Bridging the Gap:

How a *European Security Fund* can enable defence investments for asset managers

23 June 2026

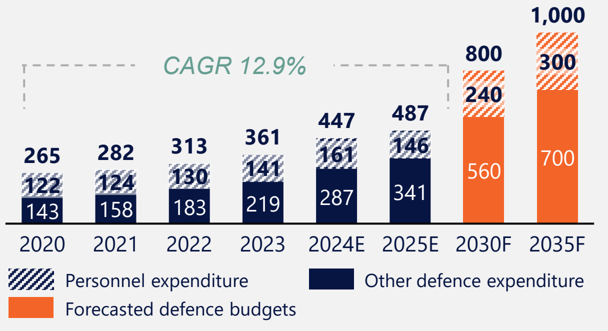
Surge in European demand

Europe's defence landscape is undergoing a structural shift. Geopolitical tensions and security risks have led NATO to strengthen its commitments, targeting 3.5% of GDP for defence spending and 1.5% for resilience and infrastructure. This paper focuses on the 3.5% target, as this most directly shapes defence spending growth and industry demand. As a result of this new target, defence expenditure is expected to surge for the Netherlands and the rest of NATO Europe.

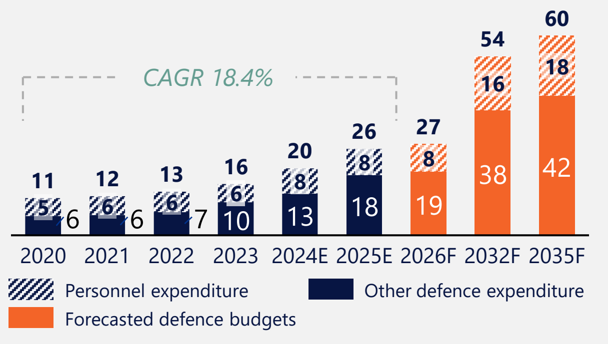
Beyond the scale of investment, **composition of spending is also shifting**. Traditional personnel-heavy budgets are moving toward technology-driven allocations. In the Netherlands, personnel costs fell from 48.5% of defence spending in 2020 to 30.6% in 2025, while operations, maintenance, and R&D rose from 26.2% to 40.3%. This signals a move toward advanced systems and greater operational capability. Comparable shifts are evident across the rest of NATO Europe.

Both **the significant increase in government budgets and shifting spending priorities are creating sustained demand for defence products and technologies**. Modernisation and innovation are becoming central to the sector, presenting opportunities for industry players and investors to engage in a rapidly evolving market.

Defence expenditure and budget NATO Europe, (€ bn, 2020-2035F)



Defence expenditure and budget NL, (€ bn, 2020-2035F)



Facts and figures:

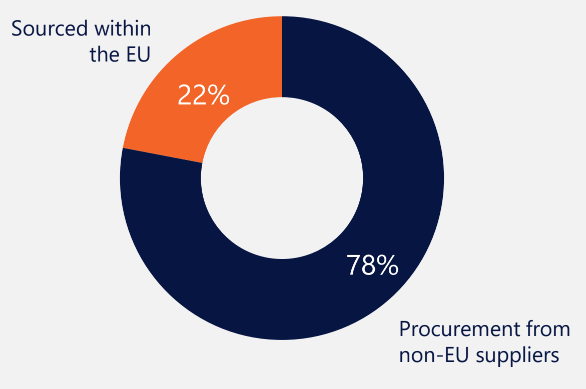
- Defence budgets across **European NATO states** are projected to **double by 2035**, reaching approximately **€1 trillion**
- For the **Netherlands**, defence spending stood at 2.5% of GDP in 2025, equivalent to €26 billion. By 2035, defence spending is expected to rise to around **€60 billion**

Europe's **surge in demand** for defence products exposes its dependence on **U.S. capabilities** and limited production capacity. The **Draghi report underscored this**, citing heavy reliance on U.S. procurement and significant industry fragmentation, which limits its scale and efficiency.

In response, the EU and its member states have launched several initiatives aimed at strengthening the defence sector. One of the most prominent is **ReArm Europe**, a program designed to accelerate defence investment, boost manufacturing capacity, and build a **unified industrial base**, reducing reliance on external partners.

The 2025 **U.S. National Strategy pushes Europe even more to assume greater defence responsibility**, driving higher military spending, accelerated industrial capacity expansion, and **stronger "buy European" policies**.

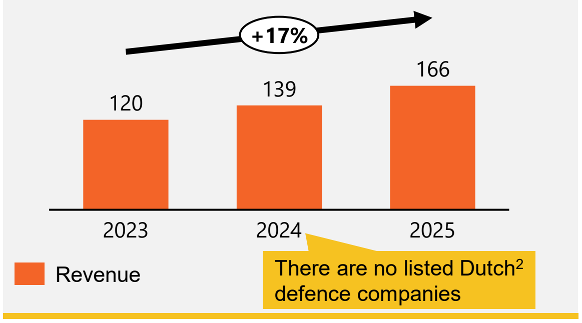
Defence procurement, (Feb 2022- Jun 2023)



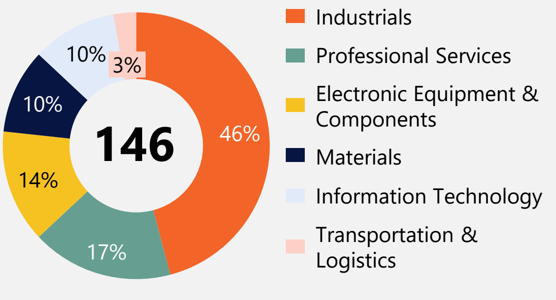
Production gap in European supply

For this analysis, we examine the revenue of listed defence companies. Defence companies include both pure-play defence firms and dual-use companies that generate defence-related revenue alongside civilian activities, such as an airplane manufacturer. Given limitations in data availability and consistency for non-listed companies, this analysis focuses on listed entities.

Defence turnover from top 100 listed defence companies (€ bn, 2023-2025[1])



Industry overview of companies with a Dutch presence and defence focus



Estimated **defence revenue** from the top 100 **European listed defence companies** is approximately €139 billion as of 2024, an increase of 16% in comparison to 2023.

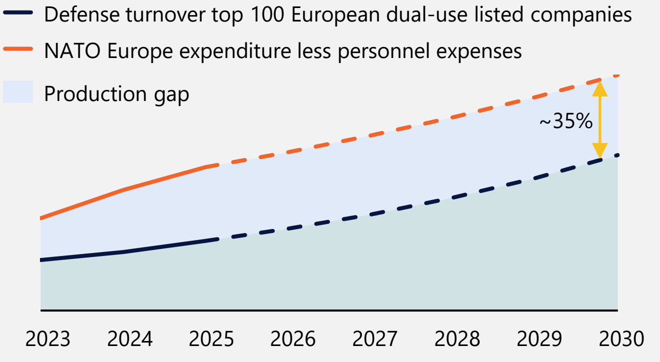
The **absence of Dutch-listed defence companies limits sector visibility** and restricts institutional investors who mainly allocate to liquid listed equities. While alternatives like debt financing exist, they are typically less liquid and can fall outside institutional mandates, leaving overall investment capacity by asset managers in the Dutch defence sector constrained.

Despite recent growth and investments, **Europe's defence production capability still operates below the scale needed to meet rising demand**. The current pace of industry expansion remains constrained by longstanding structural limitations, leaving a clear gap between today's capacity and Europe's strategic objectives.

Decades of **underinvestment** have left Europe with significant gaps in its defence production capabilities. An EC study found that **40% of defence SMEs struggle to access financing**, due to regulation, lengthy procurement cycles and a **lack of dedicated defence investment vehicles**. As a result, SMEs face a €4 billion financing gap, lagging more mature ecosystems like the US. **Europe risks falling short of its security ambitions** unless private and public investments accelerate, manufacturing capacity expands, and long-term contracts are provided to producers.

Addressing this production gap requires more than incremental improvements from established players. **Listed defence companies alone cannot deliver the needed scale and agility** to close this gap. **Funding must also reach start-ups, scale-ups and SMEs**, which are essential for innovation, flexibility and a resilient and competitive industrial base in Europe and the Netherlands. For asset managers, these companies present significant investment challenges.

Gap between defence turnover top 100 EU listed defence companies and NATO defence expenditure less personnel expenses (€ bn, 2023-2030F)



Note: (1) For companies without published FY25 annual reports, LTM figures were used. This applies to a limited number of companies included in the analysis; (2) Airbus SE is legally incorporated in The Netherlands, but its effective centre of management and leadership is in France

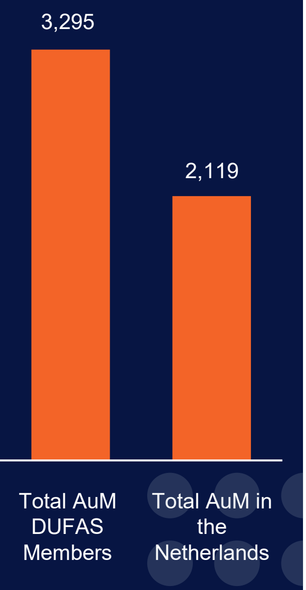
Sources: Annual reports, Capital IQ, company websites, European Commission, NATO, NIDV and KPMG Analysis.

Asset managers and the defence sector

Asset managers have substantial investment capacity and significant capital available. In 2024, DUFAS members managed a total of €3,295 billion in assets, while the total AuM in the Netherlands was €2,119 billion. Because of this scale, asset managers focus on large-ticket investments rather than small-scale opportunities due to transaction costs and risk-return rates. Furthermore, their investment strategy is **mostly limited to liquid assets**. Listed companies typically have more extensive transparency requirements, which means due diligence tends to require less effort from both parties. As a result, asset managers often lack both the mandate and the operational processes to invest directly in start-ups, scale-ups or SMEs. These companies in turn lack the absorption capacity for long-term, high-ticket investments. Taken together, a **lack of scale in a relatively fragmented market**, a **higher risk-reward ratio**, more **complex due diligence**, **unclear compliance rules**, and **lacking internal expertise** on the sector, make the defence sector a less viable investment than other sectors.

Asset managers are already investing in defence companies, demonstrating that the sector is not excluded from their portfolios. For many, ESG considerations are an integrated part of the due diligence process, to assess whether these investments align with their sustainability framework. However, their direct involvement is mostly limited to listed companies, and therefore, asset managers generally allocate less capital to privately held or non-listed defence businesses due to mandate and process constraints.

Facts and figures (€ bn, 2024):



Asset managers follow **different ESG policies**, determined within legal boundaries and based on their own and their clients' preferences. A DUFAS inventory among members shows that most managers are permitted to invest in defence-related companies but apply exclusion policies and due diligence processes in which ESG considerations are integrated. Only a few exclude the entire defence sector[1], many instead focus on prohibiting investments in controversial weapons, in accordance with laws and international treaties[2]. Asset managers that exclude arms and the defence sector as a whole are still in a position to invest in other defence and security related activities such as critical infrastructure; however, these investments are beyond the scope of this paper.

From a sustainability perspective, **defence investments are ambivalent**: they support peace and civilian protection but also involve weapons that can cause significant harm. For this reason, many asset managers do not fully exclude defence investments. This aligns with recent European Commission guidance recommending case-by-case assessment[3] and the broader shift in investor sentiment[4,5].

Legislators and supervisors provide mixed signals. The AFM has expressed a preference against labelling defence investments as ESG[6], while the European Commission states that defence can contribute to peace and is compatible with the EU sustainable finance framework. This creates ambiguity for asset managers. Still, the inventory shows that **ESG criteria do not necessarily rule out all defence investments**, and many managers still see room for certain defence-related holdings based on client needs or investment policies.

Notes: 1) Of the 17 asset managers surveyed, 2 explicitly exclude the defence industry, while 15 allow such investments. 2) SFDR principal adverse impact indicator No. 14 provides a definition of controversial weapons. Controversial weapons include cluster munitions, anti-personnel mines, chemical weapons and biological weapons (excluded under international treaties). Many asset managers also apply exclusions for involvement in white phosphorus and nuclear weapons. 3) European Commission: Commission Notice on the application of the sustainable finance framework and the Corporate Sustainability Due Diligence Directive to the defence sector. 4) Responsible Investor: ESG exclusions not preventing European defence investments, say French investors. 5) FD: Asset managers relax rules on investing in weapons. 6) Investment Officer: ESG funds trade ethics for defence.

Sources: DUFAS, EFAMA

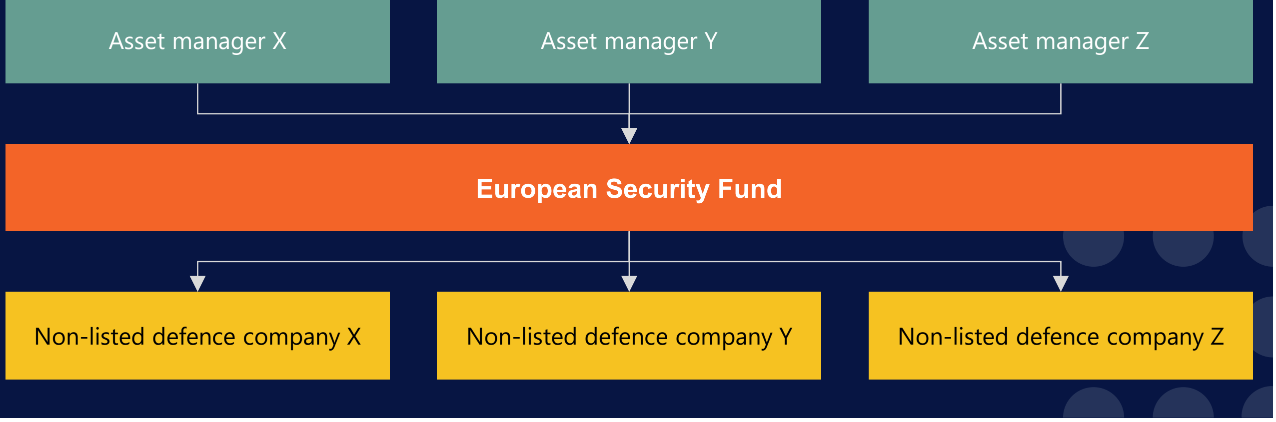
A possible solution to the financing gap

Growing defence demand increases the **need for private capital investments**, yet significant **barriers remain**. The European defence sector is fragmented and characterized by many SMEs, creating a landscape with limited scale and uneven maturity. At the same time, most asset managers lack both the mandate and operational capacity to invest directly in SMEs, while these companies themselves often can not absorb large, long-term investments. When combined with relatively higher risk profiles, complex due diligence requirements, evolving compliance frameworks, and limited sector-specific expertise, these constraints reduce the sector’s attractiveness for investments by asset managers.

A possible instrument to increase the attractiveness of investing capital into the European defence sector is a **European Security Fund (ESF)**. The ESF, established by the European Commission and/or the European Investment Bank, would provide a **structured financing instrument** aligned with broader EU-ambitions to **mobilise private capital** across the economy through the Savings and Investments Union (SIU). By aggregating projects, pooling risk and achieving sufficient ticket size, an ESF would create an investable platform that meets asset manager requirements helps mobilise private capital for the defence sector.

The ESF could operate alongside existing public instruments such as the European Defense Fund and financing by the European Investment Bank, providing a source of private capital investment alongside public initiatives. For the ESF to succeed, it must be **designed to meet the needs of both investors and participating companies**. Key considerations should include robust governance, risk-sharing arrangements, transparency, compliance with human rights and international humanitarian law standards, and an investment scope that delivers adequate expected returns.

Example of fund structure



DUFAS: Dutch Fund and Asset Management Association.

Since 2003, DUFAS has been committed to a healthy asset management sector in the Netherlands. DUFAS has more than 50 members: from large asset managers who invest Dutch pension and insurance assets to smaller, specialist asset managers. DUFAS increases awareness of the social relevance of investing, helps to develop sector standards and represents the sector in the implementation of new laws and regulations. In addition, DUFAS is committed to a single European market with equal regulations.