

3.5 Military industry and arms trade

3.5.1 What is at stake?

Weapons have a common inherent property: they are designed and developed to kill, maim or destroy. In this context they threaten the most fundamental human right, the right to live. Weapons are obviously used in wars and other armed conflicts. In 2005, a total of 17 wars and armed conflicts were recorded, amongst others in Sudan, Chechnya, Iraq, Afghanistan, Nepal and Myanmar. Non-state actors are often very prominent in these conflicts, and the limited capacity of the international community to hold them accountable for their abuse of civilians continued to pose a grave threat to human security in 2005.⁷⁴

However, weapons are not only used to kill people in wars or armed conflicts. Wherever people are able to get their hands on weapons, conflicts between individuals, within families or between groups or gangs tend to be 'solved' by the force of arms. There are an estimated 650 million small arms in the world today, nearly 60% of them in the hands of private individuals. This is a time bomb continuously ticking under today's society.

States have defended their right to individual or collective self defence and their legitimate security interests. However, such rights are also accompanied by responsibilities, such as to control and monitor the transfer and use of arms. In practice, however, there is a great lack of effectiveness by governments and multilateral bodies (such as the [UN Security Council](#)) to control the international arms trade.

Arms trade controls, arms embargoes and weapon licence systems have so far not been able to keep weapons away from dictators, conflicting parties or the heaviest abusers of human rights. None of these instruments have prevented the stockpiling and use of controversial weapons by some of the most influential members of the global community. Whilst the intention is laudable, arms embargoes and arms export controls are breached on an almost continuous basis, allowing numerous conflicts and repressive regimes. A recent report by the [Control Arms Campaign](#) revealed how the arms industry exploits existing loopholes to circumvent arms export regulations and embargoes.⁷⁵

Total world military expenditure in 2005 is estimated to have reached US\$ 1,118 billion, which corresponds to 2.5% of the global GDP. Over the period 1996-2005 military expenditure showed a real terms increase of 34%. The United States, responsible for about 80% of the expenditure increase in the year 2005, is the nation principally responsible for this trend. Weapons are clearly used to enforce power inequalities and exercise this power in a violent way. The United States now accounts for 48% of the world military expenditure, followed at a long distance by France, the United Kingdom, Japan and China with 4-5% each.⁷⁶

Another important aspect is the relationship between military spending and development. Worldwide military spending averages ten percent of national public spending. In developing countries, where there is a greater need for investment in constructive initiatives, military spending amounts to fifteen percent. According to the [Human](#)

[Development Report 2003](#) of the United Nations' Development Programme (UNDP), military expenditures are a major barrier to reaching the [UN Millennium Development Goals \(MDG\)](#) for poverty reduction, health care and the protection of the environment. Military spending competes with investments in human development; it often equals the amount spent on education and healthcare together. According to the UNDP, attaining the MDG is not possible without reducing military expenditure, since money spent on military development cannot be spent on human development.⁷⁷

The detrimental effect of military spending on the MDG is further exacerbated by the costs of military related debt. Between 15 and 20 percent of total global debt is related to military expenditure. In many developing countries, interest payments on military debt far exceed spending on healthcare and education.⁷⁸ Furthermore, while international arms trade only accounts for one percent of global trading, fifty percent of all bribes paid worldwide between 1994 and 1999 related to trade in arms.⁷⁹ Corruption can add 20 to 30 percent to the cost of government procurement and may divert public spending away from human development areas.⁸⁰

To play a legitimate role in achieving a fairer, safer and more peaceful world the military industry needs to undergo a profound and structural reform, ensuring that:

- No weapons are produced that can not distinguish between combatants and civilians;
- Weapons are not supplied to oppressive regimes, terrorist groups and conflicting parties;
- Corruption is eradicated and transparency strongly improved;
- A much smaller proportion of the GDP of developing countries is spent on weapons.

Until this profound and structural reform of the military industry has occurred, financing of any military company entails a heavy risk of involving the bank in corrupt practices, dealings with oppressive regimes and the production of controversial weapons. Under these circumstances, banks are strongly recommended to avoid financing this sector altogether. If banks are not prepared to accept this conclusion, they should screen their clients in the military industry very carefully against the best international standards available as described below.

3.5.2 Best standards available

No international standards seem to cover the military industry and arms trade as a whole. On the use of weapons the main international standard is *International Humanitarian Law (IHL)*. IHL is a set of rules which seek, for humanitarian reasons, to limit the effects of armed conflict. It protects persons who are not or are no longer participating in the hostilities and restricts the means and methods of warfare, by introducing the basic rules of proportionality and discrimination.⁸¹

Regarding the production, use, stockpiling and trade of specific weapon systems, various international treaties exist:

- The [Nuclear Non-proliferation Treaty \(NPT\)](#) of 1970 seeks to inhibit the spread of nuclear weapons;
 - The [Biological and Toxin Weapons Convention \(BWC\)](#) of 1975 outlaws biological and toxin weapons;
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- The [Convention on Certain Conventional Weapons \(CCW\)](#) of 1980 regulates conventional weapons that pose special risks of causing indiscriminate damage to civilians or unnecessary suffering;
- The [Chemical Weapons Convention \(CWC\)](#) of 1997 bans chemical weapons and requires their destruction within a specified period of time.
- The [Ottawa Convention](#) of 1997 bans anti-personnel landmines

Many more treaties have been signed between the former Cold War superpowers, the United States and Russia. A complete overview is to be found on the website of the [Arms Control Association](#).⁸²

Despite the proliferation of these treaties, many banned weapon systems continue to be produced and traded, often because major producing countries have not ratified the instruments, or are continuously breaching the spirit of the treaty. Even when there is not a specific treaty banning a weapon, the established principles of IHL often lead to the conclusion that the use or threat of that particular weapon would constitute a violation of “fundamental humanitarian principles”. This encompasses the principle of proportionality, that the potential for humanitarian suffering must be weighed against the potential military advantage, and the principle of distinction between military and civilian goals.

A recent development underlining this argument was the decision by more than 40 countries in February 2007 to commence working on an international treaty banning cluster munitions in 2008. By May 2007, this group had already grown to 75 countries. Recent research has revealed that 98% of the casualties of cluster munitions are innocent civilians.⁸³

- Regarding arms trade various international bodies, such as the United Nations, European Union and the [Organization for Security and Co-operation in Europe \(OSCE\)](#), have arms embargoes in force against countries or non-state actors, often for being involved in armed conflict or serious abuse of human rights.⁸⁴
- The [Control Arms Campaign](#) (formed by Oxfam International, Amnesty International and the International Action Network on Small Arms) over the past few years has mobilised strong support for an global *Arms Trade Treaty*. This treaty should prevent international arms transfers that fuel conflict, poverty and serious human rights violations.

In October 2006 the United Nations General Assembly’s First Committee voted overwhelming in favour of the proposal to develop an *Arms Trade Treaty*: 139 countries voted yes, with only the United States voting against. Work on the treaty started early 2007 and will without a doubt take a long period.⁸⁵ In the meantime the *Control Arms Campaign* has published the six *Global Principles for Arms Transfers*, which follow from international and regional treaties, declarations and resolutions of the United Nations and other multilateral and regional organisations, and model regulations intended for national legislation.⁸⁶

3.5.3 Content of a bank policy

International treaties and national laws on arms control rarely limit banks and other financial institutions to invest in the military industry. Only Belgium has adopted a law in July 2004 prohibiting financial institutions to invest in producers of anti-personnel mines.⁸⁷ In February 2007 this prohibition was expanded to include investments in cluster munitions producers as well.⁸⁸

Some banks have adopted voluntary restrictions on investments in the military industry, but the best practice in the financial industry is set by the Norwegian [Government Pension Fund - Global](#), the largest pension fund in the world. In December 2004 the fund adopted Ethical Guidelines, which state that it "should not make investments which constitute an unacceptable risk that the Fund may contribute to unethical acts or omissions, such as violations of fundamental humanitarian principles, serious violations of human rights, gross corruption or severe environmental damages." For this reason the fund has until now excluded 16 military companies (including majors like Lockheed Martin, Northrop Grumman and BAE Systems) from its investment universe, as these companies are involved in producing landmines, cluster munitions and/or nuclear weapons.⁸⁹

Even more than in other sectors, banks should carefully reconsider their investments in the military industry. Apart from the lethal nature of its products, the limited transparency of trade flows in this sector and the documented history of corruption and law-breaking demand a clear policy. Any investment in this industry could involve banks in transactions which are violating human rights and fuelling conflicts, corrupt practices or the production of controversial weapons. Under these circumstances, banks are strongly recommended to avoid financing this sector as a whole.

If banks are not prepared to draw this conclusion, they need to take a position vis-à-vis the existing international arms control treaties, as well as the cluster munitions and arms trade treaties which are under development. Although development of the last two treaties has only just started and other treaties are not always ratified by major weapons producing countries, this set of treaties collectively reflects the position of global civil society versus the military industry and arms trade. Banks must screen their customers before offering financial services to make sure they comply with the letter and intent of the existing international treaties as well as the two treaties under development. This screening should also include the producers of components, which are supplied to producers of complete weapon systems, licensed producers of weapons, and producers of dual-use technologies, components or systems, which can be used for both civilian and military end-products.

A more common approach among (ethical) asset managers is to exclude from their investment universe those companies which derive a certain percentage (i.e. more than 50%) of their turnover from military products. This approach is unsatisfactory, as most of the largest weapons producing companies in the world, including producers of the most controversial weapons, derive less than 50% of their turnover from producing weapons.

3.5.4 Scoring table

The considerations in the previous paragraphs lead to the following scoring table with regard to bank policies on the military industry and arms trade:

0. *The bank has no policy on this sector;*
1. *The bank's policy on this sector is vaguely worded or aspirational, with no clear commitments;*
2. *The bank's policy on this sector excludes financial services to producers of specific, clearly defined types of weapon systems or to the most controversial forms of arms trade or to companies deriving more than 50% of their turnover from weapons;*
3. *The bank's policy on this sector limits financial services to clients which were found to be fully compliant to the letter and spirit of all international arms control treaties (including the cluster munitions and arms trade treaties which are under development);*
4. *The bank's policy on this sector excludes providing any financial services to clients in the military industry.*

3.5.5 Results

Twelve banks have developed and disclosed a policy on military industry and arms trade. Two other banks, ANZ (Australia) and UniCredit (Italy), have not disclosed their military sector policies. Most policies set some form of criteria for lending to the production of, or the trade in, controversial weapons (such as anti-personnel landmines, cluster munitions or chemical weapons). However, often the policies still allow banks to finance the companies that are involved in these activities, as long as the 'controversial activities' are not financed directly.

Besides, the lending policies often allow trade financing to countries that are not considered to be 'risky'. But even many 'no risk' countries have repeatedly acted as intermediate trader, by selling weapons to controversial countries. It is for these reasons that even the Belgian banks (Fortis, ING, Dexia and KBC), where a national ban on the financing of production and trade of controversial weapons is established, do not automatically score more than 2 points.

Scores for on Military industry and Arms trade policies					
Intesa Sanpaolo	3	Banco Itaú	0	Mitsubishi UFJ	0
KBC	3	Bank Mandiri	0	Mizuho Financial Group	0
Dexia	2	Bank of America	0	Morgan Stanley	0
Fortis	2	Bank of China	0	RBS	0
ING	2	BNP Paribas	0	Saudi-American Bank	0
Rabobank	2	China Construction	0	Santander	0
Royal Bank of Canada	2	Citi	0	Scotiabank	0
Standard Chartered	2	Crédit Agricole	0	Standard Bank	0
ABN AMRO	1	Credit Suisse	0	State Bank of India	0
Barclays	1	Deutsche Bank	0	Sumitomo Mitsui	0
BBVA	1	Goldman Sachs	0	UBS	0
Société Générale	1	HSBC	0	Unicredit	0
ANZ	0	ICBC	0	WestLB	0
Banco Bradesco	0	JPMorgan Chase	0	Westpac	0
Banco do Brasil	0	Merrill Lynch	0	Nedbank	X
