

Banking on Defence

Raising more money and spending it better

BY EDWARD LUCAS AND GUY DE SELLERS

Foreword by Jo Hawley

Introduction by Tim Leunig

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Foreword

Jo Hawley, Executive Director, The Britain Project

The Britain Project exists because liberal ideas have answered Britain's hardest questions before, and because we believe they can do so again. When we set out our vision for a reinvented liberalism, we said our work would be organised around three questions: how Britain grows again, what keeps us safe, and what people can rely on and belong to. This first paper addresses the second of those, and it does so in a way that shows why the three cannot be separated.

The global security context has changed. The American guarantee that underwrote British defence for eighty years can no longer be assumed, and Russia's war in Ukraine has made the cost of that assumption plain. Britain and its allies must spend more on their own defence. But liberals have never believed that spending more is the same as doing better, and this paper's central argument is that the way we pay for defence, and the way we buy it, are as much a part of the problem as the amount.

Edward Lucas and Guy de Selliars propose a new multilateral defence bank. It is an idea that runs with the grain of everything we set out in our vision. It is pro-enterprise but not pro-incumbent: it would open defence procurement to competition and finance the small and innovative firms that the current system leaves to carry the greatest risk. It disperses power, weakening the grip of vested interests in ministries and boardrooms by making access to finance depend on decisions being taken on merit. It honours the trust each generation holds for the next, spreading the cost of rearmament over the life of what is bought, and financing it on long, predictable terms that no government can easily secure alone. And it recognises that our interests and obligations do not stop at the border: the answer to a shared threat is a shared institution, built with our European neighbours and closest allies, not another attempt to go it alone. Nor does it impinge on member countries' sovereignty in defence matters.

The idea also has some political backing. In June 2026 Sir Ed Davey, in setting out the Liberal Democrats' proposed Growth and Defence Partnership with the European Union, called for financial cooperation through a new European Rearmament Bank, alongside UK access to the EU's SAFE programme and joint defence procurement.¹ The Britain Project is independent of any party, and we publish this paper because the idea is right, not because of who has endorsed it. But it is a proposal that has already been broadly supported by the Liberal Democrats, and this paper takes it from a principle to a plan: how such a bank would be capitalised, governed and run. It also argues that it should reach beyond the EU to Canada, Ukraine and Europe's other allies.

Above all, the paper refuses a false trade-off. We are told we must choose between security and solvency, between rearming and the public services that make a country worth defending. We do not accept that choice. A well-designed bank, run on sound principles, lets us have both.

We publish this paper in the spirit of our founding commitment: to develop bold, practical, evidence-led ideas, follow the argument where it leads, and make the results available to anyone prepared to use them well. We hope those in a position to act on it will do so.

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¹ Ed Davey, "A new plan for growth, jobs and defence", speech to the European Movement, 17 June 2026: <https://www.libdems.org.uk/press/release/ed-davey-speech-on-europe-a-new-plan-for-growth-jobs-and-defence>

Executive Summary

- The Ukraine war and Trump's capriciousness are stoking Europe's security crisis. Spending more money alone will not keep us safe: we need to spend it better.
- A new multilateral bank on the model of the European Bank for Reconstruction and Development (EBRD) could help all governments, rich and poor, spread rearmament costs over many years, give industry the certainty to invest and ease the pressure on their own bond markets.
- We therefore welcome the UK's work with partners on the Multilateral Defence Mechanism (MDM) and Canada's Defence, Security and Resilience Bank (DSRB).
- With £100 billion of subscribed capital, only £10 billion of it paid in, such a bank could build up to £250 billion of lending capacity as its track record develops. It could draw in still more through private debt and equity.
- It should chiefly finance specific contracts, but also be able to support stockpiles and other projects. It would set clear conditions on scale, interoperability and innovation, without impinging on members' sovereignty in defence matters.
- It should be leanly run on sound banking principles, with no subsidies or boondoggles. Each member would borrow at its own market rate, so Germany pays no more than in the Bund market and no country subsidises another.
- Neither the British nor the Canadian initiative will succeed without Germany, France, Italy and the other major EU countries, the European Commission and NATO. They will not sign up to a scheme designed elsewhere, least of all one headquartered outside Europe: they must help create it.
- We urge EU countries and their closest allies, especially the UK, Canada and Ukraine, to build a single AAA-rated institution, starting with a political agreement on its founding principles. Those principles would underpin an international agreement, with the operating details left to professional staff under a senior management appointed by the members.
- We also urge the UK and Canada to step back from promoting their own blueprints, which will take political courage. Pride of initiative and authorship should not stand in the way of what could become an essential pillar of our collective security.

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Introduction

Tim Leunig, Policy Director, The Britain Project

Lessons from History

The world was, of course, a different place a century ago. That said, like today, it was a world full of tensions and the threat of war. Both the early 1920s Greco-Turkish war and the Irish Civil War and War of Independence had just finished. But the peace in Europe was unstable. Mussolini was already Italy's Prime Minister and Portugal's first republic had just fallen to a coup d'état that led to a dictatorship that would last 48 years. Although the Nazis' 1923 "Beer Hall" putsch failed, Hitler simply changed tactics in his march to power.

Further east, Lenin was dead, and Stalin well on his way to establishing his position as Russia's brutal dictator. Further east still, the relatively moderate and pro-democracy Taishō era was drawing to a close in Japan, with 1926's accession of Emperor Hirohito to the chrysanthemum throne inaugurating the much more militaristic Shōwa period.

In all of this, Western Europe looked bewildered. The League of Nations was ineffective. Governments came and went. There were five in the United Kingdom between 1922 and 1924 alone, led at different times by the Liberal Party, the Conservative Party and the Labour Party. France did even better – or rather worse – with 33 Presidents of the Council of Ministers (in effect, prime ministers) in the interwar period. These were not strategic times for the democracies of Western Europe.

And in all this, America stood alone, uninterested. Indeed, Republican Senator Warren G. Harding won the 1920 presidential election with the slogan "America first".

We know how that period ended. Spain had a civil war. Germany, Italy and Japan formed an alliance, and took the world to war in three stages. Russia allied with Germany to begin with, and only fought it when attacked. Poland and France fell, as did – inevitably – the Low Countries and other smaller nations. For sure, the UK, the US, the USSR and other countries around the world won – but it was a war of monumental proportions, with untold costs for those who fought on both sides, for civilians who suffered in all theatres, and above all for those who were the victims of the Holocaust.

The words "Lest we forget" are repeated every year at war memorials across our country, and have been since 1918. We should never forget any conflict, and the sacrifices involved of so many, but it is equally important that we should never forget the foolishness of so many leaders between those two world wars.

The parallels with today are obvious. We have a murderous dictator in Europe once more. Putin has shown himself to be such a person, repeatedly. We have an isolationist in the White House again, and while personally unpopular, that strand of his appeal remains deeply embedded and widespread in popular American thinking.

And in Ukraine we have a European war. It is our first since the Balkan Wars of the 1990s, when Europe failed to cover itself with glory, needing help from the US to sort things out.

It falls to us in the United Kingdom, as in other democracies close by and further away, to ask ourselves what sort of country we are, and what sort of world we want to live in, now and in future. We cannot, of course, do much alone – we are not a major power, and our population and economic heft relative to

others in the modern world preclude that. We can, however, work with others to avoid the mistakes of the 1930s. That is our challenge.

This report sets out – part of – the answers. Specifically, it outlines the need for urgent change in the way we pay for defence, and the way we spend money on defence. The world is short of money these days, and while defence is important, we must spend the money we have effectively.

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More Defence

Edward Lucas and Guy de Selliars

For decades Britain, like almost all of NATO, looked on the United States as King David looked on God in Psalm 17: “Keep me as the apple of your eye, hide me under the shadow of your wings.” Today the United States does not see any European nation, nor even Canada, as the apple of its eye, and American decision-makers are not willing to allow us to hide under the shadow of their wings. If we wish to rest there, we need to pay our share, for the disproportionate American funding of US-led alliances is over.

That deal was one-sided, although not entirely so. The US was the biggest funder and the US military did most of the work. In return the US got two things. First, it was the unquestioned political and military hegemon in the non-communist world from 1945 onwards. It really could talk quietly, for it carried a truly big stick. Second, the US defence industry became the world leader in technology and that had direct and indirect economic benefits.

Those days are over, and expectations of a return to a tranquil and orderly world of US-led alliances in Europe, or in the Pacific, are fanciful and dangerous.

The question facing Britain and other US allies in NATO and in the free world more generally is how to manage the transition. The sensible approach would be an orderly shift of the burden over a decade, whereby the US provides a gradually reducing range of extremely sophisticated and expensive capabilities, while the Europeans and others build up their strength and expertise in these areas.

The alternative is a disorderly US withdrawal, both literally, from US bases in Europe, and in terms of the weapons and systems that America makes available to its erstwhile allies. It is perfectly possible for the United States to withdraw capabilities of all kinds with little or no warning. No matter what a military treaty may say, no small country can enforce such a treaty against a larger and more powerful one that decides to renege.

The worst outcome, of course, is the US siding with Russia or another hostile power, in Europe’s backyard, or beyond.

European nations, Canada, and others need to appreciate the size of the gap left by a putative US withdrawal and the cost of filling it. These include the roughly 80,000-strong US Army presence in Europe, made up of permanently stationed forces, rotational deployments and those on exercises. These US forces currently comprise the only credible rapid-response ground force against a Russian invasion. Furthermore, NATO defence planning shows that the US is also expected to provide the bulk of rapid reinforcements, and to protect sea-lanes for their transport to Europe. The US also maintains more than 200 aircraft in Europe, made up of fighter, attack, tanker, and transport aircraft as well as helicopters. It also has frigates, cruisers, and destroyers, mostly operating out of the naval base in Naples. These provide not only sea-power, but the Aegis Ballistic Missile Defense System, which together with US Patriot systems in Poland and Romania, comprises almost all of Europe’s serious air defences.

US “enablers” such as logistics and mid-air refuelling systems are also vital to European military efforts to reach the battlefield and to sustain combat operations. The US defence-industrial base is a vital source of munitions, spare parts and other resupply. The US has unmatched intelligence, surveillance and

reconnaissance capabilities, without which modern armies cannot fight and decision-makers cannot operate – as we have seen in Ukraine.

For all that, perhaps the most important role the US has in Europe's defence is in command and control. The most important military HQ dealing with European defence is Joint Force Command in Norfolk, Virginia. As Ruben Stewart, a land warfare expert at the London-based International Institute for Strategic Studies (IISS), [notes](#),

What would disappear most critically with US withdrawal is not mass, but integration. US participation effectively acts as the Alliance's operating system, linking sensors to shooters, synchronising effects across domains, and providing the data, communications and planning architecture that allow multinational forces to fight as a coherent whole.

In short, without the US, Europe can fight at best a limited war, with limited effectiveness, for a limited time. That is a recipe for manifest defeat.

As an order of magnitude, the International Institute for Strategic Studies last year estimated the cost of replacing the US in Europe at around \$1 trillion, which is about £750 billion. A pro-rata share by population would mean the UK having to find £130bn. The EU defence commissioner, Andrius Kubilius, suggests that about half this is needed just to replace the US “enablers”.

In some countries, the answer is simple. Norway, with a GDP per head of \$100,000 and a \$2 trillion sovereign wealth fund, has simply raised its defence spending by more than half since the start of the Ukraine war. Neutral Switzerland has very low debts and has also been able to raise spending. Germany, which has the lowest sovereign borrowing costs in the EU, has relaxed its debt rules to spend significantly more on its military.

Most other European countries – including the United Kingdom – cannot afford to raise taxes or borrow a lot more money in the short term. Their need is therefore to spread the cost of rearmament over a longer period, and to draw in private capital alongside public money. We need to increase spending, but we also need to do it in a way that is acceptable both politically and to the markets.

This is not a new idea in British politics, as the authors of this paper have been discussing similar solutions at a high level for some time. The concept presented in this paper was developed with the active involvement of military procurement, financial and legal experts from the UK, France, Germany, Belgium and Poland. In June 2026 the leader of the Liberal Democrats, Sir Ed Davey, proposed a new European Rearmament Bank, together with UK access to the EU's SAFE programme and joint defence procurement, as part of a Growth and Defence Partnership with the European Union.² That is the right instinct, and this paper is in part an attempt to give it substance. The sections that follow set out how such a bank would work, how it would be capitalised and governed, and why its membership should extend beyond the EU to Canada, Ukraine and the other allies who share the same threat.

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² Ed Davey, “A new plan for growth, jobs and defence”, speech to the European Movement, 17 June 2026: <https://www.libdems.org.uk/press/release/ed-davey-speech-on-europe-a-new-plan-for-growth-jobs-and-defence>

Better Defence

For too long European countries have tried to go it alone, or in small groups. This results in higher design costs per unit produced, and high production costs caused by shorter production runs. For example, Europe has about 2,400 current generation active battle tanks, around the same number as the US. But while every US tank is an M1 Abrams, Europe has around 1,600 German Leopard tanks, used by Greece, Spain, Finland, Poland, Switzerland, Sweden and Austria and on order in Lithuania, while Britain has about 200 Challengers, the French about 200 Leclerc tanks, and Italy has about 200 Ariete tanks. Poland is now introducing Korean K2 Black Panther tanks as well. These are all fine tanks, but the logistics of maintaining supplies for five different current-generation battle tanks is obviously a European inefficiency that the US Army simply does not have to face. Indeed, until the next generation of Challenger tank comes on stream, the British Army cannot even fire the same ammunition as other NATO nations. Tanks are illustrative – the same pattern is true for helicopters, fighters, and so on, as well as for smaller armaments.

The reason for these poor outcomes is that defence procurement just does not work. Britain, like other countries, buys the wrong equipment, at the wrong price, in the wrong timeframe, with the wrong criteria for interoperability and maintenance. This leads to proper scandals – the delayed, overpriced and probably unusable £5.5bn Ajax fighting vehicle being perhaps the most salient example in the British context.

The civil service has too many generalists, politicians interfere, and military types lobby for tweaks before, during and after contracts are signed, often oblivious to the cost. Defence “primes”, the big companies, exercise pernicious political power, often thanks to having hired well-connected people. They often have nationalistic cards to play. All this is lucrative for the manufacturer but a menace when it comes to military effectiveness.

The combination of secrecy and military urgency all too often means that failure is covered up, and competition stifled. New entrants, already hamstrung by the shortage of loan finance, may go bankrupt waiting for governments to make decisions and spend money.

These national problems are compounded when it comes to organising collective procurement. Every country tries to favour its own industries and production sites. Pooling orders is agonisingly slow – meaning that equipment risks being out of date before it is ever produced. On multinational projects, progress is only as fast as the slowest member government.

The result suits some insiders but corrodes national security and erodes our defence. It makes it hard to argue for higher defence spending since the system is notoriously wasteful, and even corrupt. Proposals for change are legion but mostly unsuccessful. Everyone signs up for new rules, in the hope that they will apply to other countries, but can be bent or ignored when it comes to their own national interests.

Europe, and NATO more widely, needs more defence, but it also needs defence systems that can be produced quickly, at good prices, which can be deployed effectively together, and for which logistics are as straightforward as possible.

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Scaling Up Defence

The solution is a new multilateral bank. Multilateral banks date back to the remarkably successful reconstruction of the global economic infrastructure at the end of the Second World War. The Bretton Woods conference, held in the New Hampshire hotel of that name in 1944, led to the creation of the World Bank and the IMF. Later, regionally focused development banks include the European Investment Bank (EIB), in 1958, and the European Bank for Reconstruction and Development (EBRD) in 1991.

The idea is simple: participating governments are the founding shareholders. They subscribe capital, a small part of it paid in and the rest callable, that forms the bank's foundational capital base. The bank then borrows money from the international bond markets and lends to a range of public- and private-sector borrowers, for projects that will bring medium- and long-term returns. It makes a profit on its lending which covers its operating costs and builds reserves.

The crucial feature is that a small amount of up-front public money (“paid-in capital”) is combined with a promise of more if the bank needs it (“callable capital”). The latter is a promise to pay, in effect an IOU, from governments to the bank, but it is rarely if ever called on. Only the paid-in capital requires cash from governments up front, and statisticians are likely to treat it as a financial investment rather than spending. Callable capital is a contingent liability: disclosed, but not counted as debt unless it is called. Assuming that the bank adopts what are known as “sound banking principles” – such as no subsidised loans or political favours – it will never need to go back to its initial shareholders asking them to convert the callable capital into hard cash. This means that creating such a bank is very cheap for governments. Not costless, but very cheap.³

Although the bank has only the paid-in capital literally in its accounts, the fact that it has the legal right to the callable capital as well means that it can borrow against both amounts. A bank with £1 in paid-in capital can have a further, say, £9 in callable capital, giving £10 of subscribed capital in all. In addition, depending on the quality of its loan and investment portfolio it can borrow in excess of its subscribed capital. The European Investment Bank borrows as much as 2.5 times its subscribed capital. A new bank would start with a lower ratio and raise it as it builds an operating track record, but at that ceiling £1 of paid-in capital becomes £10 of subscribed capital and up to £25 of borrowing, which in turn becomes £25 of lending and investment capacity.

In short, governments have the power to create an institution that costs them £1, directly and unequivocally, and that could in time lend up to £25 on defence as good projects come forward and its track record is established. Loans the bank makes to governments themselves are, of course, government borrowing like any other; the leverage comes from its lending to industry and from private co-finance.

As orders of magnitude, we propose £100bn in subscribed capital, of which 10% – £10bn – would be paid in by governments as a starting point, with the remaining £90bn callable. If enough countries join, the UK would be between a tenth and a quarter of these amounts – tiny sums on the scale of the UK budget and fiscal position. The bank’s leverage would start low and rise with its operating track record, but it could ultimately borrow up to £250bn, 25 times the paid-in amount. The assets held by the bank – primarily loans that it makes to governments or to private sector borrowers largely against government

³ Sound banking principles have two big features. One is lending only to credit-worthy borrowers at rates that reflect the credit risk. The other is investing equity in companies only at terms that are compatible with the equity risk

contracts – would be very high quality, enabling substantial leverage. Unlike the EBRD, whose borrowers repay from project returns, this bank's loans would be repaid from member governments' defence budgets – either directly, when the government is the borrower, or via the procurement contract, when the contractor is. The credit risk is therefore essentially sovereign, which is what underpins the AAA rating and the leverage.

The combination of creditworthy shareholders – national governments – and a strong business model, typically gives multilateral banks such as this a triple-A credit rating. This enables them to raise money extremely cheaply in international capital markets. The bank can then lend out that money at somewhat higher rates, creating a profit that covers their operating costs. Any profits above operating costs either allow for expansion, because they expand the capital base, or are returned to shareholder governments as dividends.

In fact the effects are even stronger. Multilateral banks typically catalyse private sector finance through co-financing arrangements. Having a multilateral bank, with its clout and prestige, as the lead lender makes co-financing more attractive for commercial and other lenders.

For similar reasons, this defence bank should also be allowed to make direct equity investments in defence SMEs. This too will catalyse private-sector equity and other investors. Again similarly, the bank could support venture capital funds as an anchor investor in new firms, particularly in new defence sectors such as drone warfare.

This proposed approach is built strongly and clearly on a proven model. As an example, since its founding in 1991 with a paid-in capital of €10 billion, the EBRD has lent €220 billion to more than 7,800 projects. A defence bank, with greater capital, could do far more, far more quickly.

An important point: the defence bank should not lend on concessionary terms. This is about lending, not subsidy. Concessionary terms would be in effect a subsidy from countries such as Germany, Canada, Finland, and the Netherlands to the alliance members with higher borrowing costs. This would be politically difficult in these countries and set a bad precedent. This is a bank, nothing more and nothing less. The bank would lend at market rates. In the case of loans to Germany it would imply a small negative spread to the bank's borrowing costs that would be compensated by the positive spreads on all other loans.

In practice, each member would borrow from the bank at roughly the rate it would pay in its own bond market for the same maturity. Germany would borrow at Bund rates, which are typically below the bank's own funding cost, so the bank would make a small loss on its German loans. Other members – the UK, France, Italy, Poland and the rest – would pay their own market rates, which are above the bank's cost, so the bank would make a profit on those loans. Germany would therefore pay no more than it does today and would subsidise no one, and no member would pay less than the market already charges it. That is an important difference from proposals under which the members with the strongest credit would, in effect, subsidise the others.

The gap between the bank's AAA funding cost and members' market rates does more than cover its lending to Germany at Bund rates. The rest stays in the bank as profit: building its capital, supporting a higher leverage ratio as its track record grows and, in time, returning dividends to the governments that own it.

Members whose borrowing costs are higher than Germany's would not get cheaper money, but they would still gain a great deal: less direct pressure on their own bond markets; loans with long tenors matched to the life of the equipment; certainty that finance will be there when a programme needs it; and the procurement discipline and pooling described in the sections that follow.

All countries participating as shareholders in the bank will clearly enjoy big cash-flow timing benefits. Governments can place substantial defence orders without having to finance them in full immediately to the extent that the bank could finance the upfront costs incurred by the suppliers. They will pay in full of course in the medium term – everything has to be paid for – but the bill will come due only when they take delivery of the equipment. Given the lead times in defence procurement, this implies a cash-flow timing advantage of several years. Borrowing from the bank also puts less direct pressure on members' own bond markets. When a government issues more of its own bonds, the extra supply tends to push up the yield it pays on all its new borrowing and refinancing, not just the defence share. When it borrows from the bank instead, the bank raises the money by issuing its own AAA-rated bonds to a broad, largely international investor base, and the pressure is shared across all members. The loan still counts as government debt, and rating agencies and investors will treat it as such: the benefit lies in yields, driven by supply and demand, not in ratings. In the case of defence programmes with export potential, the bank can also amortise the development costs over future sales to non-member countries.

How It Would Be Accounted For

This is not a way of hiding defence spending. Equipment financed by the bank would be recorded in national accounts when delivered, and loans to governments would count as public debt, as they should. What stays off national balance sheets is the bank's own borrowing and its lending to industry, just as the EBRD's and EIB's do today. The advantages are real but different: long-term, predictable finance at market rates, less pressure on national bond markets, private capital drawn in alongside public money, and contractors who can start production without waiting for governments' budgets to align.

Why This Is Not PFI

A question could be raised: is spreading payments over years simply the Private Finance Initiative by another name? The comparison does not hold. PFI transferred ownership and operating risk to private consortia, which charged a premium for bearing it, and governments then paid for 25 or 30 years at private-sector rates of return. Here the lender is owned by the governments themselves; it borrows on an AAA rating and lends at market rates, and its profits are retained to build its capital or returned to the governments that own it; the assets it finances – equipment, or the contents of a stockpile fund – are owned by the participating governments, not by a private partner; and the repayment term matches the useful life of what is bought, rather than being stretched to flatter the annual budget. PFI was expensive money dressed up as cheap money. This is honestly priced money, openly accounted for.

Multilateral banks offer transparent governance, taxpayer accountability and financial firepower. They are a tried and tested solution to the need to raise large amounts of money for important medium- and long-term projects. They are understood by governments, by markets and by those who wish to borrow. They have other advantages too: they concentrate expertise, exercise clout, and can be insulated against political interference.

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Improving Procurement

The Bank's Role

As a financial institution, the bank responds to requests from governments and companies to finance specific programmes and contracts that they have initiated. Member governments remain responsible for deciding what to buy and from whom: their military authorities and procurement agencies define the requirements, identify suppliers, run the tenders, select the winners, negotiate the contracts and monitor their execution. The bank's job is to review each financing request against its policies and the conditions set in its founding treaty, and to accept or reject it on that basis. It does not substitute itself for national procurement – but by setting clear conditions for its finance, it changes the incentives that shape procurement decisions. Member governments do not lose their sovereign decision-making prerogatives in relation to defence procurement.

A new defence bank can also improve procurement, though not by taking it over. It can hire the best defence procurement experts, creating a cadre of expertise with the ability to benchmark contracts for price and quality. This team will be selected because of their skills, and not based on nationality quotas. Its job will be to review requests for finance, so that the bank backs only decisions made on merit and not on parochial considerations.

Secondly, it can promote more effective procurement decisions, by insisting on clear commercial rules. These would include:

- International tenders (when possible) with no national preferences, at both prime-contractor and subcontractor levels;
- Pooling of orders wherever possible;
- Interoperability of equipment and systems;
- Avoidance of duplication; and
- Compliance with NATO standards.

Nations choose the opposite today because each fears that unilateral virtue will simply hand contracts to others. This is a collective-action problem, and the bank's job is to change the game: the rules bind everyone equally, and the reward for accepting them is faster, more certain finance and a place in larger, pooled orders.

As one of the key objectives of the bank is to strengthen member countries' defence industry, priority should be given to financing government purchases from member countries' industries, although exceptions will need to be made for certain kinds of equipment and services that might not be readily available among the member countries. These will have to be decided on a case-by-case basis. No financing from the bank should however be allowed to companies outside of the member countries.

If a country or a contractor does not like these rules, fine: but then they must go to their finance ministry and try to get the money from them. The finance ministry's first question is likely to be "why don't you get financing from the bank?" An answer based on protectionist self-interest will be a red flag for any neutral observer. Governments thus retain full sovereign authority over defence procurement, but trade some political discretion for lower prices and better defence outcomes.

Bank financing should not be below market rates, but rather should respect "sound banking principles". It can, however, be more prompt, more plentiful and more fairly administered than what is on offer at

the moment. For example, defence contractors would be able to get financing upfront, rather than having to wait until the final procurement contract is signed. The bank can lend to the contractor on the basis of an initial letter of intent, with a “transfer of liability clause” which means that if the government abandons the order, or tries to impose changes, the bill lands there, not with the defence contractor. Commercial banks rarely offer this, because they lack the standing to negotiate such clauses with sovereign governments and cannot assess procurement risk in-house. A multilateral bank owned by those same governments can do both. That is potentially transformative, cutting a year or more out of the procurement cycle. The contractor can start building factories, buying machines and training staff with financing from the bank based on the letters of intent so that when the deal is finally signed, it can start production at once. In the current system, everything must wait until the ink is drying on the contract and the governments have found the money for the first payment.

The bank would also seek to offer finance to smaller firms in the supply chain. In the current system, these – the weakest part of the system – are too often left to carry the greatest risk.

Defence contractors large and small therefore gain not just more orders but also a simplification of the financing process, freeing them from the political and budgetary uncertainties of purchasing governments. They will also benefit from greater transparency and depoliticisation of decision-making processes. The bank would offer a “one stop shop” for defence procurement financing – not necessarily the cheapest money, since it lends at market rates, but the most predictable and the best matched to the procurement cycle – allowing contractors to concentrate on industrial matters without spending an inordinate amount of time and senior executive energy on lobbying and on financing matters.

True, those whose profits depend chiefly on such lobbying will lose out. But more broadly the defence industry will gain from a market that is more competitive and more transparent, but also larger, more predictable and faster. The main beneficiaries will be the best performing companies, big or small. Poorly performing companies that, in the current system, can survive because of political patronage, will lose out (and rightly so).

The bank will not only lend to contractors. It can lend to governments too: again, at market rates. That means they can pay on delivery, but spread repayments over a longer period, ten or fifteen years for example, or potentially also over the life-cycle of the product being bought. The equipment would still be recorded in the national accounts when delivered; what changes is when the cash is paid and how predictable it is.

The bank can and would also encourage the pooling of orders. If two countries both want to buy a particular item, the bank can help bring the orders together, so that they are produced in an orderly, cost-minimising manner. It can avoid the two countries being played off against each other by the contractors, but it can also ensure a bigger, more predictable order, and a bigger, more predictable revenue stream for the defence contractor. That will, in turn, mean a better deal from the defence contractor for the bank and thus for governments.

The bank can also deal with the problems that beset joint procurement. These include:

- **Failure to agree military requirements.** This results in over-specified equipment that meets everyone’s often rather abstruse requirements exactly.
- **Affordability.** Governments’ fiscal constraints too often mean that the programme goes at the pace of the slowest and weakest government.

- **Workshare.** The insistence that each nation receives at least the value of work equating to their investment regardless of the industrial capability available distorts the supply chain and increases both costs and risks. No major country has yet accepted this voluntarily; the nearest precedents are NATO's common-funded programmes such as AWACS and the NATO Support and Procurement Agency, where workshare is not guaranteed. The bank's leverage is that it, not the participants, controls the financing.
- **Poor management.** Consensus trumps good decision-making. A procurement agency should make rational, risk-based decisions based on evidence.

The bank, with its independence, expertise and financing clout, could help deal with these problems through the conditions it attaches to its finance:

- It can encourage participating countries to define products based around core competencies. In some cases that would be the product, in other cases, that would be an 'entry level' product that can be developed further in stages to meet a higher specification, if that is necessary. Encouraging common military requirements will not only reduce costs but also increase defence effectiveness, by ensuring interoperability.
- Similarly, in reviewing financing requests, the bank will question over-specified requirements and favour a minimum viable product delivered at pace and scalable to meet export requirements with a growth path to meet future requirements.
- The bank will finance joint programmes only where participating countries agree on a single procurement agency with the necessary skills to deliver the programme.
- The bank can set clear cash profiles based on delivery criteria. The government remains the ultimate customer and pays in full, but because the bank finances the programme, a member's annual fiscal squeeze no longer stalls production – it changes when that member pays the bank, not when the contractor gets paid.
- It will make its finance conditional on supplier selection based on what is best for the programme, irrespective of work share based on each nation's financial contribution.

The bank will also improve access to private-sector finance, offering co-financing opportunities and encouraging other forms of debt and equity investment. It can invest directly, or indirectly, as an anchor investor in venture and/or private equity funds, initiated and managed by private-sector fund managers.

The bank would also be a vehicle for innovative new defence-equipment initiatives, such as ammunition stockpiling or equipment leasing.

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Supporting Innovation

A new defence bank can and must be a catalyst for tech innovation. The former European Central Bank head Mario Draghi set out the obstacles in his 2024 report, *The Future of European Competitiveness*.⁴ These include:

- The fragmented European market and the difficulties experienced by tech companies in selling throughout Europe.
- The costs involved in penetrating many different national markets.
- The prohibitively expensive burden of regulatory requirements.
- The lack of capital available to support tech start-ups because of the small size of the venture capital industry which is often country focused and lacks pan-European capabilities.

A new defence bank can contribute to solving these problems. It would create a pan-European market for high-tech defence systems, with the market size required to justify the scale of investment needed. Countries remain free to buy different things; the bank cannot and should not dictate requirements. But it can make the choice count: pooled, interoperable orders get the fullest support – longer tenors, contractor pre-financing and transfer-of-liability protection – while requests to finance go-it-alone purchases must be justified to the bank's procurement experts. It can and should, via its founding treaty, create an obligation on governments to work to harmonise regulations and remove unnecessary ones in the defence sphere. It can publish periodic reviews of the progress made, with the ultimate sanction of reducing the amount of financing provided to those members failing to comply with this obligation.

It can mobilise venture capital into defence-related applications. It could even invest directly in tech companies which have products required for the programmes that the bank has agreed to finance. This will de-risk the investment and encourage equity investors from the private sector. As an anchor investor, the bank could also be a catalyst for a new generation of venture capital funds. Sitting at the centre of the defence-finance ecosystem it will have unparalleled understanding of future defence trends and the necessary technical knowledge to advise these new funds and de-risk their activities.

These investments could expand to support companies developing dual use technologies and to those developing products for the civilian market. The fact that spin-off technologies would potentially have significant commercial applications could significantly increase the pool of money going into the sector as well as provide a source of income for the bank itself.

In this field, the bank would cooperate with existing institutions such as the Luxembourg-based European Investment Fund (EIF) and the European Defence Agency in Brussels.

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⁴ Mario Draghi, *The Future of European Competitiveness*, report for the European Commission, September 2024: https://commission.europa.eu/topics/eu-competitiveness/draghi-report_en

Building Resilience

One of the gravest weaknesses of European defence is low stockpiles. Only the United States maintains the stocks of munitions, spare parts and equipment needed to fight a protracted war, and as the conflict in the Gulf has shown, even American stockpiles deplete alarmingly quickly. The lack of stocks weakens defence and erodes the credibility of our deterrence. That greatly increases the risk of nuclear escalation.

Hence the increasing interest in stockpiles that will be financed, owned and deployed solely by European NATO members, and perhaps allies such as Canada and Ukraine. A new defence bank is an ideal vehicle for this purpose because it has everything that is needed. This includes significant financial firepower, a sound multilateral governance structure and an international staff of highly qualified experts combining financial and military expertise.

As an example, we could imagine a group of countries deciding that they need to stockpile a great number of artillery shells. These military authorities (the “Participants”) would define the common specifications and launch a competitive tender, which the bank would review before agreeing to finance the purchases. The bank would create a new, segregated structure (the “Stockpile Fund”), owned by the countries concerned. This fund would purchase and hold the ammunition. Because the fund is owned by the participating countries, statisticians may well record its assets and borrowing as theirs, in proportion to the risks each bears. The bank would lend to the fund to finance these purchases in exchange for a commitment from the participating countries to pay an annual access charge: in effect a subscription. This subscription fee would cover above all the cost of the ammunition, through an annual depreciation charge. Even ammunition does not last forever. It would also cover the costs of storing and maintaining the ammunition. Finally, it would cover the bank’s financing costs.

Participants would have the absolute right at any time to purchase from the fund their share of the ammunition held in the stockpile. They would pay the initial acquisition price minus the annual depreciation charges already paid. They could also buy and sell their future purchase rights, not only to other participant nations, but also to other allied nations as well. If no use is made of the stockpiled ammunition by the end of its useful life it will be liquidated, by which time the fund will have recovered the full purchase cost through the annual access charges.

The ability of the bank to lend to the participants directly guarantees the timely payment and minimises the financial risks for the bank of managing the stockpiles.

Such a structure offers two main benefits. First, the cash cost to the participants of purchasing the ammunition will be spread over the useful life of the ammunition. That is economically sensible, and mitigates the immediate budgetary impact of the rearmament effort that we need to make. In addition, a joint stockpile managed in a transparent way by a third party, the bank, would allow full flexibility to rapidly reallocate the goods in the stockpile among member states without requiring case-by-case financial negotiations. Countries would have the right to agree to sell, or not, but the price of any trade would be pre-determined.

The same principles could be applied to the financing of other jointly-owned assets that benefit all members. These could include command, control and communication assets, intelligence-gathering tools and military transport capabilities. If the shareholders so wish, this could be even extended to other equipment needed for civilian security purposes such as firefighting aircraft.

The assets would be purchased by the bank at the request of some or all member nations and would be held on the balance sheet of the special entity created to buy and hold these assets on behalf of the group of members that will have mandated the bank to do so.

In order to allow extensions – such as to cover specialist firefighting planes – it would be sensible for this defence bank to follow the successful principle used when the European Bank for Reconstruction and Development was created. In the EBRD’s case, a relatively open set of initial operating guidelines – as proposed here – allowed it to evolve as circumstances changed.

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Making It Happen

At the end of his *General Theory*, John Maynard Keynes asks whether the fulfilment of his ideas was a visionary hope. Needless to say, being Keynes, he answers his own question, while denying that he has done so. He is fully cognisant that there is a risk that “the interests which they will thwart [are] stronger and more obvious than those which they will serve”. But he ends on an optimistic note, that “soon or late, it is ideas, not vested interests, which are dangerous for good or evil.”

That optimism is needed here, and there is evidence for it. The ideas contained in this report are not completely new. In 2024 a group of experts led by the former British army officer Rob Murray proposed a Defence, Security and Resilience Bank (DSRB) in a report for the [Atlantic Council](#).

Separately, in January 2025 the authors of this report, along with former British defence chief Sir Nick Carter, argued in the *Financial Times* for a slimmed-down version of this project, confined solely to European NATO members. The case was also made later in [the Times](#) and has been pushed many times in private.

There are other signs of progress. [In May 2025 the European Union launched](#) its Security Action for Europe (SAFE) facility, which provides up to €150 billion in long-maturity loans to member states for defence investments. The use of the EU’s creditworthy status is appropriate, and this step is to be celebrated. It is, however, only a small step. Specifically, the SAFE plan allows only one euro to be lent for every euro borrowed, without the benefit of leverage that a bank enjoys. That is an inefficient use of the EU’s borrowing power and creditworthiness. SAFE lending is also confined, at least for now, to EU members. This has led to protracted disputes with the UK over British access to the programme. SAFE also does little to deal with the endemic problems of defence procurement, save for encouraging the pooling of orders. The negotiations on the EU’s next budget will be difficult enough without having to expand SAFE further – yet that is what would be needed in the absence of another way of boosting EU countries’ defence spending.

In March 2026, Britain, the Netherlands and Finland issued [a joint statement](#) announcing their interest in the Multilateral Defence Mechanism. This aimed to “aggregate demand, drive joint procurement, accelerate defence investment, and increase the availability of critical capabilities such as munitions”. Again, this is to be welcomed. In the run-up to NATO’s Ankara summit in July 2026, these countries, joined now by the useful addition of Poland, issued an [update](#), highlighting “significant progress” and announcing their intention to build a broader coalition of members, and to ensure that “emerging approaches to international defence financing” were “aligned and complementary”. This is all useful and hopeful, but the number of countries should be larger. It is also unclear whether it will have defence procurement expertise, or simply finance programmes run by individual governments.

At the same Ankara summit Canada, with the leaders of Albania, Belgium, Greece, Latvia, Luxembourg, Romania, Turkey (Türkiye) and Ukraine, announced their “shared intention” to establish the DSRB. This too is welcome, and Canada’s leadership deserves credit. As currently described, however, the DSRB is focused on supporting small and medium-sized defence enterprises, chiefly by guaranteeing commercial-bank lending. That is a worthwhile aim, but a narrow one, and guarantee schemes carry a familiar risk: if projects succeed the banks are repaid, and if they fail the taxpayer pays. It is not yet an institution commensurate with the challenge we face.

There is, therefore, enough evidence of movement, in many countries, to believe that the creation of a defence bank, along the lines outlined here, is not a flight of fantasy, but a plausible reality. All of the existing proposals have strengths and weaknesses. The British-led consortium is more creditworthy, while the Canadian-led proposal has a bigger combined defence budget.

So far, however, none of the new defence-finance projects have the political and financial firepower needed for success. They are not structured to use financial leverage effectively, despite in some cases having a majority of AAA-rated shareholders.

A new initiative should include the biggest countries, both in terms of financial credibility, such as Germany, as well as defence credibility, such as France, the UK and Ukraine. A new initiative should certainly be open to Canada, which has shown real leadership in this area, and Poland, whose commitment to defence is well-proven. It must be able to involve other allies. That means it cannot be solely an EU project. It must be leanly run, operating in the interests of national security, not as a provider of sinecures and subsidies, or as a means of political grandstanding. It must have the clout to stand up to defence giants and to oppose protectionism and parochialism.

The blunt truth is that there is only room for one new AAA-rated defence institution on the international bond markets, and it needs to have a critical mass of backers. Parallel initiatives, however well-intentioned, divide that critical mass and risk becoming a diversion as much as a help. SAFE will never attract full-throated support from non-EU members. On their current trajectories, neither the Canadian-led DSRB nor the British-led MDM looks likely to incorporate the other.

It is vital to bring on board the big European countries: Germany for its financial heft, France for its military clout. Italy would also add weight to the project. With these countries, plus Britain and Canada on board, the new bank has a serious chance of success. But to gain these countries' support, it is essential to produce a single, clear, workable plan that has benefits for all countries involved. They will not simply sign up to a blueprint drawn up elsewhere, least of all one headquartered outside Europe. They must be involved in its creation from the start, alongside the European Commission and NATO.

It is therefore time to pause and agree some foundational principles. Once serious countries have given serious backing to these, the other details can be worked out. Borrowing needs unity; the lending can reflect diversity. That means asking the UK and Canada to take a step back from promoting their own blueprints. This will take political courage: pride of initiative and authorship must not stand in the way of an institution that could become an essential pillar of our collective security.

There is no time to waste. Each of the existing initiatives has something to contribute; what none of them can do alone is reach the scale that the task demands. That task is defending our freedom and deterring our enemies, and it is worth setting aside questions of authorship to get it done. If we cannot reach agreement on the financial battlefield, what chance do we have on a real one?

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Annex A – A Road Map

These draft principles should secure speedy progress among backers of the DSRB and the MDM, as well as countries that so far support neither project. They should agree on:

- 1) **Membership.** Identify founder-shareholders (chiefly Canada and European NATO), plus countries with special privileges (Ukraine).
- 2) **Purpose.** Set the aims: to increase spending on defence, to spend it better and faster, and to finance the rebuilding of member countries' defence industries.
- 3) **Capital structure.** This should be similar to other multilateral institutions, with £100 billion of subscribed capital as a starting point, of which 10% (£10 billion) would be paid in by member governments over three years and 90% callable. Leverage would start low and rise with the bank's operating track record, up to a ceiling of 2.5 times subscribed capital – 25 times paid-in capital.
- 4) **Governance.** Again, this would be similar to other multilateral financial institutions, with a board of governors and a board of directors (non-resident) composed of representatives of member countries. The presidency and nationality of top executive positions to be decided in negotiation between member countries; other staff to be hired based on competence without nationality quotas.
- 5) **Operations.** The bank would formally adhere to sound banking principles: no subsidies, favouritism or boondoggles.
 - It would lend to member governments for purchase of defence equipment produced in member countries (with limited exceptions during a transitory period).
 - It would lend at market rates to ensure that AAA-rated countries are not penalised.
 - It would lend or provide other financing support to defence companies from member countries only, including a focus on SMEs. These loans would also be made at market rates.
- 6) **Key conditions:**
 - Joint procurement when possible.
 - Open tendering focusing on member countries, including at subcontractor level.
 - No unnecessary duplication of existing systems.
 - NATO standards.

All loans and investments would be targeted to specific procurement contracts or programmes with clearly defined use of proceeds. The bank would operate with sufficient flexibility to allow for financing of stockpiles or development of major new programmes/systems or other yet unidentified need. The bank would be leanly run with a maximum headcount of 300, outsourcing operations to partner banks and organisations where possible.

How the Bank Would Be Established

Multilateral banks are created in a well-understood sequence: political declaration, treaty negotiation, signature and ratification, capitalisation, operations. The sequence can be run quickly when the will exists. The EBRD was proposed in October 1989, its founding agreement signed in May 1990, and it opened in April 1991 – eighteen months from idea to first loan. We propose the same path, in four steps.

Declaration. Senior political leaders of a potential founders' group – we suggest the UK, Canada, Germany, France, Italy, Poland, the Netherlands, Finland and Ukraine, with the European Commission and NATO as observers – would meet to agree the foundational principles. These would be published in a short joint declaration, which would also mandate a negotiating conference with a deadline and invite the sponsors of the MDM and the DSRB to bring their work into it. Decisions on the nationality of the bank's leadership and the location of its seat should be made as part of this process.

Treaty. A negotiating conference, supported by a small secretariat seconded from finance ministries, would draft the Articles of Agreement. Most of the text can be borrowed from the EBRD and AIIB articles; negotiating time should go on what is new – the procurement conditions, the transfer-of-liability mechanism and the stockpile-fund structure.

Ratification and capital. The treaty should enter into force once countries holding two-thirds of subscribed capital have ratified, as the EBRD and AIIB treaties did, so that the slowest parliament does not set the pace. The rating agencies should be engaged before signature, so that the Articles are drafted with the AAA rating in mind and an indicative rating is available at launch.

Operations. The Board of Governors officially appoints the President and management and makes the first capital call. To avoid a dead year, early lending can be done through or alongside the EIB and national development banks while the bank builds its own treasury. The inaugural bond issue and the first Stockpile Fund follow in the second year, after which the leverage ratio can begin to rise with the bank's track record.

Key Decisions for the Founders

The negotiating conference will need to settle a small number of questions that the principles leave open. Our recommendations, in brief:

- **Membership tiers.** Founders and later members on the same terms; Ukraine as a shareholder from the start, with its own borrowing guaranteed by other members until its credit standing allows otherwise. The EU should be able to take a capped stake, as it does in the EBRD, so that the Commission is a participant rather than a bystander.
- **Capital formula.** GDP-weighted subscriptions, with a ceiling of around 20% so that no country dominates. Companies can compete for contracts financed for any member, not only the country where they are based. A member that fails to meet a capital call loses voting rights and access to new lending, not membership.
- **Governance.** Voting by capital share, with a supermajority and no single-country veto for constitutional matters. A merit-based, single-term presidency rather than a permanent entitlement of the largest shareholder.
- **The existing initiatives.** MDM members become founders and its procurement work feeds the bank's conditions; the DSRB's SME facility becomes a business line of the bank; SAFE remains an EU instrument alongside which the bank can lend.
- **Rating.** Preferred-creditor status granted in the Articles, a legally unambiguous call mechanism, a conservative opening leverage ratio and a loan book weighted towards sovereign contracts in the early years.

Indicative Timetable

Months are counted from the founders' declaration. The timetable assumes signature within three months of the declaration and full operations nine months after signing.

Month	Milestone	Who
0	Founders' group adopts the foundational principles in a joint declaration and mandates a negotiating conference	Heads of government
0-3	Articles of Agreement negotiated, drawing on the EBRD and AIIB templates; capital formula and seat agreed	Negotiating conference
3	Treaty signed	Founding governments
3-9	Ratification; treaty enters into force once countries holding two-thirds of subscribed capital have ratified; rating agencies engaged	Parliaments; preparatory secretariat
9-12	Board of Governors appoints President and management; first capital call	Board of Governors
12	Bank fully operational (nine months after signing)	Management
12-24	Inaugural bond issue; first Stockpile Fund; leverage ceiling reviewed against track record at end of year two	Management; Board of Directors

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Annex B – An Illustrative Sequence: A Drone Purchase

The steps below show, in simplified form, how a member government might use the bank to buy drones.

1. **The requirement.** A member government decides to purchase drones. It defines broad specifications and identifies potential suppliers; what to buy, and to what specification, remains the government's decision.
2. **First approach to the bank.** The government approaches the bank for financing and to understand the conditions under which the bank could finance the purchase. Because bank staff are in regular dialogue with all member countries, they are well placed to identify others with similar requirements, and the bank may recommend teaming up with one or more of them to pool orders.
3. **Tender preparation.** The lead government, with input from any partner governments, prepares the tender documents and a shortlist of suitable prime contractors, and identifies potential subcontractors.
4. **Bank review.** Bank staff review these proposals to ensure that they meet the bank's conditions. The review also enables them to identify, together with the prime contractors, which subcontractors might need financing directly from the bank. Some SME subcontractors may need a combination of debt and equity to have the financial resilience to be credible suppliers.
5. **Award.** After the tender, the purchasing government chooses the prime contractor and the key subcontractors. Bank management reviews these decisions to ensure that they are compatible with the bank's conditions and are based primarily on performance and price.
6. **Letter of intent.** Once the bank's board confirms its willingness to finance the contract, the purchasing government and the chosen prime contractor prepare a binding letter of intent, co-signed by the bank. This allows the bank to provide immediate financing to the prime contractor and its subcontractors, so that they can build up capacity before the detailed contracts are signed.
7. **Transfer of liability.** The letter of intent includes a binding transfer-of-liability clause. If a purchasing government changes its mind, any liability towards the bank that the contractor has incurred under the letter of intent passes to that government, protecting both the contractor and the bank.
8. **Contract and payment.** Once the detailed contracts are agreed between the purchasing governments and the contractors, the bank finances the payments due from the governments. Each government then repays the bank over the useful life of the drones, at its own market rate.

This is a simplified illustration of a fairly straightforward case. There will be many variations on it, which is why the bank's founding treaty should give it wide flexibility to adapt its support to the varied and evolving needs of its members.

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