

EUROPEAN DEFENSE SPENDING TRILEMMA

SECURITY, AFFORDABILITY AND
DOMESTIC POPULARITY:
THE CASE OF ITALY

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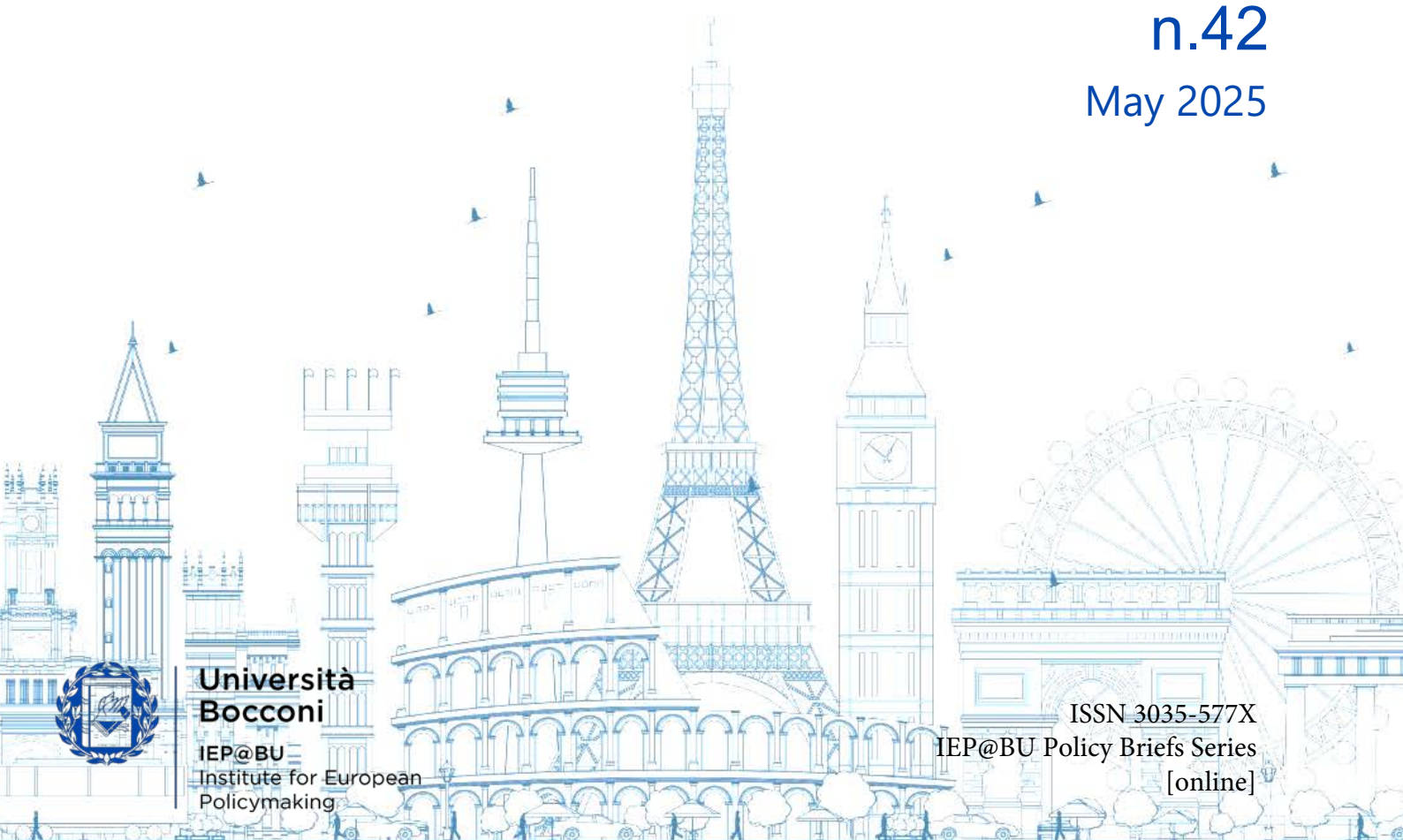
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Executive Summary^{1 2}

Recent geopolitical developments (Russia's war in Ukraine, growing instability in the Middle East, and the U.S. strategic pivot toward the Indo-Pacific) require European countries to rethink their defense strategies.

In this context, reinforcing NATO's collective security has become increasingly urgent, yet in this effort European countries are constrained by a structural trilemma involving the pursuit of security, fiscal stability, and domestic political support.

Inaction on the defense front risks further weakening the Transatlantic alliance, particularly if NATO's defense spending benchmark rises from 2 percent to 3.5 percent of GDP.

However, rapid and indiscriminate budget increases could trigger significant risks, including inflationary pressure, fiscal imbalances, and domestic opposition.

To navigate these challenges, we propose a strategy based on three integrated components. First, defense spending should increase gradually and selectively.

Although European defense budgets remain below the 2 percent threshold, there is clear room for growth. However, these increases should focus on strategically relevant areas such as research and development, joint procurement, and operational readiness.

When properly designed, such investments can yield positive macroeconomic outcomes, particularly in high-tech industrial ecosystems.

Second, structural reforms are essential in three key areas: enhanced European cooperation in procurement and operations, the creation of national innovation agencies inspired by US DARPA, and the modernization of defense planning, financial governance, and personnel management.

These reforms would improve efficiency, interoperability, and long-term strategic effectiveness. Finally, the accounting perimeter of defense should be updated.

European countries should include within their defense budgets all expenditures that substantively contribute to NATO's core missions, such as cybersecurity, critical infrastructure protection, and resilience against hybrid threats.

This methodological adjustment would reduce the gap between actual and declared efforts, enhancing national credibility and legitimacy.

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We apply this strategy to Italy. Despite being the EU's third-largest economy, Italy allocates only 1.51 percent of its GDP to defense. Raising this share to 2 percent or 3.5 percent would require increasing the defense budget from €28 billion to €40 or even €70 billion.

Without accompanying structural reforms, such growth would be politically unsustainable and economically counterproductive.

Therefore, we advocate a phased, reform-oriented, and strategically coherent approach that aligns defense effectiveness with fiscal responsibility and democratic legitimacy.



Introduction

Strategic dynamics and risks in 2025 demand urgent action from European countries to strengthen NATO's collective security. Russia's ongoing war in Ukraine, over three years from its start, has exposed Europe's military weaknesses, shortfalls and vulnerabilities. Instability in nearby regions, from Northern Africa to the Middle East, the Balkans to the Caucasus, adds additional security threats and political challenges, spanning from energy to migration. Finally, the U.S. administration uncertain commitment to European security is forcing its Allies in the Old Continent to bear greater responsibilities for their own defense.

Yet, a fundamental trilemma constrains European governments: they must choose between security (robust defense capabilities), affordability (fiscal stability amid high debts), and domestic popularity (public support at home), as achieving all three simultaneously remains unattainable.³

Inaction risks further weakening the Transatlantic link, leaving NATO vulnerable to both hybrid and conventional threats – let alone nuclear escalation. As NATO's 2% GDP defense spending target, set in 2014, is likely to be raised to 3.5% at the 2025 NATO summit in The Hague, European countries confront stark trade-offs.⁴

In this context, recent data from the Osservatorio sui Conti Pubblici Italiani (Università Cattolica di Milano) highlight the scale of Italy's challenge: in 2024, national defense spending is projected at just 1.5% of GDP, with over 59% of the budget allocated to personnel costs⁵.

In light of these considerations, we propose a three-tiered strategy. First, defense spending should increase gradually and selectively, with a focus on high-multiplier domains such as R&D, procurement and operational readiness.

Second, structural reforms – both national and EU-wide – are essential in procurement coordination, strategic planning, and personnel management.

Third, the accounting perimeter of defense must be updated to reflect current security needs, including expenditures that substantively support NATO's missions but are currently excluded from defense budgets.

We apply this strategy to the case of Italy, where the trilemma manifests with particular acuteness. On one hand, Italy plays a central role in the strategic geography of the broader Mediterranean, with

³ For a analytical discussion of the issue, see Eugene Gholz and Harvey M. Sapolsky, "Restructuring the U.S. Defense Industry," *International Security*, Vol. 24, No. 3 (Winter 1999/2000): 5-51.

⁴ "NATO discusses civil defence spending target, Swedish PM says," *Reuters*, April 14 2025.

⁵ Arcano, R., (2024) Osservatorio sui Conti Pubblici Italiani. (2024, February 21). *La spesa italiana per la difesa: Quanto lontani siamo dal requisito del 2% del PIL?* Università Cattolica del Sacro Cuore. <https://osservatoriocpi.unicatt.it/ocpi-pubblicazioni-la-spesa-italiana-per-la-difesa-quanto-lontani-siamo-dal-requisito-del-2-del-pil>



growing responsibilities in managing migration flows, ensuring energy security, and countering hybrid threats.

On the other hand, its defense spending remains modest – 1.55% of GDP – while public debt remains structurally high. In such a scenario, a linear increase in military expenditure risks triggering inflationary dynamics, diminishing the real impact of investment, generating social-political tensions, and undermining domestic political cohesion. Our three-tiered strategy applied to Italy leads to the following steps.

First, Italy must increase its defense spending, but selectively and gradually, with a focus on high-multiplier investments such as research, innovation, and procurement.

Second, structural reforms are needed to improve the efficiency of expenditure through enhanced European cooperation (which Italy already extensively pursues), multi-year strategic planning, and personnel reorganization.

Third, select areas of public spending, such as cybersecurity and critical infrastructure protection, should be logically reclassified under the defense budget, thus strengthening Italy's defense posture without worsening fiscal balances.

Although centered on Italy, this analysis offers broader implications for European countries grappling with the tension between security imperatives, fiscal constraints and political legitimacy.

The proposed approach, which combines a calibrated increase in defense spending, institutional reform and a redefinition of defense accounting, constitutes a replicable model adaptable to diverse national contexts. The Italian case thus serves as a strategic template to inform policy decisions across the Alliance.



Chapter 1: Europe's Defense Trilemma and NATO's Evolving Demands

This chapter discusses the fundamental trilemma European countries face when it comes to defense. European countries can pursue security, budgetary stability and domestic popularity.

However, most countries cannot pursue all of them simultaneously. This is particularly challenging as growing U.S. expectations towards Europe in the realm of defense will likely lead to a higher NATO target for defense expenditure, from the 2% agreed in 2014 to 3 or 3.5% at the 2025 Hague Summit this summer.

The Defense Trilemma: Security, Stability, Popularity. The European defense trilemma captures the core challenges facing European governments: most countries cannot fully maximize security, budgetary stability, and domestic popularity without compromising at least one.

Security demands increased defense spending to counter threats like Russia's aggression, hybrid and cyberattacks, and regional instability.

Yet, higher defense spending may strain budgetary stability, particularly for countries like Italy, France, or Spain, where public debt exceeds 100% of GDP. Even Germany, last February, after approving a massive increase in its public expenditure to fund its defense saw its long-term yields increase.⁶

Diverting funds from social programs – healthcare, pensions, education – risks eroding domestic popularity, as citizens prioritize immediate welfare over long-term security. The picture is obviously mixed, however, a recent analysis from Belgian think tank Bruegel's Guntram Wolff, Armin Steinbach and Jeromin Zettelmeyer unquestionably highlights the challenge: in 2024, military spending by European NATO members is highly correlated with their capital's distance from Moscow.⁷

This trilemma, in other words, is not merely theoretical. Inaction exacerbates vulnerabilities: underfunded militaries weaken NATO's collective posture, strained budgets threaten economic recovery, and unpopular policies fuel political instability – which could be further exploited by Moscow to undermine European security.⁸

NATO's Evolving Spending Demands. NATO's 2% GDP defense spending target, formalized at the 2014 Wales Summit following Russia's annexation of Crimea, aimed to ensure equitable burden-sharing and credible deterrence.⁹

⁶ Johanna Treeck, "Germany's spending bazooka propels euro and borrowing costs higher," *PoliticoPro*, March 6 2025.

⁷ Guntram B. Wolff, Armin Steinbach and Jeromin Zettelmeyer, "The Governance and funding of European rearmament," *Policy Brief* (Brussels: Bruegel, 2025)

⁸ Seth G. Jones, "Russia's Shadow War Against the West," *CSIS Brief* (Washington, DC: Center for Strategic and International Studies, 2025).

⁹ Tim Haesebrouck, "NATO Burden Sharing after the Wales Summit: A Generalized Set Qualitative Analysis," *Defence and Peace Economics*, Vol. 33, No. 6 (2022): 637-654.



The accompanying 20% guideline – allocating 20% of budgets to equipment and research and development (R&D) – underscored the need for modernization over personnel-heavy budgets.¹⁰ By 2023, 11 of 31 Allies met the 2% target, up from three in 2014, but Europe's collective spending still averaged 1.7%, a €100 billion shortfall.¹¹ By 2024, 23 Allies met the 2% guideline, and NATO Europe's collective spending reached 2.02% of GDP, amounting to over \$485 billion.¹²

Discussions for a 3.5% target by 2025, spurred by Ukraine's fallout and hybrid threats, would widen this gap to €200 billion, requiring transformative fiscal policies and political commitments.

The 2% scenario represents NATO's current baseline, sufficient for incremental modernization but strained by new threats – especially in a context in which the U.S. wants European countries to contribute more significantly to their defense.

The 3.5% scenario represents, at this stage, a future likely target which could permit European countries to meet the bulk of their security challenges. However, this would not come without its own problems.

Economic Opportunities and Challenges. Increasing defense spending presents both opportunities and challenge. With respect of opportunities, three aspects deserve attention.

First, historically, defense expenditure has displayed a positive fiscal multiplier.¹³ This is particularly true in recession times, like the one we are going to enter. In other words, defense spending not only impacts negatively budgetary stability but can also contribute to economic growth.¹⁴

Second, and related, defense expenditure can foster long-term technological innovation and disruption. While it is true that nowadays a great share of innovation occurs outside of the defense world, this is partially due to cuts to defense research budgets and stringent regulations affecting defense organizations.¹⁵

In other words, defense expenditure can address some of the market failures characterizing early technological innovation, thus spurring major waves of economic growth.¹⁶

Last but not least, and closely related, defense spending can lead to commercial spin-offs which benefit the society as a whole: beside the internet, x-rays, lasers, satellites and the microchips,

¹⁰ Alexander Mattelaer, "Revisiting the Principles of NATO Burden-Sharing," *Parameters*, Vol. 46, No. 1 (Spring 2016): 25-33.

¹¹ NATO (2023). Defence Expenditure of NATO Countries (2014–2023). NATO Press Release PR/CP(2023)080, 21 March 2023 - https://www.nato.int/cps/en/natohq/news_216897.htm

¹² NATO (2024). Defence Expenditure of NATO Countries (2024 Estimates). NATO Public Diplomacy Division, 21 March 2024 - https://www.nato.int/cps/en/natohq/news_226465.htm

¹³ Viacheslav Sheremirov and Sandra Spirovska, "Fiscal multipliers in advanced and developing countries: Evidence from military spending," *Journal of Public Economics*, Vol. 208 (April 2022): 104631

¹⁴ Bryan Rooney, Grant Johnson and Mirand Priebe, "How Does Defense Spending Affect Economic Growth?," *Research Report* (Santa Monica, CA: RAND Corporation, 2021).

¹⁵ Steve Blank

¹⁶ Elhanan Helpman (ed.), *General Purpose Technologies and Economic Growth* (Cambridge, MA: The MIT Press, 1995).



defense investments also promoted fundamental studies in oceanography, aerodynamics, astrophysics which have then led to major scientific discoveries in the following decades.¹⁷

Defense expenditure, however, also presents significant macroeconomic challenges. First and foremost, as already hinted, major defense spending increases are likely to fuel inflationary waves – especially in contexts of limited industrial capacity and rigid labor markets.¹⁸

Second, they may crowd out other private investments, giving private companies an incentive to halt their own investments.¹⁹

Finally, but related, under tight fiscal constraints, a substantial increase in defense spending may directly compete with other sources of public expenditure – from healthcare to education, infrastructure to social protection – thus reducing the fiscal space available for non-military areas.

This effect is particularly pronounced in high-debt countries, where even modest increases in expenditure may raise borrowing costs by driving up long-term interest rates.

Moreover, reliance on established defense industries risks reinforcing regional inequalities, channeling resources toward already-industrialized areas at the expense of peripheral or underdeveloped regions.

The broader risk is that increased spending fails to translate into real gains in national resilience, instead generating regressive redistributive effects or systemic inefficiencies.

Overall, these challenges underscore the need to plan defense budgets growth accurately accompanying them with structural reforms capable of maximizing positive economic impacts, minimizing distortions, and strengthening the overall effectiveness of public intervention in defense.

¹⁷ Jacob Darwin Hamblin, *Oceanographers and the Cold War: Disciples of Marine Science* (Seattle, WA: University of Washington, Press, 2005); Naomi Oreskes, *Science on a Mission How Military Funding Shaped What We Do and Don't Know about the Ocean* (Chicago, IL: University of Chicago Press, 2021).

¹⁸ Ramey, V. A., "Government Spending and Private Activity," *NBER Macroeconomics Annual*, vol. 27, 2012; <https://www.nber.org/papers/w17787>

¹⁹ **Barro, R. J. (1987).** *Government Spending, Interest Rates, Prices, and Budget Deficits in the United Kingdom, 1701–1918.* *Journal of Monetary Economics*, 20(2), 221–247 - <http://piketty.pse.ens.fr/files/Barro1987.pdf>



Chapter 2: A Three-Tiered Strategy to Navigate the Trilemma

In this chapter we propose a three-tiered strategy to navigate the security-affordability-popularity trilemma so that European countries can increase their military capabilities without incurring either in financial challenges or in negative domestic pressures.

This strategy includes three steps. First, defense spending needs to grow in many European countries, to reach the 2% target and, even more, if NATO Allies will agree with 3.5%. Second, structural reforms must be implemented to optimize efficiency and impact, both at the national level (through multi-year planning, procurement reform, and personnel rationalization) and at the European level (via procurement cooperation and the establishment of a defense innovation agency). Third, the defense accounting perimeter should be updated to include all expenditures that meaningfully contribute to NATO's core missions, such as cybersecurity, critical infrastructure protection, and hybrid threat response.

Tier 1: Increase Defense Spending. NATO Europe's defense spending on GDP has increased from 1.5% in 2014 to 1.9% in 2023 and 2.02% in 2024. This figure, however, includes also Norway, Turkey and the UK. If we focus only on EU countries, in 2024, the average defense spending across Europe was still slightly below 2%.

In absolute terms, the investment gap between Europe and the United States remains stark: the U.S. accounts for 68% of the Alliance's total defense expenditure.²⁰ Bridging this gap entirely is, however, neither feasible nor necessary – given that the U.S. expenditure is also directed towards other areas of the world.²¹

Much of the adjustment toward the 2% benchmark has already occurred. Most European countries either already meet the 2% target or would need less than additional 0.2-0.4% budgetary increases.²²

Either that the 2% remains unchanged (unlikely) or that the target is raised to 3.5% (more likely) as some suggest, European defense expenditure will have to grow in quality and, eventually, also in quantity.

While on the battlefield, it is open to debate whether quantity has a quality on its own, this is definitively not true on economics. For this reason, European countries' path to 2% or any higher level of defense expenditure should be phased, coherent, organized – as implied by the 2024 Draghi report.²³

²⁰ NATO, Defence Expenditure of NATO Countries (2014 2023).

²¹ Anthony H. Cordesman, *NATO's Pointless Burden Sharing Debates: The Need to Replace a Mathematically Ridiculous 2% of GDP Goal with Real Force Planning* (Washington, DC: Center for Strategic and International Studies, 2019).

²² European Defence Agency, *Defence Data report 2023-24*

²³ Mario Draghi, *The Future of European Competitiveness* (Brussels: European Commission, 2024)



A prominent example is Denmark, which in 2024 committed to exceeding 3% of GDP in defense spending through a DKK 50 billion extraordinary fund. This decision was motivated by the perceived urgency to enhance military capabilities in light of a possible Russian threat within two years.

However, alongside new investments, Denmark also reclassified several existing expenditures – including pensions, healthcare for defense personnel, and interministerial activities – as part of its NATO-compatible defense budget. This reclassification resulted in a marked discrepancy between the national accounting of defense spending (DKK 36.2 billion) and the NATO definition (DKK 68.7 billion), raising questions about the change and long-term sustainability of such a budgetary shift.²⁴

Tier 2: Optimize Resources Through Reforms. Along with growth in defense expenditure, European countries should also pursue several reforms or policy changes with the goal of optimizing resource allocations and thus ultimately increasing both efficiency and effectiveness in their national defense.

- **EU-Wide Cooperation on Procurement and Operations.** Defense expenditure has five main components: R&D, procurement, operations and maintenance, personnel and infrastructures. In Europe, R&D and procurement are 25-30% combined, operations and maintenance around 20%, personnel 50%, and the rest goes to infrastructures.²⁵ Cooperation can, realistically, be pursued only in R&D, procurement and operations: this would enhance security and affordability without sacrificing popularity. Europe's fragmented defense market – 27 national systems versus the U.S.'s unified approach – creates inefficiencies costing €25–100 billion, according to the European Parliament.²⁶ More widespread reliance on EU joint procurement could, in contrast, generate savings of at least €20-40bn, per year.²⁷ Additionally, scaling initiatives like the European Defence Fund (€8 billion, 2021–2027) and EDIRPA (€310 million) to €5 billion could help standardize platforms, boost interoperability and cut costs up to 30%.²⁸

²⁴ Danish Ministry of Defence. (2024). *Danish Defence Expenditures: Annual Report*. Retrieved April 17, 2025, from <https://www.fmn.dk/globalassets/fmn/dokumenter/aarsrapporter/-2024-danish-defence-expenditures-.pdf> The effectiveness of Denmark's rapid defense spending increase has been the subject of criticism. According to the Centre for Eastern Studies, a significant portion of the additional funds is allocated to closing existing capability gaps such as basic ground force equipment and air defense development, rather than introducing new advanced capacities. Furthermore, recent missile system failures on naval platforms and the dismissal of the Chief of Defence have cast doubts over Denmark's managerial capacity and the actual feasibility of such a rapid military buildup (Centre for Eastern Studies 2024; Associated Press 2024).

²⁵ European Defence Agency (EDA), "Defence Data 2022–2023," Brussels, 2024; NATO, "Defence Expenditure of NATO Countries (2014–2024)," Press Release PR/CP(2024)021, March 2024; European Parliament, "Report on the State of the Defence Union," Committee on Security and Defence, 2023.

²⁶ Christof Erich Cesnovar, Meenakshi Fernandes, Aleksandra Heflich, Lenka Jancova, Christa Kammerhofer-Schlegel, Cecilia Navarra, Lauro Panella and Jerome Leon Saulnier, "Mapping the cost of nonEurope report Theoretical foundations and practical considerations," *Study* (Brussels: European Parliamentary Research Service, 2023).

²⁷ Carlo Cottarelli and Leoluca Viridagamo, "Defense Expenditure in EU Countries," *Policy Brief*, No. 20 (Milan: Institute for European Policy-Making, 2024).

²⁸ Juan Mejino-Lopez and Guntram Wolf, "A European defence industrial strategy in a hostile world," *Policy*



- **Establish a European Defense Innovation Agency (EDIA) and National Counterparts.**

Cooperation on R&D may be warranted for major projects, like CERN on nuclear issues.

Alternatively, this can be pursued for advanced technological development where a large suppliers' base would not be sustainable. In other more blue-sky research areas, there is no reason to have a concentrated R&D effort.

In fact, European countries should reform their broader research activity, including defense, modeled on the U.S. DARPA, for creating a European Defense Innovation Agency (EDIA), complemented by independent national agencies. This would help address Europe's lag in high-tech defense innovation where the United States does not just have a quantitative but also qualitative advantage.²⁹

An EDIA, with an annual €5 billion budget (2.5% of EU's €200 billion budget), would drive high-risk, high-reward projects. National agencies, with budgets from €100m to €1bn each per year, would tailor innovations to country-specific needs. Since DARPA with a \$3-4bn budget generates \$10bn in U.S. impact, this proposal could generate €20-30bn in impact between the European and the national agencies. The EDIA would operate with dedicated project managers (unlike the European Innovation Council's overstretched staff), ensuring agility and expertise, and prioritize disruptive technologies over mid-tech stagnation. National agencies, leveraging each country's R&D, would integrate with EU efforts, saving resources via co-funded projects.

- **Internal reforms.** European countries should also conduct some internal reforms when it comes to their defense policy in order to ensure efficiency and effectiveness. Three priority areas emerge: strategic planning, procurement, and personnel management.

- **Multi-year strategic planning.** Several European countries lack binding multi-annual defense budget laws. The absence of clear and stable strategic horizons hampers coherent investment planning, delays industrial cycles, and discourages public-private collaboration.^{30,31}

Introducing a multi-year planning law – modeled on France's *Loi de programmation militaire* – would align resources with objectives and operational capabilities, improve predictability for suppliers, and enhance political accountability. Similarly, in the U.S., every administration is required by law to generate a set of programmatic strategic documents (such as the *National Security Strategy*, *National Defense Strategy*,

Brief, No. 29 (Brussels: Bruegel, 2024).

²⁹ The U.S. allocates almost 20% of its defense budget to military R&D, in contrast to 1% in Europe. A big difference, however, also concerns how this expenditure is conducted. Eurostat, *R&D expenditure in the EU at 2.27% of GDP in 2022* (Brussels: European Commission, March 2024); National Center for Science and Engineering Statistics, *U.S. R&D expenditures rise to \$791.9 billion in 2021* (Washington, DC: NCSES, 2024).

³⁰ As confirmed by both institutional audits and academic literature, the lack of codified multi-annual frameworks constitutes a structural obstacle to strategic defense coherence in several EU countries

³¹ European Court of Auditors, "EU Defence Policy: Multiannual Planning and Capability Gaps," Special Report No. 16/2022; European Defence Agency (EDA), "Defence Data 2022–2023," Brussels, 2024; Andrea Gilli and Massimo Marrone, "Capability Planning in European Defence," *Journal of Strategic Studies*, vol. 45, no. 3, 2022.



Quadriennial Defense Review) which similarly help actors and stakeholders organize their activities.

- **Procurement reform.** In contrast to the United States and the United Kingdom, European countries do not face major challenges when it comes to military acquisition: their programs are not massively and recurrently out of time and out of costs.

However, with a reform of strategic planning, defense procurement may benefit, especially when it comes to the part related to maintenance and operations as well as supply-chain. Stable, multi-year strategic planning may in fact help stakeholders plan and organize their activities, with savings both upstream and downstream.

The adoption of performance-based procurement frameworks at the European, coupled with the integration of advanced technological standards, could also enhance operational effectiveness while supporting resilient industrial ecosystems. However, any reform must avoid structural dependency on dominant suppliers from other member states, in order to preserve strategic autonomy and protect domestic technological capabilities.³²

- **Personnel Cost Rationalization.** European countries spend around 50% of their budget on personnel – which stays at 15% in Sweden (the top performer) and around 30% in the United States.

Self-evidently, as defense spending grows in R&D, procurement and operations, the ratio allocated to personnel is due to shrink. Some rationalization is, however, in any case possible, not much in terms of cuts, but more in terms of functional reallocation of existing workforce.

In particular, by adopting an integrated model that includes civilian and technical staff from other government ministries – such as interior, infrastructure, or technological innovation – as well as other realms, European countries could recalibrate their national defense workforce, optimizing existing human capital. This would allow a more effective concentration of resources on priority areas such as training, operational readiness, advanced equipment, and R&D – accelerating modernization without the delays inherent in large-scale recruitment cycles.

Such a reform would also improve coordination between the military and civilian components of the defense-security domain, foster interministerial integration, streamline decision-making, and contribute to a more agile and effective national defense posture. A smarter redeployment of personnel would additionally enhance adaptability to hybrid threats and multidimensional missions, increasing overall system responsiveness and resilience.

Tier 3. Reclassifying public expenditure under defense. The third tier of the proposed strategy concerns the methodological redefinition of defense expenditure with the purpose of selectively

³² Brzuska, K. (2025, January 23). *The Economies of Scale of Joint Defence Procurement*. Finabel - <https://finabel.org/the-economies-of-scale-of-joint-defence-procurement/>



reclassifying existing public spending items that, while not currently included in official defense budgets, contribute materially to both national and collective security.³³

This accounting reform has two core aims. On the one hand, it aligns national reporting with NATO's strategic mandates of deterrence and defense, crisis prevention and management and cooperative security.

On the other, by increasing defense spending, it enhances transparency and accountability, potentially raising the public perception of defense. In an era of hybrid threats, systemic instability and blurred lines between civilian and military domains, the concept of security has expanded well beyond its traditional boundaries.

Activities such as critical infrastructure protection, cyber defense, civil emergency management, counter-disinformation operations and energy resilience are now functionally indistinguishable from national security. These, and others, are areas on which not only NATO currently works but which are deemed essential for its deterrence and defense posture: societal resilience is the best example in this respect.³⁴

Civilian institutions responsible for public health, data protection and foreign influence mitigation play a central role in non-conventional deterrence and crisis response. Recent studies, including those by NATO³⁵ itself, emphasize the need for an integrated approach to security in which domains like cyber resilience and infrastructure protection are treated as core components of allied defense capacity (NATO 2023). Formally including these domains in defense budgets thus permits to align financial reporting with operational realities.

Why Reclassification is a Strategic (not merely Accounting) Choice

A reasoned extension of the defense budget perimeter would allow the inclusion of functionally relevant sectors such as, for instance, the Italian Coast Guard, the National Cybersecurity Agency (ACN), or Meteorological Service, and other civilian entities involved in critical infrastructure protection, emergency management, and national resilience.

Although not formally part of the Armed Forces, these sectors increasingly play central roles in non-conventional deterrence, critical infrastructure protection, and hybrid threat response – functions that align with NATO's deterrence and defense core task. Including them within the defense expenditure perimeter would enable the mobilization of already available human resources, reducing the costs associated with recruitment and military training, while accelerating the shift toward a multidimensional and inter-institutional defense model.

This approach is particularly advantageous for Italy, where demographic contraction and the decline of the working-age population impose structural limits on military expansion, making a horizontal rationalization of the national security apparatus a more viable and efficient alternative.

³³ Daniel Michaels and Laurence Norman, "Trump Wants NATO to Spend More. Europe Pitches Redefining Defense to Get There," *Wall Street Journal*, April 1 2025.

³⁴ Andrea Gilli and Danilo Mattera Trimonti, "The unbearable weakness of efficiency? Military power, globalization and critical infrastructures protection," in Carlo Secchi and Alessandro Gili (Eds.), *Infrastructure, Grids, and Networks: The Challenge Ahead, Amid Security and Efficiency* (Milan: Istituto Studi per la Politica Internazionale, 2025).

³⁵ NATO. 2023. *Resilience and Article 3: How Allies are adapting to hybrid threats*. https://www.nato.int/cps/en/natolive/topics_132722.htm



Two additional considerations are in order. First, many European countries are reclassifying their public expenditure to formally increase their defense spending. Our effort, by identifying clear parameters, contributes to these developments ensuring coherency and well as rationality. Second, and related, we thus believe that such a reclassification should occur across all countries, but following analogous metrics to ensure both superior coherency and a clearer picture of the overall effort.



Chapter 3: Italy's Defense Challenges in a European Context

In this chapter we apply the three-tiered strategy discussed in the previous chapter to the case of Italy. This chapter is thus divided in four parts: after illustrating the rationale underlying our focus on Italy, we focus on the application of the strategy to this case.

Case study selection: Italy. There are three main reasons why we focus on Italy. First, as a founding member of both the EU and NATO, the third economy in the EU and a G7 member, Italy carries significant weight – not least because of its leading defense industry and its advanced armed forces.³⁶ Second, the deterioration of Europe's security environment has made NATO's 2% of GDP defense spending target even obsolete, with discussions already emerging around a possible increase to 3.5% in the coming years.³⁷

Italy, however, currently allocates only approximately 1.55% of its GDP to defense, equivalent to €28 billion.³⁸ The country is thus among those asked to make major steps. Finally, Italy's geographical positioning towards the Middle East, extensive coastlines, foreign energy dependency (primarily through undersea pipelines), dense and vulnerable transportation network as well as experience with Russia's disinformation, coupled with its high public debt, highlight the need of enhancing military capabilities, addressing a plurality of threats but at the same time preserve fiscal stability. In the next three paragraphs, we discuss how our strategy can be applied to Italy.

While it is time for Italy to assume greater responsibility, a massive and concentrated increase in defense investment would be politically unsustainable and fiscally unfeasible. Moreover, such an approach may be strategically counterproductive, as it risks reinforcing inefficiencies embedded in the current defense budget structure, particularly the disproportionate allocation to personnel costs, and failing to address the multidimensional nature of contemporary security challenges.

For this reason, Italy requires a pragmatic and systemic strategy. Instead of focusing exclusively on nominal spending increases, the country should pursue a strategic realignment of its defense posture. This includes reclassifying functionally relevant expenditures, enhancing institutional coordination and investing selectively in capabilities that offer high strategic returns, all while initiating structural reforms to maximize efficiency and long-term resilience.

Tier 1: Increasing spending. The first tier of our strategy entails increasing defense spending. In this respect, we consider two scenarios:

- In the first 2% scenario, reaching NATO's baseline threshold of 2 percent of GDP would require increasing defense spending from €28 billion to approximately €40 billion. This could

³⁶ Currently, in Europe, Italy has among the biggest and most advanced air forces and almost unrivalled naval power projection capabilities.

³⁷ NATO Public Diplomacy Division (2023). Defence Expenditure of NATO Countries (2014–2023). NATO Press Release (PR/CP(2023)080), 21 March 2023. https://www.nato.int/cps/en/natohq/news_221825.htm

³⁸ ANSA English (2023). Italy's military spending 1.51% of GDP in 2022 – NATO. Published 21 March 2023 - <https://www.ansa.it/english/news/world/2023/03/21/italys-military-spending-1.51-of-gdp-in-2022-nato>



be achieved through annual increments of €1-3bn, focused on procurement, operations and research and development.

- In a more ambitious 3.5% scenario, Italy would need increase by 250% its defense budget to reach approximately €70bn. This would entail scaling spending by €3-10bn.

While these increases would contribute significantly to Italy's defense posture and industrial capacity, they also carry macroeconomic and political risks. Inflationary pressures, administrative absorption limits and potential public backlash must be carefully managed. For this reason, any spending increase must follow a structured and phased logic. Public communication campaigns should emphasize the strategic value of defense for national employment, technological sovereignty and energy resilience.

Furthermore, since defense inflation could reduce the real purchasing power of budgetary allocations by €2-4bn, quantitative targets must be matched with qualitative discipline. In line with NATO's 20 percent guideline for equipment and R&D, Italy should prioritize high-impact investments that strengthen its contribution to allied deterrence and national resilience, while maintaining fiscal responsibility and political legitimacy.

Tier 2: Reforms. Italy's ability to convert growing defense expenditure into effective capabilities depends not only on funding levels but on also structural reforms. Italy already extensively cooperate with partners on procurement: the country cooperates with France on space and surface warships, on aerial vehicles with the U.S. as well as the UK and Japan, on drones with Turkey, on land systems and submarines with Germany.

With respect to procurement, while more can be done, Italy already does a lot in terms of multinational cooperation. For this reason, for the second tier of our strategy, we look only at innovation, planning and procurement, as well as personnel.

- **DARPA.** Italy lacks a single high-risk, high-reward innovation authority in defense. A national agency modeled after the U.S. DARPA – or coordinated with the proposed European Defense Innovation Agency (EDIA) – could promote breakthrough capabilities in so-called emerging and disruptive technologies. Such an agency could start with a budget of €500–700 million annually, involve civilian-military R&D centers, and adopt flexible contracting schemes. The aim is to catalyze dual-use innovation and reduce dependence on foreign technology. Italy has extensive and advanced science and research latent capacity which, however, does not unleash all its technological, technological and commercial potentials.³⁹
- **Strategic Planning and Procurement Reform.** Italy currently lacks a legally binding multi-year defense programming law.

³⁹ Daniel Castro, Michael McLaughlin and Eline Chivot, *Who Is Winning the AI Race: China, the EU or the United States?* (Washington, DC: Center for Data Innovation, 2019).



- Introducing a comprehensive planning framework (similar to France's *Loi de programmation militaire*) would improve continuity, predictability and alignment between strategic objectives and available resources. Such a legislative instrument would offer long-term visibility to both defense institutions and industrial partners, facilitating coherent investment cycles and strengthening public accountability
- Such a reform would also improve procurement performance, as suppliers could plan for longer, multi-year contracts. However, procurement procedures, while well established, would benefit from a process of rationalization aimed at enhancing efficiency and responsiveness. Reform priorities may include the consolidation of acquisition structures to improve coordination and scale, the adoption of competitive criteria based on performance and innovation, and the synchronization of procurement planning with that of key European allies.

These measures would generate cost savings, reduce procedural delays and support the development of a more autonomous and integrated European defense technological base.

- **Personnel Cost Restructuring.** Approximately 70 percent of Italy's defense budget is currently allocated to personnel costs, including salaries, benefits and pensions. This structural imbalance severely constrains available resources for modernization, research, operational readiness and training.

Given this context, further large-scale recruitment is not only fiscally unsustainable but also demographically unfeasible, as Italy ranks among the OECD countries with the lowest youth-to-population ratios and its working-age population is shrinking steadily.

Reforming the personnel structure must therefore prioritize functional rationalization over numerical expansion.

Italy should revise its force composition by integrating civilian and technical capabilities from other ministries—such as the Ministry of the Interior, and from other ministries and agencies—into a unified national defense and security framework. In parallel, the introduction of standardized joint training across military and civilian entities would enhance interoperability, mission readiness and deployment flexibility.

The digital transformation of administrative and logistical processes should also be accelerated to reduce fixed costs and increase transparency and accountability. Moreover, reskilling programs and interministerial secondments would allow for a more flexible, integrated and productive use of existing public sector personnel. This approach would reinforce the State's comprehensive response capacity while minimizing redundancy and preserving fiscal sustainability.

A realistic yet ambitious benchmark can be found in the 2011 Law (Law No. 244), which set a target of reducing the share of personnel expenditure to below 50 percent of the total



defense budget.⁴⁰ This objective, although never fully achieved, remains analytically sound. Italy should reaffirm this target and commit to reaching it by 2030. Doing so would free up an estimated 5 to 7 billion euros annually for strategic reinvestment in high-priority domains such as R&D, cyber capabilities, and joint operational platforms.

Tier 3: Reclassify Expenditures. The third tier of the strategy focuses on reclassifying the public expenditure functionally contributing to NATO's core tasks (deterrence and defense, crisis prevention and management and cooperative security) but currently accounted for outside the official defense budget.

This methodological refinement improves the alignment between financial reporting and operational reality, especially in an era where the boundaries between civil and military security domains have become increasingly porous. Additionally, this also enables Italy to strengthen its strategic credibility while alleviating fiscal pressure.

Italy's efforts in cybersecurity, maritime security and infrastructure protection already fulfill essential roles in collective defense. Reclassifying selected expenditures in these areas is not merely a statistical adjustment but a conceptual update that acknowledges the evolving nature of threats and the cross-sectoral structure of modern defense.

Two categories stand out for immediate consideration:

- The Italian Coast Guard, which plays a vital role in Mediterranean stability through search and rescue, anti-smuggling, and the protection of maritime corridors, contributes directly to NATO's crisis management objectives. Reallocating a portion of its budget (estimated at approximately €700 million) to the defense perimeter would reflect this contribution.
- National Cybersecurity Programs addressing resilience in energy, health, and data systems are central to hybrid deterrence. Approximately €700 million currently allocated in civilian budgets could likewise be reclassified. These reassignments would elevate Italy's declared defense spending to around 1.59 percent of GDP, narrowing the gap to the 2 percent benchmark without generating new fiscal costs.

⁴⁰ Repubblica Italiana. 2011. Legge 31 dicembre 2012, n. 244. *Revisione dello strumento militare nazionale*. - <https://www.normattiva.it/uri-res/N2Ls?urn:nir:stato:legge:2012-12-31;244>



Conclusions and Policy Recommendations

Italy's defense posture stands at a critical juncture. The convergence of mounting international insecurity, persistent fiscal constraints and rising expectations from NATO and the European Union demands a strategic reassessment of how defense policy is conceived and executed. Italy cannot afford either strategic inertia or a simplistic expansion of military expenditure.

What is needed instead is an integrated model that balances effectiveness, fiscal sustainability and political legitimacy.

This model rests on three mutually reinforcing components.

1. First, defense investments must increase in a selective and gradual manner, targeting high-value sectors such as joint procurement, research and development, cyber defense and operational readiness. Sudden or indiscriminate increases risk inflationary pressures, administrative delays and political backlash, especially in a country facing public debt pressures and demographic constraints⁴¹
2. Second, structural reform is essential. Italy must adopt a legally binding multi-year defense programming law, similar to France's *Loi de programmation militaire*⁴². It must also restructure its procurement system to align with European investment cycles and reduce the imbalance caused by personnel costs, which still absorb approximately 70 percent of the defense budget⁴³. Reaffirming the 2011 objective to bring this share below 50 percent by 2030 would free up substantial resources for strategic reinvestment⁴⁴.
3. Third, Italy must redefine the scope of what counts as defense. Modern threats do not respect institutional boundaries. Activities such as cyber resilience, infrastructure protection and maritime security contribute directly to NATO's core missions and should be counted accordingly. Reclassifying these expenditures is not a statistical maneuver but a strategic update. It would increase transparency, align Italy's accounting with NATO principles and reduce the nominal gap between effort and reporting⁴⁵.

⁴¹ Amante, A., & Fonte, G. (2024, April 4). Struggling to meet NATO goal, Italy mulls stretching defence budget. Reuters. <https://www.reuters.com/world/europe/struggling-meet-nato-goal-italy-mulls-stretching-defence-budget-2025-04-04>

⁴² NATO (2023a). Defence Expenditure of NATO Countries (2014–2023). NATO Press Release, 21 March 2023 - https://www.nato.int/cps/en/natohq/news_221825.htm

⁴³ Ministero della Difesa (2023). Nota aggiuntiva allo stato di previsione del Ministero della Difesa per l'anno 2023 - <https://www.difesa.it/Content/Pagine/Notaintegrativa.aspx>

⁴⁴ Repubblica Italiana. (2012). *Legge 31 dicembre 2012, n. 244. Revisione dello strumento militare nazionale*. Retrieved from <https://www.normattiva.it/uri-res/N2Ls?urn:nir:stato:legge:2012-12-31;244>

⁴⁵ Baird Maritime (2024). Italy mulls stretching defence budget as it struggles to meet NATO targets - <https://www.bairdmaritime.com/security/non-naval-security/coast-guard/italy-mulls-stretching-defence-budget-as-it-struggles-to-meet-nato-targets>



Taken together, these reforms would allow Italy to move credibly toward the two percent target while preserving macroeconomic balance and political cohesion. This model may also serve as a replicable strategy for other European allies navigating the same trilemma between security, fiscal constraints and domestic legitimacy.



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