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INVESTMENT AND FINANCING MODELS IN THE DEFENSE INDUSTRY

THE GROWING ROLE OF PRIVATE CAPITAL, FOREIGN INVESTORS, AND ALTERNATIVE FUNDING APPROACHES



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For much of the modern era, defense spending followed a predictable and centralized path. In recent conversations with defense executives, institutional investors, and policy advisers across multiple regions, one theme has surfaced repeatedly: traditional funding models are under strain. Governments defined national security priorities, allocated public budgets, and funded defense programmes almost entirely through state expenditure. Defense contractors responded to those mandates, and capital flowed directly from public treasuries into military and security assets.

That model still exists, but it no longer operates in isolation.

Today, defense systems are more technologically complex, development timelines are longer, and production costs have increased materially. At the same time, governments face growing fiscal pressure from healthcare, infrastructure, and social spending, even as security concerns

intensify across multiple regions. These competing demands are forcing defense ministries to reconsider how capabilities are funded, delivered, and sustained over time.

As a result, the defense industry is increasingly adopting financing approaches long used in infrastructure, energy, and advanced technology sectors. Private capital, structured finance, and carefully regulated foreign investment are no longer peripheral. They are becoming essential components of the modern defense ecosystem.

STRUCTURAL FORCES DRIVING CHANGE

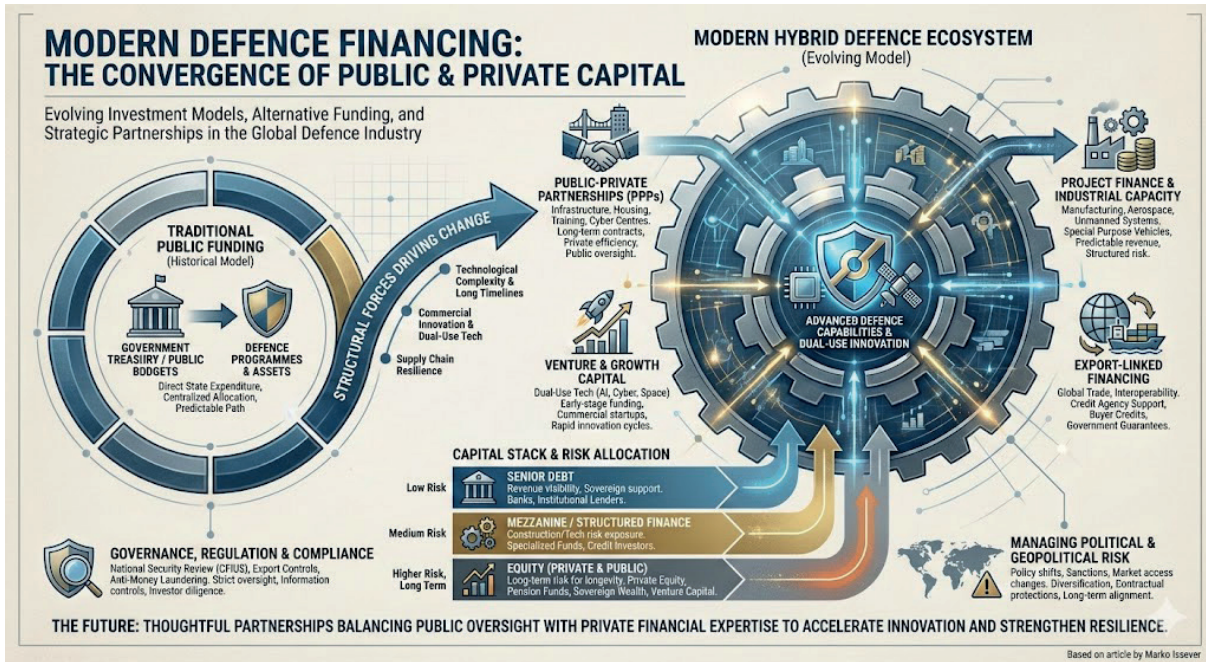
Several long-term forces explain why defense finance is evolving.

First, modern defense capabilities require sustained investment well before operational deployment. Advanced aerospace platforms, autonomous systems, cyber capabilities, and space-based technologies demand years of research, develop-

ment, and testing. Public budgets alone often struggle to absorb these long lead-time costs without creating delays or capability gaps.

Second, innovation increasingly originates outside traditional defense contractors. Commercial technology firms and startups are driving breakthroughs in software, data-analytics, artificial intelligence, robotics, and advanced manufacturing. These companies depend on private capital during early growth stages, well before defense procurement becomes viable.

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Third, supply chain resilience has emerged as a strategic priority. Governments now seek to localize or diversify production of critical components ranging from semi-conductors to propulsion systems and advanced materials. Building this capacity often requires upfront private investment before firm government orders are in place.

Together, these forces are reshaping how defense programmes are financed and executed, often faster than existing procurement frameworks were designed to accommodate.

PUBLIC-PRIVATE PARTNERSHIPS IN DEFENSE INFRASTRUCTURE

Public-private partnerships have become one of the most established alternative financing tools in the defense sector. While once associated mainly with civilian infrastructure, these structures are now widely used for defense related assets.

Military housing, training facilities, logistics hubs, cybersecurity centres, data infrastructure, and command facilities are increasingly developed through partnership models. Under

these arrangements, governments retain strategic oversight while private partners finance, build, and often operate assets under long-term contractual frameworks.

This approach allows defense ministries to spread costs over time while benefiting from private sector efficiency, lifecycle management expertise, and access to institutional capital. It also improves asset maintenance, operational continuity, and cost predictability over multi-decade horizons.

PROJECT FINANCE AND INDUSTRIAL CAPACITY

Project finance structures are also gaining relevance in defense manufacturing. In areas such as munitions, aerospace components, unmanned systems, naval platforms, and propulsion technologies, production facilities are increasingly financed through dedicated special-purpose vehicles.

These vehicles are typically supported by long-term supply or offtake agreements that provide predictable revenue streams. Capital structures may include senior debt, subordinated financing, and equity

Based on article by Marko Issever

contributions, often complemented by export credit agency support or government-backed guarantees.

This approach allows manufacturers to expand capacity more rapidly while reducing reliance on direct government funding. It also enables institutional investors to participate in defense production through structured vehicles with clearly defined risk profiles.

CAPITAL STACK DESIGN AND RISK ALLOCATION

One of the most important developments in defense finance, and one that is often underappreciated outside specialist circles, is the growing sophistication of capital stack design. Defense projects increasingly resemble large-scale infrastructure investments where risk must be carefully allocated among stakeholders.

Senior lenders typically focus on revenue visibility, contract enforceability, and sovereign support. Mezzanine investors assume exposure to

construction, technology, or early operational risk. Equity investors accept long-term risk in exchange for participation in program longevity and expansion.

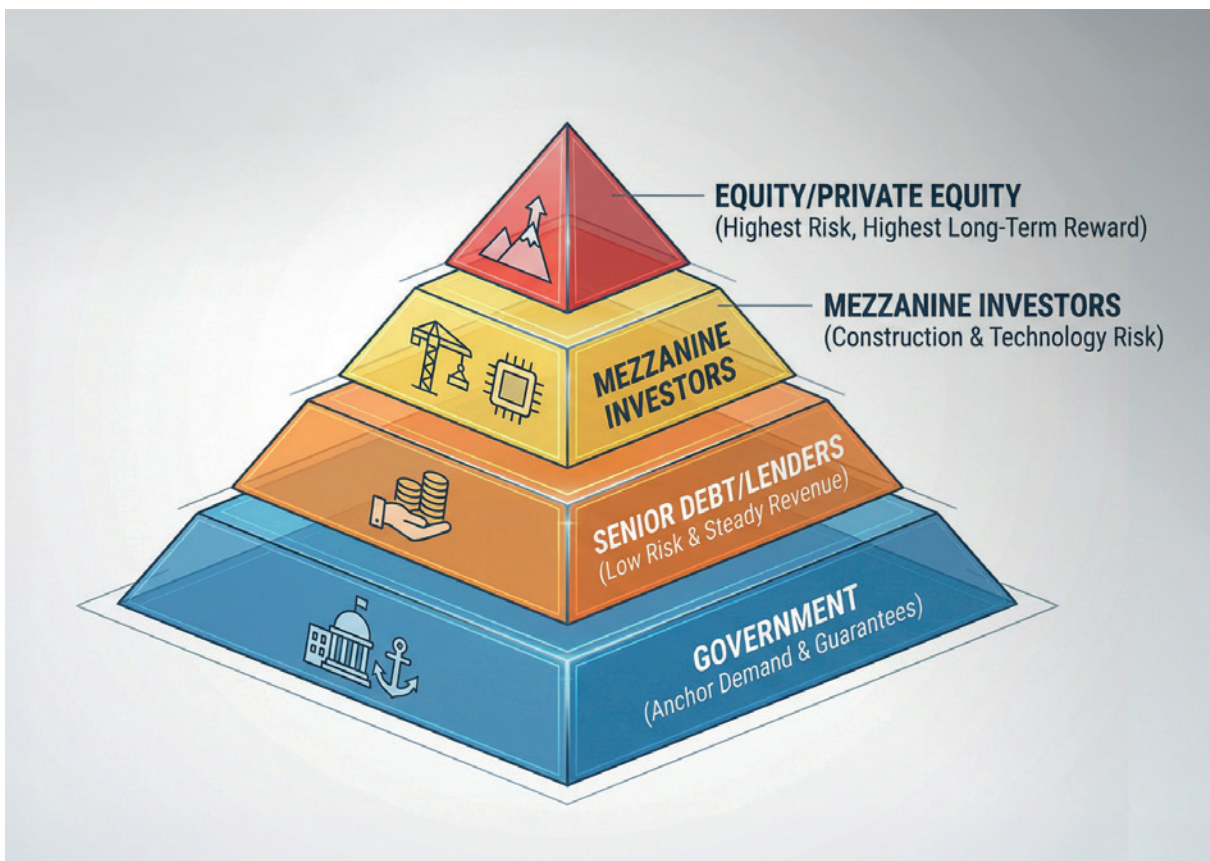
Governments play a central role by anchoring demand, setting regulatory parameters, and in some cases providing guarantees or minimum purchase commitments. When structured effectively, this layered approach allows risk to be borne by parties best positioned to manage it.

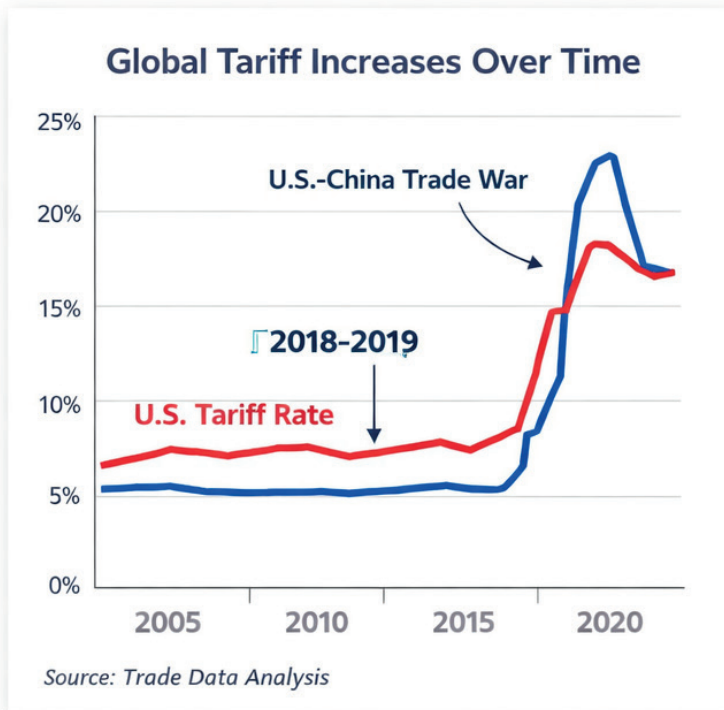
VENTURE AND GROWTH CAPITAL IN DUAL-USE TECHNOLOGIES

The most dynamic shift in defense finance is occurring in dual-use technologies. These innovations serve both civilian and defense markets and often originate in the commercial sector.

Artificial intelligence, autonomous platforms, cybersecurity solutions, satellite systems, advanced sensors, quantum technologies, and next

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generation aerospace platforms all fall into this category. Many of the companies developing these capabilities begin as commercial startups and only later engage with defense customers.

Venture-capital and growth equity play a critical role in this transition. Private investors provide early funding, operational guidance, and scale capital, enabling firms to mature before entering defense procurement processes.

This model has shortened innovation cycles, broadened supplier diversity, and expanded the range of technologies available to defense ministries.

EXPORT-LINKED FINANCING AND GLOBAL TRADE

Defense manufacturers serving international markets frequently rely on export-linked financing structures. These include export-credit agency support, buyer credit facilities, and long tenor government backed guarantees.

Such mechanisms reduce financing risk for foreign buyers and facilitate large-scale procurement even when

domestic budgets are constrained. They also allow manufacturers to align production investment with confirmed demand rather than speculative forecasts.

Export-linked financing has become a central feature of defense trade among allied nations and strategic partners, supporting interoperability and long-term industrial cooperation.

Venture capital and growth equity play a critical role in enabling dual-use technology companies to mature before entering defense procurement processes.

DEFENSE AS AN INVESTABLE SECTOR

From an investor perspective, defense is increasingly viewed as part of a broader national security industrial base rather than a narrow or restricted category.

Several characteristics support this view. Defense demand tends to be long-term and policy-driven. Revenue streams are often anchored by government contracts. Supply chains are protected and strategically important. Dual-use technologies offer exposure to both civilian growth and defense stability.

These attributes have attracted private equity firms, institutional investors, pension funds, sovereign wealth funds, and cross-border venture capital groups, particularly in jurisdictions with transparent regulatory frameworks and clear investment rules.

GOVERNANCE AND INVESTOR EXPECTATIONS

As private capital becomes more involved in defense, governance standards have risen accordingly. Investors increasingly expect disciplined capital allocation, clear reporting, and robust compliance practices.

Board oversight, information controls, and strict separation between commercial operations and sensitive activities are essential. Proactive engagement with regulators and defense authorities has become a core expectation rather than an afterthought.

Strong governance not only mitigates regulatory risk but also lowers the cost of capital by increasing investor confidence.

FOREIGN INVESTMENT AND STRATEGIC ALIGNMENT

Foreign direct investment in defense remains sensitive, but many jurisdictions now permit participation under carefully defined conditions.



Typically, foreign investors are limited to minority or non-controlling positions. Governance structures restrict access to sensitive technologies, operational control, and classified information. National security screening processes ensure alignment with strategic objectives.

In certain cases, foreign investment is encouraged when it supports co-production, technology transfer, or supply-chain diversification among allied nations. When structured carefully, foreign capital can strengthen domestic defense industries while preserving national-security interests.

REGULATORY AND COMPLIANCE ENVIRONMENT

Defense investment operates under a higher regulatory standard than most other sectors.

National security review frameworks such as Committee on Foreign Investment in the United States (CFIUS) in the United States and foreign-investment screening regimes across Europe evaluate ownership, influence, and control. Export control regimes govern technology transfer, data access, and international collaboration. Anti-money laundering and

beneficial ownership requirements demand full transparency of capital sources.

Investors must therefore adopt robust compliance frameworks, governance structures, and internal controls. In many respects, the level of diligence exceeds that required in other cross border investment contexts.

MANAGING POLITICAL AND GEOPOLITICAL RISK

Defense investments are inherently exposed to political and geopolitical risk. Procurement priorities may shift with changes in government leadership. Export-permission regimes can be revised. Sanctions regimes can alter market access and counterparties.

Successful investors account for these risks through diversification, conservative capital structures, contractual protections, and sustained engagement with public authorities. Long-term alignment with national-security objectives is essential for capital stability.

CONCLUSION

The defense industry is entering a new phase in which public funding remains central but no longer oper-

ates alone. Private capital, structured finance, and carefully regulated foreign investment are now integral to the development of defense capabilities.

For investors, the sector offers access to stable and strategically anchored opportunities when capital is deployed with discipline, transparency, and regulatory awareness. For governments, collaboration with private capital can accelerate innovation, expand production capacity, and strengthen industrial resilience.

As defense and finance continue to converge, the future of the sector will depend on thoughtful partnerships that balance public oversight with private financial expertise.



The defense industry is entering a new phase in which public funding remains central but no longer operates alone.