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Royal United Services Institute
for Defence and Security Studies
Whitehall
London SW1A 2ET
United Kingdom
+44 (0)20 7747 2600
www.rusi.org
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Executive Summary

TO DELIVER ON its commitment to spend 3% of GDP on defence by 2030, Liz Truss's government will need to increase defence spending by about 60% in real terms.

This is equivalent to about £157 billion in additional spending over the next eight years, compared with current planning assumptions. By comparison, the 2020 Spending Review, and the associated Integrated Review, allocated an extra £16.5 billion over four years.

This would be the biggest increase since the early 1950s, when concern that the Korean War might escalate to a wider war with the Soviet Union led to UK defence spending increasing from 6.6% of GDP in 1950 to 9.6% in 1952, before falling back to 5.9% by 1960.

The first indication of whether the new government is serious about the 3% target will come in the next Spending Review, likely to take place by November 2022.

For the 3% commitment to be credible, the Ministry of Defence (MoD) would expect to be compensated for the extra inflation since the 2021 Spending Review, and for planned real-terms cuts in the resource budget for the next two years to be reversed.

To ensure that the 60% increase in real-terms spending leads to a commensurate rise in military capability – and is not eaten up by increased inefficiencies – careful planning and preparation will be essential. This means investing in new industrial capacities capable of increasing production volumes, putting in place the process for building a larger service personnel workforce, and agreeing the additional physical infrastructure that a bigger force structure would require.

Given the immediate capacity constraints, the pace of spending growth is likely to be slower in the early years, before accelerating towards 2030. This could mean that defence spending rises from 2.2% of GDP in 2022/23 to 2.5% in 2026/27, before increasing to a full 3% over the following four years.

These extra funds would allow the MoD to pay for capabilities that are not fully funded under current planning assumptions. To spend 3% effectively, the defence budget will require a significant increase in the size of the frontline – numbers of formations and platforms.

An increase in service personnel numbers of 25–30% is likely to be needed to support an overall 60% increase of defence spending. This would increase total numbers of regular personnel from 148,000 today to around 190,000 in 2030, returning to the level last seen in 2010.

If the government is to raise defence spending to 3% of GDP, it will need to argue the case for doing so in the context of wider fiscal priorities. In contrast to the funding of spending

increases for the NHS and social care under the last government, there has been very little attempt to ready the British public for the sacrifices that will be needed for a similar level of increase for defence.

If it were to be entirely funded from taxation, the plan would require a 5p in the pound increase in the standard and higher rates of income tax by the end of the decade, or an increase in the standard VAT rate from 20% to 25%. Alternatively, it would require a significant cut in the GDP percentage spent on other public services and/or other international spending commitments. The credibility of the new government's commitment to spending 3% of GDP on defence by 2030 will depend on whether the Spending Review sets out a plan for financing this increase.

From Famine to Feast? The Implications of 3% for the UK Defence Budget

The 3% Chorus

THERE ARE GROWING calls for the UK to spend a lot more on defence. Former Cabinet Secretary and National Security Adviser Mark Sedwill has called for spending '2.5% or 2.75%' on defence, as part of a broader 4% commitment to international spending.[1] Former Foreign Secretary Jeremy Hunt has called for a 'step change' in defence spending.[2] Chair of the Commons Foreign Affairs Committee Tom Tugendhat has called for spending 3% on defence,[3] as has Chair of the Commons Defence Committee Tobias Ellwood.[4]

At the NATO summit in Madrid in June 2022, Prime Minister Boris Johnson began to respond to these pressures by suggesting that, to fund planned commitments, the UK would need to spend 2.5% of GDP by the end of this decade, up from current plans to spend around 2.0% in 2024.[5] Foreign Secretary Liz Truss has gone further as part of her leadership campaign, arguing for spending 2.5% of GDP by 2026 and 3% of GDP by 2030.[6]

This paper offers some thoughts on what these increases might mean, both for the size and capabilities of the armed forces, and for the UK's wider fiscal priorities. It begins by setting the historical context for the 3% proposal, which would reverse the trend of three decades of decline in the share of GDP going to defence. It then examines the immediate challenges facing defence budget planners, both from wider inflation pressures and from the demands of the Russia–Ukraine war. It goes on to calculate the additional financial resources that would be

1. Tom Newton Dunn, 'Military and Spying Budget Must Rise to Counter Russia's Threat, Insists Lord Sedwill', *The Times*, 28 March 2022.
2. Ben Riley-Smith, 'Jeremy Hunt Calls for Massive Boost in UK Defence Spending', *The Times*, 11 March 2022.
3. Oliver Wright, 'Vow to Level Up by Tom Tugendhat in Tory Leadership Race', *The Times*, 13 July 2022.
4. Henry Zeffman, 'Tobias Ellwood: 3% of GDP Should Be Spent on Defence', *The Times*, 3 May 2022.
5. Andrew Chuter, 'Johnson Vows Defense Budget Hike by 2030, But Critics Want It Sooner', *Defense News*, 30 June 2022.
6. Dan Sabbagh and Jessica Elgot, 'Defence Secretary Appears Unenthused by Liz Truss Spending Pledge', *The Guardian*, 19 July 2022.

required to meet the 2030 3% target. Finally, the paper estimates what these extra resources could be spent on.

The End of the Peace Dividend

Examination of future defence spending will necessarily be part of a wider discussion on the implications of heightening geopolitical tensions for the UK's long-term economic health and fiscal priorities. Since the mid-1950s, the UK has been able to fund the growing share of its national income devoted to the NHS and state pensions through cuts in the GDP share spent on defence, allowing the overall level of taxation to remain relatively stable. As the Office for Budget Responsibility (OBR) recently pointed out:

> Between 1952 and 2005, defence spending fell from just under 10 per cent of GDP to 2 per cent … In an arithmetic sense, the 8 per cent of GDP reduction can be thought of as funding the entire increase in health and welfare spending over the same 53-year period, which increased from 8 to 16 per cent of GDP.[7]

This growing 'peace dividend' was accompanied by a 'globalisation dividend', with rapid international economic integration widely believed to have played a key role in the UK's high rate of economic growth throughout this half century, given its relatively open economic model.[8]

The two dividends were closely related. The reduction in the defence burden was made possible by the relaxation in tension between the major powers, both during and after the Cold War. The UK's peace dividend was parallelled by similarly sharp reductions in defence spending as a proportion of national income in its main NATO allies, as well as in China and, after 1991, in Russia. The willingness to accept growing levels of economic interdependence was, similarly, only made possible by declining concern over the possibility of conflict – between European states in the decades after 1945, and, for two decades after 1990, between the West and Russia. The rapid transition of China from a largely autarkic economy to the world's largest trading state, strongly supported by the US and its allies, was in turn predicated on an assumption that the risks of major power war were low.

In contrast, the subsequent period has seen a marked increase in concern over possible major power conflict (especially after the 2014 invasion of Ukraine), alongside a slowdown in economic globalisation after the 2008 financial crisis. For the UK, this has opened the prospect that both of its post-war 'dividends' may begin to be eroded, although the magnitude and pace of these shifts remain uncertain. Further global economic fragmentation – 'onshoring' of critical supply chains, sanctions against Russia and China, increased US protectionism – could (on current Treasury models) threaten UK economic growth, adding to the negative pressures on growth

7. Office for Budget Responsibility (OBR), *Fiscal Risks and Sustainability*, CP 702 (London: The Stationery Office, 2022), p. 31.
8. *Ibid.*, p. 32.

as a result of the UK's withdrawal from the EU's Single Market and Customs Union.[9] In parallel, growing concern over the threats to the UK posed by Russia and China is adding to pressure both to spend more on defence and security, and to do more to reduce economic dependence on them (for example in relation to energy supplies and inward investment).

If defence spending is now to be increased, both as a proportion of national income and as a proportion of overall government spending, it would be a radical shift in priorities. In the November 2021 Spending Review (SR21), the government confirmed that defence spending was due to increase, in real terms, by an average of 1.5% between 2019/20 and 2024/25.[10] By comparison, most other government departments were awarded larger real-terms increases: Business, Energy and Industrial Strategy received 9.9% annually in real terms; Health and Social Care 3.5%; Justice 4.1%; Education 2.4%; Transport 5.5%; and the Home Office 3.6%.[11] Moreover, since the defence spending settlement was front-loaded into the first two years of the Spending Review period, Ministry of Defence (MoD) spending was due to fall in real terms in both 2023/24 and 2024/25.

A new Spending Review is set to take place this autumn, reflecting the priorities of the incoming prime minister. This will be an opportunity for the government to set out in detail its revised plans for defence spending for the next financial year, and possibly for the next two to three years, and perhaps beyond.

If the new prime minister remains committed to reaching 3% by 2030, the Spending Review will also be an opportunity for the government to explain its plan for getting to this target – which would require a real-terms increase of around 60% in total defence spending by 2030/31. The latter is equivalent to a cumulative increase of about £157 billion in defence spending over the next eight years, compared with current plans.[12]

The last time that increases of this magnitude took place was in the early 1950s, when the Korean War led to increased concerns over Soviet aggression in Europe. In response, UK defence spending increased from 6.6% of GDP in 1950 to 9.6% in 1952, before falling back to 5.9% by 1960.[13] Comparisons can also be made with the mid-1930s, when defence spending increased from 2.5% of GDP in 1934, the year after Adolf Hitler came to power, to 3.5% in 1936 and then to 6.5% in 1938.[14]

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9. *Ibid.*, Chapter 2.
10. HM Treasury, *Autumn Budget and Spending Review 2021: A Stronger Economy for the British People*, HC 822 (London: The Stationery Office, 2021), p. 182.
11. *Ibid.*, p. 182.
12. See Tables 1 and 2 for details.
13. See notes for Chart 2.4 in OBR, 'July 2022 Fiscal Risks and Sustainability: Charts and Tables', Chart 2.4, <https://obr.uk/frs/fiscal-risks-and-sustainability-july-2022/>, accessed 30 August 2022.
14. *Ibid.*

Table 1: Current Spending Plans

	2022/23	2023/24	2024/25	2025/26	2026/27	2027/28	2028/29	2029/30	2030/31
£m Cash	50,200	48,000	48,600	49,795	51,045	52,327	53,640	54,986	56,366
£m 2021/22 Prices	47,300	43,726	43,468	43,685	43,904	44,123	44,344	44,566	44,788
Real Change	2.8%	-7.6%	-0.6%	0.5%	0.5%	0.5%	0.5%	0.5%	0.5%
Projected % GDP	2.19	2.06	2.00	1.98	1.95	1.93	1.91	1.89	1.87

Table 2: Spending Profile for Getting to 3%

	2022/23	2023/24	2024/25	2025/26	2026/27	2027/28	2028/29	2029/30	2030/31
£m Cash	50,200	54,253	57,841	62,228	66,558	72,192	78,407	85,761	94,492
£m 2021/22 Prices	47,300	49,422	51,733	54,592	57,247	60,874	64,819	69,508	75,083
Real Change	2.8%	4.5%	4.7%	5.5%	4.9%	6.3%	6.5%	7.2%	8.0%
Projected % GDP	2.19	2.24	2.30	2.38	2.45	2.56	2.68	2.82	3.00

Sources and Notes for both tables:

Cash defence spending based on HM Treasury, Autumn Budget and Spending Review 2021: A Stronger Economy for the British People*, HC 822 (London: The Stationery Office, 2021), along with 0.5% real growth after 2024/25.*

Inflation adjustment to 2021/22 prices, and GDP projections, from HM Treasury, 'GDP Deflators at Market Prices, and Money GDP June 2022 (Quarterly National Accounts)', 30 June 2022, <https://www.gov.uk/government/statistics/gdp-deflators-at-market-prices-and-money-gdp-june-2022-quarterly-national-accounts>, accessed 30 August 2022. There is an adjustment for additional GDP deflator growth of 2% in 2022/23 and 1% in 2023/24.

For years after 2026/27, it is assumed that the GDP deflator grows at 2% per annum, and that real GDP grows at 1.5% per annum.

Total Ukraine spending for 2022/23 is assumed to be £2.3 billion, although this allocation will be largely used up by December 2022, and the government is likely to decide to replenish it.

Table 2 assumes that growth in total defence spending accelerates in the last four years of the projection. The reasons for this assumption are explained in the text.

Defence and the 2020 Spending Review

The current framework for defence budget planning was established in the November 2020 Spending Review (SR20).[15] The subsequent Integrated Review[16] and Defence Command Paper[17] explained the wider foreign and defence policy rationale.

The Integrated Review identified Russia as the 'most acute direct threat' to the UK's security, and the Euro-Atlantic area as the main focus of its defence efforts. But it also signalled an increased focus on the Indo-Pacific region, in part as a consequence of increasing 'systemic competition' with China, seen as 'the biggest state-based threat to the UK's economic security'.[18]

The reviews gave particular priority to the contribution which defence investment made to prosperity and national competitiveness. The subsequent AUKUS deal with Australia and the US,[19] and the prospect of close cooperation with Japan on the Future Combat Air System (FCAS),[20] reinforced the case for working more closely with Indo-Pacific allies in the development of defence capabilities.

While the previous strategic review – the 2015 Strategic Defence and Security Review (SDSR) – had insisted on maintaining the personnel strength of the armed forces, despite a modest overall spending settlement, the main focus of the more generous SR20 settlement was a sharp increase in defence capital spending, amounting to about 40% in real terms over five years.[21] Total 10-year equipment spending, as a result, was increased from £190 billion to £248 billion for the 10 years from 2021/22.[22] For the first time in many years, procurement plans were fully funded, at least for the period up to 2024/25. In recent months, this has come under increasing

15. HM Treasury, *Spending Review 2020*, CP 330 (London: The Stationery Office, 2020).
16. HM Government, *Global Britain in a Competitive Age: The Integrated Review of Security, Defence, Development and Foreign Policy*, CP 403 (London: The Stationery Office, 2021).
17. The Defence Command Paper sets out the future for the UK's armed forces. MoD, *Defence in a Competitive Age*, CP 411 (London: The Stationery Office, 2021).
18. HM Government, *Global Britain in a Competitive Age*, p. 62.
19. Strategic Command, 'The Defence Command Paper Sets Out the Future for Our Armed Forces', News Story, 23 March 2021, <https://www.gov.uk/government/news/the-defence-command-paper-sets-out-the-future-for-our-armed-forces>, accessed 30 August 2022.
20. Ministry of Defence (MoD), 'UK Builds Momentum on Combat Air Programme with Demonstrator Set to Fly Within Five Years', 18 July 2022, <https://www.gov.uk/government/news/uk-builds-momentum-on-combat-air-programme-with-demonstrator-set-to-fly-within-five-years>, accessed 30 August 2022.
21. Malcolm Chalmers, 'The Spending Review and the UK's Strategic Priorities', *RUSI Whitehall Report*, 3-21 (December 2021).
22. MoD, 'The Defence Equipment Plan: 2021-2031', 2022, <https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1055953/Defence_Equipment_Plan_2021.pdf>, accessed 30 August 2022.

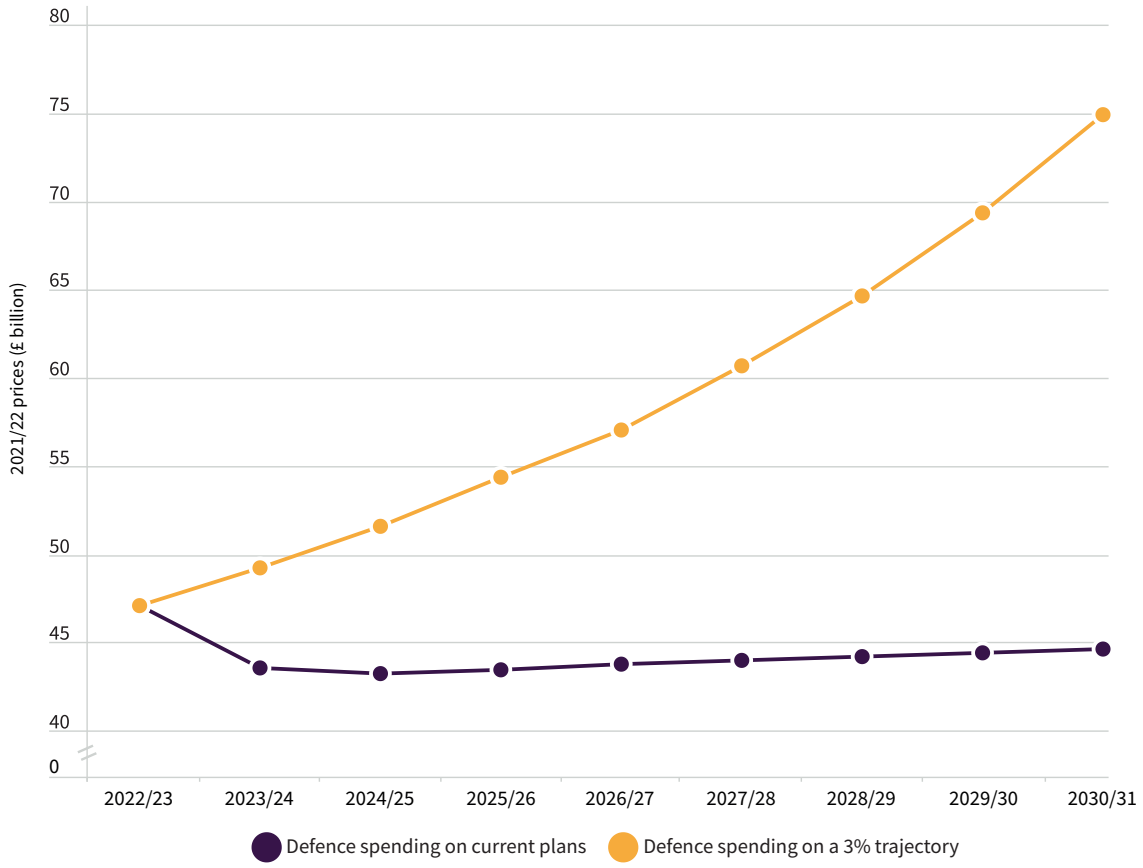
pressure as a result of the intense cost pressures facing defence contractors.[23] In order to maintain the equipment programme over time, the MoD is likely to need compensation for much of this unanticipated inflation. So far, however, these cost pressures have been mitigated by greater delays in programme delivery, themselves a result of supply chain problems.

After the inflation adjustments made in SR21, average annual real-terms growth in defence spending for the five years from 2019/20 to 2024/25 amounted to about 1.5% per annum, with all the growth taking place in the first three years.[24] Using the inflation assumptions current at that time, resource spending was due to fall by about 3% in real terms during this period.[25] It was assumed by MoD planners that this could be made possible by continuing restraint in pay levels, savings from retirement of older weapon systems, and reductions in both service and civilian personnel numbers. The reductions in regular army personnel numbers have proven controversial. As part of a wider Whitehall process initiated in 2022, the MoD has also been asked to model the impact of cutting its civilian numbers by 20% or more.[26]

Because inflation – even on the Treasury's preferred 'GDP deflator' measure – is set to be higher than assumed in SR21, defence spending in real terms is set to fall more sharply than previously planned over the next two years. The below-inflation pay settlement for the armed forces – averaging only 3.75%,[27] significantly less than those offered to teachers and most NHS workers – will help the MoD to cope with the strains produced by increased general inflation, as will the fixed-price nature of many of its contracts. Even so, without additional funding, the MoD will find it harder to meet existing resource budget commitments over the next two years (2023/24 and 2024/25).

23. Author interviews with senior officials, London, July and August 2022.
24. HM Treasury, *Autumn Budget and Spending Review 2021*, p. 182.
25. *Ibid.*, p. 184.
26. Rhys Clyne, 'Civil Service Cuts Will Force Ministers to Choose Between Painful Options', Comment, Institute for Government, 13 May 2022, <https://www.instituteforgovernment.org.uk/blog/civil-service-cuts-will-force-ministers>, accessed 30 August 2022.
27. Armed Forces' Pay Review Body, *Armed Forces' Pay Review Body: Fifty-First Report 2022*, CP 720 (London: The Stationery Office, 2022).

Figure 1: Getting to 3% of GDP



Source: See sources for Tables 1 and 2.

The Defence Budget and the War in Ukraine

The war in Ukraine has changed the debate on defence spending in the UK, and across NATO. But – as in the 'war scares' of both the late 1930s and the early 1950s – its long-term impact remains highly uncertain. It will depend, above all, on the war's outcome.

On the one hand, the risk that the UK's armed forces could be involved in direct conflict with Russia at any time has risen sharply. Although the UK and its allies are not engaged directly in the fighting, they are arming, supporting and training Ukrainian forces on a massive scale. Until this conflict comes to an end, or at least settles into a new lower-level equilibrium, the risks of escalation to direct conflict between Russian and NATO forces, either in Ukraine itself or elsewhere, remain considerable. Even then, the UK and its allies will need to be prepared for a range of Russia-related scenarios, both in the Ukraine theatre and elsewhere.

On the other hand, the longer the war continues, the greater the losses in its warfighting capabilities that Russia will suffer, and the more limited its ability to prosecute a similar campaign, at least for the next few years. Russia has lost many of its most capable professional personnel and modern weapons.[28] Moreover, its capacity for rebuilding its capabilities is likely to be limited by Western sanctions, given how reliant its defence industry has become on technology imports from the US and its allies.[29] While China might eventually provide an alternative source for many key components, this will take time. At least over the next few years, therefore, Russia is likely to be in much worse shape for a future war with NATO than it appeared to be in January 2022.

The key will be what happens next. The UK's strategy towards the war is driven by three key objectives: helping Ukraine to defeat Russia; weakening Russia's ability to launch military operations against others in the future; and avoiding escalation to a wider NATO–Russia war.

Even in an optimistic scenario, getting Russia to accept a decisive Ukraine victory is likely to take several years. And, even if all three are achieved, Russia will be an unpredictable and dangerous neighbour for NATO for some time to come. But the correlation of forces will have changed fundamentally in NATO's favour. Sweden and Finland will be full members, and the forward presence of NATO troops – including UK forces – will have been massively reinforced.[30] Russia's ability to relaunch its invasion will, hopefully, have been eroded by sustained post-war assistance to the Ukrainian military. Economic sanctions will weaken Russia's ability to support the rearmament of its military machine. Increasingly, Russia would, in this scenario, be on the strategic defensive, perhaps even facing threats to long-held positions in Belarus, Moldova, Georgia, and elsewhere.

Such a benign scenario is, however, far from inevitable. The Russian leadership still appears to believe that the war in Ukraine can be won. The much-publicised Ukrainian counteroffensive could fail, NATO resolve could weaken in the face of Russia's energy sanctions and Moscow could yet emerge with significant territorial gains beyond those of 2014. If Ukraine were to fall, as seemed likely only a few short months ago, then every one of Russia's NATO neighbours would fear they could be next.

A protracted armed stalemate, punctuated by unpredictable crisis, is also possible. For current planning purposes, therefore, it must be assumed that Russia will remain the most important conventional military threat to NATO through the next decade.

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28. *The Economist*, 'Russia's Army Is in a Woeful State', 30 April 2022.
29. James Byrne et al., 'Silicon Lifeline: Western Electronics at the Heart of Russia's War Machine', RUSI, 8 August 2022.
30. As part of this reinforcement, the UK has assigned additional capabilities to NATO and increased the scale and lethality of its presence in Estonia. MoD and Ben Wallace, 'UK to Make More Forces Available to NATO to Counter Future Threats', Press Release, 29 June 2022, <https://www.gov.uk/government/news/uk-to-make-more-forces-available-to-nato-to-counter-future-threats>, accessed 30 August 2022. This has added to the case for new funding.

The Short-Term Challenge

The UK's defence planners therefore need to focus their energies on what needs to be done now to support Ukraine at this critical moment, and over the next few years, while ensuring that its own forces are as ready as possible for a conflict with Russia that could erupt at any time.

The most urgent requirement will be to do whatever it takes, in close cooperation with its allies, to support Ukraine's war effort. The UK is already Europe's most generous contributor of military aid to Ukraine, with some £2.3 billion so far pledged, much of which is already being delivered. Although the US remains the largest, and most indispensable, provider of military aid, the UK's contribution has often been especially timely and adaptive – for example in its large-scale provision of training in the UK for Ukrainian forces, which has built on a well-established relationship to considerable effect.[31]

If, as is probable, the war continues through this winter, there will be a requirement for more UK contributions – direct transfers from UK stocks, the financing of supplies from third parties, training in the new NATO-standard systems which will, increasingly, provide the backbone of Ukrainian defences. Other states and organisations – especially the EU and the international financial institutions – are well-placed to provide the fiscal support necessary to keep the Ukrainian state alive. The UK should be prepared to make a proportionate contribution to this effort. But – given the more limited scale of assistance from France and Germany – the UK's primary comparative advantage is likely to remain the provision of military assistance.[32] This assistance is paying considerable dividends, both on the battlefield and in the high regard with which the UK is held in many of the capitals of northern and eastern NATO states.

If the war continues at its recent intensity, £2.3 billion will probably not be enough for FY 2022/23. A good working assumption is that the UK defence budget will need an additional £3 billion per annum to fund the additional costs of the war in Ukraine.[33] In addition to grants-in-aid to Ukraine, this figure includes financing the UK armed forces to rebuild their own equipment stocks, where these have been depleted by transfers to Ukraine and were not previously scheduled for immediate replacement.

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31. Nicholas Fiorenza, 'Ukraine Conflict: Dutch Soldiers Arrive in UK to Help Train Ukrainians', *Janes*, 26 August 2022, <https://www.janes.com/defence-news/defence/latest/ukraine-conflict-dutch-soldiers-arrive-in-uk-to-help-train-ukrainians>, accessed 30 August 2022.
32. Kiel Institute for the World Economy, 'Ukraine Support Tracker', <https://www.ifw-kiel.de/topics/war-against-ukraine/ukraine-support-tracker/?cookieLevel=not-set>, accessed 30 August 2022.
33. This is based on the assumptions that (a) the current £2.3-billion allocation will be exhausted by the end of 2022, and will be replenished; (b) the total level of demand for UK assistance, and the UK's willingness to meet this demand, will continue at current levels as long as the war continues at around its current intensity.

NATO's latest tabulation of planned UK defence spending for 2022/23 records total spending (on the NATO definition) of £53,878 million, estimated to be equivalent to about 2.12% of GDP.[34] These figures do not include the additional estimated £2.3 billion to Ukraine, the addition of which would bring the total to about 2.19% of GDP. This could increase further in coming months if more assistance is provided. This would be a higher proportion of GDP spent on defence than any other NATO European member has reported to NATO, with the exceptions of Estonia, Greece, Lithuania and Poland.

Yet the recent increase in spending on the Ukraine operation is taking place at a time when the boost to core defence spending announced in SR20 has come to an end. Inflation is also likely to be much higher than anticipated in current budget allocations. Without further allocations to the core defence budget, there is likely to be a real-terms decline in core defence spending in 2022/23, and further real-terms declines in 2023/24 and 2024/25.[35] This could bring core defence spending in 2024/25, depending on growth in GDP, close to the 2% floor.

In 2022/23, the pay settlement for the armed forces, recommended by the Armed Forces' Pay Review Body, is for an increase of 3.75%. This should be affordable from the additional 2.5% which the MoD had provisioned for 2022/23, using the extra resources made available in SR21.[36] While contract prices are now starting to rise as a result of wider inflation, and planned reductions in personnel numbers are taking place more slowly than planned, the effect on the defence programme from these trends is being cushioned in the short term by the high proportion of contracts that are on a fixed-price basis, and by unplanned delays in project delivery.

Yet the pressures are set to grow markedly over the next two years, when there is now a very strong case for revisiting the core budget allocation, both because of inflation and because of the wider case for a longer-term war-related uplift.

The costs of future defence contracts are likely to increase, both in response to growing input costs and because of growing global demand for defence products. And it will be hard to justify another below-inflation increase for the armed forces, especially given the higher rises in other parts of the public sector. The need for a more competitive pay offer will only increase if new defence plans include plans to stabilise, and then increase, the number of service personnel.

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34. NATO, 'Defence Expenditures of NATO Countries (2014-2022)', Press Release (2022) 105, 27 June 2022, <https://www.nato.int/cps/en/natohq/news_197050.htm>, accessed 30 August 2022.
35. The current OBR projection for GDP deflator inflation in 2022/23 remains 4.05%. HM Treasury, 'GDP Deflators at Market Prices, and Money GDP June 2022 (Quarterly National Accounts)', 30 June 2022, <https://www.gov.uk/government/statistics/gdp-deflators-at-market-prices-and-money-gdp-june-2022-quarterly-national-accounts>, accessed 30 August 2022. This leaves core defence spending level in real terms in 2022/23. If GDP deflator growth were to be revised upwards, which is likely, real-terms core spending will fall this year. On current plans and inflation estimates, real core defence spending (TDEL) is currently due to fall by some 2.1% in 2023/24 and 0.6% in 2024/25.
36. Armed Forces' Pay Review Body, *Armed Forces' Pay Review Body: Fifty-First Report 2022*, p. 40.

Towards 3% of GDP

The commitment to spend at least 2% of GDP on defence, the longstanding NATO target, is now part of the UK's cross-party political consensus. When there was a risk that the UK might fall below this level after 2015 (when spending fell to only 2.01%), then-Prime Minister David Cameron came under considerable pressure from US President Barack Obama not to do so. This played an important role – alongside Russia's annexation of Crimea in 2014 – in the decision to exempt defence from the wider austerity measures of the 2015 Spending Review. It subsequently proved of considerable diplomatic value after Donald Trump became president, with the UK largely exempt from his tirades against low-spending allies (especially Germany). During this latter period, the existence of the 2% goal became a visible performance target for a growing number of member states, especially in Eastern Europe. By 2022, seven of the 'frontline' states (the three Baltic states, Poland, Romania and Slovakia) were meeting the 2% target, and only one (Hungary) did not.[37]

Now that UK leaders are considering a major increase in defence spending, domestic political reality means that high-level attention has mainly been focused on whether the 2% target should be altered. The next defence review – which could begin before the end of 2022 – is therefore likely to start with a total budget, expressed in terms of GDP percentage, for which the MoD is then asked to propose a capability package that fits within this allocation.

Current Plans and the 2% Target

On current plans, set out in SR21,[38] core defence spending (TDEL) is due to increase from £46.0 billion in 2021/22 to £47.8 billion, £48.0 billion and £48.6 billion in 2022/23, 2023/24 and 2024/25 respectively (all in cash terms). On the basis of then-prevailing inflation assumptions, SR21 calculated that TDEL would fall by an average of 0.4% per annum in real terms over this three-year period.[39] Because of significant increases over the previous two years, however, the real-terms defence budget was due to increase, on average, by 1.5% per annum between 2019/20 and 2024/25.[40]

Since last October, however, the level of inflation has risen sharply above forecast levels. The increase has been most pronounced for indices which include the costs of imported food and energy, such as the consumer price index. But it has also begun to affect the GDP deflator for domestic costs, the index used by the Treasury to estimate the real level of government spending. The most recent estimate for the GDP deflator was published by the OBR alongside the March 2022 Budget. This showed GDP deflator inflation of 4.05% in 2022/23 and 2.41% in 2023/24. Because of increased inflation experienced since then, this paper now assumes that

37. NATO, 'Defence Expenditures of NATO Countries (2014-2022)'.
38. HM Treasury, *Autumn Budget and Spending Review 2021*.
39. *Ibid.*, Table E.2.
40. *Ibid.*

these figures should be increased to 6.05% and 3.41% respectively.[41] On this basis, core TDEL defence spending is due to fall in real terms by 1.9% in 2022/23, 3.1% in 2023/24 and 0.6% in 2024/25. Given the extent to which inflation has increased recently, this may underestimate the changes to inflation assumptions which the OBR will make alongside this year's Spending Review.

For the six years after 2024/25, the MoD is planning its equipment programme on the assumption of an annual increase in its total budget (TDEL) of 0.5% per annum in real terms, with most of this growth used for capital spending.[42] On this assumption, the implications of which are set out in detail in Table 1, MoD TDEL rises to £56.4 billion (cash) in 2030/31, up from £50.2 billion in 2022/23.

In this baseline case, the UK remains compliant with NATO's 2% target in 2022/23 and (barely) in 2023/24, with core spending of 2.19% and 2.06% respectively. Thereafter, it becomes increasingly dependent on supplementary spending – for example in relation to Ukraine – or slower GDP growth to keep above the 2% mark.

Admittedly, the margins are small. If £2 billion is spent annually on military aid and/or operations, and if GDP grows at 1% per annum in real terms rather than the 1.5% rate assumed by the OBR, spending could still be some 2.01% in 2030/31. It is not beyond the bounds of possibility, therefore, that the UK meets the 2% target without revising the current planning assumptions.

Famine to Feast

Such a modest increase, however, would pose serious challenges to the MoD's ability to deliver on its existing plans through to the end of the decade. And it would make it much more difficult to respond to the new priorities for its defence capabilities which have emerged as a result of the war.

To respond to these concerns, and reflecting the increased political salience of defence preparedness as a result of the war, Truss has promised that, should she become prime minister, her government would commit to spending 3% of GDP on defence by 2030.[43] This would be a step change in the priority given to defence, with no peacetime parallel since the late 1930s. While the Korean War saw a sharper increase in 1951 and 1952, this was soon reversed, paving the way for steady reductions through the rest of the decade. There was a smaller increase in the early 1980s, when the UK met the NATO target of annual 3% spending increases before

41. This is close to the estimate from Ben Zaranko of the Institute for Fiscal Studies, who suggests that the GDP deflator for the three years from 2021/22 to 2024/25 is likely to be revised to an average of 3.7% per annum, compared with 2.8% per annum in the OBR's March 2022 forecast. Ben Zaranko, 'The Inflation Squeeze on Public Services', Comment, Institute for Fiscal Studies, 10 August 2022.
42. MoD, 'The Defence Equipment Plan: 2021-2031', p. 13.
43. Liz Truss, 'Britain Will Expose Putin's Lies to the World', *The Telegraph*, 23 August 2022.

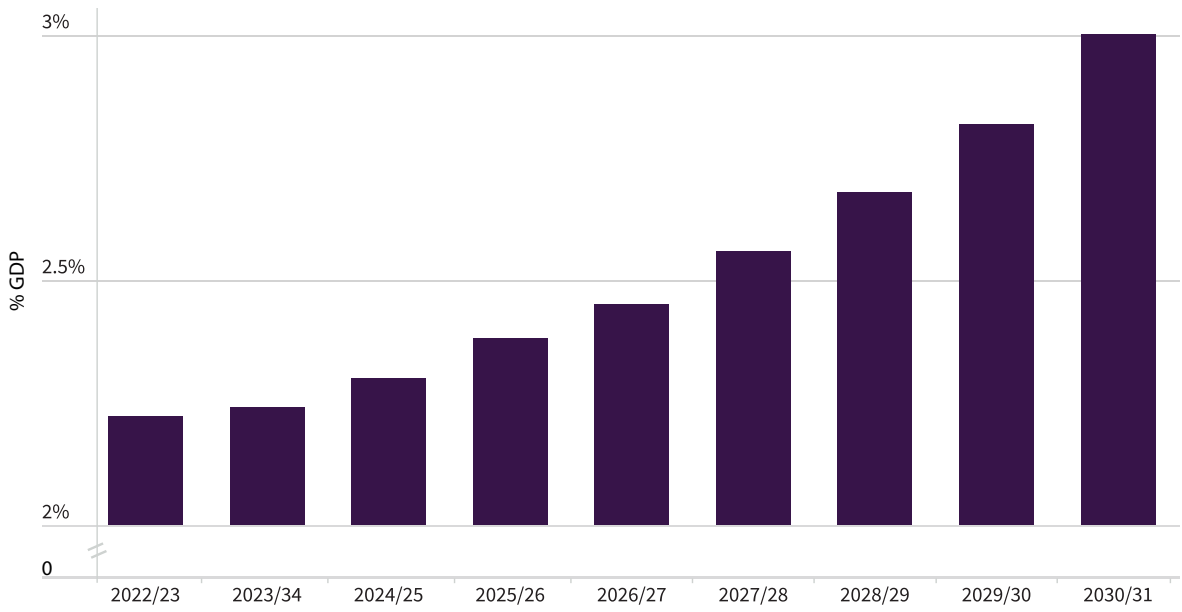
reversing these after 1984.[44] An increase to 3% of GDP by the end of the decade, if sustained thereafter, would be proportionately more significant than either of these periods of short-lived increases – even if it would not return the defence burden to the levels of either the 1950s or the 1980s.

So what would a 3% target mean, first for defence spending and then for defence capabilities?

To calculate the first of these, this paper makes the following assumptions.

- First, MoD defence spending (TDEL + AME) remains a constant proportion of total NATO-reported defence spending. This assumes that non-MoD defence spending (for example by the security services) increases at the same pace as that controlled by the MoD. No account is taken of possible future adjustments in the items which the UK reports to NATO.
- Second, it assumes GDP and the GDP deflator increase at the rate assumed by the OBR in March 2022 up to 2026/27, with an adjustment of 2% and a further 1% respectively in 2022/23 and 2023/24, to reflect subsequent increased inflation projections. After 2026/27, it is assumed that the GDP deflator increases by 2% per annum, and that GDP increases by 1.5% per annum in real terms.

Figure 2: Getting to 3% Defence Expenditure



Source: See sources for Tables 1 and 2.

44. Institute for Fiscal Studies, 'Defence Spending', Fiscal Facts, last updated 29 September 2015, <https://ifs.org.uk/tools_and_resources/fiscal_facts/public_spending_survey/defence>, accessed 13 August 2022.

On the basis of these assumptions, the paper calculates that TDEL MoD spending would have to rise to £95 billion in cash terms in order for the UK to meet its new 3% target by 2030/31.

This is £38 billion higher than is assumed in current cash planning assumptions for 2030/31 and is equivalent to a cumulative real-terms increase of 59% over the next eight years.

It will take time for the MoD to mobilise all the resources – planning and procurement, frontline and support personnel, basing infrastructure and industrial capacity – necessary to spend efficiently at this increased level. One can therefore assume, for illustrative purposes, that the rate of increase in the budget accelerates over time. This is set out in Table 2.

In this scenario, the MoD would receive an additional £157 billion over eight years, compared with current plans. Compared with flat cash, the MoD would receive an additional £188 billion over eight years. To put this in context, it compares with the 2020 Integrated Review and associated Spending Review, which provided the MoD with an additional £16.5 billion over four years, compared with previous plans for a 0.5% annual real-terms increase, and an extra £24.1 billion compared with flat cash.[45]

Box 1: Key Implications of Increasing to 3% of GDP by 2030

- Total MoD TDEL cash spending rises from £50 billion in 2022/23 to £95 billion in 2030/31.
- This is a real-terms increase of 59% over eight years.
- It adds £38 billion to 2030/31 spending compared with current planning assumptions.
- MoD spending increases by £157 billion over eight years, compared with current assumptions.
- Service personnel numbers increase by around 25–30%.

45. 10 Downing Street, 'PM to Announce Largest Military Investment in 30 Years', Press Release, 19 November 2020, <https://www.gov.uk/government/news/pm-to-announce-largest-military-investment-in-30-years>, accessed 30 August 2022.

Implications for Service Personnel Numbers

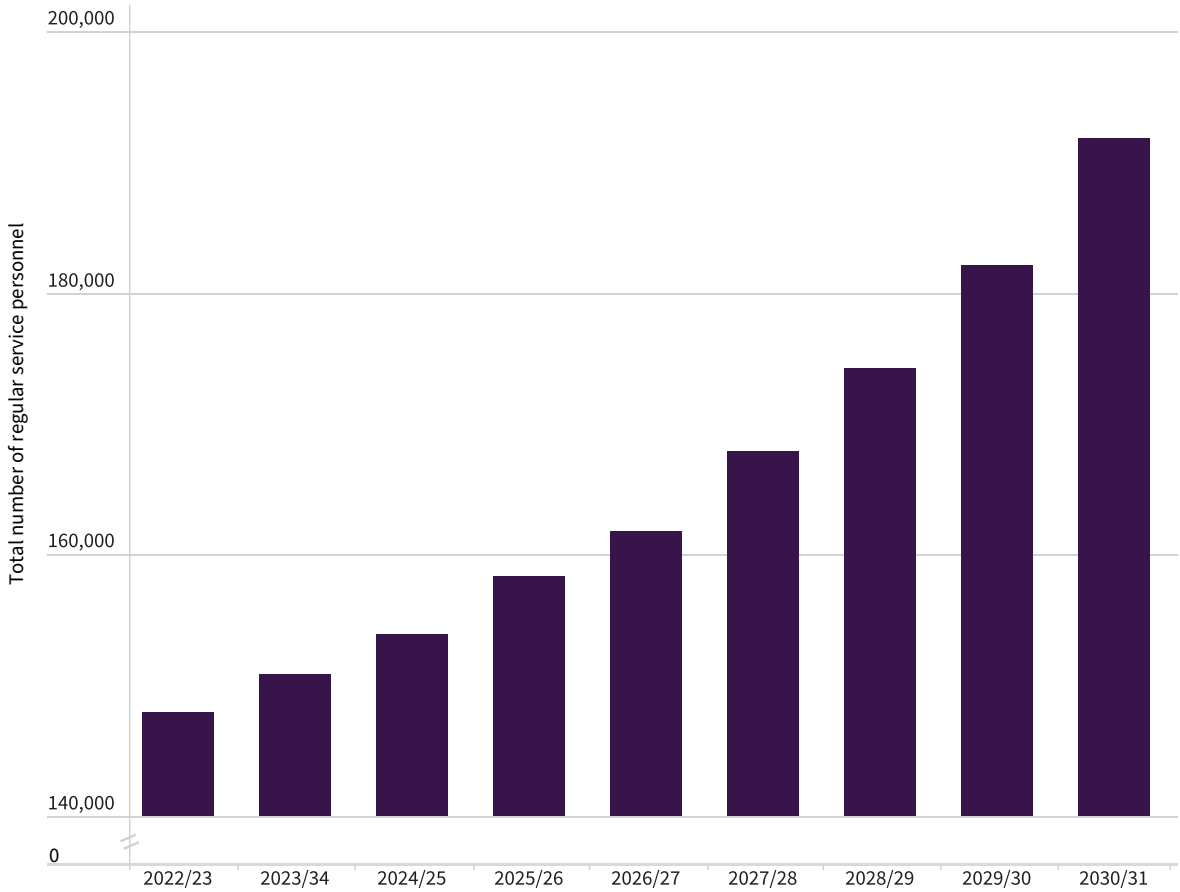
Historically, the number of service personnel tends to fall over time compared with the level of total defence spending. This reflects improvements in labour productivity as a result of investments in both frontline capabilities and support services, as well as improved processes. Over the past decade, and especially in recent years, it has also reflected increased priority given to capital spending, whose employment effects are felt primarily with defence contractors rather than MoD employees.

Between April 2010 and April 2022, total full-time service personnel (excluding volunteer reserves and Gurkhas) fell by 22.8%.[46] Total defence spending (PESA22) rose by 0.7% in real terms.[47] 'Service personnel intensity' of defence spending was therefore falling at an average rate of 2.1% per annum.

If this trend were to continue between April 2022 and April 2030, total service numbers would be expected to increase by 33.8% over this period. There are some reasons to expect that the service personnel intensity of spending could decline rather more rapidly at a time of rapid overall growth. Many new investments – in both capabilities and support infrastructure – are intended, in part, to economise on the use of personnel (both military and civilian). To the extent that a disproportionate share of new spending is on new equipment, more of the employment benefits would be felt outside government. A return to real growth in service personnel salaries, after the real-terms reduction since 2010, could also incentivise further labour-saving. Proportionately greater use could be made of less expensive, and more flexible, civilian employees and contractors.

46. MoD, 'UK Armed Forces Quarterly Service Personnel Statistics: 1 April 2022', 23 June 2022, Table 1, <www.gov.uk/government/statistics/quarterly-service-personnel-statistics-2022>, accessed 30 August 2022; MoD, 'UK Armed Forces Quarterly Personnel Report: 1 January 2013', 14 February 2013, Table 3a, <https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/280435/1_january_2013.pdf>, accessed 30 August 2022.
47. HM Treasury, 'Public Expenditure Statistical Analyses 2022', 20 July 2022, Table 4.2, <https://view.officeapps.live.com/op/view.aspx?src=https%3A%2F%2Fassets.publishing.service.gov.uk%2Fgovernment%2Fuploads%2Fsystem%2Fuploads%2Fattachment_data%2Ffile%2F1091956%2FPESA_2022_CP_Chapter_4_tables.xlsx&wdOrigin=BROWSELINK>, accessed 30 August 2022.

Figure 3: Projections for Service Personnel Numbers



Source: Table 3. These projections assume that service-personnel intensity declines by 2.5% per annum, slightly higher than the historical rate of 2.1% per annum.

Even so, it is hard to see how the MoD could sustain spending at 3% of GDP from 2030 onwards without increasing service personnel numbers by around 25–30%. At the heart of such an expanded programme is likely to be an expanded frontline capability – measured in ships, squadrons, battalions and bases – as well as increased capabilities in multiple support services. Each of these will require more people to operate them efficiently. It would be especially important to invest at an early stage in the expanded training programmes necessary to produce the skilled people who would be needed to operate the increased numbers of aircraft, drones, ships, combat vehicles and satellites which 3% would enable the MoD to buy.

Gearing Up the Machine

Table 3 sets out a plausible scenario for additional items of spending, over and above those included in current plans, which spending 3% of GDP in 2030/31 would make possible. It is based on the author's own judgements, on official reports and on several confidential conversations.

For the purposes of this 'back-of-the-envelope' paper, this single-year focus is a useful starting point. Because of the single-year focus, Table 3 excludes additional spending that would be largely completed before 2030. A more sophisticated analysis could include annual spending by programme and capability area for the whole period up until 2030.

The early years of any eight-year spending plan, if the 3% target is to be maintained, will have to involve significant investments in the preparatory capabilities needed to allow force size increases to take place later in the decade. These might include investing in expanded training contracts (for example, for scarce pilots and nuclear engineers), increased recruitment of new service personnel, expanding the resources devoted to defence procurement and increasing the production potential of defence industrial facilities (aircraft and missile factories, shipyards). The latter could include 'contracts for resilience', giving contractors a financial incentive to maintain production capability – for example, for the anti-tank missiles used extensively in Ukraine – even when there is a gap in the order book.

None of this will be easy, and it will all take time. In the 1930s, growing arms production was made possible, in part, by the ability to convert large parts of the UK's extensive manufacturing capability – for example for motor cars – from civil to military use. Given the specialist nature of many defence products and the UK's relatively small manufacturing sector, however, the government may also have to increase procurement from abroad if it is to meet its 3% target on time. Certainly, this is the experience of Poland, whose own plans to increase spending to 3% involve a large deal to buy tanks (and other equipment) from South Korea.[48] A lack of domestic capacity is also proving a major problem for Germany, whose pledge to increase spending to 2% immediately seems set to fall foul of the inability of its industry to provide the systems required on such a rapid timetable.[49]

The gradual acceleration in the pace of increase in defence spending mapped out in Table 2 is chosen bearing in mind the capacity constraints that would likely limit growing spending more rapidly without unacceptable losses in value for money. Thus, as Table 2 shows, defence spending as a percentage of GDP rises by 0.26% over the first half of the 8-year period – from 2.19% of GDP in 2022/23 to 2.45% in 2026/27. The pace of change then accelerates, with the GDP percentage increasing by 0.55% over the next four years.

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48. Brad Lendon and Yoonjung Seo, 'Poland to Buy Hundreds of South Korean Tanks, Howitzers after Sending Arms to Ukraine', *CNN*, 28 July 2022.
49. Army Technology, 'Germany Lacks Defence Industrial Strategy Despite Budget Hike', Analysis, 8 August 2022, <https://www.army-technology.com/analysis/germany-lacks-defence-industrial-plan-despite-budget/>, accessed 30 August 2022.

This trajectory also provides the government a range of options for a future Spending Review in or around 2026. Depending on the evolution of the geopolitical environment (especially in relation to threats from Russia and China) and competing demands on the public purse, the government could decide to relax the pace at which it moves towards 3%, or indeed abandon the target altogether. Alternatively, if the threats worsen and political support for increased spending grows, the government could start to plan for further increases, above 3% of GDP, in the years after 2030.

How To Spend It

The numbers below are rough estimates for the full costs to the defence budget of extra commitments that are not currently funded under SR21 and Equipment Plan. They include personnel and infrastructure, as well as equipment, costs.

Table 3: Possible Additional Cash Commitments in 2030/31 (Above Planning Assumption)

Item	Cost (TDEL)	Explanation
Compensate for 3% extra GDP deflator inflation in 2022/23 and 2023/24	£3 bn	3% of 2030/31 spending.
Direct aid to Ukraine and others	£1 bn	Long-term budget provision for such aid, based on proven value in current war.
Weapon stocks and supplies, for platforms currently in service or planned	£2 bn	Maintain increased investment levels for longer, more intense conflicts.
Future Combat Air System	£1.2 bn	UK cost share, assuming collaboration with major partners, and total UK capital cost of around £20–25 bn. Assumes production underway by 2030.
Dreadnought – extra use of contingency	£0.3 bn	By 2030, well into production of boat 2.
Nuclear warhead and AWE infrastructure	£2 bn	Very little in budget at present. In addition to current AWE £1 bn per annum.
New SSN/AUKUS	£1.5 bn	Accelerate next-gen SSN, improved weapon systems, aim at 10 submarines.
Space, to match French level	£1.5 bn	Comms / ISR.
Warfighting division	£2 bn	More artillery and fires, air defence, logistic support, more personnel.
Deep precision strike for RAF and Royal Navy, including resilience/stocks	£1.5 bn	Carrier + FCAS long-range missiles, prompt-strike hypersonic for SSN.
Added P8 + E7 + A400M aircraft	£0.5 bn	Procurement of additional 1.5 aircraft per annum.
Anti-missile (ballistic + hypersonic) capabilities, ground or sea based	£1 bn	New capabilities for both homeland defence and carrier protection.
Increase frigate numbers	£1 bn	Production increased to 1.5 per annum, now one per 18 months.
T45 replacement	£0.5 bn	Type 83 destroyer, for entry into service in late 2030s.
Extra real-terms pay increase	£3 bn	Assumes 2% annual real pay increase, total service-personnel numbers rise by 30% by 2030/31, civilian-personnel numbers rise in similar proportion.
SUB TOTAL	**£22 bn**	
Underestimation of procurement cost of current programme	£2 bn	= 20% total planned procurement for 2030/31.
UNALLOCATED	**£14 bn**	
TOTAL	**£38 bn**	

- The first item – worth some £3 billion in 2030/31 – is the amount necessary to fully compensate the MoD for the additional inflation which, it is assumed, will take place in 2022/23 and 2023/24, and which has so far not been included in spending plans. This follows the precedent set in SR21, which increased MoD spending above Integrated Review (and SR20) levels in order to compensate for then-predicted inflation.
- The calculation assumes that post-war Ukraine will require substantial ongoing external support for its armed forces, especially if (as is likely) the threat of a renewed invasion from a rejuvenated Russia remains a distinct possibility. This item might also include military aid to other lower-income 'frontline' states, for example Moldova and Georgia.
- The war has been a wake-up call for defence planners in many respects, particularly in relation to the pace at which conventional warfare between advanced armies uses up stocks of munitions and spare parts. This has exposed the low levels of stocks across military capabilities, and rebuilding these stocks is likely to be a top priority through the rest of the decade. While a large part of the most urgent requirement will have been fulfilled by 2030, this paper assumes a continuing need for higher levels of investment in stocks and munition supplies, compared with current plans.
- The largest conventional procurement programme of the next two decades is set to be the programme to replace the Typhoon fighter with the FCAS, including a new crewed aircraft and a wide range of associated capabilities. Because the final decision to go ahead has not yet been made, there is no provision for production of this system in current equipment plans. If it does go ahead, however, total capital spending is likely to be around £25–30 billion over 10–15 years. This assumes that unit costs can be kept under control through close cooperation with major partners, of which Italy and Japan are currently the most likely candidates. Total 2030/31 spending here is based on spreading this extra cost over the programme's lifetime.
- The MoD has a separate contingency budget for the *Dreadnought* submarine, which it can draw on without having to make savings elsewhere in the budget. With the first submarine having been produced by 2030, however, the risk of further cost escalation is relatively modest. This is reflected in the estimate given.
- There is much more risk involved in the programme to design and build a new nuclear warhead for the Trident missile, for which only limited provision is made in the current budget. The MoD is still trying to narrow down the uncertainties in relation to what this programme might cost. To keep the programme on track to deliver without undue delay, however, this paper estimates that an extra £2 billion per annum could be required. This is in addition to baseline Atomic Weapons Establishment (AWE) spending of around £1 billion per year.
- In announcing to NATO's June summit that the UK was now on track to be spending 2.5% of GDP on defence by 2030, Boris Johnson referred to the additional costs of AUKUS for the UK. This is a reference to the need for serious extra spending on a new generation of SSN to replace the *Astute* class – the SSN-R. Depending on the extent to which Australia decides to develop its own new SSN in cooperation with the UK, it is possible that large parts of this programme could be a joint venture, potentially including production, weapon systems, training and infrastructure. The added funding included here would allow the MoD to proceed at pace to build this new generation

of SSN. It could also be used to increase the size of the SSN fleet from 7 (the current level) to 10. This would increase the UK's ability to deploy worldwide, including in the Indo-Pacific, while maintaining the levels necessary to counter Russian threats in the North Atlantic and the Arctic.

- The extra provision for space would allow the UK to deploy a much wider range of defence satellites, with a particular focus on ISR and communications. This would be a step change in the (now relatively low) priority given to space and would allow the UK to increase spending to levels roughly comparable to France. It would respond to the rapid growth in space investments in other potential adversary powers, and China in particular.
- Although the current Equipment Plan already makes provision for significant investment in new land forces equipment, the army is still planning to make significant cuts in its personnel strength, to 72,500 by 2025,[50] a reduction that would likely have to continue under current spending assumptions. This line item would allow increased investment in army warfighting capability, including new equipment and added personnel requirements. The war in Ukraine has highlighted, in particular, the importance of longer-range ground-based fires, ground-based air defences, logistic support and a wide variety of drones. This item would allow the UK to be able to deploy a warfighting division on NATO's frontline that could fight with confidence alongside the US, Germany and other key allies.
- The next item provides for increased investment in conventional deep-strike capabilities for the other two services – including MBDA's long-range Spear 3/5 surface attack missile for the RAF (including carrier-based F-35Bs) and increased stocks of land-attack missiles for the Royal Navy's surface ships and submarines.
- To maintain space in its programme for other priorities, the RAF has had to reduce its planned buys for new P8 maritime patrol aircraft, E7 Wedgetail AEW aircraft, and A400M transport aircraft. This item would allow a multi-year programme for increasing the size of these capabilities, including necessary additional personnel spending. It could, among other things, allow some of these aircraft to play a more prominent role in power projection, as well as provide a greater wartime attrition margin.
- With the threat from conventional ballistic missiles growing, especially from Russia, China and Iran, this item would allow the UK to deploy a capability to defend against these missiles. This could potentially include point defence of critical military infrastructure – for example in Faslane or Cyprus – and/or defence of the aircraft carrier.
- Over time, the UK could decide to increase the pace at which it produces frigates, which would in turn allow it to maintain a larger fleet.
- Finally, Table 3 adds an option to increase service pay at 2% per annum above the rate of inflation. This would be a marked change from the post-2010 period, during which service pay has declined in real terms (albeit with a generous pensions offer maintained). If the MoD wants to increase service personnel numbers sharply over the next decade, however, this may be a necessary corollary cost. The argument would be especially pertinent for scarce technical skills, both for service personnel and for key civilians (such as research scientists).

50. MoD, *Defence in a Competitive Age*, p. 53.

Added together, these costs come to around £22 billion. To this, one might prudently add about £2 billion to allow for the optimism bias that may exist in the current Equipment Plan. This still leaves about £14 billion left to spend. One can imagine some possible uses of this extra money. The MoD could aim, for example, to field an additional warfighting division by the mid-2030s, double its planned purchases of FCAS, or build a third aircraft carrier. But the timetable is tight. While many things are possible with time, defence leaders have only begun to think about how to spend the full 60% increase by 2030 in a manner that delivers a commensurate increase in capabilities.

Defence Spending in an Alliance Context

Many of NATO's smaller military powers, especially in exposed states in Northern and Eastern Europe, are now increasing spending to 2% of GDP or above. Perhaps the most important comparators for the UK defence effort, however, are Germany and France. Currently, each country spends less on defence than the UK.

Germany has expressed a desire to increase its budget to 2% of GDP.[51] If it does so within the next 2–3 years, it is likely to overtake the UK as NATO's largest European spender. Even if it does so, however, the UK is likely to remain Europe's most capable military power. Germany has a much larger backlog of underinvestment in key capabilities, and it has no desire to invest in many of the areas – nuclear weapons, power projection and world-class intelligence – in which the UK will remain relatively unique.[52]

The most relevant comparator, therefore, is likely to remain France, which currently spends just under 2% of its GDP on defence.[53] Its strategic ambitions, and military capabilities, mirror those of the UK in many respects.[54] Insofar as UK defence plans depend in part on maintaining its relative position in NATO's military hierarchy, France will be the country to watch most, not Germany.

The American Connection

A central driver for the level and composition of UK defence spending is the state of the relationship with the US. As long as it is fully engaged in a crisis, the US provides a large majority of total NATO resources, as the current war support effort shows. The UK's defence effort – and, at present, the scale and ambition of its military aid to Ukraine – plays a key role in persuading the US to remain engaged in European security. It also plays a role in providing a hedge against the possibility that the US might not be engaged in support of UK interests in a future crisis,

51. Erika Solomon, 'Germany Unveils "New Era" in Defence Policy with Big Military Spending Jump', *Financial Times*, 27 February 2022.
52. Peter Hille and Nina Werkhäuser, 'Germany's Army: Will €100 Billion Make It Strong?', *DW*, 3 March 2022.
53. NATO, 'Defence Expenditure of NATO Countries (2014-2022)'.
54. King's College London and Institut Montaigne, 'The UK–France Defence and Security Relationship: How to Improve Cooperation', Report of the UK–France Taskforce, November 2018.

or at least that an adversary might believe that this would be the case. This seems more likely in non-Article 5 scenarios. In the long term, under new presidents and congresses that may become increasingly China-focused, nothing should be taken for granted. This is the central reason why the UK maintains an independent nuclear deterrent. Were faith in the US security guarantee to erode, the UK would face a much more challenging set of choices on both its foreign policy ambitions and its military capabilities.

The China Factor

Most of the UK's military capabilities (nuclear and conventional) are relatively 'geography-agnostic' and 'adversary-agnostic', in the sense that forces required to deter Russia in Europe – for example – could, with some tweaks, be repurposed to deter China in the Pacific. Even so, the balance of investment across capabilities is likely to be affected, in part, by whether Russia or China is seen as the pacing threat for the 2030s. If Russian military capability fades over time, in the wake of a defeat in Ukraine, then it may become less important for the UK to invest in greatly improved capabilities for fighting at scale on land. Naval and long-range air capabilities, by contrast, may become more important if China becomes the pacing threat for the UK, for example in the wake of a successful annexation of Taiwan.

The UK is not there yet, by any means. And a shift towards viewing China as the primary threat to UK security would have profound implications across government, of which the military consequences would be only one part. What is clear is that – despite the ongoing war in Europe – any new cross-government Integrated Review is likely to signal more focus on China, not less.

Paying for 3%

The fiscal consequences of increasing defence spending to 3% will depend on how far this is funded through reduced spending on other international commitments, cuts in domestic spending programmes, and/or increasing the overall tax burden (as a percentage of GDP).

The next Integrated Review and associated Spending Review will consider plans for defence spending alongside those for other security and international commitments. Of these, the two most substantial are the budgets for international aid (that is, Official Development Assistance, ODA), currently capped at 0.5% of gross national income (GNI),[55] and the whole-economy costs of meeting the UK's commitment to move to Net Zero, recently estimated to be around 0.4% of GDP per year on average.[56] The Labour Party is committed to increasing climate investment to about £28 billion annually (equivalent to some 1% of GDP) if it is elected to government.[57]

55. HM Treasury, *Autumn Budget and Spending Review 2021*.
56. OBR, *Fiscal Risks and Sustainability*, p. 109.
57. Keir Starmer, 'Keir Starmer Speech on Labour's Mission for Economic Growth', speech given in Liverpool, 25 July 2022, <https://labour.org.uk/press/keir-starmer-speech-on-labours-mission-for-economic-growth/>, accessed 30 August 2022.

A decision to fund defence spending increases primarily through cuts in spending on ODA and climate security would be a very significant shift in the nature of the UK's international role, undermining the careful balancing of aspirations and commitments set out in the 2020 Integrated Review.

A rapidly growing proportion of the current ODA budget is being devoted to fiscal support for Ukraine, as well as the initial support costs for refugees from Afghanistan, Ukraine and cross-Channel migrants. As a result, other parts of the ODA budget – including bilateral development assistance – are already facing sharp cuts, over and above those imposed as a result of the SR20 decision to reduce overall spend from 0.7% to 0.5% of GNI. Even if it were to be decided to cut total ODA to 0.3% of GNI once Ukraine and refugee-driven demands had faded, moreover, a cut from 0.5% to 0.3% of GNI would only fund one-fifth of the proposed increase in defence. The climate spending commitments of the current government are also relatively modest.

In principle, savings might be made by reducing the share of GDP taken by other public services. Yet this would require a reversal of the Johnson government's approach in SR20, which saw significant real-terms increases in most major domestic departments. To achieve a reduction in the GDP percentage, it would also likely require real-terms cuts over the next eight years in several of the big spending areas – health and social care, education, police and prisons, business, energy and transport. There has been little indication, so far, that a Truss-led administration would be prepared to make the difficult decisions that cuts in these areas would require.

Given the difficulties involved in generating the required scale of savings from either international or domestic departmental spending, the most likely source of funding for most of the increase in defence spending would be an increase in taxation revenues. If the entire cost of the defence increase were to be funded in this way, it would be equivalent to an additional 1% of GDP by the end of the decade. This amounts to around 5p in the pound added to the standard and higher rates of income tax, and/or a 5p increase in the standard VAT rate. So far, and in contrast to the funding of spending increases for the NHS and social care through increases in National Insurance contributions, there has been little attempt to ready the British public for the sacrifices that will be needed for a similar level of increase for defence.

Malcolm Chalmers *is Deputy Director-General of RUSI and directs its growing portfolio of research into contemporary defence and security issues. His own work is focused on UK defence, foreign and security policy. His most recent papers have been on national interest and UK foreign policy, tensions between the rules-based international systems, UK defence budgeting, and the security implications of Brexit. He has been an Adviser to Parliament's Joint Committee on the National Security Strategy since 2012, and was Senior Special Adviser to Foreign Secretaries Jack Straw and Margaret Beckett.*