Carlsquare/Vontobel weekly trading note: Higher European defence spending could boost interest rates

The Greenland crisis between the US and Denmark has caused European defence stocks to rise. However, the funding and risk associated with the higher interest rates because of increased European defence spending over the next decade have not been discounted in the same way. The reporting season for S&P 500 companies in the US started well, with 79% of companies reporting positive earnings surprises.

Pressure from the US for European NATO allies to increase their military spending from 2% to 5% of annual GDP, as well as President Trump's threat to take over Greenland, has increased the value of European defence stocks. The easiest way for European politicians to finance these sharply increased defence costs over the next decade would be to increase government lending. However, the average national debt of EU countries is already over 80% of GDP, with the UK's being over 90%. Increasing this debt-to-GDP ratio to 110–120% over the next ten years would reduce the creditworthiness of European countries and push up interest rates.

So far, 7% of S&P 500 companies have reported their results for Q4 2025. According to Earnings Insight, of those companies, 79% reported a positive earnings per share (EPS) surprise and 67% reported a positive revenue surprise.

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