

Eurosif discussion paper: Sustainable investment and defence



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Introduction

Driven by escalating geopolitical tensions, security and defence is now a major concern across European countries. To address financing challenges and ensure the security of citizens, public defence budgets are being strengthened across the continent. Any perceived barriers to scaling up the defence sector¹ and capacities are now under increased scrutiny. This includes whether market practices, European regulations, or national laws could be limiting investment towards the sector.

In this context, recent political debates have increasingly focused on the links between sustainable finance and defence. In response, some European regulators have provided clarification on the legal interactions between sustainable investing and the defence sector, while some asset managers and national industry organisations are updating their practices. Political, regulatory, and financial actors have now started to position themselves on this question.

Eurosif, the European Sustainable Investment Forum, acknowledges the need to boost European defence capabilities in the current geopolitical landscape. Ensuring the safety and security of citizens is crucial, and European countries must have the necessary resources to achieve that objective. However, whether, and if so to which extent, sustainable investments by private actors should play a role in achieving these goals is a highly sensitive and complex topic. It requires composing with divergent viewpoints emanating from different cultural, historical, geographical and ethical perspectives. The debate and associated policy decisions also have significant business impacts for the investment industry.

The objective of this discussion paper is to clearly establish the current market and regulatory dynamics between private finance and the defence sector and explore the different viewpoints around sustainable investing in the defence industry, by outlining the core arguments shaping the conversation across Europe.

This discussion paper does not present policy proposals or a formal position from Eurosif, Eurosif members/observers, or Eurosif partners.

It aims to provide a state-of-play on investors' varied perspectives on these issues as they are being discussed across Europe.

¹ For the purpose of this discussion paper, the “defence sector” refers to the defence and aerospace sector and companies selling military equipment, technology, and services to government armed forces and other clients.

I. The financing challenge: distinguishing the roles of public expenditures and private investments

Considering recent political debates on the topic, a first question should be to delineate what type of financing contributes to scale-up European defence capacities and whether mobilising sustainable investments, as part of private investments, is necessary to do so.

I. Financing channels to developing defence capacities

The role of governments and public authorities

Financing needs are one of the key challenges for scaling-up European defence. European governments already mobilise important amounts for this objective. In this regard, it is key to clearly separate the roles of different actors: governments and public authorities responsible for ensuring the safety of their citizens via their total expenditures on defence (including public investment), from financial institution's role related to private investments in defence companies.

Total expenditures on defence represent the global budget allocated by governments to defence – including investments, but also resources dedicated to maintenance of infrastructures and armed forces. EU member state's defence expenditures totalled **€326bn in 2024**, an EU average of 1.9% of GDP, and are undergoing significant pressure to increase this figure to **5% of GDP**. In the same period, UK defence spending has reached almost **€66bn** and is expected to rise to **€69bn** in 2026.

Public investment in defence is a subset of this global budget allocated to defence and constitutes spending for scaling-up, improving and modernising defence capabilities, often by providing direct capital in support of specific projects. It is mainly composed of **public procurement** – where governments are acting as customers, buying defence equipment, technology and services from companies that produce them is a significant part of countries' national defence investments: for EU countries, it amounted for 80% of public defence investment in 2024, with €88 billion.²

Investments in defence also seek to fund specific projects or research and development capacities. Several public programs have been implemented to support these investments at national and EU levels. In the EU, public programs amounted to €4 billion a year in 2024³, including programmes such as the European Defence fund, Connecting Europe Facility or the European defence industry programme (EDIP).⁴ Recently, the European Investment Bank (EIB) also widened its eligibility criteria to include defence investments.⁵

² <https://www.consilium.europa.eu/en/policies/defence-numbers/>

³ <https://www.bruegel.org/policy-brief/governance-and-funding-european-rearmament>

⁴ <https://www.consilium.europa.eu/en/policies/defence-numbers/>

⁵ [https://www.eib.org/en/press/all/2025-156-eib-steps-up-financing-for-european-security-and-defence-and-critical-raw-materials#:~:text=The%20European%20Investment%20Bank%20\(EIB\)%20is%20the,%20Critical%20infrastructur%20*%20De%2Dmining%20and%20de%2Dcontamination](https://www.eib.org/en/press/all/2025-156-eib-steps-up-financing-for-european-security-and-defence-and-critical-raw-materials#:~:text=The%20European%20Investment%20Bank%20(EIB)%20is%20the,%20Critical%20infrastructur%20*%20De%2Dmining%20and%20de%2Dcontamination)

The contribution of private finance flows and financial institutions

There is a fundamental difference between the role of financial institutions and the role of governments or public authorities when it comes to investments in defence.

Mobilisation of investments from private actors, such as financial institutions, towards the defence sector can support scaling-up defence investments, given the current tight context on public budgets and spending. The European Commission's ReArm Europe/Readiness 2030⁶ plans and the Defence Equity Facility aim, among other goals, to further mobilise private investments towards EU defence companies.⁷

However, while some investors may provide targeted funding for specific defence projects, private financial institutions more commonly purchase shares and other securities issued by defence companies on secondary markets. This can still indirectly support a company's growth by improving liquidity and lowering its cost of capital, but portfolio construction is ultimately guided by the institution's fiduciary duty and the mandate it receives from end clients, e.g. retail investors or institutional asset owners. In practice, that means selecting assets to deliver appropriate risk-adjusted returns while reflecting client preferences, including how they want their capital managed from a risk, sustainability, and ethical standpoint.

A widely held view among investors is that financial institutions should not be tasked with the responsibility to directly finance the development of defence capacities, which is the task of governments and public authorities.

2. Sustainable investments and defence: a varied landscape

The combination of the willingness from some investors to support European defence capacity-building and the important hikes in defence public procurement expenditures have led to consistent growth of the defence companies and high performance of defence stocks. European defence firms' stock price nearly tripled since 2022 while rising by 9% in the first three quarters of 2025 alone.⁸ For these reasons, the flow of private investments to defence companies has significantly increased in recent years.

Sustainable investments – as a subset of overall private investments – apply additional lenses to the selection of assets in a portfolio. These often consists of one or a combination of specific investment approaches, such as positive and negative screening, integration of ESG factors in the investment decision-making process, engagement with investee companies, focus on specific themes or trends, and/or focus on achieving real-world impact.⁹ Consequently, the landscape of investment funds incorporating an ESG approach (“ESG-

⁶ [https://www.europarl.europa.eu/RegData/etudes/BRIE/2025/769566/EPRS_BRI\(2025\)769566_EN.pdf](https://www.europarl.europa.eu/RegData/etudes/BRIE/2025/769566/EPRS_BRI(2025)769566_EN.pdf)

⁷ https://defence-industry-space.ec.europa.eu/document/download/513de692-d08c-40cc-80c3-cb6611ace178_en?filename=EU-Defence-Industry-Transformation-Roadmap.pdf#:~:text=5%20Private%20investment%20into%20European%20deep%20tech,marking%20a%20fivefold%20surge%20compared%20to%202019.

⁸ <https://www.reuters.com/business/aerospace-defense/european-defence-stocks-move-up-after-trumps-ukraine-comments-2025-09-24/>

⁹ <https://www.gsi-alliance.org/wp-content/uploads/2023/12/GSIA-Report-2022.pdf>

related funds”) is as diverse as the policies of financial institutions and the underlying preferences of their end clients. This explains a significant level of divergence in whether, and how, ESG-related funds can integrate exposures to the defence sector.

In the EU, over half of funds promoting Environmental or Social characteristics¹⁰ were exposed to the defence sector in Q2 2025, a significant change from end 2021 where only a third of these funds presented these exposures.¹¹ During the same time frame, exposures of funds promoting sustainable investments to the defence sector decreased, from 30% to around 21%.¹² ESG-related funds remain on average much less exposed than mainstream funds, 66% of which were exposed to the defence sector in Q2 2025.¹³

Average weighted exposure of mainstream funds to the defence sector rose dramatically between early 2024 and end 2025, from 1.75% to 2.52%. This increased focus is also verified for funds promoting Environmental or Social characteristics, where exposures to the defence sector amounted to 1.42% by end 2025, a stark increase from the 0.8% recorded in early 2024. Funds with a sustainable investment objective saw a much more limited rise in their weighted exposure to the sector - from 0.29% in early 2024 to 0.47% in end 2025.¹⁴

These figures demonstrate an increase in the overall exposure of ESG-related funds to the defence industry driven by the high performance of defence stocks mentioned above, as well as a redefinition of some investors’ exclusion policies considering the current political context. Indeed, **regulations across Europe are sector-agnostic and leave the possibility for investors that wish to do so to invest – or not – in the defence sector.** The next chapter will focus on some of the regulations currently applicable in Europe and how they interact with the defence sector.

¹⁰ So called "Article 8" funds under SFDR

¹¹ <https://www.sustainalytics.com/esg-research/resource/investors-esg-blog/eu-esg-funds--exposure-to-defense-continues-to-increase>

¹² So called "Article 9" funds under SFDR

¹³ <https://www.sustainalytics.com/esg-research/resource/investors-esg-blog/eu-esg-funds--exposure-to-defense-continues-to-increase>

¹⁴ <https://clarity.ai/in-the-news/article-8-funds-increase-defence-exposure-by-nearly-60-in-one-year-clarity-ai-data-shows/>

II. Sustainable finance rules and the defence sector

I. The necessity to maintain sector-neutrality of regulatory frameworks

A perspective that gained some level of traction in recent years – pushed in part by the defence industry itself¹⁵ – is that defence can be seen as socially beneficial, and hence that it could be considered as socially sustainable. This is because at the most basic level the lack of defence capabilities endangers peace and fundamental social and human rights, and that defence goods and services should be considered socially sustainable on the basis of their contribution to European peace, security and stability. This view takes an uncompromising approach, implying that virtually all investments in defence can be considered sustainable in the interest of self-preservation. It is generally accompanied by a criticism of the current sustainable finance regulations, presented as *de facto* preventing investments in the defence sector and hindering the scaling-up of European defence capacities.

However, this is a contentious point that many investors disagree with. Such an approach would bypass the consideration of the specific ESG risks of the defence sector (see [Part III.2](#)), and the assessment of the policies of investors and the preferences of their end clients. Stakeholders against this view also highlight that it would change the principle of sector neutrality that underpins sustainability frameworks across Europe and ultimately risks weakening the credibility of sustainable finance.

Indeed, in response to this push, some institutional actors such as the European Commission have started publicly flagging that while **investments in defence** are not prohibited under the EU sustainable finance framework, they also **cannot be considered by default as (socially) sustainable**, as they must respect certain criteria for that effect. This was recently clarified in a notice¹⁶ issued by the European Commission on how the EU sustainable finance framework applies to defence investments. This document also specifies that investments in the defence sector cannot automatically be considered as socially sustainable. In the UK, the Financial Conduct Authority (FCA) also provided a similar clarification.¹⁷

2. Sustainable Finance Disclosure Regulation (SFDR) review and minimum exclusions

The SFDR permits the inclusion of any company, provided the investment strategy is properly disclosed and justifiable against sustainability objectives. The SFDR introduces a “Do No Significant Harm” (DNSH) principle to determine whether an investment is sustainable and must disclose in line with the requirements of Article 9. Under SFDR, an investment cannot be deemed sustainable if it causes significant harm to any EU environmental or social objective. However, the regulation does not specify at what point exposure to some activities

¹⁵ <https://www.asd-europe.org/news-media/publications/asd-position-papers/sustainability-and-the-european-defence-industry/>

¹⁶ https://defence-industry-space.ec.europa.eu/document/download/ac79ebc7-d2f1-4e7a-a79c-71a06a5fdbf8_en?filename=notice-application-sustainable-finance-framework-and-corporate-sustainability.pdf

¹⁷ <https://www.fca.org.uk/news/statements/our-position-sustainability-regulations-and-uk-defence>

constitutes significant harm and largely leaves it up to financial institutions to determine it. To do so, financial market participants can use a set of mandatory Principal Adverse Impact (PAI) indicators, among which PAI 14 on investment exposure to controversial weapons – listed under the SFDR Delegated Regulation as antipersonnel mines, cluster munitions, biological and chemical weapons – and PAI 10, on violation of human rights conventions (mentioning the UN Global Compact and OECD Guidelines for Multinational Enterprises).¹⁸ The European Commission has emphasised¹⁹ that the EU’s SFDR is sector-agnostic and hence, does not prohibit investments in defence companies.

In their proposal for a review of SFDR published on 20 November 2025,²⁰ the European Commission suggests establishing three formal categories of sustainability-related products, underpinned by minimum criteria. Among these criteria, minimum exclusions referencing the ones applied under the EU climate benchmarks (Paris-Aligned Benchmarks - PAB, Climate Transition Benchmarks - CTB). These notably cover exclusions of companies found in violation of the United Nations Global Compact (UNGC) principles or the OECD Guidelines for Multinational Enterprises and companies involved in any activities related to “controversial weapons”, defined as *“those referred to in international treaties and conventions, United Nations principles and, where applicable, national legislation”*.

In a recent amendment²¹ to the EU Benchmarks Regulation, the term of “controversial weapons” used for PAB/CTB exclusions is replaced by the term of “prohibited weapons”, with a finite list corresponding to the four types of weapons already listed under the SFDR Delegated Regulation: antipersonnel land mines, cluster munitions, biological weapons and chemical weapons.²² It is important to note that exclusions based on this list – as well as exclusions of other “controversial” weapons – are already widely adopted by investors (see [Part III.3.i.](#)), and have a very limited impact on the European defence and aerospace sector, as almost none of the European listed companies are involved in their manufacture.²³ However this may change in the future, considering announcements by some European countries of their withdrawal from some of the international treaties related to controversial weapons.^{24,25}

In consequence, while the SFDR review is still being discussed between legislators, it is possible that future funds categorised under the SFDR framework may have to exclude

¹⁸ In the 2023 review report of PAI indicators, the ESAs suggested the replacement of the UN Global Compact reference with the UN Guiding Principles, which are more aligned with the OECD guidelines.

¹⁹ https://defence-industry-space.ec.europa.eu/document/download/ac79ebc7-d2f1-4e7a-a79c-71a06a5fdbf8_en?filename=notice-application-sustainable-finance-framework-and-corporate-sustainability.pdf

²⁰ <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52025PC0841>

²¹ <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A02020R1818-20260119>

²² “[...] prohibited weapons shall mean anti-personnel mines, cluster munitions, biological and chemical weapons the use, possession, development, transfer, manufacture, and stockpiling of which is expressly prohibited by the international arms conventions to which the majority of Member States are parties [...]”.

²³

https://assets.contentstack.io/v3/assets/blt4eb669caa7dc65b2/blt0800586197539ecb/678181749c83122034b48298/Global_Defense_Sector_Landscape.pdf#page=75

²⁴ <https://valtioneuvosto.fi/en/-/finland-presented-the-instrument-of-withdrawal-from-the-ottawa-anti-personnel-landmines-convention>

²⁵ <https://www.clusterconvention.org/statement-of-the-13msp-presidency-on-lithuanias-effective-withdrawal-from-the-convention-on-cluster-munitions/>

investments in companies found in breach of human rights conventions and involved in any activities related to “prohibited weapons”.

To conclude, while limited exclusions connected to “prohibited” weapons and human rights breaches apply, **European laws, including the EU sustainable finance framework, do not prevent investments in the defence sector.** Whether investments in defence can be considered sustainable is largely left to the discretion of financial institutions and end investors.

The next chapter of this discussion paper dives into the different factors and perspectives that explain how and the extent to which investors and their clients consider the inclusion of the defence sector in investment portfolios.

III. The investor perspective: sustainable investment and defence

Sustainable investing in the defence sector is a complex and sensitive topic, often characterised by diverse and strongly held views, formed via a range of national, cultural, historical and geographical factors. In this section, we aim to summarise the diverse perspectives of investors and their clients.

I. *A priori* exclusions on ethical grounds

Some financial institutions may **exclude the defence sector from their sustainable investments on ethical or values-based grounds.** Such exclusions may reflect their own principles and/or explicit client requirements; for example, faith-based asset owners whose investment policies prohibit certain activities. Investors adopting this stance typically take a precautionary approach, either applying blanket exclusions to defence-related activities or setting strict revenue thresholds to limit meaningful exposure.

These investors draw on broad definitions of sustainability to support this position. For instance, the United Nations (UN) frames sustainability as ensuring prosperity and environmental protection “*without compromising the ability of future generations to meet their own needs.*”²⁶ On that basis, they argue that investing in companies involved in weapons production is inherently incompatible with sustainability-focused strategies because such activities can contribute directly to physical harm and societal disruption. Similarly, while many financial institutions use the UN’s Sustainable Development Goals (SDGs) as a guiding framework for their investments, investing in the defence sector may be seen as contradicting the SDG 16 to “*promote peaceful and inclusive societies for sustainable development*”.²⁷

Proponents of exclusion further point to the nature of arms production; the scale of harm associated with military operations (including impacts on civilians) and the wider social consequences of arms proliferation. They also emphasise a practical challenge: it can be

²⁶ <http://www.un-documents.net/our-common-future.pdf>

²⁷ <https://www.un.org/sustainabledevelopment/peace-justice/>

difficult to determine how defence companies' products and services will ultimately be used, whether for defensive or offensive purposes and in the case of "dual-use" goods and services, whether they will serve civilian applications or military ends (see [Part II.3.iii.](#)).

Finally, some investors question whether security objectives are best advanced through financing weapons development. They contend that long-term stability may be better supported by investment in environmental resilience and social protection (for example, reducing resource-related conflict drivers or mitigating climate risks such as drought). From this perspective, allocating capital to defence is seen not only as ethically problematic, but also as potentially diverting funding away from initiatives that could reduce underlying systemic risks over the long term.

2. ESG risk assessment and selectivity of the defence sector

Some other investors take the perspective that investments in defence, to the extent that they either meet environmental, social or governance criteria, or do not cause significant harm to the environment, *can* be included in sustainable investments. For these investors, the rationale may be financial, reflecting the sector's strong growth prospects (see [Part I.2.](#)), and/or it may be driven by client preferences, including explicit mandates from asset owners seeking to support defence efforts.

That said, the sector's inclusion is often approached cautiously as defence companies are typically seen as carrying elevated Environmental, Social and Governance (ESG) risks that can translate into material financial impacts. Ratings by third parties to identify the ESG risks associated with investments in companies usually flag a "medium" to "high" ESG risk rating for the defence sector²⁸, reflecting both the nature of its operations and the complexity of its value chains.

As an example, the defence sector is among the most polluting industrial sectors globally due to its reliance on heavy industries, with an estimated 5.5% of worldwide Greenhouse Gas (GHG) emissions – potentially more due to the lack of reliable data.²⁹ These risks are amplified when considering Scope 3 emissions, where complex supply chains and the full lifecycle impacts of products, from manufacturing through use and eventual decommissioning, can be substantial. The sector's dependence on raw materials, sometimes sourced from conflict-affected regions, and its use of hazardous substances and chemicals further heighten environmental and supply-chain risk exposure.

On the social and legal side, a key concern for investors is downstream misuse: products, systems, or weapons may be used in ways that contribute to violations of international law. This risk can arise where companies manufacture weapons prohibited under international treaties and conventions, or where lawful products are exported into contexts in which they

²⁸https://assets.contentstack.io/v3/assets/blt4eb669caa7dc65b2/blt0800586197539ecb/678181749c83122034b48298/Global_Defense_Sector_Landscape.pdf

²⁹<https://2025.cedare.org/contribution-of-military-and-war-to-global-emissions-2/>

may be deployed for repression or violence, creating significant exposure to legal, reputational, and regulatory risks for both issuers and investors.

Governance risks are also considered more acute in defence. Companies in the sector often face heightened cybersecurity threats, while the prevalence of large public procurement contracts and close relationships with governments can increase exposure to corruption, bribery, and opaque contracting practices.

Compounding these challenges, investors frequently encounter data and transparency constraints: because defence firms operate in a national security context and are bound by confidentiality obligations, it can be difficult to obtain sufficiently detailed information on the precise destination of products, goods and services, their use, or the risk management, due diligence, and response to human right breaches processes of these companies across their value chains.³⁰

As a result, some investors exclude certain defence companies not primarily for ethical reasons, but as a matter of risk management considering potential financial, legal, and reputational risks. Nevertheless, depending on an investor's risk appetite and the selectivity of their screening criteria, defence companies that demonstrate comparatively stronger ESG performance through credible governance, robust compliance, clearer oversight of sales and end use, and more measurable environmental management may still be considered eligible for inclusion in sustainable investment portfolios.

3. Due diligence and norm-based screening

Many investors also refine their defence-sector investment decisions by looking beyond sector exposure and examining companies' specific processes, activities, and value-chain practices.

A frequent starting point is to assess whether investee companies align with key international legal and normative frameworks, and to exclude companies implicated in human rights breaches. In this context, the UN Guiding Principles on Business and Human Rights (UNGPs) are often used as a reference point, setting expectations around public policy commitments, ongoing human rights due diligence, and access to remediation where harms occur. These expectations are reinforced by the OECD Guidelines for Multinational Enterprises and the International Labour Organisation's fundamental conventions and protocols, which together are widely treated as core standards for responsible business conduct; moreover, elements of the UNGPs have increasingly been reflected in legislative requirements across several jurisdictions, including within the EU (see [Part II](#)).

Alongside these international standards, investors commonly rely on national and supranational export-control regimes to gauge how effectively defence companies manage end-use and end-user risks. National authorities regulate arms transfers through export licensing systems that are informed by frameworks such as the EU Common Position on Arms Exports³¹ and the UN Arms Trade Treaty (ATT),³² with the aim of ensuring transfers comply

³⁰ <https://docs.un.org/en/A/HRC/56/42>

³¹ <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex%3A32008E0944>

³² <https://legal.un.org/avl/ha/att/att.html>

with legal obligations and align with national policy constraints. Investors can assess whether defence companies comply with the export rules and conventions ratified in the country in which they operate, when these rules are considered robust enough.

While investors are expected to conduct due diligence, often through engagement with investee companies to understand controls, escalation procedures, and governance, there are practical limits to what they can independently verify. In practice, they remain dependent on the robustness of government and EU-level implementation of export controls, as well as on the quality and transparency of company disclosures regarding export compliance, risk management, and due diligence processes.

i. Controversial weapons

A common way investors operationalise compliance with international treaties and responsible business frameworks is by distinguishing companies that are involved in “controversial” weapons.

In practice, ESG-oriented investors almost universally exclude exposure to controversial weapons, with 92% of funds that pursue either a sustainable investment objective or have Environmental / Social characteristics applying such exclusions, demonstrating a similar approach to these exclusions across a wide range of sustainability-related investment strategies.³³ This approach is reinforced by regulation and market standards in several jurisdictions: in some countries, investments linked to controversial weapons are prohibited, with for example Belgium, Ireland, Italy and Luxembourg prohibiting investments in cluster munitions producers.³⁴ Many national sustainability labels similarly bar or restrict such exposure, making controversial weapons a widely accepted red line for inclusion in sustainability-related portfolios.³⁵

While the exact definition of “controversial” weapons varies depending on countries and actors, it is often based on international treaties, such as the Ottawa Convention, the Chemical Weapons Convention, the Convention on Cluster Munitions or the Anti-Personnel Mine Ban Convention. Some definitions of “controversial” weapons include nuclear weapons, depleted uranium, and white phosphorus munitions,³⁶ and others can add incendiary weapons as well as laser-blinding weapons. Furthermore, exclusions can differ on whether they apply to the whole value chain (e.g. manufacturing, development, usage, storage, marketing or distribution) or only to a subset of these activities. The extent of these exclusions is ultimately a decision of the investor and may reflect the preferences of their end clients.

The European Commission recently clarified a subset of controversial weapons that would be “prohibited” under certain EU rules, which includes cluster munitions, anti-personnel

³³ <https://www.sustainalytics.com/esg-research/resource/investors-esg-blog/eu-esg-funds--exposure-to-defense-continues-to-increase>

³⁴ <https://www.clusterconvention.org/files/organization/List-of-specific-national-laws-to-implement-the-CCM-Feb-2019.pdf>

³⁵ https://www.lelabelisr.fr/wp-content/uploads/EN_Referentiel_Label-ISR-mars24.pdf

³⁶ https://www.sustainalytics.com/esg-research/resource/investors-esg-blog/controversial-weapons-regulatory-landscape-and-best-practices#_ftnl

landmines, chemical and biological weapons (see [Part II.2.](#)). It is important to note that exclusions of “controversial” weapons (when they are not understood as covering nuclear weapons) and “prohibited” weapons have a very limited impact on the European defence and aerospace sector, as almost no European listed companies are involved in the manufacture of these types of weapons.³⁷ However this may change in the future, considering the willingness of some European countries to withdraw from some of the abovementioned international treaties.^{38,39}

ii. Nuclear weapons

Nuclear weapons are often treated as a distinct category in responsible investment frameworks because policymakers frequently frame them as strategic deterrents, which can lead to different risk assessments than those applied to other controversial weapons. Reflecting this nuance, many financial institutions voluntarily exclude nuclear weapons involvement from ESG strategies, while others continue to invest where the exposure is linked to companies operating in countries that are parties to the Treaty on Non-Proliferation of Nuclear Weapons.⁴⁰

In practice, nuclear weapon exclusion rates vary by fund type: in Q1 2025, 28% of funds with a sustainable investment objective excluded companies deriving revenue from nuclear weapons, compared with 16% of funds with Environmental or Social characteristics, and 4% of mainstream funds without such objectives.⁴¹

iii. Dual-use goods and services

As more technologies originally designed for civilian markets, such as logistics services, surveillance capabilities, and cybersecurity software, are increasingly adopted for military and security applications, investors are paying closer attention to so-called “dual-use” goods and services. Although definitions vary and continue to evolve, dual-use items are also typically subject to export controls⁴² because they can be diverted or misused in ways that may contribute to breaches of international law.⁴³

This dual-use dynamic creates challenges for companies’ tracking and by extension for investor due diligence: by their nature, these products and services can be difficult to trace to a clear end-use or end-user, complicating assessments of both compliance with export-control requirements and the real-world risks associated with deployment. It also expands the scope

³⁷ https://assets.contentstack.io/v3/assets/blt4eb669caa7dc65b2/blt0800586197539ecb/678181749c83122034b48298/Global_Defense_Sector_Landscape.pdf#page=75

³⁸ <https://valtioneuvosto.fi/en/-/finland-presented-the-instrument-of-withdrawal-from-the-ottawa-anti-personnel-landmines-convention>

³⁹ <https://www.clusterconvention.org/statement-of-the-13msp-presidency-on-lithuanias-effective-withdrawal-from-the-convention-on-cluster-munitions/>

⁴⁰ <https://treaties.un.org/doc/publication/unts/volume%20729/volume-729-i-10485-english.pdf>

⁴¹ <https://www.bruegel.org/analysis/sustainability-rules-are-not-block-eu-defence-financing-reputational-fears-are>

⁴² https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A02021R0821-20251115#tit_I

⁴³ <https://international-review.icrc.org/articles/digital-technologies-humanitarian-law-policy-action-913>

of companies that may be considered part of the defence value chain, bringing in non-traditional actors such as tech companies.

The rapid emergence of new technologies applied to these “dual-use” goods and services, including artificial intelligence, adds further complexity for investors, as questions of accountability, decision-making responsibility, and downstream impacts can be harder to define and may sit in a “grey area” between developer, customer, and operator responsibilities.

4. Engagement and treatment of controversies

As active owners of shares and other financial instruments, investors can use their shareholder rights to influence the strategic direction and risk management of investee companies. Engagement can take several forms, including direct dialogue with senior management or the board, exercising voting rights, and submitting or co-filing shareholder resolutions at a company’s Annual General Meeting (AGM). These engagement strategies are typically structured in stages, with clear objectives and timelines; where progress is limited, investors may escalate by increasing the intensity of dialogue, collaborating with other shareholders, or signalling concern more publicly. If meaningful improvements still do not materialise, investors may ultimately consider disinvestment as a last resort.

In the defence sector specifically, engagement is often used to ensure ongoing compliance with the investor’s inclusion criteria and to drive improvements in policies, processes, and practices. Investors can encourage companies to make a clear public commitment to internationally recognised standards and to demonstrate that this commitment is embedded in operational practice through robust due diligence across the full lifecycle of products and services. They can also push for effective, ongoing risk monitoring that tracks implementation and performance over time, including clear oversight and accountability for human rights and export control policies. In addition, investors can promote stronger alert and escalation mechanisms to ensure potential or actual human rights impacts are identified and addressed across the value chain.

Conclusion

Overall, Europe’s drive to scale up defence capability is primarily a public-policy task funded through government defence budgets and procurement, while private finance can only complement these efforts within the constraints of fiduciary duty and client mandates.

Although rising procurement and strong stock performance have increased private flows into defence, bringing higher exposure even among many ESG-related funds, the extent and acceptability of such exposure remain shaped by differing sustainability objectives, screening approaches, and end-investor preferences. The question of whether defence investments can be considered sustainable demonstrates divergences in interpretations among the sustainable finance landscape.

For some investors, whether to include exposures to the defence industry is an unequivocal no, grounded in their ethical principles and/or the ones of their clients. For others, the answer

depends on context, risk management, returns profile, and end clients' expectations. These approaches can be viewed as being consistent with ESG principles, provided companies operate under strong governance frameworks, demonstrate responsible conduct, and are subject to national export controls – which investors must verify through thorough risk assessment and due diligence.

Eurosif will continue to reflect and engage on this topic as the regulatory and political context evolves. This paper provides a foundation for further discussion, not to resolve the debate, but to frame it more clearly for informed decision-making.