

Analysis Criterion

Defence Contracts

Storebrand Sustainability Team



Storebrand aims to invest in companies that contribute actively to sustainable development. We believe such practices – when integrated into core business – will be financially rewarded. Storebrand will not invest in companies with more than 10 percent of their income deriving from defence contracts.

Definition

A defence contract is the production, maintenance, or storage of arms, armament, ammunition, munitions or machinery, or the construction or installation of an infrastructure made explicitly for military purposes, under contract for a defence agency.

Background

Global military expenditure amounts to around USD 800 billion a year, equivalent to 2.5 percent of world GDP. Industrialised countries account for approximately 80 percent of global military expenditure, of which the US defence budget alone constitutes about 50 percent¹. Currently 80 percent of global military spending is on conventional weapons and weapons systems².

The largest military spending countries are also the biggest arms producers. The US accounts for almost half of the world's total arms production, France and the UK produce 10 percent each while Germany, Russia and Japan each represent roughly 4 percent³.

Two major trends have emerged in the defence industry over the past few years. Firstly, through a series of mergers and acquisitions, the number of companies has fallen significantly and the biggest players continue to grow. Secondly, there is a trend in production towards high-technology weapons that are smart, fast and mobile. To that end, several companies in the defence industry have invested in hardware and software companies that focus on government customers, as the Stockholm International Peace Research Institute (SIPRI) points out: "The rapid development of military technology and the processes of concentration, internationalization and privatization in the arms production industry present new challenges regarding the control of arms procurement, [and governments' control of] costs, competition and technology"^{5,6}.

The UN goals of disarmament and arms limitation have always been central to its efforts to maintain international peace and security⁷. The main focus of the UN Department of Disarmament Affairs (DDA) is the elimination of weapons of mass destruction, illicit transfers of conventional arms and excess weapons stockpiles. Acknowledging that disarmament alone will not result in world peace, the DDA nevertheless states that these measures will reduce the effects of wars, eliminate some key incentives to start new conflicts and free up resources to improve living conditions, including the natural environment⁸.

Even though the elimination of nuclear, chemical and biological weapons, and landmines are central to the UN's work on disarmament, the oversupply and proliferation of conventional

weapons have received increased attention since the end of the Cold War⁹. The DDA points to several negative effects of their oversupply; it prolongs conflicts, makes war more likely and deadly, hampers humanitarian aid, threatens peace agreements and hinders economic development. Furthermore, "in recent conflicts around the world, small arms and light weapons have been the cause of four out of five casualties. The vast majority of victims have been non-combatants. Most are women and children"¹⁰.

In addition, illegal trade is a known problem in the defence industry; of the USD 30 billion annual global trade in conventional arms, nearly 70 percent represent imports by developing countries¹¹. Of concern is the fact that, according to the DDA, "an estimated 40 to 60 percent of the world's trade in small arms is illicit"¹². Bearing in mind SIPRI's comment on the new trends in the defence industry that "it is more difficult [for governments] to monitor and control international technology transfers if they take place within large transnational corporations"¹³, the problem of illicit trade in arms provides continued concern.

Scope

The purpose of this criterion is to exclude companies producing arms explicitly for the military, as well as infrastructure such as computer systems if it is developed explicitly for military purposes. Products and services that are also available to consumers on the open market are not covered by this criterion.

Methodology and data sources:

If a company is detected to generate revenues from defence contracts as screened by either of the data providers Sustainalytics or ISS-Ethix, the company will be excluded.

Example of excluded company

An American defence contractor is excluded from investment as the company delivers defence products such as missiles, precision strike weapons, F-16 fighters and submarine warfare systems.

Key Resources

¹ The Foreign Policy Association - http://www.fpa.org/newsletter_info2584/newsletter_info.htm

^{4,5} Simonetta, Joe (2003), "Aerospace & Defense. Overview", Hoover's

^{1,6,13} SIPRI Yearbook 2003 - <http://editors.sipri.se/pubs/yb03/ch10.html>;
<http://editors.sipri.org/pubs/yb03/ch11.html>

^{1,2,3,7,8,9,10,11,12} United Nations Department for Disarmament Affairs - <http://disarmament2.un.org/index.html>

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