

Goldman Sachs Global Institute

# The Security Supercycle

## Investing in Innovation, Resilience, and Rearmament

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# For Decades Post–Cold War, Global Economic Integration Was Presumed to Mitigate Security Risks

Countries deprioritized their security spending, confident that defense spending could fluctuate at the margins because the underlying global system felt stable.

That era is over, hastened by the proliferation of global conflict and a heightened focus on geopolitical competition. States are increasingly reorganizing around resilience, sovereignty, and strategic autonomy.

The result is a global rush toward rearmament in which governments are pulling defense back into the core of their economic and industrial strategies. Strategic competition is raising the baseline demand for security as states confront a wider range of threats, less stable alliances, and greater pressure to maintain credible defensive capabilities.

This shift is about more than just increased military spending. The tools of conflict are changing—becoming cheaper and more widely accessible. Combat effectiveness is increasingly a question of technological edge and the rate of innovation. The adoption and successful deployment of AI-enabled defense technologies, particularly unmanned systems and defense software, is becoming critical to building and sustaining deterrent capabilities. Governments are reassessing not just how much they spend on defense, but how to evolve their strategy and invest in modern platforms that are more agile and cost efficient.

Unlike cyclical surges in defense spending, structural shifts have the power to durably reshape institutions, supply chains, and political priorities. Increased spending on dual-use technologies is already providing a tailwind to other segments of the industrial economy, supporting growth in areas such as advanced manufacturing and energy technology. And as both governments and companies look to secure industrial scale, the conditions are forming for a new wave of cross-border partnerships, joint ventures, and acquisitions. This paper examines the factors shaping this global rearmament, how capital allocation is shifting as a result, and what it means for the global economy.

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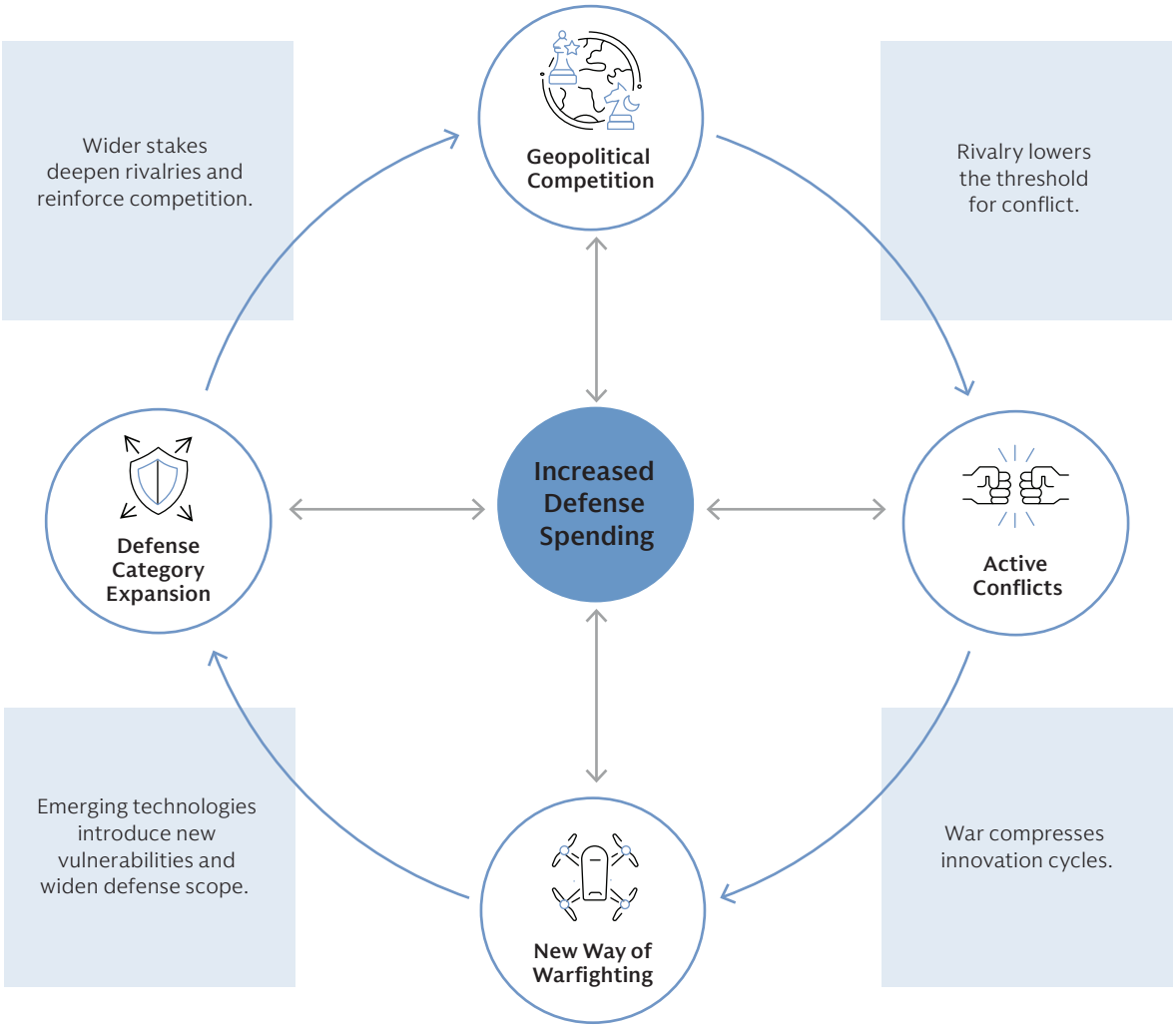


# The Rearmament Flywheel: Four Forces Reinforcing Global Defense Investment

The world is rearming. Global defense spending has grown[1] by 41% over the past decade, reaching a record $2.89 trillion[2] in 2025—equivalent to 2.5% of global GDP,[3] its highest level since 2009. Spending has risen in every region of the world and among virtually every major economy, driven by a confluence of reinforcing pressures: geopolitical competition, active conflict, technological innovation, and a broadening definition of national security and strategic infrastructure.

Rather than operating independently, each of these factors drives spending and amplifies the spending it generates. The result is a self-reinforcing system that gains momentum with every turn—a flywheel.

**The rearmament flywheel**



## Geopolitical competition is driving a sustained rise in defense spending.

The geopolitical fragmentation of the post–Cold War international system and the return of great power competition have resulted in a more fluid dynamic of geopolitical alignment, hedging, and rivalry. The resulting spread of geopolitical risks and an increasingly interconnected threat environment create pressure for states to maintain their current capabilities amid uncertainty, and increase defense spending to meet their changing needs.

The United States remains by far the world's largest military spender, a position it has held since the Second World War. Although US defense spending as a share of GDP has declined,[4] real spending levels have risen[5] significantly over the past decade, surpassing[6] $1 trillion in FY2026. The Trump administration has requested[7] a further increase—a record $1.5 trillion for its FY2027 defense budget. If enacted, this would represent a 38% real increase[8] over FY2026 spending levels and exceed[9] the previous historical peak for defense outlays set in 1945.

While the United States maintains a significant military advantage over its adversaries, its long-term planning is influenced by China,[10] its leading competitor and the world's second-largest defense spender. China's defense spending has grown by more than 13x[11] since 1995. Chinese leader Xi Jinping has made defense modernization a national priority, directing a comprehensive transformation[12] of the People's Liberation Army (PLA) by 2035. Although China's overall spending remains far below that of the United States, its investment is closing key capability gaps: It now operates the world's largest naval fleet[13] and leading missile arsenal, has doubled[14] the size of its nuclear arsenal relative to 2019 levels, and is investing[15] heavily in drone and unmanned systems integration.

Strategic competition lends a systemic force to defense expenditure. Generalized military buildup across multiple theaters pressures nations of all sizes to increase defense spending to shore up their relative security, creating an action-reaction dynamic that sustains itself even in the absence of active conflict.

For example, China's growing assertiveness[16] in the Indo-Pacific—evidenced through an increase[17] in military activity in areas like the Taiwan Strait and South China Sea, around Japan, and beyond the First Island Chain—and the buildup of both US and Chinese military capabilities in the region are pushing other Asian countries to respond. Japan, which historically capped[18] defense spending at 1% of GDP, increased defense spending by almost 10%[19] in 2025 alone and is reportedly[20] considering raising its spending target to 3.5% (from a current target of 2%). Others in the region, including India (+9%), Taiwan (+14%), and the Philippines (+12%), have made similar[21] spending increases over the past year. These dynamics are observable in theaters beyond the Indo-Pacific, and they point to a fundamental driver of today's age of rearmament.

## Active conflicts reshape threat perceptions and accelerate spending decisions.

Intensifying geopolitical rivalries have several downstream effects, including lowering the threshold for conflict. In 2025 there were eight direct conflicts[22] between individual states, the highest number since 1946—and notably a figure that does not include the current regional war in the Middle East. Wars provide their own impetus for rearmament as states expend their arsenals, prompting faster procurement and industrial expansion.

The most significant rearmament cycle in the world today is underway in Europe, catalyzed by Russia's full-scale invasion of Ukraine in 2022. Europe's defense spending rose by more than 101%[23] over the past decade, including a 14% increase in 2025 alone. Ukraine and Russia account for much of that growth, but the war has also transformed budgets across Western and Central Europe: Defense spending among European NATO members reached an estimated $563 billion[24] in 2025, 55% higher than in 2022, and is set for further growth as governments move toward the alliance's new 3.5% of GDP target for core defense spending.

The Middle East could be on the cusp of a similar trend. Defense spending as a share of GDP is already high across the region,[25] led by Israel (7.8%), Saudi Arabia (6.5%), and Oman (5.7%). And while total regional expenditures plateaued last year, the escalation of major conflicts will likely drive further spending. Israel's defense spending has grown 97%[26] since 2022 as the country fights on multiple fronts. Saudi Arabia, the seventh-largest defense spender in the world and the largest in the region, increased spending by 26%[27] in the first quarter of 2026 as a response to the war with Iran, an early indication of how defense resilience is being prioritized—and one that is likely to be reflected elsewhere in the region.

# Technological innovation changes the cost and character of warfighting—and the price of deterrence.

Part of what makes this rearmament cycle distinct from previous cycles is that countries are preparing for a new style of warfare—one that relies heavily on unmanned systems and AI-enabled software. The spread of new and emerging defense technologies is supported both by surging investment, which can accelerate innovation, and increased conflict, which forces the compression of innovation cycles further.

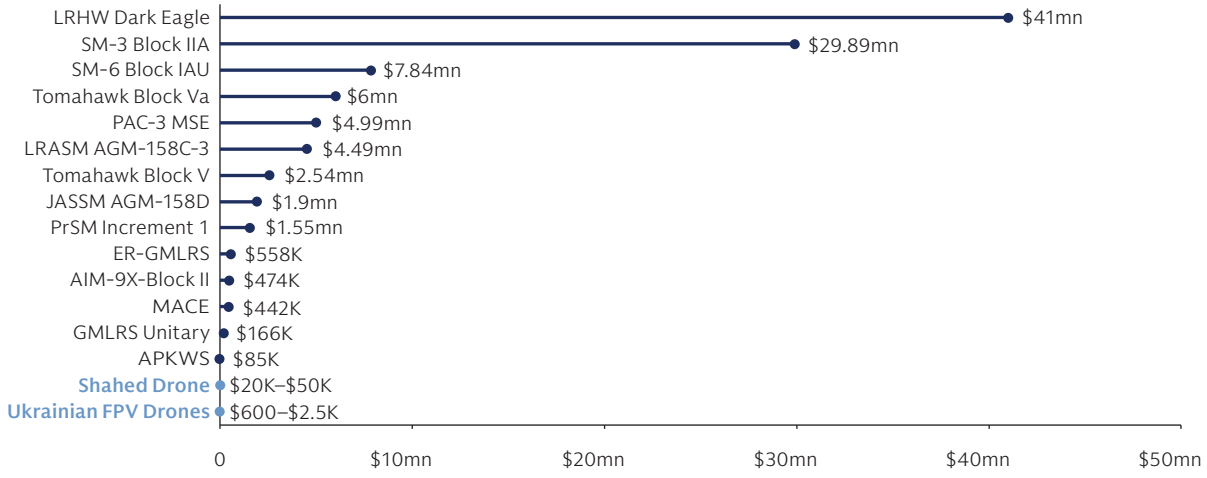
Nowhere is this clearer than in Ukraine, which serves as a laboratory for the technologies and operational tactics that are shaping the future of warfighting. Unmanned systems, particularly drones, have become so ubiquitous that Ukraine's commanders say drones now account for more than 80%[28] of strikes against enemy targets.

The low cost and modularity of these unmanned systems—often built utilizing commercial components rather than complex, specialized defense supply chains[29]—have several transformative implications for the way wars are fought.

- **These systems can be modified much more quickly, easily, and cheaply than legacy platforms** in response to developments on the battlefield, and rapid iteration is increasingly shaping battlefield outcomes.
- Because these weapons are built from consumer technology, **competition for commercial supply chains is increasingly pivotal to the strategic competition between states.**
- Cheap, unmanned platforms are **changing the incremental economics of warfare by lowering the cost of precision strikes and expanding the range of actors that can project power over land, sea, and sky.**

The conflict in the Middle East illustrates the cost asymmetry of modern warfare, in which relatively inexpensive offensive systems can impose outsize costs on advanced defensive architectures. Iranian Shahed drones are estimated to cost[30] anywhere from $35,000 to $50,000 per unit. In contrast, the American-made Patriot missile interceptors that are being used to defend against thousands of Iranian strikes cost an estimated $4 million,[31] and experts are already warning that increasing production to replenish depleted stockpiles will take several years.[32] Adapting to these new realities is another factor driving the pace of defense spending today.

**Cost asymmetry of modern weapons (cost per round)**




Sources: Andreessen Horowitz (September 2026); CSIS (February 2025); *Military Times* (March 2026)
Note: US missile costs are according to the FY2027 budget request. Iranian and Ukrainian estimates are based on recent news reporting.

"The technologies that are transforming the battlefield are also making it easier to target an adversary's economy."

## Modern warfare broadens the definition of national security to include economic resilience.

The technologies that are transforming the battlefield are also making it easier to target an adversary's economy. Advances in AI are increasing the threat and scale of cyberattacks[33] against critical infrastructure. The wars in Ukraine and the Middle East have both underscored that critical infrastructure like energy grids, ports, pipelines, undersea cables, and industrial facilities are now primary targets in conflict: Ukraine has used long-range drones to strike Russian refineries and export terminals more than a thousand kilometers[34] from the front, while US and Iranian strikes on power and water infrastructure have become a key coercive tactic[35] of the war in the Middle East.

This strategic reality is likely to drive a growing focus on integrated defense architectures and resilient, cost-effective performance. It also coincides with a heightened focus on technological sovereignty, and energy and supply chain security. The result is an expanding conception of national security to include economic resilience, with implications for what budgets must cover as countries focus on protecting critical infrastructure, building strategic stockpiles of things like munitions and critical minerals, ensuring cyber and network resilience, and maintaining industrial capacity.

The results of this shift are already becoming visible. Earlier this year, the United States launched a large-scale effort, Project Vault,[36] to create a strategic critical mineral reserve. Gulf States are rushing to expand international oil stockpiles[37] as domestic ones come under threat, while states without strategic reserves are looking to create them.[38] Ukraine has turned toward distributed and modular energy solutions[39] to shore up the energy resilience for critical infrastructure like hospitals.

Companies may even look to commercial defensive technologies in response to physical threats—as demonstrated by the reported[40] contract by defense tech startup Powerus to provide drone detection equipment to an energy company in the Gulf. In fact, the very nature of dual-use technology encourages commercial use cases for many of the products made by defense tech startups. For example, many aerial and maritime drone makers also market[41] their products for critical infrastructure surveillance and repair, while energy technology companies specializing in off-grid energy solutions are finding military offtakers interested in distributed power solutions to support operations.

This broadened mandate is now being written directly into defense spending commitments. Of the 5%-of-GDP[42] target NATO members agreed to at the 2025 Hague summit, up to 1.5% is dedicated not to core defense requirements but to defense-related investments to protect critical infrastructure, defend networks, and strengthen the defense industrial base.

In practice, this means that defense is becoming a pillar of industrial policy. It also means the perimeter of geopolitical competition keeps widening, feeding back into the rivalry where this cycle began. Finally, it should be noted that increasingly sophisticated dual-use technology also poses unique challenges for governments, as non-state actors[43] can use technology like commercial drones to perpetuate civilian and state conflicts, strengthen smuggling networks, or conduct reconnaissance. This is already observable in places like Sudan, where inexpensive drones have been deployed by both sides of the current civil war, extending the conflict's reach and exacerbating the scale of violence against civilians, including the massacre in El Fasher.[44]

# Shifting Force Design: Survivable, Attritable, Consumable

The defense industrial model that coalesced after the Cold War concentrated spending on a small number of expensive, human-crewed platforms—traditional assets like fighter jets, tanks, and warships—known as survivable systems: assets designed to complete their mission and return to be used again. Today, that model is changing as militaries integrate new AI-enabled defense technologies.

Future force posture will likely increasingly depend on combat power that layers[45] survivable systems with attritable systems (mid-cost, unmanned platforms) and consumable mass (low-cost, single-use weapons). Underpinning this shift is an increasingly critical AI-driven data analytics and software layer. Depending on the tool, this can function as a digital nervous system for military forces, processing large amounts of multisource sensor data to create an enhanced operational picture for human decision-makers, or as embedded software that runs directly on unmanned systems, enabling autonomous operation even in contested environments.

At the high end of this spectrum, the industrial model dominated by defense primes still achieves what it was designed to do, which is to develop and produce long-lead-time, expensive, and highly complex hardware. Order books for these systems are surging on the back of rising defense investment, giving established manufacturers multiyear revenue visibility that is allowing many of them to significantly increase production plans.

And the frontier of exquisite capability keeps advancing, as militaries prioritize the development of next-generation aircraft, nuclear modernization, hypersonic weapons, and space-based missile defense. Cost estimates[46] for the Trump administration's Golden Dome architecture alone run to $1.2 trillion. Developing these capabilities requires long lead times and capital-intensive programs that remain the province of a handful of defense primes and, increasingly, neo-primes.

At the other end of the spectrum, countries now face an imperative to invest in the AI-enabled systems and low-cost, attritable mass that have proven so critical on the modern battlefield. But fielding these capabilities upends many of the parameters that define modern defense industrial bases, including consolidated contractors, low-volume production runs, specialized supply chains, multiyear procurement timelines, and rigid government contracting models. This friction is driving many governments to formulate strategies to expand their industrial bases, boost private sector investment and collaboration, and accelerate acquisition and adoption timelines.

Together, these dynamics are reshaping where defense capital flows, who captures it, and how governments procure new supplies and capabilities.

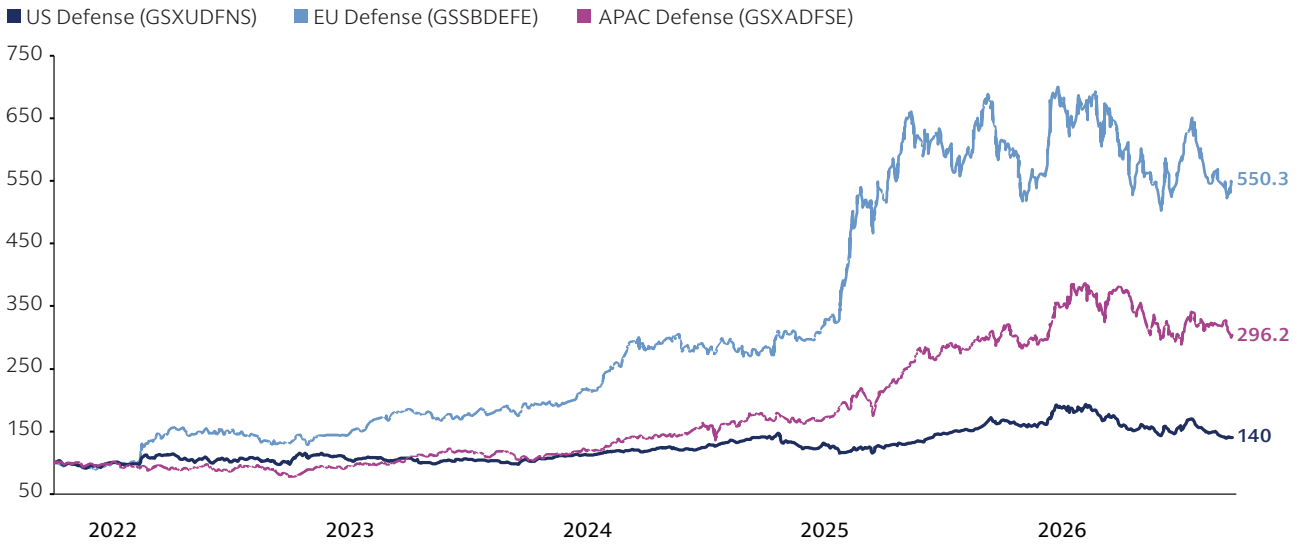


# Rearmament Is Driving New Priorities for Defense Investment

The world's top 100 defense companies earned a record $679 billion[47] in 2024, $214 billion of which was generated by just the top five[48] companies (four of which are US primes). Behind those revenues sit historically large order books that are helping fuel industrial expansion. Lockheed Martin reported a record $230 billion backlog[49] in July 2026, up $64 billion year-over-year. In Europe, Germany's Rheinmetall, one of the leaders of Europe's rearmament, has an order backlog[50] of $93 billion as of July 2026, with company guidance pointing to roughly $151 billion by year-end 2026.

Equity markets have reflected these broader trends. In the United States, defense company stocks have rallied alongside growing defense budgets. European defense companies, which have historically traded at a discount to American peers amid the limitations of smaller markets and fragmented procurement practices, have seen that discount shrink, fueling a wave of corporate M&A[51] as companies look for ways to scale despite the limitations of Europe's fragmented capital market.

**Performance of Goldman Sachs baskets of US, European, and Asian defense stocks**




Source: Goldman Sachs Marquee MarketView[52]

Sudden demand shocks tend to boost cross-border defense orders as domestic defense industrial bases come under strain. Just as companies pursue cross-border M&A to overcome capital constraints and achieve scale, governments turn to international orders when their resilience needs exceed their domestic industrial capacity. For example, South Korea's defense industry has grown[53] by about 100% over the past five years because of a surge in European orders following the outbreak of war in Ukraine. Now that dynamic is rotating to the Middle East, where Persian Gulf countries have announced more than $5 billion[54] in additional defense contracts from American, European, and Asian companies since the war began.

Ultimately however, the search for domestic resilience provides a strong incentive for domestic reindustrialization. For example, in Germany, which has been at the vanguard of defense spending increases in Europe, 50% of defense orders since 2022 have gone to German companies and another 35% to German-foreign partnerships, according to Goldman Sachs Investment Research.[55] Similarly, Gulf countries like Saudi Arabia and the United Arab Emirates, which already have ambitious defense localization targets,[56] are looking to pivot from buyers to defense industrial partners as investment ramps and capabilities expand. This doesn't mean that countries will no longer purchase foreign equipment. But it does mean that countries are increasingly looking to leverage durable commercial relationships into joint ventures, local production arrangements, and deeper relationships built around maintenance and training that can facilitate technology transfer, or joint production that uplevels domestic industrial capabilities.

### The reorientation toward low-cost, autonomous systems has made defense tech one of the fastest-growing sectors.

The US defense sector has already broadened significantly with the growth of defense tech startups and increased integration between Silicon Valley and the Pentagon, supported by initiatives like DARPA and Defense Innovation Unit. Through May 2026, US defense tech startups have already raised[57] a record $14.6 billion, surpassing the $9.6 billion raised in all of 2025. Two of the most prominent US players in this space, Anduril and Palantir, are increasingly capable of acting as primes in their own right: Anduril raised[58] $5 billion in May 2026 at a $61 billion valuation, one of the largest funding rounds for a venture-backed defense company.

Europe's defense spending surge, supported by reforms to support the growth of its defense industrial base, has also propelled a rise in investment for European defense technology firms. European defense tech startups raised a record $8.7 billion[59] in venture funding in 2025, a 55% year-over-year increase. Unlike in previous cycles, this capital was increasingly concentrated in late-stage rounds, signaling a transition from experimental R&D to industrial scaling. Although this market is still nascent, Europe now boasts a growing handful of defense startups with unicorn status[60]—minting three in 2025 and four so far in 2026—led by Munich-based Helsing, which raised $1.8 billion[61] in July 2026 at an $18 billion valuation.

This growth in funding for defense tech reflects the new force design. Startups focused on autonomous systems, unmanned platforms, and defense software accounted[62] for many of the largest funding rounds in the space, and manufacturing-focused defense investment nearly doubled[63] in 2025 as the sector focuses on increasing production capacity alongside technology.

The primes themselves are increasingly acting as venture investors. A record $4.1 billion[64] of VC funding rounds for defense tech startups in 2026 had participation from defense primes. And 13 of the largest defense companies in the world have increased their own R&D budgets[65] by at least 25% over the past five years, another indication that primes are recognizing the need to develop and integrate emerging defense technologies.

## Cross-Border Partnerships and Industrial Policies Are Expanding Defense Production

### Ukraine is emerging as an important pillar of the global defense industrial ecosystem.

Perhaps the most dynamic element of this new ecosystem is the evolution of the Ukrainian defense sector. Having matured under the pressures of high-intensity conflict, Ukraine's defense technology sector is one of the most innovative and productive in Europe, valued at approximately $6.8 billion.[66] This sector is defined by more than 1,000[67] manufacturers, the vast majority of which are small and privately owned. In 2025, investment[68] in Ukrainian defense companies rose to $105 million, up from just $1.1 million three years ago. This ecosystem benefits from an unprecedented repository of real-world combat data, including millions of hours[69] of drone footage, which Ukraine is seeking to leverage to train advanced AI models and drive new capability development in partnership with Western firms.

Ukraine is now converting that capability into an export industry that is allowing the country to forge a new class of international and industrial partnerships. In March 2026, the government of Ukraine signed[70] 10-year defense cooperation agreements with Saudi Arabia, Qatar, and the United Arab Emirates. Just a month later, in April 2026, Ukraine authorized[71] the export of surplus defense equipment, including drones, and announced plans for 10 weapon export centers across Europe.

As governments around the world move to expand and operationalize their drone fleets, Ukraine is positioning itself as a central partner in that effort. Kyiv has signed 10[72] drone cooperation agreements to date, mostly with European and Middle Eastern states, and is now looking to expand cooperation with Asian economies like Japan.[73] This has dovetailed with a growing number of joint ventures[74] with international defense tech firms aimed at expanding Ukraine's industrial scale and growing international interest[75] in buying or taking stakes in Ukrainian startups.

## Joint development and prime-startup partnerships are modernizing Western defense capability.

Multinational cooperation to develop new defense capabilities is also expanding. For example, AUKUS anchors Australia, the United Kingdom, and the United States in a decades-long partnership to help Australia acquire conventionally armed, nuclear-powered submarines, in addition to a second pillar focused on trilateral development of advanced military capabilities. Similarly, the governments of the United Kingdom, Italy, and Japan are collaborating on the Global Combat Air Programme (GCAP) to develop a sixth-generation fighter, supported by a dedicated industrial joint venture. NATO has also launched a number of High Visibility Projects (HVPs)[76] to oversee multinational development of new or upleveled capabilities, such as fielding ground-based precision strike capabilities, deep-strike drones, or uncrewed maritime systems.

This sort of collaboration is also making its way deeper into the private sector in the form of a growing number of joint ventures between defense tech startups and established contractors, such as Rheinmetall's partnerships with Finland's ICEYE[77] or Switzerland's Destinus.[78] The UAE's EDGE Group,[79] which was created to acquire and develop indigenous defense tech capabilities through international partnerships, has formed joint production ventures with companies like Anduril[80] and Leonardo.[81] The benefits of these arrangements are mutual: Startups can benefit from the greater production capacity, government relationships, and established procurement channels of primes, while incumbents benefit from access to cutting-edge commercial technology and the iterative speed of defense tech startups.

Joint development can help nations field capabilities more quickly and cost-effectively than they could individually by pooling industrial expertise and capacity, sharing costs, and generating economies of scale. Among allies and partners, such cooperation can also strengthen interoperability and enhance supply chain resilience. As states face increasing incentives to rearm and to modernize their militaries, this sort of industrial collaboration may prove increasingly attractive among partners.

## Industrial policy is accelerating the development of autonomous and AI-enabled systems.

While the private capital flowing into defense tech reflects momentum within the industry, many militaries still lack the procurement systems and production capacity to field autonomous systems at the scale required for modern warfare. Closing that gap has become a major focus of defense industrial policies around the world.

The United States, for example, has prioritized building a sovereign drone industrial base. The Pentagon's Replicator[82] initiative, launched in 2023, was the first major attempt to field low-cost autonomous systems by the thousands, but it fell short of that goal, delivering only hundreds over a two-year period. The US administration has since pushed further under the banner of its Drone Dominance[83] program, which aims to spend $1 billion to field 300,000 cheap drones by 2027. To support this goal, the Pentagon has paired the Drone Dominance program's push to buy low-cost small drones at scale with the creation[84] of the Defense Autonomous Warfare Group (DAWG), which is intended to coordinate testing, integration, and fielding across US forces.

"Joint development can help nations field capabilities more quickly and cost-effectively than they could individually by pooling industrial expertise and capacity, sharing costs, and generating economies of scale."

Other states are mounting similar efforts. In February 2026, defense ministers from the United Kingdom, France, Germany, Italy, and Poland announced[85] the Low-Cost Effectors and Autonomous Platforms (LEAP) initiative to jointly develop and produce low-cost autonomous air defense systems such as interceptor drones. The United Kingdom was the first of the group to issue contracts under the program, awarding ~$4.3 million[86] to three European defense tech startups to develop low-cost interceptors, one of which already has a contract to supply[87] its low-cost interceptors to several Gulf countries. Meanwhile, Australia plans to invest roughly A$22 billion[88] (US$15.3 billion) in drone and counter-drone defenses over the next decade, with a focus on domestic suppliers. Taiwan, too, has approved an additional $7 billion[89] in funding to support its homegrown drone industry as it notes the lessons of wars in Ukraine and Iran.

Whether procurement reforms and industrial initiatives can translate into production at scale for low-end capabilities remains a critical challenge for governments. One problem, demonstrated on the battlefield between Russia and Ukraine, is the speed at which these systems become obsolete as innovation cycles compress. Traditional procurement practices and government contracts have not yet fully adapted to the speed and scale required for this new industrial base.

## From Rearmament to Industrial Resilience

If the security supercycle thesis is right, the structural forces shaping today's rearmament have the potential to change not only how governments spend on defense, but also how much industrial capacity they maintain. In a prolonged period of geopolitical competition, governments will need to prioritize replenishing inventories, replacing losses, adapting systems, and securing the inputs on which all that depends. As a result, production capacity, reliable supply chains, and speed of iteration are all becoming sources of strategic advantage. Meeting these demands will broaden the defense ecosystem to include defense-adjacent companies and cross-border partnerships that can scale capabilities beyond the limits of individual national markets.

The commercial implication is more complicated than headlines about rising defense spending suggest. A larger market won't reward every new entrant, and owning strategically important technology doesn't automatically translate into attractive economics. The strongest opportunities in the defense supercycle may be those that capture a readiness premium, rewarding businesses whose specialized capabilities deliver the assured capacity



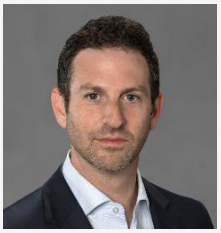
"The strongest opportunities in the defense supercycle may be those that capture a readiness premium, rewarding businesses whose specialized capabilities deliver the assured capacity that customers must structurally maintain across cycles."

that customers must structurally maintain across cycles. Investors will have to distinguish announcements from funded programs, pilot projects from repeat orders, and urgent purchases from durable changes in procurement. The important question is which companies can turn a moment of political urgency and attention into a strong position in the production system.

For businesses, that argues for building around specific constraints rather than broad themes. The companies that make components that limit output, new manufacturing processes that shorten delivery times, software that makes existing systems more effective, or infrastructure that allows new suppliers to enter the market—these are the companies that will have an advantage amid increasing competition. Commercial technology will drive much of this innovation, but governments will have to offer enough demand predictability to make private investment in resilience economically rational.

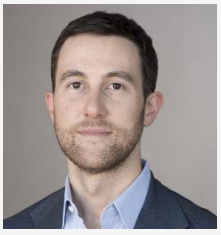
The deeper implication is that security and resilience become more explicit considerations for how economies allocate capital. The search for resilience will lead governments to deliberately pursue some redundancy, spare capacity, and supply diversity, even when they raise near-term costs. Manufacturing readiness—the ability to produce repeatedly, quickly, and at scale—will be an increasingly important variable shaping government procurement. The security supercycle will ultimately reward the companies that can turn governments' commitment to defense reindustrialization into durable commercial value.

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# Endnotes


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