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**Research Report**

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# The German Armed Forces and the Financial Crisis

## Towards National Restructuring and European Economies of Scale

*Sophie-Charlotte Brune, Marcel Dickow, Hilmar Linnenkamp and Christian Mölling*

With the economic crisis making no exceptions for the German defence budget the pocket calculator could soon become vital equipment for the Bundeswehr. How can the armed forces continue making a dependable, efficient and affordable contribution to German and European security and defence? It is not enough to focus exclusively on the German context here. Quite the opposite: it is time to break with the tradition of national thinking in defence planning and tap instead the potential of economies of scale at the European level. When considering the future of the Bundeswehr we must ask how such an about-turn can be accomplished in harmony with alliance responsibilities, the ongoing transformation process and operational requirements.

The economic and financial crisis has created a situation of enduring crisis in state budgets throughout the European Union, with Germany no exception. The EU Commission expects the average eurozone deficit to reach almost 7 percent in 2010. After massive debt-financed recovery programmes fiscal consolidation will be inevitable. In Germany the debt cap recently added to the constitution will exercise additional pressure on all ministry budgets. What we are looking at is not a blip but a lasting reduction in revenues and spending, so the consolidation process will have to aim beyond short-term cuts to seek structural spending reforms designed to bite in the medium term.

Quite apart from the budget shortfalls caused by crisis, sustained foreign operations and rising personnel costs are squeezing the resources available for research, development and procurement. The first spectacular planning corrections are already on the table. The United Kingdom is looking to cut its strategic nuclear submarine fleet from four to three, London and Berlin are both downsizing their Euro-fighter orders and France is reducing the size of its armed forces.

The required adaptations demand efforts on two levels by all states involved. Firstly, identification of internal restructuring and rationalisation potentials; secondly, cooperation with alliance partners and specialisa-

tion, especially in the scope of the Common Security and Defence Policy (CSDP; formerly European Security and Defence Policy, ESDP). Savings can be achieved through international cooperation and by internationalising defence production.

### **Restructuring and Rationalisation**

Despite a hefty defence budget of about thirty billion euros that has remained stable over the years, the Bundeswehr is struggling to meet the challenges of an “army in operation”. With public purse-strings tightening reform is more vital than ever. Where do structure, personnel and procurement offer scope for long-term savings?

#### **Structure**

The transformation process launched in 2004 is designed to enable the Bundeswehr to fulfil its principal tasks more effectively, above all international crisis management. Despite far-reaching internal restructuring and a division of the Bundeswehr into new force categories the Bundeswehr has yet to achieve the deployment target defined in 2004 (up to five brigades with 14,000 troops ready to deploy on stabilisation missions). Instead, with about 8,300 servicemen and -women currently serving abroad it is already operating at its present limit.

The Bundeswehr does not yet have adequate forces ready in sufficient numbers. Too great a part of the force is still dedicated to national defence and not deployable abroad. Even within the mobile contingents there are chronic shortages in particular categories, for example infantry and mechanised forces. Whereas Germany provides a meaningful and politically expedient reserve for the NATO Response Force and the EU battle groups, it suffers critical shortages of transport helicopters, military police and medics. Corrections made in recent years have yet to take full effect. Organisational structures that correspond more closely to deployment

requirements should thus be introduced more thoroughly than hitherto.

#### **Personnel**

The first place to look for financial savings in the personnel structure of the Bundeswehr itself and the defence ministry would be administrative rationalisation. Chancellor Angela Merkel’s coalition agreement of October 2009 calls for a commission to scrutinise the organisation and management procedures of defence ministry and armed forces in search of efficiency improvements. The commission will need to draw on external expertise if it is to deliver tangible results. The 2009 Gray Report on rationalising defence procurement in the United Kingdom contained far-reaching proposals for cuts and restructuring in defence bureaucracy and could serve as the model for the German commission. The ongoing transformation of the Bundeswehr must be based on a coherent long-term strategy to increase the availability and readiness of German contingents for international operations (led by the UN, NATO or the EU) and equip them accordingly.

Yet, the most pressing question is the possibility of abolishing compulsory military service. Cutting the administration of conscription, re-tasking the staff in charge of conscripted troops and transforming the Bundeswehr into an army of 160,000 to 180,000 career and enlisted soldiers would allow more force to be projected at less cost. The reality of the early twenty-first century is that the German Bundeswehr is an army in operation for international crisis management. Yet in an army of about 250,000 Germany still affords about 50,000 conscripts who take no part in such missions.

The coalition agreement of 2009 proposes cutting military service to six months from 2011. Six months corresponds to the duration of basic and specialist training, and represents a half-hearted exit strategy with overwhelming disadvantages for army

and conscripts alike. Recruits would experience nothing of everyday military life after completing their training; their service would amount to little more than an internship with on-the-job training. Although the current plan is to keep conscripts as close as possible to deployable forces, six-month military service is unlikely to do much to persuade recruits to sign up for longer. On the other hand, running the infrastructure required for military service will continue to place a heavy burden on the Bundeswehr and training conscripts will tie up the time and energy of career and enlisted soldiers.

There can be no denying that military service holds an important place in post-Second World War Germany. But in an age of professional crisis management and robust interventions it is simply outdated. Secondary political effects (recruiting pool, the importance of civilian alternative service in particular fields of social work, etc.) cannot justify the exception from the constitutional freedom of occupation made for German military service. National defence places a duty on citizens that other domestic or foreign policy goals cannot – however honourable they may be.

### **Procurement**

German defence planning is failing to keep up with both transformational and operational needs. The Bundeswehr needs to acknowledge these significant shifts and adapt its planning and procurement processes accordingly. Projects in the development stage have not so far been adjusted to fit the changing needs. Furthermore, maximalist requirements for procurement projects are rigidly adhered to, even though the last 10 to 20 percent of performance are liable to increase costs disproportionately and delay delivery. Second-best solutions – ready on time and affordable – ought to be favoured over the pursuit of maximum performance. The way the current deficiencies cause problems with procurement can be seen both in operational reality on the

ground (armoured vehicles, NH-90 multi-purpose helicopter), and in major projects in the pipeline (A400M airlifter, Herkules). Last year's annual report from the Federal Audit Office highlights the lack of transparency in the defence procurement process, citing the example of the Taifun attack drone.

Although capabilities such as force protection, strategic mobility, global reconnaissance and interoperability of command and communication systems are defined as priorities in the transformation process, there are still deficits in implementation. Even now, only 70 percent of the vehicles deployed in Afghanistan are fitted with mine protection.

The urgency of finding solutions for operations already under way leaves no leeway for time-consuming research and development activities. Here there is a need for flexible instruments allowing faster responses, for example "fast track" procedures. In many cases products already on the market would allow capabilities to be procured quickly. In some fields the Bundeswehr is already making use of this option, for example recently leasing Israeli drones for use in Afghanistan. The necessity to adjust to reduced budgets will make no exception for national participation in major international projects either. The huge price tags involved – in particular for the A400M military airlifter and the Eurofighter – are only one part of the equation. Experience shows that ensuing life cycle costs (operation, servicing, repairs, product enhancement) add about the same amount again to the overall cost of a system.

The discussion about the Airbus A400M is dominated by non-military arguments unrelated to capability. Aside from the cost explosion and the three-year delay, it remains unclear whether the requested specifications can ever be achieved (range, payload, volume, etc.). From the purely business perspective it would be time to demand fulfilment of the contract and impose penalties for the considerable delays – or to cancel the deal. But given

their state investment in the Airbus parent EADS and the resultant industrial policy interests, France and Spain in particular are willing to renegotiate the existing contract, while EADS is upping the stakes by openly threatening to abandon the project.

At its heart the debate is about the possibility and political repercussions of cancelling the A400M. The project was conceived as a beacon of European defence industry cooperation: abandoning it would represent a significant set-back for European efforts in this field. From 2013 it would also leave Germany lacking strategic airlift capabilities that planners are already depending on. The Bundeswehr would then have to source that capacity from other companies. Purchasing aircraft from American suppliers and extending the practice of leasing civil aircraft through the Strategic Airlift Interim Solution (SALIS) represent two compatible options. The German government needs to weigh the cost of staying with the A400M against its alternatives.

Cost overruns in the Eurofighter programme have left Germany's defence budget short of the funds for its last batch of 37 jets. Chancellor Merkel's new government has already abandoned the original commitment to purchase 180 aircraft for the Luftwaffe, proposing instead to resolve the budget impasse by selling Tranche 3B on to foreign buyers. It would be in the interests of all the partners (Germany, United Kingdom, Italy, Spain) if the German government could state clearly that it can do without these 37 aircraft. That would give the Luftwaffe a clear basis on which to plan and, by cutting a whole squadron, lead to structural savings. It would also save Berlin from being forced to make potentially controversial arms exports dictated by financial need but following no foreign policy rationale.

## **Cooperation beyond National Horizons**

In the EU, twenty-seven defence ministers and their twenty-seven ministries currently administer nearly two million soldiers. Yet, this impressive number contrasts with a deployability that is less than 10 percent and with an annual cost of €200 billion. For the CSDP this raises the question how long the member states will be willing and able to fund their shared practice of wasting resources at the national level under the pretext of national sovereignty. At the same time no EU member state has the capability to provide effective crisis prevention and management on its own.

The way out of this quandary is to implement exactly those answers all national security policies of EU member states already provide: international cooperation, integration, division of labour and rationalisation.

## **European defence procurement – outlining the deficits**

Back in 2006 the ESDP defence ministers (i.e. from all EU member states but Denmark) declared that: "... a fully adequate DTIB [defence technological and industrial base] is no longer sustainable on a strictly national basis – and that we must therefore press on with developing a truly European DTIB, as something more than a sum of its national parts. We cannot continue routinely to determine our equipment requirements on separate national bases, develop them through separate national R&D efforts, and realise them through separate national procurements. This approach is no longer economically sustainable – and in a world of multinational operations it is operationally unacceptable, too."

An increasingly integrated European DTIB and an EU market for defence goods were thus already high on the agenda four years ago. But to this day the EU has been unable to organise procurement policy according to shared priorities. Likewise, the closely linked sphere of industrial policy

remains the business of the individual states with all the corresponding consequences.

General overcapacity in the defence industry and widespread duplication in production burden defence budgets. Even in multilateral procurement projects, maintaining domestic development and production capacities is regularly given priority over the acquisition of the militarily necessary from the technically most competent and economically most effective supplier. This is seen for example in the procurement of armoured vehicles for the Bundeswehr or with the French Leclerc main battle tank.

There are three central reasons why national procurement regimes are not coordinated with one another: Firstly, many arms-producing states believe that keeping their own arms industry is vital for preserving their national independence and ensuring security of supply for their armed forces. Therefore, they seek to keep the broadest possible spectrum of national production capacity. Secondly, diverging national security concepts lead to different capability configurations and accordingly different requirements for the national defence industry. Thirdly, there is no consensus about the role of the state as regulator, owner and customer in the defence sector: some are free-market and competition-orientated, others protectionist and happy to hand out subsidies.

### **A European imperative**

The dream of national security of supply as a condition for independence in defence matters has become unaffordable. Moreover, it no longer fits with the reality of the EU. Today, national armed forces are highly dependent on external service providers and suppliers. The question is no longer how much national independence would cost, but simply how Europe can uphold an effective spectrum of capabilities and the associated DITB.

The financial crisis increases the pressure on all EU member states to seek resource-saving solutions and increases the incentives to examine the potentials of European procurement cooperation. The necessary instruments for this have already been created, including the European Defence Agency and the Permanent Structured Cooperation set up under the Lisbon Treaty. But increasing efficiency will only be possible if governments agree on shared concepts.

Firstly, politicians must open the way for Europeanisation of the defence equipment sector, with procurement and competition rules to place domestic and foreign suppliers and purchasers on an equal footing. Transfer and export regulations should ease industrial cooperation and production. The EU Commission's 2009 "Defence Package" shows the way (European Procurement Directive 2009/81/EC). Its Implementation in national law must be ensured.

Secondly, the common policy must be led by an overarching security concept. The EU's "comprehensive approach" offers such guidance. It emphasises the combination of military and civilian means as a crucial ingredient of successful crisis response. The material demands of crisis intervention may call for a broad spectrum of tools – from armoured vehicles to warplanes, from radios to trucks. Within this range there is scope for identifying capabilities and equipment that can be planned, procured and used jointly, with the greater volumes leading to lower unit costs. That applies for example to logistics, as well as central communications infrastructure, medical care and intelligence.

### **European Defence Agency**

The European Defence Agency (EDA) was founded in 2004 to support the EU member states in developing military capabilities for crisis management operations. Hence, the Agency is concerned with all aspects of EU defence procurement. The EDA has already undertaken the first steps towards a more

Europeanised procurement policy, incorporating projects of the rather inefficient WEAO (Western European Armaments Organisation). The intergovernmental defence procurement regime set up in 2006 and the joint investment programmes in the field of research and technology are already reaping their first rewards. Beyond that, the EDA has proven its usefulness and ability to respond to acute needs of the EU member states through programmes for example to improve logistics concepts or train helicopter crews.

But the scope of the EDA is limited. As an intergovernmental institution its role is to support the member states. It can act as an initiator and catalyst of cooperation but cannot compensate where the EU member states lack clear policy or are unable to co-operate.

However, with the instrument of Permanent Structured Cooperation (PSC) the Treaty of Lisbon opens up an opportunity for the agency to transcend some of these limitations. Under PSC the EDA is to regularly assess the member states' contributions to CSDP capabilities and report annually. This would make the agency a kind of secretariat of the PSC.

### **Permanent Structured Cooperation**

In the longer run it will be essential to consider much further-reaching European cooperation models, also in order to cut national costs. The PSC should offer the opportunity to those member states that already contribute significantly to EU defence efforts to cooperate even more closely in order to further improve their military capabilities. The possibilities are legion. One first step could be to intensify the coordinated use of existing national capabilities (pooling). The option of making the Eurofighter the heart of an autonomous European air policing capability under PSC should be weighed up. One example of the effectiveness of such an approach is the way a group of mainly European NATO members has been patrolling Baltic airspace

since 2004. Although not due until the end of this decade, the European Air Transport Fleet (EATF) goes in a similar direction. The twelve EU member states cooperating under the EATF could also share command and operation of the A400M transporter. Allied states already agreed to share sea transport capacity. Analogous pools could be built under PSC to establish a European fleet of drones (UAVs) or of transport helicopters.

A comprehensive reform of the EU DTIB could imply developing a "PSC-inspired" European industrial policy for the benefit of the Union as a whole. It would organise and implement a consensus about the sensible distribution of national core competences. The precondition for this would be to define strategic priorities for the joint capability portfolio the EU wishes to maintain and promote. Special attention should be given to those technologies that ensure a certain independence over other actors or where the EU already has a comparative advantage.

### **More effective military structures**

Substantial potential for savings can be found in the largest budget item: personnel. As already mentioned, the twenty-six states participating in the CSDP still foot the bill for nearly two million soldiers. This number is based neither on current nor on future needs for crisis management operations. Hence, structural reform can produce savings without harm to operational readiness, modernisation or procurement. However, a fundamental change of national force structures would require coordinating or even overcoming the practice of parallel national military planning.

The EU battlegroups represent a first, small step in this direction. As well as creating a quick response capacity for the EU, they have also already positively influenced defence diplomacy between the respective troop contributors with regard to common operations concepts, training and equipment. The underlying mecha-

nism for generating European capabilities should be expanded to more units. Such an expanded modular force structure and complementary scheduling of national contributions would allow the overall readiness of such a combined EU force to be increased.

Another option is role specialisation, with individual states limiting themselves to particular military capabilities. Through coordination with partners the alliance as a whole could still provide all required capabilities. That naturally means a greater degree of mutual interdependence. But this can be reduced – and a degree of focussed redundancy introduced – if critical capabilities are provided by a small group of states rather than just one.

## Conclusions

Confronting the assumption of fiscal stringency in response to crisis with the outlined panorama of adaptation, rationalisation and cooperation, we arrive at three recommendations to government and parliament concerning the Bundeswehr:

- ▶ A rigorous examination of the extent to which the current conscription model remains necessary is indispensable. Otherwise the scope for painful adaptations cannot be assessed. With the structure of the Bundeswehr not yet reflecting the new operational realities, the option of a fully professional army must at last be investigated without heed to taboos.
- ▶ The Bundeswehr's procurement and structural planning must make a clean break with the illusion that the German army acts largely on its own and therefore does not need to cooperate. Instead, all options for institutionalised cooperation with European partners must be explored. Going beyond ad hoc working arrangements, synergies must be harnessed in a European alliance where individual partners contribute those capabilities for which their history, tradition and equipment predispose them.

- ▶ With the European Defence Agency and Permanent Structured Cooperation the EU has all the necessary instruments at hand. For political, economic and financial reasons the German government should make active use of these.

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