House of Commons Business and Trade Committee: UK Defence and resilience inquiry - TheCityUK written evidence

Overview

1. The UK has a mature and investible defence sector and substantial pools of private sector capital. Investment has been constrained by several factors, including the absence of a clear demand signal from government while the Defence Investment Plan (DIP) was repeatedly delayed, overlapping regulation and complex procurement pipelines. Previously reported constraints arising from environmental, social and governance (ESG) investment approaches are now a much-reduced factor in decision-making.

2. The financial and related professional services industry stands ready to support the government's national security, defence and resilience objectives. Our industry is keen to work with government and policymakers to ensure that private capital can play a vital role in growing our defence industry both as a key to national security and as one of the eight sectors in the government's Modern Industrial Strategy.

3. Channelling more private capital into defence and resilience would reduce fiscal pressures which constrain government expenditure. Even the more straightforward investment opportunities such as military housing, taken on by responsible private capital providers with due risk exposures, would enable as much as £7bn of government funds to be deployed elsewhere[1].

4. The aim of TheCityUK's Defence and Resilience Group is to develop actionable solutions that enable more private sector capital to be deployed more quickly into defence. We see a particular need to support smaller companies, including start-ups and scale-ups, in the supply chains of the major defence primes, including BAE Systems, Babcock International, Leonardo UK and Thales UK.

5. A move by government to engage meaningfully with private capital is urgently required. The UK is not the only country scaling up defence spending, and there are multiple competing opportunities for investment, including in Europe, particularly Germany, Ukraine and Poland, and beyond. There is also a strong case for engaging UK private capital in multilateral opportunities such as the Defence Security Resilience Bank (DSRB) and Multilateral Defence Mechanism (MDM).

[1] DRG estimate reflecting Annington Homes repurchase price and valuation estimates.

Opportunities

6. According to ADS, the UK defence sector's economic contribution is estimated at £15bn. Its direct turnover is approximately £36bn, supporting over 460,000 direct and indirect jobs and over £13bn of exports. It consists of a blend of major primes and thousands of small and medium-sized enterprises (SMEs), both in the supply chains of the primes and as research and tech-led start-ups. The gap, as we see it, is primarily in the funding of SMEs, both with working capital and to meet capital expenditure requirements when they win contracts and need to scale up rapidly. In part, this reflects the broader challenge of scale-up funding for growth companies in the UK, but there are additional defence-specific issues, including procurement delays, classified information and overlapping compliance requirements.

7. In addition to a mature and investible defence sector, the UK is a world-leading international financial and related professional services centre, with substantial pools of private capital that could be crowded in to support and leverage increased government spending on defence and broader resilience, provided there is a clear demand signal from government. Relevant capital pools in the UK include pensions, private equity and bank lending capacity, as follows:
    - UK defined benefit, defined contribution and Local Government Pension Scheme assets exceed £3 trillion, according to the Pensions Policy Institute.
    - UK bank lending to businesses last year was **£582bn**, 34% of which was to SMEs.[2]
    - UK managed Private Equity / Venture Capital funds raised **£59.7bn** in investments in 2025 with substantial funds committed but still pending investment ('dry powder').[3]

8. There is also substantial international capital from trusted jurisdictions. For example, TheCityUK member J.P. Morgan has a well-publicised $1.5 trillion fund earmarked to invest in defence worldwide. Just 5% of this total would equate to around £50bn, over three times what the DIP will deliver from public expenditure. Goldman Sachs' research has recently highlighted UK defence investment opportunities and UK export strengths, including in aerospace, naval systems and next-generation technologies. TheCityUK's membership includes European firms such as BNP Paribas, the largest funder of defence in the EU.

9. Collectively, private capital could multiply government defence expenditure by two to three times. Successfully delivering these capital flows requires appropriate and targeted presentation of investment cases to the relevant capital providers, backed by policy commitment and action to remove blockages and frictions.

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[2] *Financial and related professional services industry continues to drive UK prosperity,* TheCityUK, June 2026 available at www.thecityuk.com/news/financial-and-related-professional-services-industry-continues-to-drive-uk-prosperity/

[3] *Report on investment activity 2025,* UK Private Capital, 5 May 2026, available at www.ukprivatecapital.co.uk/research/investment-activity.html

10. Respectively, these pools of capital each seek distinct opportunities depending on their balance sheet requirements – hence our work has been focused on the following: bank lending to SMEs in defence supply chains; venture capital/private equity; defence infrastructure for patient capital, and cross-cutting frictions and barriers to investment.

11. The investible categories in defence and resilience go significantly beyond the obvious areas of military hardware and energetics. There are opportunities to work alongside government to fund stronger supply chains, strengthen resilience in critical minerals and improve sovereign data and AI capabilities. Much future defence investment will also need to support technologies and assets with dual-use capabilities.

Obstacles

12. There are however blockers in the UK which prevent the effective deployment of these resources into UK defence and resilience. First, the delays to the DIP announcement have damaged confidence. Survey research conducted in June 2026 by TechUK reported 73% of firms had experienced a declining market characterised by contract suspensions and funding delays in the last year. The right demand signal from government could however still activate substantial private investment from domestic and international capital pools to double or triple government defence expenditure.

13. In some cases, co-investment may be required, and government needs to be more imaginative in the use of guarantees and co-investment alongside public finance institutions (PFIs, or also known as 'PuFins'). Work has been done in this space, but better engagement and greater pace are needed. Private capital needs to earn a return for its owners, but investors and lenders are acutely aware of the need to provide value for money for taxpayers where they are working alongside government-funded investment. Co-investment in defence is a realistic goal, and the PFIs, which include the National Wealth Fund (NWF), British Business Bank (BBB), National Housing Bank and UK Export Finance (UKEF), have a role in catalysing and co-investing in public-private partnership (PPP) models. These could be designed and structured to better allocate investment and delivery risk across partnerships, without replicating flawed Private Finance Initiative (PFI) models of the past. More recent infrastructure projects have demonstrated this is possible. Military infrastructure is discussed below at paragraph 19.

14. Defence procurement is a particular problem. The six-and-a-half-year period to win a contract is well documented, but during this period lending is difficult because there is often no clear asset or revenue stream to lend against, and information that is vital to credit decisions may be classified. Technology could offer a solution to this with trusted and suitably cleared banking partners. Overlapping regulation is similarly a friction: repetitive Know Your Customer (KYC) and anti-money laundering (AML) requirements are applied by

both the Ministry of Defence (MoD) and banks, when a compliance passport approach should suffice.

15. A commitment to the defence sector that is sufficiently credible to attract finance requires a cross-government approach. This includes the Department for Business and Trade (DBT), through the Industrial Strategy, which already features defence as one of the eight growth sectors, the Office for Investment and HM Treasury. Finance is highly regulated, both in conduct and capital terms, through the Financial Conduct Authority (FCA), Prudential Regulation Authority (PRA) and Bank of England (BoE). The regulators are acutely aware of the need for defence investment and are able to be supportive.

Practical Solutions

16. The workstreams established within the DRG reflect the types of capital that could be deployed and are designed to address current weaknesses in the broader financing system. They focus on:
    i. Bank funding (for £2-10m companies supplying primes);
    ii. Venture capital and private equity for growth companies;
    iii. Patient capital from pensions and insurers for defence infrastructure including military accommodation; and
    iv. A horizontal workstream addressing regulatory and policy blockages, especially in procurement and overlapping regulation.

17. **Bank funding for supply-chain SMEs**: The UK domestic banks as well as other investors are shifting their strategic approach to defence investment and are aware of the need to support smaller companies in the defence supply chain – provided the policy and regulatory environment supports the viability of these companies. The major focus of this workstream has therefore been to support and add to guarantees from public finance institutions through a collective approach – hence tackling what is essentially a credit approval challenge for working capital during and after procurement, whilst also seeking to provide solutions to duplicative regulation in, for example, Know Your Customer (KYC) and anti-Money Laundering (AML) processes.

18. **Venture capital and private equity:** One challenge has been the inadvertent exclusion of a wide range of defence investments under legacy ESG clauses in standard mandate letters and fund agreements. However, an early success from our work has been to alter standard "agreement to fund" language. Invest Europe, the industry body, has agreed to make specific changes to limited partner-general partner agreement letters to avoid investment into broad defence and dual-use categories being inadvertently restricted by default. The revised standard wording takes a narrower definition and excludes only UN-prohibited weapons, with all other defence investment expressly permitted.

19. **Military infrastructure:** The MoD owns approximately 1.4% of the UK's total land mass. The UK's military infrastructure, including operational headquarters, air bases, ports and military housing, is sub-standard. The MoD's status as a landowner could form the basis for an innovative programme to fund improved facilities. The financing of improved military housing, estimated as requiring £6-9bn of investment, is in principle no different to the financing of social and affordable housing or student accommodation, and would create an attractive asset class for institutional investors such as pension annuity funds. This is recognised by the Defence Investment Advisory Group (DIAG). The challenge here is the historical legacy of Annington Homes, which was described by the National Audit Office (NAO) as a poor contract and was negotiated 30 years ago, when there was little to no market competition. The subsequent growth of the pensions buyout market has created £40-50bn of new capital flow in search of this type of asset, and hence the potential for government and funders to negotiate very different, and much fairer, contracts, avoiding, for example, the challenge of maintenance liability and ensuring the housing assets can revert to the MoD free at the end of the contract.

20. **Regulatory and policy frictions**: this horizontal workstream is focused on removing practical barriers that currently prevent capital from flowing into defence and resilience. These include long procurement timelines, overlapping MoD and financial services compliance requirements, duplication in Know Your Customer (KYC) and anti-money laundering (AML) checks, and uncertainty created by delayed or unclear demand signals. A compliance passport approach, and stronger cross-government coordination and earlier engagement between MoD, regulators and finance providers would help reduce frictions while maintaining appropriate safeguards.

How policymakers can help

21. One of TheCityUK's defining goals is to deepen the strong and collaborative partnership between industry, government and regulators to support national missions, from supporting the energy transition and delivering inclusive growth to boosting infrastructure and defence investment.

22. To get to a point where investment starts to flow requires above all a credible demand signal built around the DIP. Direct engagement with "the City" by defence ministers and senior officials including the National Armaments Director and DIAG, as well as by the PuFins is vital. TheCityUK is already making efforts to support such engagement between our industry, the MoD and the UK's armed services. We would be willing to support further efforts in this area.

23. There are set-piece events, including the Budget and the Chancellor's annual Mansion House speech, that need to be used. We have already seen from the Mansion House agreements the scale of commitments from pension funds that can be obtained where

trusted relationships, backed by appropriate technical skillsets, are created. TheCityUK has senior access to financial institutions and is neutral between institutions, so could create and manage an engagement programme for the MoD in a very short time.

24. The urgency of this cannot be overstated. Capital is highly mobile and other countries, not least Ukraine, are pitching hard for investment. The DSRB now being created in Canada creates a new competitive focus. However, US capital sees opportunities in the UK so we need to activate this before the focus moves elsewhere.

25. The vital first step will be to engage with a trusted senior group from the City, including banks, insurers, investors and professional advisors. Just this signal will catalyse further supportive work to ensure the government's expenditure on defence can crowd-in responsible private sector capital at scale.

About TheCityUK

26. TheCityUK is the industry-led body representing UK-based financial and related professional services. We champion and support the success of the ecosystem, and thereby our members, promoting policies in the UK and internationally that drive competitiveness, support job creation and enable long-term economic growth. The industry contributes over 12% of the UK's total economic output and employs almost 2.5 million people, with two-thirds of these jobs outside London across the country's regions and nations. It pays more corporation tax than any other sector and is the UK's largest net exporting industry. The industry also plays a key role in the transition to net zero and driving economic growth across the wider economy through its provision of capital, investment, professional advice and insurance. It also makes a real difference to people in their daily lives, helping them save for the future, buy a home, invest in a business and manage risk.

Our Defence & Resilience work programme

27. TheCityUK's work on defence is led by our Defence and Resilience Group (DRG). The DRG was formed in December 2025 in response to member demand, and with active encouragement from the Department for Business and Trade, which had recognised defence as one of the eight priority growth sectors in the Modern Industrial Strategy, and from the FCA, whose CEO, Nikhil Rathi, attended our inaugural meeting. The DRG's 60-strong membership is drawn from TheCityUK's broader membership and includes banks, insurers, asset managers and related professional service providers. The DRG is co-chaired by General Sir Richard Barrons, who co-authored the government's Strategic Defence Review, and Joe Cassidy, a senior partner at KPMG, and therefore combines defence and financial expertise. The DRG is practitioner-led and unusually includes non-members of TheCityUK, including defence primes and providers of UK critical infrastructure.