

# DGAP POLICY BRIEF

## German Defense Spending

### A Repeat of the Past Instead of a New Era



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The historic aspiration of Germany's *Zeitenwende* – the new era in its foreign and security policy – will fail without the proposed funding. The growing tension between its demands for the Bundeswehr and missing resources is already driving Germany back to the old and shortsighted approach of cutting and stretching budgets and fragile procurement plans. The country needs a security decade: a ten-year systematic spending effort that closes its substantial security gap. Without sustainable funding for military security and other existential government tasks, Germany will continue to pose a risk to itself and others.

– Faced with the biggest land war in Europe in 75 years, Germany is confronted by a historic challenge: restoring its military capabilities and thus meeting its commitments to Europe and NATO.

– So far, the *Zeitenwende* is failing due to the continuing structural underfunding of the Bundeswehr. German policy-makers are not providing enough resources on a sustainable basis for its existing and future tasks.

– The Federal Ministry of Defense should adopt a ten-year phased plan to credibly demonstrate that it has the will to tackle the problems. This would boost acceptance of higher spending.

## STATE FAILURE AND THE ZEITENWENDE

If not for Russia's war in Ukraine, the current debate about German defense funding might be met with a shrug: Isn't it normal for there not to be enough money in the public coffers? For the defense minister, just like many of his colleagues, to make the case for more money for his area of responsibility but to have to make do with less?

Yet the biggest war in 75 years is, in fact, currently raging in Europe. In response to this watershed moment, the German government and parliament have pledged to restore Germany's military capabilities and provide far-reaching support to Ukraine.

This is a historic response in view of three factors:

- The magnitude of the preceding state failure
- The political significance of the success or failure of German rearmament
- The scale of the challenge for policy-makers and society

**State failure in the field of military security:** The German state has failed to fulfill a duty established by the constitution and will be unable to fulfill it for the foreseeable future. Article 87a of the German constitution, the Basic Law, requires the federal state to establish armed forces for the purpose of defense. Since the end of the Cold War, successive governments and parliaments have continued to maintain armed forces, but have failed to ensure these forces were capable of defense. The state has thus neglected its security responsibilities. Germany has been free riding on security, especially on the contributions of the United States. According to the logic of deterrence, this actually increased the risk of war.

**A historic decision point** for Germany and consequently for Europe: What happens now will determine whether Germany manages to change its political course and mindset and then stand up, including in military terms, for Europe's security, or whether it will go back to its old ways after a brief moment of alarm. This decision has massive implications for Germany's role in the EU, NATO, and on

the international stage. It is also being made at a time when the European security order is being reshaped.

**The scale of the challenge:** There will only be a turning point in German defense policy if Germany takes on the huge challenge of rebuilding its army. The review of military capabilities undertaken as part of the *Zeitenwende* documents the scale of the Bundeswehr's structural impotence. While it has still been able to carry out its international missions, that is only because the German government can set the mandates and thus the requirements. The unexpected evacuation from Afghanistan showed Germany the limits of this, in both political and military terms: if the mission conditions are controlled by an adversary rather than by the Bundeswehr, then operational readiness shrinks rapidly. The priority area – restoring Germany's collective and national defense capability by making an effective contribution to NATO – can only be rebuilt over a time frame of ten to fifteen years.

## THE STRONGEST CONVENTIONAL ARMY IN EUROPE

The German Economic Institute (IW) estimates that the historic underfunding of the Bundeswehr, relative to NATO standards, is at least 394 billion euros.<sup>1</sup> While the point is not to make up that amount, the figure does make clear the fiscal dimension of rebuilding the Bundeswehr. Given the drastic shift in the geostrategic situation, the Bundeswehr is supposed to once again become the strongest conventional army in Europe, as it was at the end of the Cold War. To achieve this, Chancellor Olaf Scholz has formulated two interim objectives, which have also been endorsed by his cabinet and a majority in the Bundestag:

**The establishment of a special fund for the Bundeswehr. This is intended to lead to improvements in three key areas:**

- **Sufficient total funding in the defense procurement budget:** As the budget for the Federal Ministry of Defense as a whole, the departmental budget 14 (DB 14), was too small, funding actually intended for investment in armaments was consumed by personnel costs and operational expenses.

<sup>1</sup> Klaus-Heiner Röhl, Hubertus Bardt, Barbara Engels, "Zeitenwende für die Verteidigungswirtschaft" [A New Era for the Defense Economy], IW-Policy Paper, No. 4, 2022, p. 7–8.

- **Guaranteed multi-year funding certainty for investments:** The Bundeswehr is only allowed to plan procurement projects if their funding is secure. This planning certainty requires a horizon of several years. While DB 14 has been regularly increased in recent years, these one-off payments were a mixed blessing: they came at too short notice to be used for defense procurement planning, especially as it was unclear whether funding would be available again the following year. The special fund can be stretched over the period to 2031, and thus offers a major improvement in the Bundeswehr's ability to plan.
- **Closing the capability gaps:** The size of the special fund, the clear commitment that it will be used solely for armaments projects, and the fact that it covers a multi-year period: all of this is meant to allow priority armaments projects to be tackled that Germany has been promising NATO since as far back as 2014.
- **"Cold-start" capability, i.e., the ability to mobilize a high level of combat power very rapidly**
- **Full operational readiness of the Bundeswehr as a whole, not just individual contingents involved in missions abroad at the expense of other units**

What is required of the armed forces is not as arbitrary as has been implied to a domestic audience in recent decades. The NATO countries, i.e., Germany and its 30 allies, have reached a detailed joint agreement on what is needed for effective collective security preparedness and what contribution should be made by each member. This joint NATO definition of military security also determines the requirements regarding the Bundeswehr's capabilities to a very large extent.<sup>3</sup>

These international requirements are currently in flux. This is partly due to NATO's new Strategic Concept, but it is also the result of the objectives of NATO's New Force Model (NFM), which were formulated at its summit in Madrid in June 2022. The refinement of these objectives in the next NATO Defense Planning Process (NDPP) will probably lead to even more ambitious requirements than is currently the case. There will be a reassessment of the mix of quality and size, technology, and rapid availability, as well as the organization of the armed forces and the resilience of civilian infrastructure.<sup>4</sup>

## STRUCTURAL UNDERFUNDING

How the Bundeswehr is supposed to meet even more demanding requirements is unclear. In reality, the financial resources that have been made available are still not enough to put an end to the structural underfunding of the armed forces. At the time of its announcement, the special fund worth one hundred billion euros sounded like a game changer. Yet, measured against Germany's ambitions and obligations within NATO, the financial requirements in all areas (armaments, personnel, day-to-day operational expenses) were already higher, irrespective of the two-percent target.<sup>5</sup> The one hundred billion eu-

### Meeting NATO's two-percent target:

Chancellor Scholz announced in 2022 that Germany will spend above two percent of its gross domestic product on defense from now on. The NATO countries reaffirmed their commitment to this target in 2014. The regular defense budget counts toward this target, together with spending from the special fund, and a share of around ten percent coming from other ministries' budgets. This would mark the first time that Germany has met this politically important NATO commitment. This represents a political turning point. Until now, the chancellor's own party, the SPD, and the Greens were opposed to meeting this commitment.<sup>2</sup>

## GROWING MILITARY AMBITIONS

The focus is not just on inputs, but also on outputs – i.e., what should be achieved with the money. Germany has decided that it wants to have the most capable conventional army in Europe. Several important qualitative goals have been established that have financial implications:

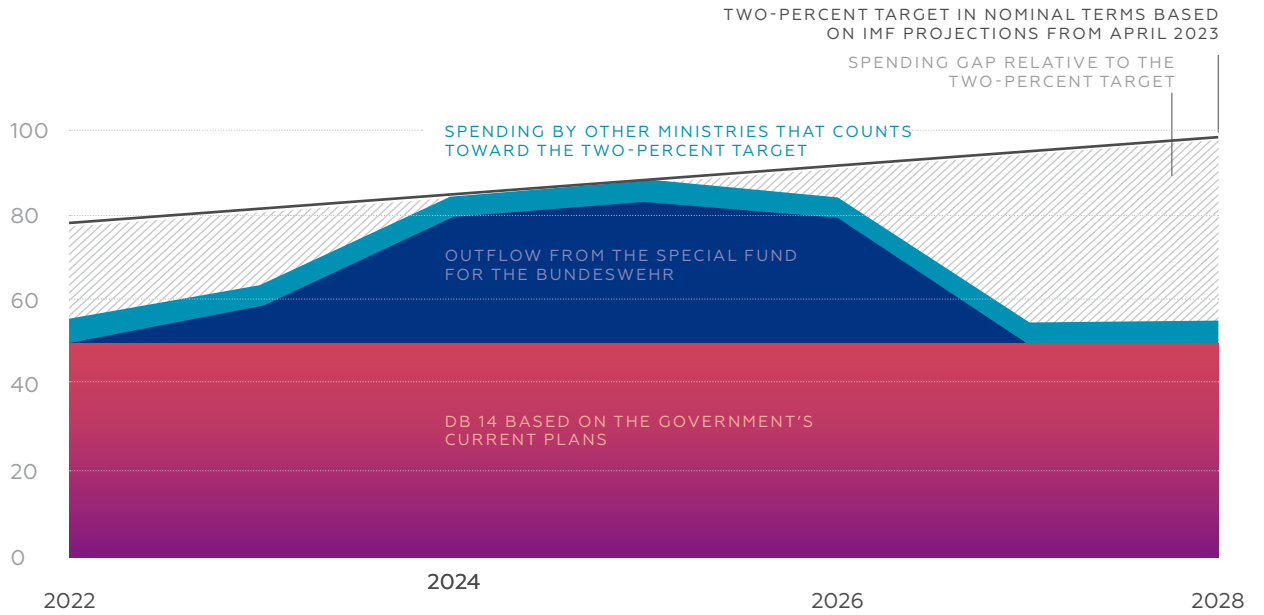
2 See Frankfurter Allgemeine Zeitung, "Mützenich fordert Abkehr vom Zwei-Prozent-Ziel der Nato" [Mützenich Calls for the Abandonment of NATO's Two-Percent Target], April 28, 2021, <https://www.faz.net/aktuell/politik/inland/ruestungsausgaben-muetzenich-fordert-abkehr-von-zwei-prozent-ziel-der-nato-17316429.html> (accessed June 12, 2023).

3 These objectives are largely identical to those of the EU.

4 See The Federal Government, "Rede von Bundeskanzler Olaf Scholz bei der Bundeswehrtagung am 16. September 2022" [Speech by Chancellor Olaf Scholz at the Bundeswehr Conference on September 16, 2022], September 16, 2022, <https://www.bundesregierung.de/breg-de/suche/rede-von-bundeskanzler-scholz-bei-der-bundeswehrtagung-am-16-september-2022-2127078> (accessed June 12, 2023).

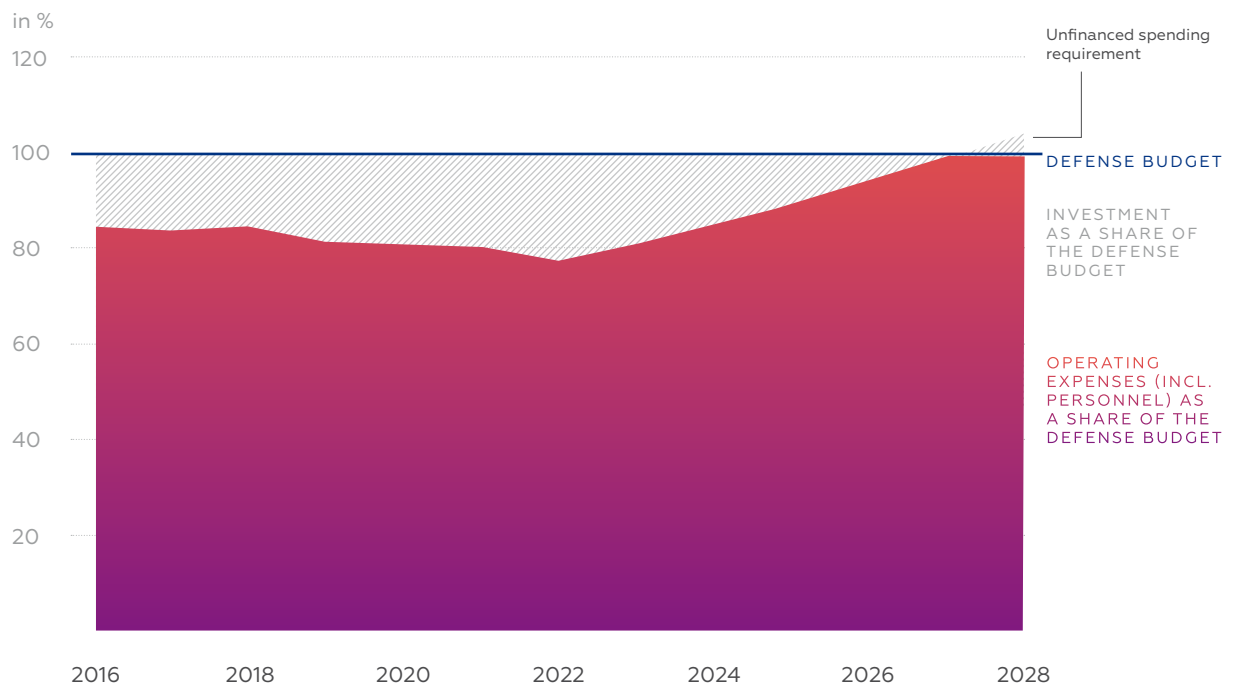
5 Christian Mölling, Torben Schütz, "Zeitenwende in der Verteidigungspolitik" [The Zeitenwende in Defense Policy], in: DGAP Policy Brief 16/2022, <https://dgap.org/de/forschung/publikationen/zeitenwende-der-verteidigungspolitik> (accessed June 13, 2023).

**Fig. 1 – German Defense Spending Based on the German Government’s Current Plans**



Sources: IMF World Economic Outlook April 2023 for GDP data (past and projections), the 2022–2026 federal fiscal plan for the projections for departmental budget 14 (DB 14), the federal budget for DB 14 (past), NATO defense expenditure data as the basis for the estimate of non-DB 14 NATO spending, own calculations of annual spending from the special fund and gaps

**Fig. 2 – The Bundeswehr’s Personnel Costs and Operating Expenses as a Share of the Defense Budget**



Source: Federal budget, own trend calculation based on developments from 2016 to 2028

ros could only have covered a portion of these requirements, and then only in the field of armaments. It was therefore clear from the outset that Germany cannot restore its defensive capabilities without increasing the size of the regular defense budget. Today, the one hundred billion euros in the special fund are no longer even enough to close the capability gaps relating to NATO commitments for which this sum was envisaged.

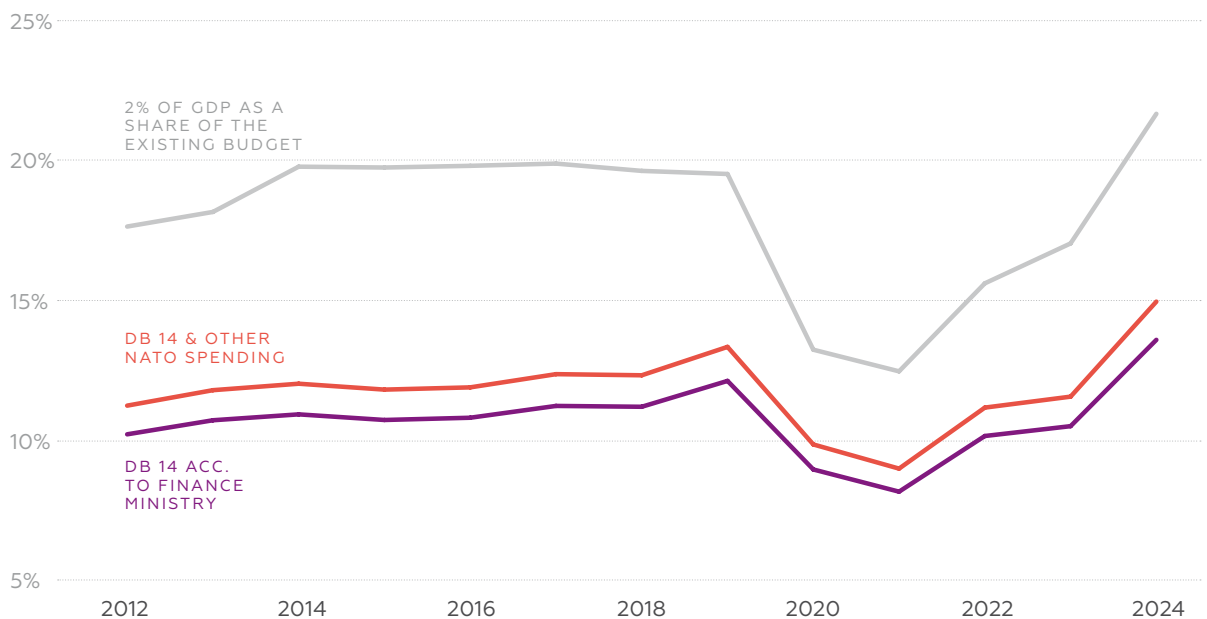
The wider picture of the financial resources for the *Zeitenwende* includes the fact that the overall defense budget has been set at 50.1 billion euros in the planning for the next few years. Even in normal times, the defense budget loses around two to three percent of its purchasing power each year. Given the high level of inflation in the eurozone, the loss of purchasing power is currently much higher. If the German government sticks to the current budget ceiling, rising personnel costs and inflation in operating expenses will eat up the defense procurement budget, because they take priority over new investment in armaments.

Although a rise in defense spending is now being discussed in the media, the increase falls short of compensating for inflation, let alone putting an end to structural underfunding. Even if the special fund is spent quickly – which would run counter to the logic underpinning it – the two-percent target could only be met at the expense of defense spending in the next electoral term.

### A BATTLE FOR RESOURCES BETWEEN THE MINISTRIES

Germany’s new defense minister, Boris Pistorius, has prioritized time as a driving factor for procurement. One reason why this factor is so important is because the amount of money that parliament will make available for defense in the next few years is likely to depend on there being some initial successes to show with regard to procurement. It will be a difficult debate, as the departmental budget for defense already faces a shortfall in 2024, estimated by the Federal Ministry of Defense at around ten billion

Fig. 3 – Defense Spending as a Share of the Federal Budget



Source: Federal budget (data for 2012 to 2023), own estimate for 2024

euros, due to the structural reasons set out above. At the same time, the tax revenue estimate for 2024 suggests that there will be no leeway in the form of additional tax revenue that has not yet been earmarked. Instead, the federal budget will face a total shortfall of 20 billion euros.<sup>6</sup>

The battle for resources is already under way, and this is reflected in the delay of the government's budget bill. There is opposition to increasing departmental budget 14 at the expense of other ministries. Simply reaching the currently planned amount for DB 14 would mean it receiving a larger share of the overall budget than in recent years – around 13 percent (blue line), compared to 11 percent on average previously. If spending were to reach the target of two percent of GDP, the departmental budget for defense would rise to over 20 percent of the overall budget (gray line) – a level that was the norm during the Cold War.

Moreover, the fiscal leeway in the federal budget is likely to diminish over the next few years. Between 2015 and 2022, annual rises in the defense budget were possible in a positive economic climate; however, the political obstacles to such increases will be considerably higher in the coming years, at least if the debt limit is still maintained. This is mainly due to the fact that interest payments on federal debt will be significantly higher than has previously been the case.<sup>7</sup>

## THE RISK: A REPEAT OF THE PAST INSTEAD OF A NEW ERA

The gap between Germany's aims for the Bundeswehr and the resources that are being provided is at risk of growing ever larger in the coming years. While there are often fears that money will be wasted if too much is made available, in reality the danger is that taxpayers' money that has already been spent or earmarked will be lost because projects cannot be completed as planned. There is a risk of a relapse into old habits: procurement plans being stretched out indefinitely, smaller quantities being purchased

at higher prices, or projects even being cancelled or expiring. If, as a result, the investments now being made prove not to be sustainable, that will undermine the Bundeswehr's military capabilities, and thus German and European security.

In light of the capabilities that Germany has pledged to its NATO allies – in particular its cold-start capability – the Bundeswehr can be described as a “hollow force.” This term refers to armed forces that appear mission-ready on paper but, on closer inspection, suffer from shortages of personnel and equipment, and from deficiencies in terms of operational readiness or training.<sup>8,9</sup> It is no secret that the Bundeswehr is experiencing a shortage of personnel, and deficiencies with regard to equipment and operational readiness.<sup>10</sup>

## OPTIONS FOR ACTION

### Making more flexible use of the special fund

In the short term, some of the defense funding problems could be solved by approving the use of parts of the special fund to cover necessary short-term spending. To ensure that this solution does not open the floodgates, approval of this option should be made contingent on the establishment of the following firewall: for a two-year period, a maximum of 20 percent of the original special fund would be allowed to be used for short-term procurement, e.g., of ammunition, and operating expenses, e.g., for exercises.

This step would be an acknowledgement of the short-term domestic political reality: the budget situation for 2024 will be poor. Nonetheless, the Federal Ministry of Defense and sympathetic parliamentarians in the Bundestag need tangible successes they can point to before the end of this electoral term if there is to be any chance of continuing the *Zeitenwende* in the next electoral term and receiving additional funding for this.

The drawback of this option is that the political and legal barriers are high. The biggest issue with a more flexible approach is that it would clash with the fun-

6 See Hans-Joachim Viewegger, “Dämpfer bei der Steuerschätzung” [Dampened Hopes Regarding the Tax Revenue Estimate], in: tagesschau, May 11, 2023, <https://www.tagesschau.de/inland/innenpolitik/steuerschaetzung-bund-lindner-102.html> (accessed June 12, 2023).

7 See Das Parlament, “Die Warnung” [The Warning], No. 48, November 2022, p. 4, <https://epaper.das-parlament.de/2022/48/index.html#4> (accessed June 12, 2022).

8 See Andrew Feickert, Stephen Dagget, “A Historical Perspective on ‘Hollow Forces,’” Congressional Research Service, p. 1, <https://sgp.fas.org/crs/natsec/R42334.pdf> (accessed June 12, 2023).

9 See Jack Miller, “Hollow Force: The Tradeoff Between Readiness and Modernization,” The Modern War Institute, August 24, 2014, <https://mwi.usma.edu/hollow-force> (accessed June 12, 2023).

10 See Frank Specht, “Ein Jahr nach der Zeitenwende-Rede des Kanzlers: Bundeswehr steht noch schlechter da” [One Year On from the Chancellor's Zeitenwende Speech: The Bundeswehr Is Even Worse Off], in: Handelsblatt, February 27, 2023, <https://www.handelsblatt.com/politik/deutschland/streitkraefte-ein-jahr-nach-der-zeitenwende-rede-des-kanzlers-bundeswehr-steht-noch-schlechter-da/29002302.html> (accessed June 12, 2023).

damental aims of the special fund, which was meant to increase the ability to plan by having a guaranteed volume and an unlimited funding period.

#### **Increasing the size of the annual budget**

Even if the special fund is allowed to be used to cover smaller expenses for a short period, the annual defense budget needs to be increased. This is necessary to facilitate regular procurement and to avoid a return, within a few years, to a situation in which the budget can only cover operating expenses and personnel. The lack of small but necessary procurements jeopardizes the Bundeswehr's operational readiness.

Increasing the size of DB 14 would also prevent overall defense expenditure from plummeting when the special fund comes to an end. Even if the fund is spent as quickly as possible, in 2026 there will already be a shortfall of around 8 billion euros to meet the two-percent target, rising to an incredible 40 billion euros in 2027. The overall gap until 2028 comprises about 90 billion euros.

Federal elections are also due to take place in 2025 – the potential new leadership of the Federal Ministry of Defense would face almost insurmountable challenges in the first year of a new government.

#### **Raising the threshold for 25-million-euro requests**

Bundeswehr procurements are subject to strict parliamentary scrutiny. Expenditure above 25 million euros requires the approval of the Bundestag's budget committee, which votes on all such proposals, known as "25-million-euro requests." Raising this threshold to 50 million euros would speed up procurement, which could facilitate the approval of higher defense spending. It would save time if fewer requests had to be submitted to the committee, discussed at length, and voted on; there would also be fewer opportunities for special interests to influence the procurement process. Another argument in favor of this change is that the threshold has not been adjusted for inflation since its introduction in 1981 (when they were "50-million-mark requests"). If inflation is taken into account, 50 million deutsche marks in those days is equivalent to around 42 million euros today.

#### **An armaments strategy for a defense technological and industrial base**

In the longer term, limited funding means that managing the selection and implementation of the projects is particularly important. The German gov-

ernment should therefore develop an armaments strategy. This should have a strategic focus, in the sense that it should view the development and maintenance of a defense technological and industrial base as part of the German defense sector's security of supply, rather than seeing it simply as a normal industry that supplies something. This means it is necessary to clarify which measures and projects can ensure security of supply, technological capabilities, and the ability to cooperate.

In this context, it is essential to define and adhere to medium- and long-term objectives in armaments policy, despite the need to speed up materiel procurement. It may therefore make sense to close the most urgent capability gaps by purchasing off-the-shelf systems, for example from the United States, in order to avoid lengthy development and production processes. In the medium and long term, however, Germany should not lose sight of strategic objectives such as national or European sovereignty.

The German government should recognize that its procurement decisions are also a form of industrial and technological policy-making, and take a thought-out rather than a random approach. Accordingly, it is important to identify trade-offs (for example between greater European cooperation and retaining production capabilities in Germany) and take a solution-oriented approach to dealing with them.

One obstacle to European armaments coordination is the protection of key national technologies. Even on cost grounds alone, however, cooperation is often necessary; then there are issues such as economies of scale and interoperability. In other words, it is important to take a measured approach when determining which key technologies can be obtained from European partners or developed jointly, without this diminishing security.

#### **A security decade**

The erosion of military security means that a major effort must now be made to address this. But the same is true of many other areas of public life, such as climate action or cybersecurity. Security risks are becoming more varied and threatening. Against this backdrop, the efforts made to date in the existing financial framework seem inadequate and ineffectual.

One part of the solution could be determining spending and revenue for a longer period: by declaring a security decade, Germany would redefine the strategic framework. This would also extend the

**Fig. 4 – Phased Plan for Sustainable Funding**

Source: Authors' own compilation

time horizon in which key stakeholders look at government spending and give their assessment. This is true of the ministries, but also of the Bundesrechnungshof (Germany's supreme audit institution), the German Taxpayers Federation, the parliamentary budget committee, and other experts. The decade could begin when the next government takes office. At that point, the special fund for defense would be almost entirely used up.

Making the transition to a functioning defense sector would require additional spending equivalent to around 0.5 percent of GDP – the current gap relative to the two-percent target – which the German government should provide. A similar amount is likely to be required for climate action.<sup>11</sup> On top of this, there are other areas with significant investment needs, such as digital transformation. All told, Germany would have to spend somewhat more than one percent of its GDP, on top of the two-percent target, for a ten-year period in order to be able to comprehensively protect its population, companies, and political institutions.

As a starting point, the German government should develop a comprehensive security concept setting out clear priorities. It should avoid pitting one dimension of security against another, such as climate against defense, or the protection of minorities against energy security.

The security concept should build on the National Security Strategy. The initial groundwork for the security decade should be carried out by a taskforce during the current electoral term. This includes drawing up a plan for a reform of public funding so that shocks and crises can be handled better than in the past.

#### Europeanization and greater efficiency

A security decade will only win support if the opportunity is also taken to improve efficiency. At the national level, this is covered by the armaments strategy (see above). However, there is also potential for efficiency to be boosted at European level. European armaments cooperation is an important lever in this context. It promises huge benefits for the countries involved: lower costs as a result of joint development, greater economies of scale as a result of higher quantities, enhanced interoperability and standardization, and a reduction in overcapacity and duplication on the side of industry.

That said, past cooperation projects, such as the A400M, the Eurofighter, or the NH90, have not really lived up to these expectations. National industrial interests or political symbolism took center stage, rather than European efficiency. There are signs of similar problems with current projects, such as the Future Combat Air System (FCAS). A new balance needs to be struck between protecting national cen-

<sup>11</sup> See Zsolt Darvas, Guntram B. Wolff, "A Green Fiscal Pact for the EU: Increasing Climate Investments While Consolidating Budgets," in: Climate Policy No. 4, December 2022, p. 412.



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ters of industry and meeting the overarching aims of using funds efficiently and strengthening common European defense. National autonomy in the military sector is an illusion for European countries. Even if budgets increase in the medium term, it will be impossible even for large economies such as Germany to operate independently and ensure their own security autonomously.<sup>12</sup> If Europe wants to retain its ability to act, it can only do so by working together. However, this requires a much greater degree of vertical integration of Europe's armed forces.

Such ambitious steps in the field of defense will only be taken if it is credibly shown in advance that they are achievable. This will probably only be possible when short-term elements are in place, such as the armaments strategy and the first successful projects. It makes sense to take a phased approach to the various solutions (see Figure 4).

## CONCLUSION

As long as the structural problems exist, an increase in defense spending will always be viewed with a great deal of skepticism, both by the public and by the Federal Ministry of Finance or the Bundesrechnungshof, for example. Only when the Federal Ministry of Defense can credibly demonstrate that it has both the will and a plan to address the problems will there be less pressure to justify new spending. Embarking on reforms can also build trust, paving the way for a short-term increase in the departmental budget for defense.

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12 See Sophia Becker, Torben Schütz, "Reform oder Irrelevanz" [Reform or Irrelevance], in: Internationale Politik, January/February 2022, pp. 42–46.

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