware of the EBB's existence and operates exclusively within Article 346 exemptions despite their product having a largely commoditized status within the European arms market¹⁵⁷. Another was unashamedly dismissive and accused the EDA of 'beating its own drum' over the EBB while they on the industry side have seen no improvement in cross-border orders.¹⁵⁸ In the end of the day it matters whether the EBB facilitates cross-border contract awards and not whether it was simply advertised at the EU level but ultimately handed to a national supplier regardless. Considering the pessimistic views presented on cross-border trade and persisting Article 346 usage it would be largely implausible if not contradictory to consider the EBB a major success as part of the CoC's soft law regime.

4.2.3 Views from demand side practitioners

The most notable difference when speaking to the demand side practitioners was the manner in which they answered questions. Whereas the policy makers and supply side practitioners were willing to speak candidly and expressed their personal opinions about the CoC and any impact it may have had, demand side practitioners gave answers that sounded more like a department press releases or

¹⁵² Apologies for the horrendous pun.

¹⁵³ Chalmers et al., *European Union Law* 2nd Edition (Cambridge University Press: 2010) p.102-103

¹⁵⁴ Trubek, D. Et al., *Hard and Soft Law in European Integration* in J. Scott and G. De Burca (eds.), *New Governance and Constitutionalism* (Oxford, Hart, 2005)

¹⁵⁵ Interview 06: Director of international affairs, defence industry association, USA

¹⁵⁶ Interview 02: Exports & overseas director, defence industry association, large Member State, Interview 04: Exports director, defence industry association, medium sized Member State & Interview 07: Official, defence exports support agency, large Member State

¹⁵⁷ Interview 03: Public Affairs Director, medium sized supplier, medium sized Member State

¹⁵⁸ Interview 11: Vice-President of European affairs, large prime contractor, medium sized Member State

lines to take. For example, when asked if their ministry/government had changed its approach to defence procurement after the CoC was introduced the answers seemed generic and prescribed rather than specific and motivated i.e. “*our long standing policy is to buy goods, works and services under an open and fair procurement process, which maximises the use of competition in order to seek best value for money*”¹⁵⁹ or “[*our ministry*]... *applies the European Defence Agency (EDA) Code of Conduct on Defence Procurement (the Code) to all contracts for goods and services above the specified threshold of 1,000,000 Euros that meet the criteria for the Article 346 "warlike stores" exemption.*”¹⁶⁰ As the demand side actors in the market are ones who need to change their behaviour and are therewith the target of the CoC it is perhaps not surprising that answers did not provide a more nuanced interpretation of events. After all, which public servant wishes to be the one who outs his own government as a free rider? As soft law regimes largely depend on peer pressure to change behaviour¹⁶¹ it would be logical for actors to at least state their commitment to the agreed rules rather than providing a more complex answer that could show their party to the agreement in bad light.

In terms of assessing how successful the CoC has been statements again focussed on the idea that transparency had been increased¹⁶², that the EDA’s reporting regime for Article 346 exemptions functioned well and may yet prove useful in any attempt to monitor and police the market once directive 2009/81/EC comes into full force.¹⁶³ One respondent did claim that the code “*opened up procurement to cross border competition amongst EDA Member States*”¹⁶⁴ but suggested the EDA would be better informed on the statistical performance. Incidentally they are not, and as witnessed above, are decidedly less optimistic about the success of their CoC in increasing cross border trade.

Examples also arose of how defence procurement still is not conducted on a price competitive basis as would be expected in other forms of public procurement. It was stated that due to the technical nature of defence procurement it often requires non-competitive selection of suppliers.¹⁶⁵ For example, when supply is urgent or in scenarios where only original equipment manufacturers have the necessary expertise needed to upgrade or modify existing systems. Interestingly one respondent from a large Member State explained how their ministry defined ‘competitive procurement’. It was defined as “*securing the best mix of effectiveness, efficiency and economy in the use of resources and impact on society as a whole over the period of use and disposal of the goods, works or services acquired*”¹⁶⁶. If one want to read into these criteria more specifically the

¹⁵⁹ Interview 09: Procurement official, ministry of defence, large Member State

¹⁶⁰ Interview 09: Procurement official, ministry of defence, large Member State

¹⁶¹ Chalmers et al. (2010) *European Union Law* 2nd Edition (Cambridge University Press) p.102-103

¹⁶² Interview 09: Procurement official, ministry of defence, large Member State

¹⁶³ Interview 08: Head of defence industrial engagement policy, trade ministry, large Member State

¹⁶⁴ Interview 09: Procurement official, ministry of defence, large Member State

¹⁶⁵ Interview 09: Procurement official, ministry of defence, large Member State

¹⁶⁶ Interview 09: Procurement official, ministry of defence, large Member State

phrase “impact on society as a whole” could be seen as a legitimizing stamp for all sorts of uncompetitive procurement choice provided they maintain strategic manufacturing jobs or specific technical knowhow within national borders.

Finally, and perhaps most interestingly, the demand side interviews provide a certain insight in terms of what actions were not taken rather than ones which were. When speaking to the head of defence industrial participation from a large Member State they noted that their approximately 20 year old defence industrial participation policy* was in the process of being updated to bring it in line with directive 2009/81/EC.¹⁶⁷ This implies that no reform measures were undertaken in 2005-2006 to bring the policy in line with the CoC. Furthermore, the defence procurement specialist, incidentally from the same Member State, stated that they have not changed the above quoted procurement criteria in recent years either.¹⁶⁸ Thus it seems that either a) the Member State in question felt its procurement and industrial participation programmes were in line with the promises of the CoC or b) they didn't care to change them or their behaviour. Purely speculating, the fact that changes are being made for the hard law directive and no changes were made for the CoC implies that the latter did not instil the same sense of commitment among the target actor. However, as said, purely speculative.

4.3 Soft law and soft results

The results of the quantitative study seemed to largely support the hypothesis that the EDA's CoC and corresponding EBB had led to a rise in the cross-border trade of conventional weapons among EU Member States. It was expected that Member States would open up their procurement budgets to foreign competition and select suppliers on a cost competitive basis. However, the results of the qualitative study are less conclusive. Although some indications of minor success for SME's were presented, overall there was little commitment to the idea that the CoC had led to any observable rise in cross-border trade or reduced the use of Article 346.

The most problematic obstacle faced by the CoC is unsurprisingly its own soft law form. Many respondents noted that in the field of defence procurement it is exceedingly problematic to use legal remedies to challenge the outcome of a tender due to the structure of this quasi-market.¹⁶⁹ As the customer base is incredibly narrow, i.e. limited to national governments, there is a strong incentive for suppliers not to challenge unjust outcomes. Rather, through obsequious

* Countries use defence industrial participation policy to negotiate offsets deals when procuring defence equipment. These offsets are market distorting and unequivocally violate single market rules and would thus only be available as an option on procurements.

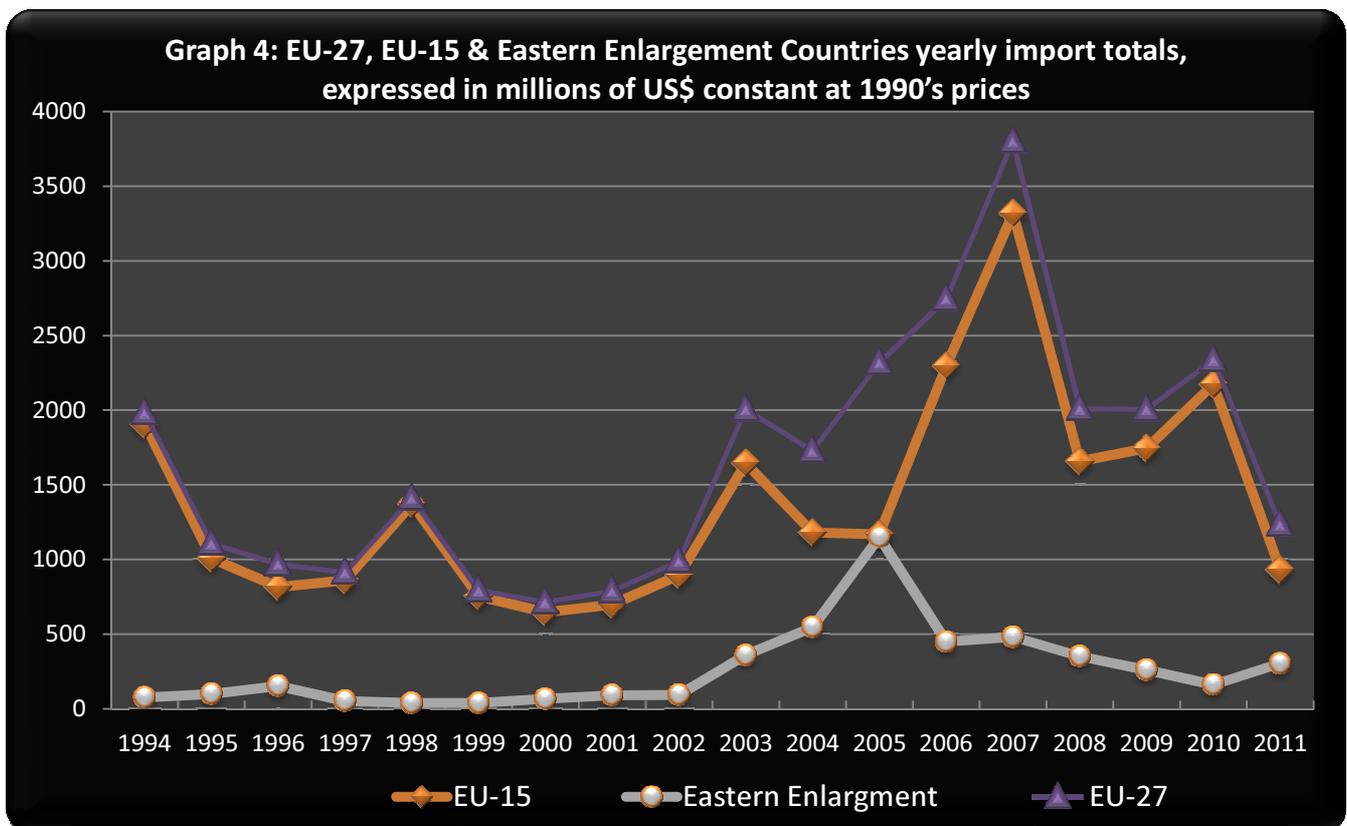
¹⁶⁷ Interview 08: Head of defence industrial engagement policy, trade ministry, large Member State

¹⁶⁸ Interview 08: Head of defence industrial engagement policy, trade ministry, large Member State

¹⁶⁹ Interview 06: Director of international affairs, defence industry association, USA, Interview 02: Exports & overseas director, defence industry association, large Member State & Interview 10: Legal Officer DG MARKT, European Commission.

behaviour suppliers wish to curry favour with the said government in the hope of winning the next contract when it arises. This in part has led to there being rather little case law on defence procurement in general and no single case challenging an Article 346 application.¹⁷⁰ Critically there has been no ‘landmark case’ to challenge the current status quo of how Member States have chosen to interpret Article 346.¹⁷¹ Some also appeared sceptical on the idea that the binding hard law of Directive 2009/81/EC would be able to change this problematic supplier customer relationship. Yet the respondent from prime contractor held an alternate view suggesting that with pressure on procurement budgets and orders the big players would soon no longer be able to sit idle in hope of winning the next contract and would, pending the full transposition of 2009/81/EC, start resorting to legal remedies where they feel unfairly treated. The respondent also noted that his company alone has had several cases in past years where they felt that with a stronger legal framework they most certainly could have overturned a procurement decision.¹⁷² This very much supports the idea that the CoC had little effect as ultimately firms had no faith in it as a legal remedy.

A second doubt arises over the timing of the proposed impact witnessed in the statistical study. If we look to **graph 4** the import statistics are presented on a year by year basis rather than in the three periods as in previous graphs. This allows for some interesting observations. For example, imports to the EU-15 skyrocket 2006 and 2007 namely the same year and following year of the CoC coming into force.



¹⁷⁰ Interview 10: Legal officer DG MARKT, European Commission

¹⁷¹ Interview 08: Head of defence industrial engagement policy, trade ministry, large Member State

¹⁷² Interview 11: Vice-President of European affairs, large prime contractor, medium sized Member State

Such an immediate effect is cause for suspicion as the SIPRI data indicates the date of delivery not the date of order, suggesting that perhaps other earlier factors played a bigger role than the CoC. For reference, when speaking to policy makers they expected the impact of 2009/81/EC to be relatively modest and slow as it will take time for case law to emerge and have therefore scheduled the first review of it for 2016.¹⁷³ These modest expectations were espoused by supply side respondents as well.¹⁷⁴ Furthermore, defence procurement is often a protracted and cautious process again suggesting that such an immediate impact of the CoC in 2006-2007 is very unlikely.

Interestingly the import statistics for the Eastern Enlargement countries show a steady rise leading up to a 2004-2005 peak around the time of their accession where after they plateau into a slow decline. This supports the idea that in expectation of pending membership the new Member States started to procure more intentionally from the EU. Perhaps even more interestingly after falling from P1-2 imports to the new Member States from outside the EU (most notably from the USA) actually rise by a very substantial 105% between P2 and P3. Considering how imports from fellow EU Member States taper off in P3 this implies that the new Member States, once having secured membership of the EU swiftly re-orientated their procurement preferences across the Atlantic. This could very well be a reality as the US has had a strong influence on the new Member States who had also recently joined NATO. In fact when speaking to one Western European respondent about offsets they noted, somewhat in disapproval, that the new Member States had been extremely effective in negotiating hefty civilian FDI packages when making offset deals.¹⁷⁵

So what is the most plausible answer as to whether the CoC has led to the marketization of the European defence equipment market by way of more competitive procurement and increasing cross-border trade? It seems that ‘modest impact’ might be the best prognosis for now. Although the respondents were less than enthusiastic about the CoC’s impact, they had little hard data to contradict what is observed in the statistical part of this study. Thus, it seems that slow progress towards open procurement and increasing cross-border trade is happening, but not exclusively due to the CoC. Rather it is a contributory factor. In the next section other possible explanations will be explored with the aim of further clarifying the results of the statistical study.

¹⁷³ Interview 10: Legal officer DG MARKT, European Commission & Interview 01: Principle markets specialist, European Defence Agency

¹⁷⁴ Interview 11: Vice-President of European affairs, large prime contractor, medium sized Member State & Interview 04: Exports director, defence industry association, medium sized Member State

¹⁷⁵ Interview 08: Head of defence industrial engagement policy, trade ministry, large Member State

5 In search of causation

If we propose that CoC had a small impact on the marketization efforts in the EDEM, then what other factors were there? This chapter will attempt to find a more plausible explanation for what is behind the trends observed in the statistical study.

5.1 The unlikely and dismissible

In this first section the aim is to dismiss some of the other factors that may be considered to have had an impact on the statistical trends observed.

5.1.1 The European Commission's 2006 Communicative Interpretation

In 2006 the European Commission published an 'interpretative communication' in which it sought to clarify, from its perspective at least, the continued misinterpretation of Article 346.¹⁷⁶ According to the Commission, the wide and almost default application of the exemption by Member States is at odds with the original intentions of the exemption and that many states may be violating Single Market rules. However, its explanatory power when considering the rise in intra-EU trading observed is subject to exactly the same two pitfalls of the CoC; namely, it is also a soft law instrument¹⁷⁷ and its questionable timing in relation to the trends observed.

As a soft law instrument it would, much like the CoC, not be able to form a precise enough legal framework in which companies would feel confident enough to challenge unfair procurement decisions. Coupling this with the statements made during the interview about the lack of case law on Article 346 application¹⁷⁸ and it is unlikely that the communication managed to change behaviour.

¹⁷⁶ European Commission, *Interpretative Communication on the application of Article 296 of the Treaty in the field of defence procurement* (7th December 2006)

¹⁷⁷ Chalmers et al., *European Union Law* 2nd Edition (Cambridge University Press: 2010) p.102

¹⁷⁸ Interview 10: Legal officer DG MARKT, European Commission & Interview 02: Exports & overseas director, defence industry association, large Member State

In terms of timing, the interpretative communication is even less likely than the CoC to be a contributory factor as it was only released in December 2006. Remember that the peak trading years witnessed in **graph 4** were 2006-2007 and that such an immediate impact in a field where the procurement process is protracted is not likely. Again the evidence does not suggest the interpretative communication played any significant role in explaining the trends observed.

5.1.2 The financial crisis and budgetary pressure

Another notion to be entertained, and suggested by some peers, is the idea that the financial crisis and consequent recession may have pushed Member States to procure in a much more rational and cost effective manner, as opposed to continuing support for dilapidated and underperforming national suppliers. While this might be the advice given by many a rational economist it is rarely the response taken by politicians when confronted with rising unemployment and an upcoming election. In fact in general and across the economy as a whole the typical knee jerk response in such times of crisis is towards protectionism.¹⁷⁹ In fact the incentives to pursue protectionist policies in the field of defence procurement are especially strong. As EU Member States cannot subvert the rules of the Single Market among each other, defence procurement and the Article 346 exemption is possibly one of the few fields where they can get away with protectionist policies. Furthermore, on the EU level defence spending on equipment procurement has actually remained remarkably consistent with pre crisis levels.¹⁸⁰ As Member States can channel such defence spending within their own borders it is often seen a credible way to provide a high skilled sector of the economy with a counter cyclical stimulus in true Keynesian fashion. Thus, ultimately one would expect, if anything, that the financial crisis and recession would push states more towards defence protectionism than the opposite.

5.1.3 Collaboration under OCCAR

As the only remaining relevant institution in the post 2000 period for facilitating collaborative European defence procurement programmes (aside from the EDA) the *Organisation conjointe de coopération en matière d'armement* or OCCAR may too have played a role in the rise of cross-border trade, even if not through competitive procurement. Yet an examination of its major programmes post-2000 reveals it is unlikely to be responsible for our P3 rise in cross-border trade either. For example, despite originally having the UK on board the Boxer armoured

¹⁷⁹ Time Magazine, *Protectionism on the Rise in Europe?* (February 4th 2009) & European Commission, *EU sounds alarm over sharp rise in protectionism across G20*, Press Release (Brussels June 6th 2012)

¹⁸⁰ European Defence Agency, *Defence Data 2010* (Brussels: 2011)

personnel carrier programme was soon reduced to a bilateral programme involving the Netherlands and Germany. Surprise, surprise full production is taking place in both countries.¹⁸¹ Furthermore, aside from some demonstrators, deliveries for deployment purposes only started in early 2012 putting it outside the timeframe of the data in our statistical study. The A400m airlifter can be excluded for the same reasons due to the fact that aside from demonstrator and test units, no deliveries have been made as of October 2012¹⁸². Regarding the FREMM naval vessel programme, again production is divided and completed nationally in the two participating Member States.¹⁸³ Finally, in the case of the Tiger Helicopter production is again divided and duplicated across the three participating countries¹⁸⁴ and deliveries have been across Period 2 and 3¹⁸⁵ meaning it too would not serve to explain the rise observed after 2006. Thus ultimately OCCAR may contribute somewhat to the cross-border trade in conventional weapons among its participating states but its projects certainly do not explain the trends seen in our statistical study.

5.1.4 Increased demand from the Iraqi and Afghan wars

Eight Member States took part in the Iraq war and fully 23, to varying degrees, deployed troops with the International Security Assistance Force (ISAF) in Afghanistan. Did the extra demand for equipment caused by these military engagements lead to a rise in cross-border procurement? But what would drive Member States to change their priorities on where they source such extra procurements? Or in other words why would it lead to an increasing tendency to shop cross-border. Here the explanation might be that a suitable national supplier for unpredictable custom equipment or urgently required items needed for deployment cannot be found. Hence Member States must rely on suppliers from other Member States. This theory might well explain some of the increases observed and a good way to analyse it for example in the Iraq case would be to isolate the eight participating nations and compare their imports growth to that observed in the remaining group. However, this would also require some scaling of the degree to which each Member States was engaged in the war; e.g. the UK troop and equipment contribution to Iraq was several times the size of the remaining seven participants from the EU. This task is unfortunately outside the scope of this paper. Yet what can be done is to look at the overall import statistics (EU originating & extra EU originating) of the EU-27 and try to determine if imports have risen overall. The results of this inquiry can be seen below in **graph 5**.

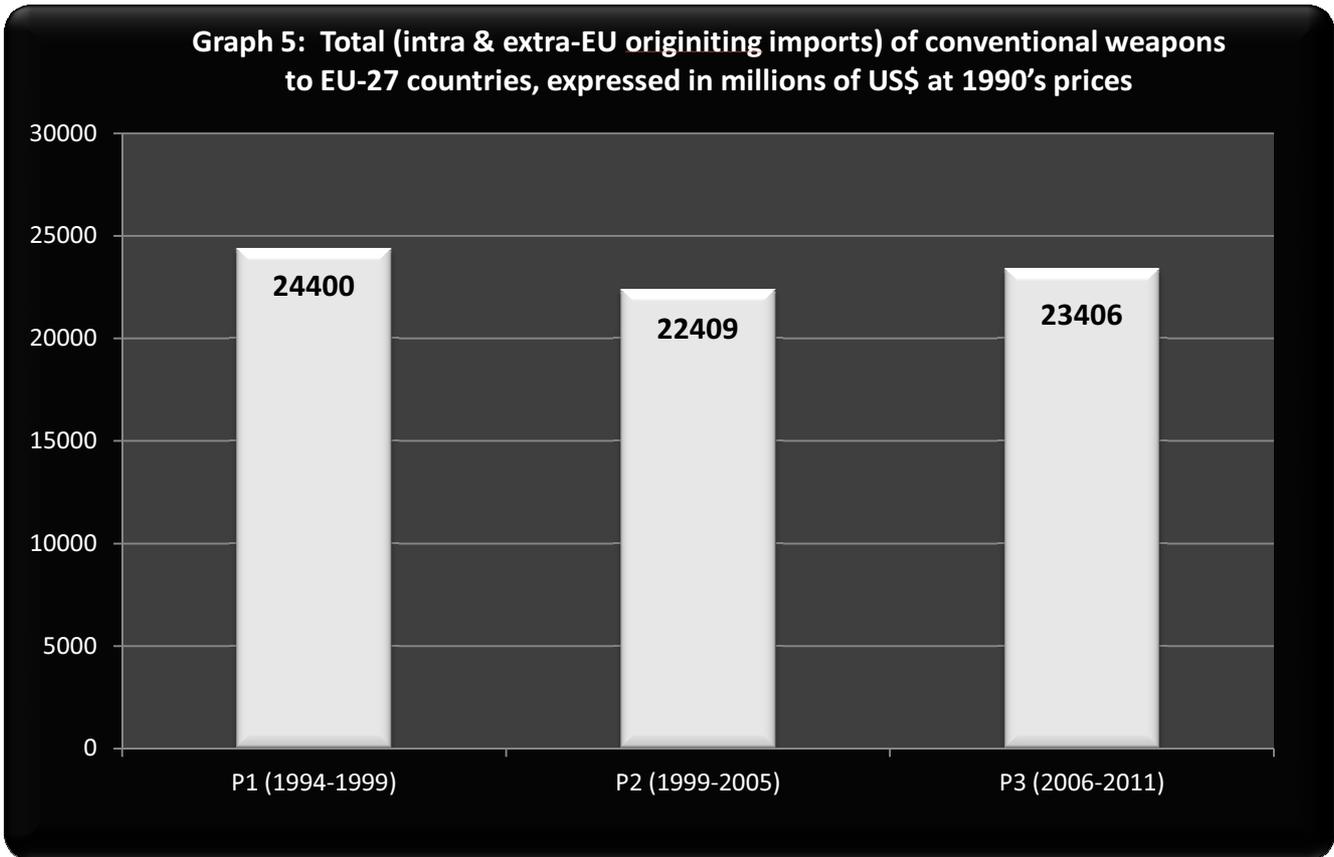
¹⁸¹ Defence Industry Daily, *The Fighter Still Remains...The Boxer MRAV APC Family* (May 11th 2012)

¹⁸² Airbus Military, *The versatile airlifter for the 21st Century* (2012)

¹⁸³ OCCAR, *FREMM – Fregate Europee Multi-Missione* (2012)

¹⁸⁴ OCCAR, *Tiger – A New Generation of Helicopters* (2012)

¹⁸⁵ OCCAR, *The Tiger variants* (2012)

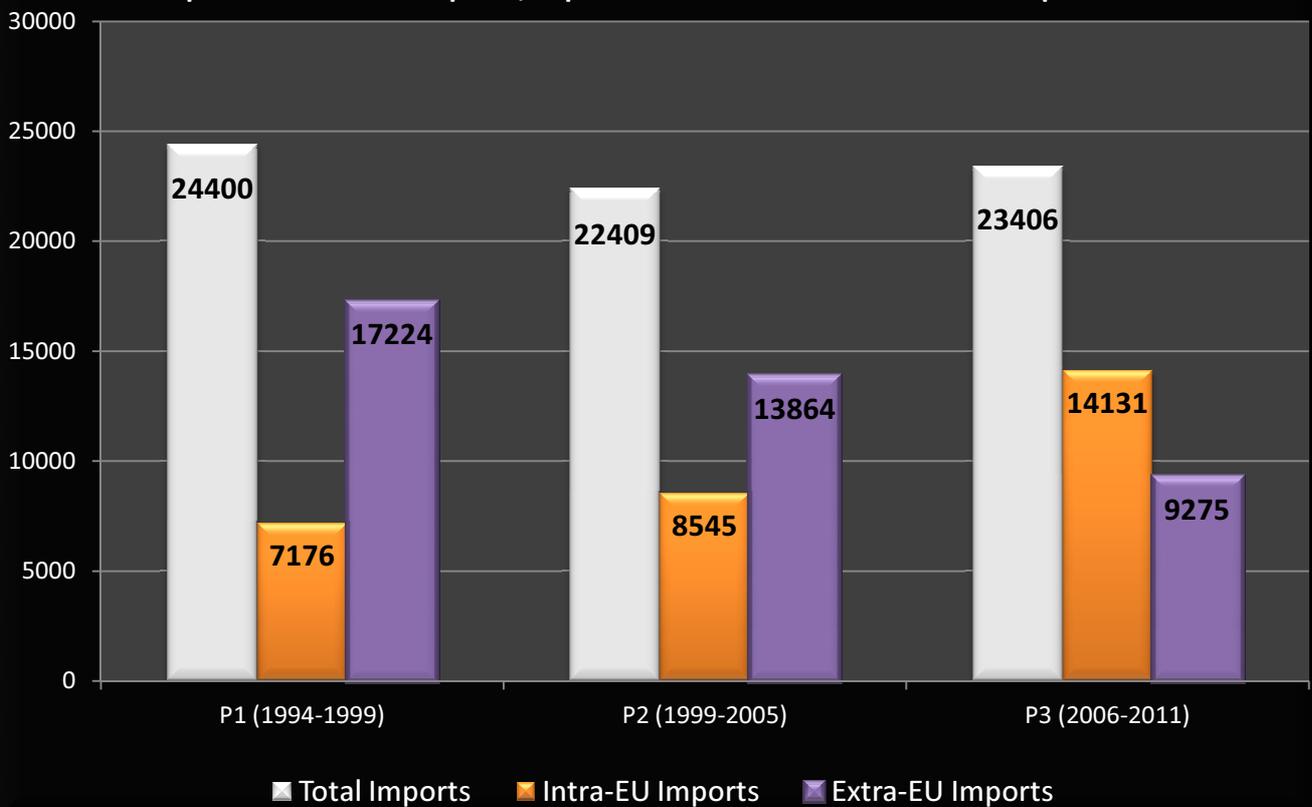


As observable, when total imports are considered across the three periods the trends are remarkably different from the ones seen when only trade among EU Member States are considered. Imports in total are actually more or less flat across the three periods showing only minor fluctuations. This indicates that Member States did not spend more of their budget abroad overall. This somewhat discounts the theory that the extraordinary demands of operations is what fuelled the growth in cross-border trade. What is extremely interesting and what will be considered in the next section is that if intra-EU trading has increased so significantly after 2006 but overall imports have remained more or less constant, what has happened to imports of conventional weapons from outside the EU?

5.2 Fortress Europa

When transforming the data for the statistical study of this paper it produced some very interesting figures that can now be utilised to investigate the relationship between intra and extra-EU originating imports to the EU-27. Essentially import values for each Member State were sorted by origin, thus when the EU originating imports were isolated it left the rest or extra-EU originating ones left over. This enabled, with little extra effort, the revisiting of the statistical data in order to explore the trend relationship between EU-originating and non- EU originating as seen in **graph 6**.

Graph 6: Total EU imports of conventional weapons compared to Intra-EU imports & Extra-EU imports, expressed in millions of US\$ at 1990's prices



Looking first to the level of total imports: the values for the 3 different periods are actually very stable fluctuating about a mean of 23405 million US\$ across the three periods of the study by just a little more than 4% up and down. As EU procurement spending has remained resilient despite budgetary pressure¹⁸⁶ (cost savings have been made through personnel downsizing rather than cuts to equipment investment) it is proposed that the proportion of defence procurement budgets that go overseas have remained largely static too. Turning to the figures on extra-EU imports and we can see a very defined and constant decline in correlation to the rises seen in intra-EU imports. Across the three periods intra-EU imports rise by 6995 million US\$ whereas imports from outside the EU fall by 7949 million US\$. These are very significant long term trends and seem to indicate, when viewed in conjunction with the largely steady overall imports and defence procurement spending trends, that rather than opening more of their budgets to overseas suppliers on a competitive basis EU Member States are rather reallocating foreign spending to keep it amongst themselves.

¹⁸⁶ European Defence Agency, *Defence Data 2010* (Brussels: 2011) p.8

These findings do not necessarily challenge the notion that a form of marketization is taking place in the EDEM; however, they pose some serious questions about the form that very market is taking. It seems that the market being built is a closed one and that EU membership is becoming a prerequisite for participation in it. This scenario, in which the European arms market becomes an ever more impenetrable fortress, was proposed in the Centre for European Reform paper as early as 1999¹⁸⁷ and the logic driving Europe's apparent outwardly protectionist strategy is not difficult to motivate.

Europe's defence trade relationship with the US has long been an asymmetric one and has been described as a "one way street"¹⁸⁸. The US has had huge success in exporting major weapons systems to Europe yet when the opposite is attempted there is more than often a closed door.¹⁸⁹ This set-up was tolerated during the Cold War and seen as a trade off for the US's European military presence. In addition, by virtue of having the world's largest single defence market coupled with significantly higher levels of research and development spending, US defence products were consistently more cost competitive and technologically advanced than their European counterparts.¹⁹⁰ However, this supremacy is not longer absolute across the board and in many areas the European DTIB is on par and even exceeds its global competitors¹⁹¹. Yet closing the technological and cost competitiveness gap has not helped Europe win contracts from the US Department of Defence further confirming Washington's determination not to let major defence procurements go abroad.¹⁹² The protectionism in US defence procurement is unsurprising when looking at the regulatory landscape underpinning it. US firms are supported by an explicit "Buy American Act"¹⁹³ of which there is no European equivalent.¹⁹⁴ This act necessitates that US suppliers be given priority, has a fund to support them when they are uncompetitive and even goes as far as to promote only the use of US made machine tools for the production of said procurements.¹⁹⁵

In addition to this already stressed relationship the US has been perceived to use its *International Traffic in Arms Regulations* (ITAR) to hamper and even sabotage potential competition from European suppliers of systems which integrate US made ITAR listed sub-components. Essentially the US can veto the export of any EU made system with an ITAR component. The fear of this

¹⁸⁷ Ashbourne, Alex, *Opening up the US Defence Market*, Center for European Reform (1999)

¹⁸⁸ Schmitt, Burkard. *European and Transatlantic Defence Industrial Strategies: A European Perspective*, Analysis no. 0, EUISS (January 2002)

¹⁸⁹ Ditchley Foundation, The. *The defence industrial base: European rationalisation and transatlantic cooperation* (September 2000)

¹⁹⁰ Ashbourne, Alex, *Opening up the US Defence Market*, Center for European Reform (1999) p.6

¹⁹¹ Hofbauer, J., *European Defence Trends: Budgets, Regulatory Frameworks and the Industrial Base*, CSIS Defence Initiatives Report (November 2010)

¹⁹² BBC. *EADS hit as tanker deal reopened* (July 10th 2008)

¹⁹³ Jones, Seth G., *The Rise of European Security Cooperation* (Cambridge University Press:2007) p.175

¹⁹⁴ Guay, Terrence, *The Transatlantic Defence Industrial Base: Restructuring Scenarios and their Implications*, Strategic Studies Institute (April 2005), p.15

¹⁹⁵ Guay, Terrence, *The Transatlantic Defence Industrial Base: Restructuring Scenarios and their Implications*, Strategic Studies Institute (April 2005)p.11

scenario drove several Member States to abandon plans to arm the Eurofighter with an American air-to-air missile despite written reassurances from the Clinton administration not to block exports.¹⁹⁶ One of the respondents noted that the US has even been known to use this strategy to block or delay intra-EU procurements in which the direct competitor is a US alternative.¹⁹⁷ This has prompted EU Member States to collaborate and develop “ITAR FREE” systems to avoid such complications.¹⁹⁸ It seems that both the huge defence trade deficit and the risk of using US made ITAR listed components have pushed Europe towards creating a much more closed defence equipment market. Yet, if as claimed by some¹⁹⁹, the EU has no ‘buy European clause’ then how is such a strategic shift occurring? Some clues were provided during the interviews and a closer look at the CoC indicates it may have some rather protectionist wording in it which supports our observed trends.

When speaking to the director of international affairs from a defence industry association in the US a few significant points were made. Firstly, the progressive closing off of the European defence equipment market to external suppliers was an experience most definitely experienced by members of the association. Secondly, in terms of what was driving this strategic shift the European Commission and the EDA were named as the driving forces behind this long term trend and more recently the determination to create a pan-European defence procurement community with an integrated European DTIB.²⁰⁰ It was also noted that although ITAR items do pose problems for European producers, until the recent coming into force of the Defence Transfers Directive 2009/43/EC it has actually not necessarily been any easier to transfer defence equipment between Member States than with extra-EU states.²⁰¹ This indicates that binding hard law of the EU has not until present played a role causing this observed shift towards fortress Europa. However, once the new licensing system of the directive comes into force this will make intra-EU arms transfers considerable easier than extra-EU ones suggesting our observed trends will continue along their present trajectory.

Finally, is it possible to link the EDA CoC to these trends after all? Perhaps it has not created the open and competitive market desired by some, yet it may have had an impact on the creation of Fortress Europa. At first glance the CoC is about promoting open and transparent competition in defence procurement. Concerning selection criteria during procurement the CoC prescribes that “*All companies will be evaluated on the basis of transparent and objective standards, such as*

¹⁹⁶ Ashbourne, Alex, *Opening up the US Defence Market*, Center for European Reform (1999)p.12

¹⁹⁷ Interview 02: Exports & overseas director, defence industry association, large Member State

¹⁹⁸ *ibid*

¹⁹⁹ Volkman, Alfred G. , *European Defence Industry Perspectives: The American Viewpoint*, The DISAM Journal (Spring 1998) p.88 & Guay, Terrence, *The Transatlantic Defence Industrial Base: Restructuring Scenarios and their Implications*, Strategic Studies Institute (April 2005), p.15

²⁰⁰ Interview 06: Director of international affairs, defence industry association, USA

²⁰¹ Interview 05: Policy officer DG ENTR, European Commission

possession of security clearance, required know-how and previous experience”. However, it also stipulates that the CoC is

*“...aimed at encouraging application of competition in this segment of Defence procurement, **on a reciprocal basis between those subscribing to the regime.**”*

that

*“The regime will operate on the basis of sovereign Member States voluntarily choosing to align their policies and practices, **on a reciprocal basis, in this area.**”*

and that

*“We wish to maximise opportunities for **all suppliers based on each others’ territories to compete in our competitions.**”*

In light of the above extracts from the CoC it seems that Europe has at least the elements of a soft law ‘buy European clause’. This may well have contributed to the trends observed, however, whether to classify it as a step towards the ‘marketization’ of defence procurement in Europe is more difficult. This shift has not led to a higher proportion of Member State procurement budgets being spent abroad; instead it has come at the expense of extra-EU suppliers being progressively excluded from contracts in the EU.

6 Conclusions

Answering the research problem with a high degree of certainty was always going to be a challenge. The dynamics at play that may have impacted the level of intra-EU trade in conventional weapons are wide and determining equifinality of causation is therefore a less than straightforward exercise. Nonetheless, both parts of this study make unique empirical contributions to knowledge in their own right. In terms of answering the research problem it concluded that the EDA's CoC has had at best a very limited impact on the process marketizing defence procurement in the European Union.

6.1.1 Contribution to knowledge

The statistical part of this study has played a largely confirmatory role. Whereas other literature in the field has referred to increasing European collaboration on arms projects or suggested that the US is selling less conventional weapons to Europe in the post Cold-War period, this paper confirms these trends from 1994-2011. It has confirmed that the European Union Member States are progressively trading more conventional weapons amongst each other. Furthermore, it shows that the level of growth in intra-EU trading has been accelerating over time suggesting the formation of a European defence procurement community. However, the study also confirmed that the overall level imports, or in other words the proportion of EU defence procurement budgets spend abroad, have remained static across the whole period of the study. The logical consequence of these first observations is that extra-EU sales of conventional weapons to Europe have been in a steady decline since the end of the Cold War and continue to fall in the final period covered in this study.

The qualitative part of the study has also presented new knowledge collected from specialists across the spectrum of the defence procurement establishment. Evidence showed that practitioners from the field largely framed the success of the CoC in other terms than successful market creation per se. Rather than citing cross-border trade or competitive procurement, success was framed much more modestly in term of increasing transparency and openness. It also confirmed that, as predicted in the legal literature, soft law measures will not have much success in creating or regulating markets. Responses displayed that the CoC fell short of providing any form of 'legal remedy', seen as necessary in market creation. As firms have no legal certainty governments face a very slim chance of being challenged over acting in a protectionist manner. On top of this, respondents also indicated that even with legal certainty the structure of the market with its narrow customer base acts as a disincentive for firms to antagonise relations with Member

States. Thus all in all the prospect of free-ridership remains high and is more than likely rife across the sector, reinforcing the continued hesitance to allow genuinely competitive procurement.

6.1.2 Modest measures, modest impact

In light of the empirical findings can the EDA's CoC be convincingly linked to the marketization of defence procurement in Europe? In one word: no. Despite the statistical study providing a 'false-positive' of sorts the overall findings suggest that the CoC had little impact on marketization.

Initially the trends observed in the statistical study showed that there had been a marked and noticeable increase in the level of intra-EU trading in conventional weapons. This at first suggested that the CoC had had quite a significant impact on cross-border trade and had therewith promoted more open, fair and competitive procurement. However, once contextualised against the backdrop of the overall levels of imports (including extra-EU originating ones) and considering the rather cohesive views gathered during the expert interviews, it is clear that movement towards marketization has progressed at turtles pace and the likelihood of the CoC having had an impact is very slim indeed.

What appears to be happening is the creation of a European defence procurement community in which European Union Member States have become progressively more protectionist towards defence imports from outside the union. The result has been the redistribution of foreign defence procurement spending from outside the Union to inside the Union. At face value these trends do not necessarily exclude the notion that a form marketization is occurring. Indeed, disgruntled with the one-way nature of the transatlantic defence trade it is not inconceivable that the EU Member States are seeking to form an exclusive market for defence equipment amongst themselves. This strategy could very plausibly be employed to mitigate the threats posed by the preponderate U.S. defence sector and give European firms a larger 'home market' from which to compete on a global scale. However, even if this strategy is play, it is unlikely that a real cost competitive market is being behind the rise observed in Intra-EU transfers.

Several findings undermine the idea that competitive procurement has led to the rise in intra-EU trading. Firstly, the prominent and immediate impact seen 2006 and 2007 were shown to be too early to be attributed to the CoC. Secondly, the expert interviews showed that the CoC did not provide the legal remedies necessary for market creation. Thirdly, the supply side practitioners and policy makers seemed sceptical that governments had changed their procurement behaviour a fact seemingly confirmed by demand side respondents who noted that procurement policies were only now being updated in accordance with 2009/EC/81.

So what can explain the rises seen in intra-EU trading? One thing which must be noted is that the cross-border market for arms in the EU was overall very small. Thus, even seemingly large percentage gains need not represent a revolutionary change in procurement behaviour. Rather it is proposed that the rises seen can be

attributed to increased opening-up in the supply chain across the European defence industry as indicated by the respondents. Although this can be seen as a form of marketization and merited as a step towards rationalisation, firms were not the intended target of the CoC on Defence Procurement, governments were. It was intended to open up procurement at the end-user stage and this it did not convincingly do.

Thus it is most plausible that the CoC on Defence Procurement had little or no impact on the marketization of defence procurement among the Member States of the EU. Its impact is limited to the creation of a reporting system for the use of Article 346 and success can be measured in terms of greater transparency and openness in the use of the exemption. Yet ultimately it did not lead to a reduction in the use of the exemption and therewith also failed to introduce fair and cost based competitive procurement.

6.1.3 Future prospects & further research

The transposition deadlines for both the Defence Procurement Directive 2009/81/EC and the Defence Transfers Directive 2009/43/EC passed in 2012. Pending a few stragglers against who the Commission has started infringement proceedings the new hard law regime should soon be in full force.²⁰² Expectations are mixed and its success will, as experience has shown, continue to hang on how Member States and the Court of Justice choose to interpret Article 346.²⁰³ One respondent whose company lobbied hard for 2009/81/EC noted that it became known colloquially as the “Swiss-cheese” directive as it was riddled with so many loopholes and exemptions.²⁰⁴ Although some of the initial loopholes have been closed, several respondents remained unconvinced that the directive would change the status quo significantly.²⁰⁵ However, there are a few positive elements which should help open procurement. The procurement directive defines more concretely what constitutes an abuse of Article 346 and importantly, specifies that whole programmes can no longer be exempted. Rather each individual part of a programme must be merited an exemption in its own right.²⁰⁶ As for the defence transfers directive, it will for the first time standardise the intra-EU transfer of arms making it significantly less bureaucratic and costly for European firms to collaborate and for Member States to procure cross-border.²⁰⁷ The expected impact here will be the continuation of the trend to towards an ‘exclusive’

²⁰² Interview 01: Principle markets specialist, European Defence Agency & Interview 05: Policy officer DG ENTR, European Commission

²⁰³ Interview 08: Head of defence industrial engagement policy, trade ministry, large Member State

²⁰⁴ Interview 11: Vice-President of European affairs, large prime contractor, medium sized Member State

²⁰⁵ Interview 04: Exports director, defence industry association, medium sized Member State & Interview 01: Principle markets specialist, European Defence Agency

²⁰⁶ Interview 08: Head of defence industrial engagement policy, trade ministry, large Member State

²⁰⁷ Interview 05: Policy officer DG ENTR, European Commission

European defence procurement community. Interestingly the single respondent from the U.S. noted that transfer's directive has finally kicked Washington into action over reforming the ITAR system.²⁰⁸ This was seen as necessary to ensure collaboration with and procurement from the U.S. does not become, relatively, even more unattractive for Member States due to the pending easing of intra-EU transfers.

Several avenues could be pursued to further the knowledge in this field. Most notably this study took a rather simplistic view, treating defence procurement in Europe as a cohesive whole. It would be interesting to embark on a more detailed country by country analysis in order to determine if some Member States are opening defence procurement more while others appear to free-ride. Another exercise might be to try and verify the accuracy of the SIPRI data utilized in this study. Indeed its values cannot be compared directly with Member States exact transfer values. However, one could take official statistics from a handful of states where they are available and compare the percentage change in imports from other EU members across the same periods in this study. If the SIPRI figures are somewhat representative of reality the percentage change in transfers across the periods should be fairly similar. Finally, under the new hard law regime it is hoped that uniform official statistics on the defence sector at the EU level become more readily available making future studies in the field both more reliable and a great deal more straightforward.

²⁰⁸ Interview 06: Director of international affairs, defence industry association, USA

7 Executive Summary

Research problem and aim

Defence and security materials have been exempted from the European Union's Single Market leaving Europe with a highly fragmented defence technological and industrial base. Dating back to the Treaty of Rome the present day Article 346 TEU ensures Member States can bypass Single Market rules on defence and security materials which are considered to be 'essential' to their security interests. Rather than functioning as a targeted, specific and seldom used exemption for high tech items such as nuclear or cryptographic technologies, Member States have interpreted and applied Article 346 more or less to all defence procurement be it essential to security or not.

While this approach was somewhat sustainable under Cold War defence expenditure patterns it has become increasingly untenable as the 1990's ushered in the so called 'peace dividend' that saw European defence budgets slashed by more than half. Tighter budgets and smaller production runs have made it an increasing challenge for Member States to sustain individual national weapons programmes. This is compounded by the fact that the cost of high-end weapons systems is rising at a pace significantly faster than inflation. Several Member States have tried to export their way out of this conundrum. The idea here has been to achieve longer production runs and hence gain economies of scale, thereby lowering the per-unit cost for the Member State who developed it. While this strategy has not been wholly unsuccessful it must contend with one crucial and problematic fact. In the mid 1990's the United States drastically rationalised their defence sector to form a handful of global defence behemoths. With internal demand in excess of the entire compiled EU demand, many US programmes have already achieved long production runs and lower unit costs well before their products arrive on the international market making them very price competitive.

Another approach to counteract the issue of limited and fragmented demand in Europe has been to embark on collaborative procurement programmes. While these programmes have produced some convincing products in terms of ability and technological advancement, they have failed to bring the desired economic benefits of pooled resources. Such collaboration has been conducted on the principle of *juste retour* under which each participating Member State receives a share of R&D and production contracts in terms of both value and man hours relative to their share of investment. This leads to sub-optimal selection of suppliers and experience has shown that in most cases the entire final production lines are multiplied across the participating Member States, significant reducing the desired economic gains. Additionally this set up has arguably done more to

sustain ailing national suppliers than allow the wholesale reduction in capacity needed by way of increased mergers & acquisitions.

After several decades of this collaborative arms procurement conducted on *juste retour* principles the Member States of the European Union are finally moving towards market based solutions in their attempts to maintain a competitive and sustainable defence technological and industrial base on the continent. In the early 2000's while still unprepared to allow the Commission to lead a supranationalisation of the defence sector Member States opted for an intergovernmental solution under the aegis of the European Defence Agency. This paper seeks to conduct a baseline study on the impact of the European Defence Agency's 2005/6 Code of Conduct on Defence Procurement (CoC), the first explicitly market based measures taken to confront the challenges facing the defence industry across the continent. The research question to be answered is:

Has the EDA's CoC been successful in promoting the marketization of defence procurement in the European Union?

Methodology

The research design employs mixed methods in the following manner: A) a preliminary statistical study into the volume of intra-European trade in conventional weapons from 1994-2011 (cross-border trade is treated as a proxy for the occurrence marketization), and B) a series of semi-structured interviews with policy makers, as well as policy practitioners from both the supply and demand side of the defence procurement equation.

The objective of the preliminary statistical study is to establish what trends the trade in conventional weapons in Europe have been taking. The eighteen year period is broken down into three six year periods. Thus the six years since the Code of Conduct came into force will be compared with the six years previous to highlight any changes in trading levels. The earliest six year period will act as a control to determine if changes witnessed pre and post CoC can be separated from the general trajectory of trends across the entire timescale of the study. As the CoC is not the only action taken to address the issue of persistent Article 346 use the objective of the expert interviews was to attribute causation to any changes seen in the trade trends from the statistical study.

Empirical data

For the statistical study a self compiled dataset was generated using the Trade Indicator Value (TIV) tables sourced from the Stockholm International Peace Research Institute (SIPRI). Once collated and transformed this dataset functioned as a powerful and unique source for trade level trend observation at a macro level. The qualitative part of the study involved 11 expert interviews conducted with respondents from across five countries. Interviewees were initially questioned on how they perceived the CoC and what motivations they would give for its

success/failure in marketizing the defence procurement process in Europe. Thereafter, other measures in the legislative and legal landscape were explored for their potential explanatory power in relation to the observed trends.

Findings

Results indicate that at best the measures have had a small impact on marketization. Although the initial results of the preliminary statistical study are decisive, equifinality in causation is ultimately difficult to attribute to the Code of Conduct as many complex dynamics ultimately affect the trends observed.

The statistical study displays very clearly that post 2006 the level of intra European trade in conventional weapons accelerates at an unprecedented rate implying there has been some shift in policy or actions that caused it. However, the link between the CoC and this rise appeared to be weak once the evidence from the expert interviews was considered. This prompted a wider analysis of EU Member State imports to include imports from 3rd party countries. Once considered in this wider context it is clear that Member States have not per se increased imports, rather they appear to be pursuing a ‘buy European’ policy at the expense of imports from outside the Union. Furthermore, respondents indicated that the supply chains of European defence firms have seen considerable opening up to cross border procurement at the sub-systems level. Although, both these trends can be seen as a modest success, the CoC has seemingly not managed to change behaviour at the end-user stage of procurement i.e. it was aimed to make governments procure on a market orientated cost-competitive basis and this was not convincingly achieved. That said, it is possible to talk of the progressive forming of an ‘exclusive’ European defence procurement community.

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- Interview 04: *Exports director, defence industry association of medium sized Member State. (2012-09-14)*
- Interview 05: *Policy officer DG ENTR, European Commission. (2012-09-19)*
- Interview 06: *Director of international affairs, defence industry association, USA. (2012-09-26)*
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9 Annexes

Annex 1

TIV of arms exports to UK, 1995-2011
Generated: 29 March 2012

Figures are SIPRI Trend Indicator Values (TIVs) expressed in US\$ m. at constant (1990) prices.
Figures may not add up due to the conventions of rounding.
A '0' indicates that the value of deliveries is less than US\$0.5m
For more information, see <http://www.sipri.org/databases/armstransfers/background>

UK	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011 Total		
Austria														29	1			30		
Denmark													5					5		
France				4	11	26	18	15	12							108	103	438		
Germany	1			4	37	5	300	310	5					30	10	22	22	20	756	
Italy						200								20	33	8		261		
Netherlands										10	10		152	192	15	35	30	484		
Sweden	1	4	11	226	22	22	55	20	337	330	34	11	192	242	59	178	211	198	2166	
Singapore																25	4	25		
South Africa				1						14								16		
USA	412	457	497	488	514	514	87	782	1247	388	440	155	15	138	298	476	316	365	210	7335
Australia															5			5		
Canada														138				138		
Israel													2	35	10			47		
Russia												1	1					2		
Japan																		75		
New Zealand				10														10		
Norway									3	8						2		13		
	817	467	577	800	514	98	782	1347	901	808	179	16	148	871	801	918	300	918	7670	

