

The Strategic Compass: how to ensure security of supply and enhance the EU's resilience?



Ministry of Defence
Republic of Latvia



A report based on a conference co-organised by the Finnish Ministry of Defence, the Latvian Ministry of Defence and the EU Institute for Security Studies (EU ISS), on 4 June 2021.

Report

INTRODUCTION

Security of supply is an essential pillar of the EU's resilience and there is a need to guarantee the supply of raw materials, critical components and technologies. The Covid-19 pandemic has revealed vulnerabilities in the EU's strategic value chains and geopolitical competition has already raised questions about the resilience of supply chains. The Strategic Compass provides an opportunity to highlight the importance of security of supply for EU security and defence. It could also help stress the need for cross-border cooperation between EU Member States and European defence industries, especially in relation to developing critical European know-how, technologies, capacities and logistical arrangements. In this respect, a truly comprehensive approach for security of supply is required that brings together Member States, industry and EU institutions.

SUPPLY RESILIENCE

The constraints in medical equipment at the start of the pandemic and the current shortage of semiconductors are just some of the examples that highlight the critical importance of security of supply. Supply and logistical resilience is a multi-dimensional topic that includes legal, economic, industrial, environmental and strategic aspects. There is no agreed EU definition of what security of supply means in the defence sector, but there is wide recognition that it is critically important if Member States are to discharge their defence commitments at a national and international level. In fact, the 10 May 2021 Council Conclusions on security and defence underlined the need to strengthen and improve security of supply for defence products and technologies.

For the defence sector, supply constraints for key raw materials and technological components could undermine the performance and maintenance of defence capabilities and equipment. Due to the fact that certain critical raw materials are in the hands of only a few countries, the risk of harmful dependences is quite high. In its work on security of supply, the European Defence Agency (EDA) has identified 18 areas that are critical for

security of supply including defence procurement, supply chain security, disruptive technologies, raw materials, trust and skills. Security of supply in defence has already led to strategic stockpiling at the national level and investments in new technological innovations such as additive manufacturing ("3D printing").

Yet it is not just defence equipment that matters as security of supply is fundamental to the functioning of critical infrastructure in the EU. The security of the Union's financial services, health systems, transportation and digital economy is also dependent on supply and logistics resilience. In this respect, security of supply has internal and external dimensions: the internal focusing on the proper functioning of the single market and technological and industrial capacities; the external focusing on supply chain resilience, diversification and strategic supply partnerships.

Even though the defence sector has specific supply and logistics requirements, it is also important to have a clearer idea of how supply chains function. For example, the semiconductor supply chain is global and extremely complex. Modern microchips are produced with approximately 300-400 chemicals from Japan, South Korea and the United States; 50 different types of highly specialised equipment found in the US, Europe and Japan; and silicon wafers that are produced by only 4 companies found in Japan, Taiwan and South Korea. In this respect, not only does the EU have a high degree of dependence on external suppliers for semiconductors, but the idea of EU self-sufficiency in this sector appears implausible.

CHANGING MINDSETS AND POLICIES

Traditionally, the EU has put its faith in a free market mentality that has not always been appreciative of the potential political manipulation of materials and supply. The 'just in time' logic may actually lead to supply vulnerabilities, even if it makes sense from an economic point of view. China is helping to shift this mindset and EU policy is already responding. For example, in May 2021 the European Commission adopted its updated industrial strategy and this called for more sector-specific public-private alliances to address critical supply in areas such as microprocessors. Furthermore, since October 2020 a screening mechanism for foreign direct investment has been in place in order to dissuade and identify potentially harmful acquisitions of key infrastructure and supply chains. Finally, the Commission adopted a Strategy on Critical Raw Materials in September 2020 to better analyse supply vulnerabilities.

There are also valuable experiences at the EU Member State level that can provide useful lessons learned for the Union as a whole. In Finland, for example, there is a National Emergency Supply Agency that coordinates and budgets all security of supply efforts for critical infrastructure, production and services and national defence. There has also been an active approach to developing public and private networks including government ministries, defence forces, industry and universities. The aim has been to strengthen Finland's overall knowledge base in order to invest in supply-relevant research

over the longer term. This way the Finnish defence forces are better prepared for supply shocks in increasingly complex areas such as cyber defence, military platform development and telecommunications.

In Latvia, there has been a focus on security of supply in defence and this has led to steps to improve warehousing and stockpiling capacities, as well as investing in secure communications. The country has worked to ensure that key national infrastructure such as rail hubs can meet the needs of defence forces. Latvia has also invested in its domestic defence industries, integrated the issue of resilience in its acquisition strategies and it has worked with government and civil partners in the Baltic region to diversify supply. Telecommunications has also become an important feature of Latvia's defence and resilience, with government and national technology firms seeking to develop secure communications without the involvement of harmful suppliers in the value chain. Such an approach has led to increased networking among private actors in the European telecommunications sector.

THE STRATEGIC COMPASS AND SUPPLY

One key challenge facing the EU relates to emerging and disruptive technologies, the development of which can bring both challenges and opportunities in relation to security of supply. The EU has a vested interest in investing in emerging defence technologies in order to maintain a technological edge. However, these technologies are still dependent on potentially precarious supply chains and industrial capacities. The EU needs to think about the best way of ensuring that it has a minimum level of technological production capacity, especially in critical supply and technology domains. However, in order to do this, the EU needs a capacity to monitor new technological developments and critical dependencies. In this respect, new initiatives such as the 'EU Observatory of Critical Technologies' could lead to better resource and supply chain mapping.

Another key feature of security of supply that perhaps does not receive dedicated attention is skills. Without skills and talent, the EU and its Member States will not be able to develop, master and use new technologies. This is why initiatives such as the EU 'Pact for Skills' are important, and the aerospace and defence sectors are a key focus for training programmes and skills development. Talent development and retention in critical economic sectors are essential if innovative approaches to supply resilience are to be created.

Another key challenge is managing cross-border supply chains in the EU. Solidarity within the Union was in short supply at the start of the pandemic, which resulted in border restrictions and a lack of trust between EU Member States. In this respect, having in place a coherent national security of supply strategy does not necessarily safeguard a country from cross-border supply shocks. Stockpiling can help in certain regards, but there is a need to enhance

the EU single market so that supply is maintained during crises such as pandemics.

This, of course, has a direct bearing on defence because any cross-border restraints that might appear between EU Member States and NATO allies could seriously undermine military mobility and the supply of equipment, fuel, replacement parts and ammunition. It is worth recalling here existing EU legislation, especially the directives on defence procurement and defence transfers that were adopted in 2009. Both of these regulatory tools, which were designed to enhance security of supply in defence within the EU, have not yet reached their full potential.

It is not easy or advised to go for a 'one size fits all' approach to security of supply and defence in the EU. Member States have in place different national security of supply strategies and these reflect their geographical location, threat perception and defence interests. In this respect, security of supply solutions need to be targeted or tailored to diverse national needs. However, it is also true that no coherent EU approach to security of supply in defence can emerge without the Member States' willingness and cooperation.

In this respect, the Strategic Compass could represent a means to re-emphasise the importance of cross-border security of supply resilience and propose concrete ways to move forward. It could also contribute to creating greater awareness of the importance of supply during periods of crisis and strengthening European commitments and arrangements to ensure Member States' access to critical resources in times of crisis. Additionally, EU security and defence tools such as the CARD, PESCO and the EDF can assist in generating supply resilience by stimulating industrial collaboration and innovation. Finally, the Compass can also underline the importance of partnerships as critical global supply chains will require closer strategic coordination between suppliers, manufacturers and end-users. Enhancing security of supply will require active involvement and continued efforts from the Member States, the EDA, the Commission and defence industry, but also close cooperation with key partners, notably NATO.