



CRA Closer Look

“Defense-21”

Drivers of Change in the 21st Century

May 2010

CRA Charles River
Associates

“Defense-21”: Summary

This issue of CRA’s Closer Look examines the drivers of change for the business of defense in the 21st century

It has become a conventional wisdom that the defense industry is crossing an inflection point, which is changing its business in fundamental ways. CRA set out to test that proposition by examining what has changed and how, as well as the significance any inflection may hold for companies. To perform this test, we first surveyed macroscopic drivers of change on the landscape that forms the strategic context for the business of defense. Then we examined the microeconomic dynamics of the market for defense products and services. From these tests, we conclude that the industry has indeed crossed a threshold that is resetting the business of defense.

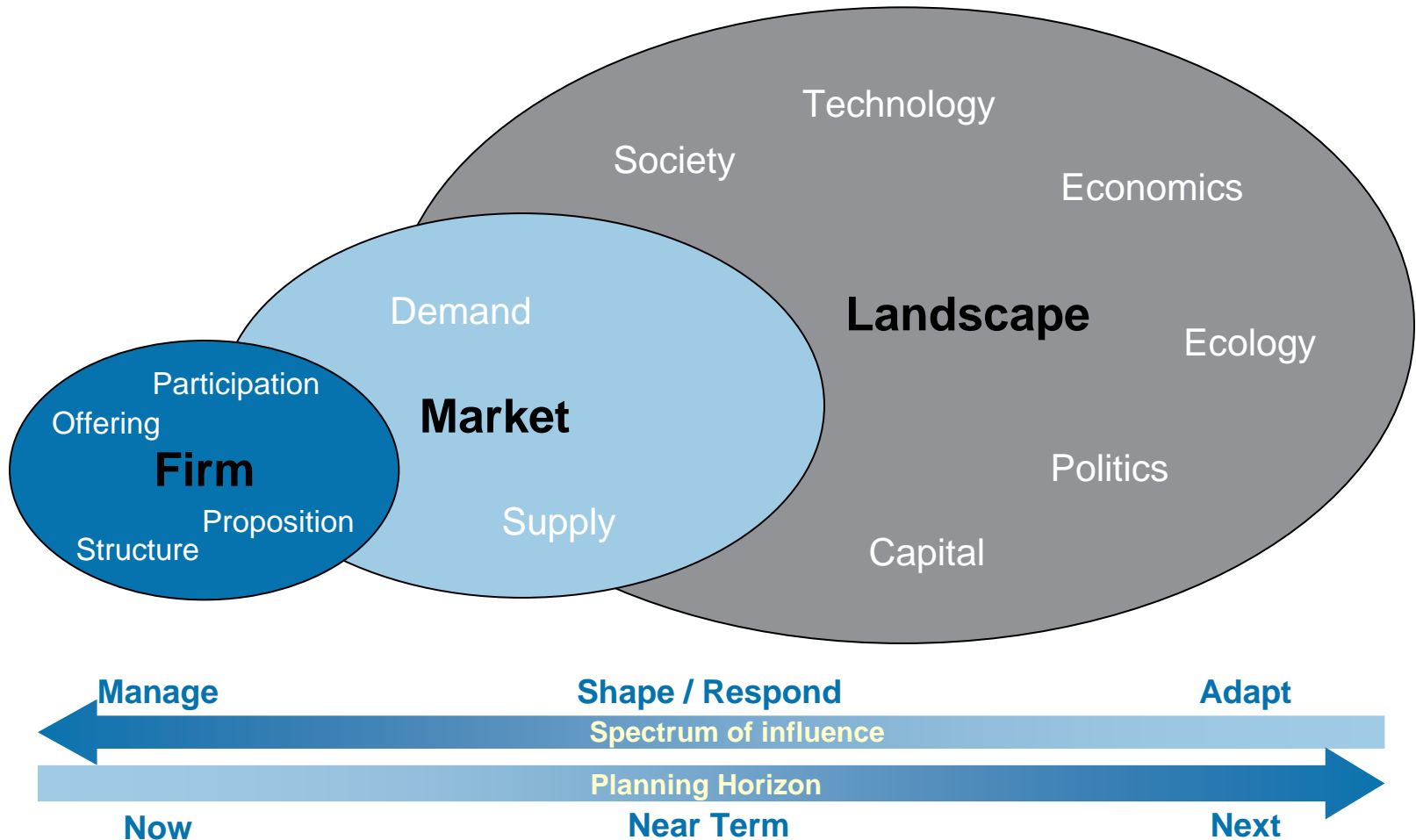
In this new, post-Iraq War era, a globalized landscape of macroscopic drivers is reshaping the precepts of the strategic context. Inflection along these dimensions will not tend to change the business of defense overnight, but it does have the effect over time of reshaping the foundations of customer demand and the infrastructure of resources on which companies rely. The significance for corporate strategy of inflections on this landscape, therefore, is not their urgency but the large magnitude and reach of their effects, and the corresponding adaptations of strategic postures which they compel.

At the same time, mature industry dynamics are recalibrating customer requirements and the bases of competition among suppliers. Inflection-point change in the market dimensions of defense holds the potential to reset customer needs and expectations and to instigate innovative competitor conduct. For corporate strategy, therefore, the key significance of changes in the dynamics of the market is their immediacy and the corresponding urgency for action to shape these evolutions, where possible, or otherwise quickly adjust strategic postures to their imperatives.

The implications of these changes should prompt a reconsideration of the key tenets of strategic posture in defense companies: In which markets to participate? What portfolio of products and services to offer? How to gain competitive advantage? How best to structure assets?

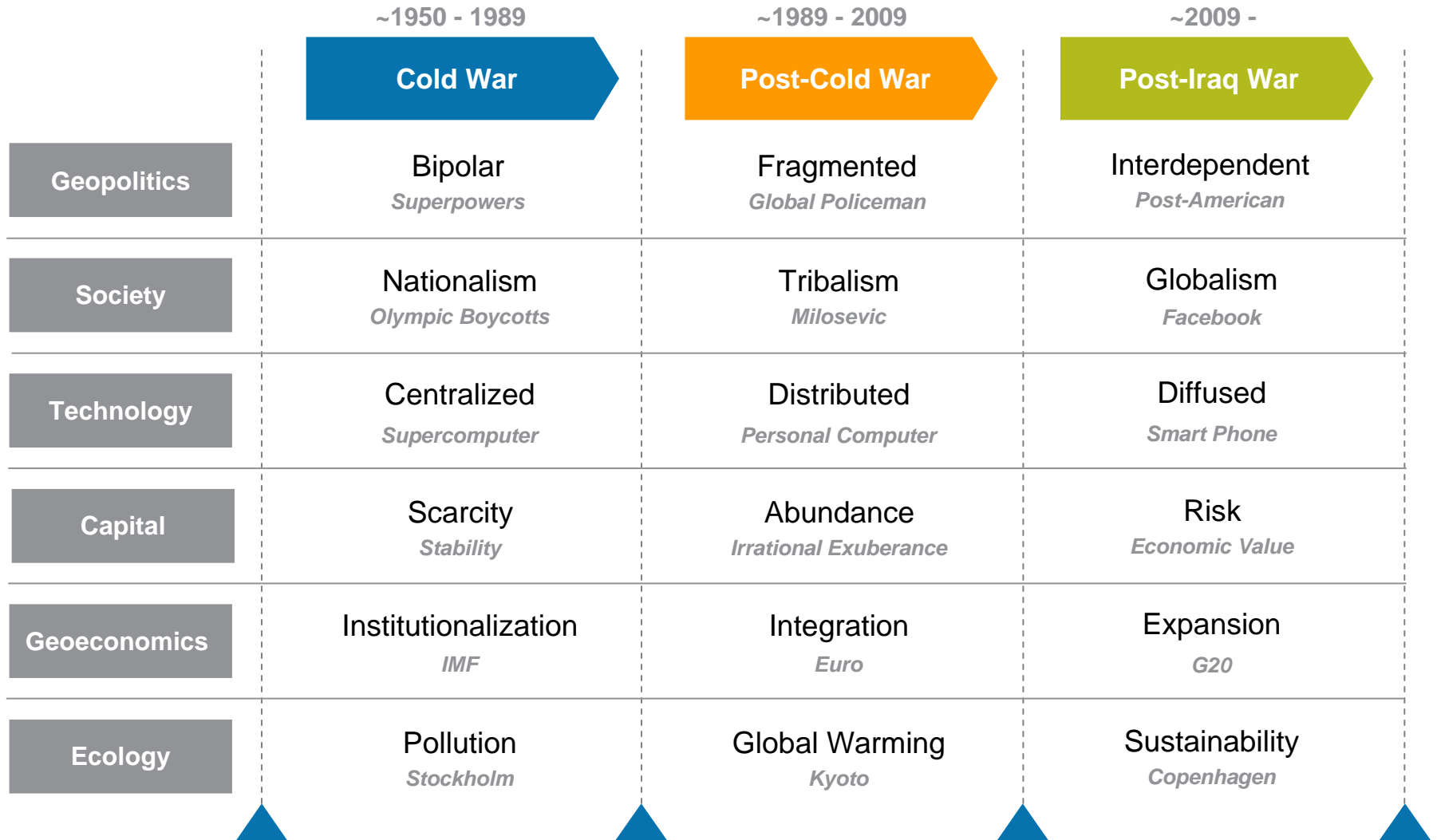
“Defense-21”: Introduction

The 21st century defense enterprise must adjust its strategic posture to an evolving macroscopic landscape and dynamic marketplace



“Defense-21” Landscape: Overview

Inflection on the strategic landscape of defense in the 21st century is summarized in captions of the key drivers and iconic emblems of change over time



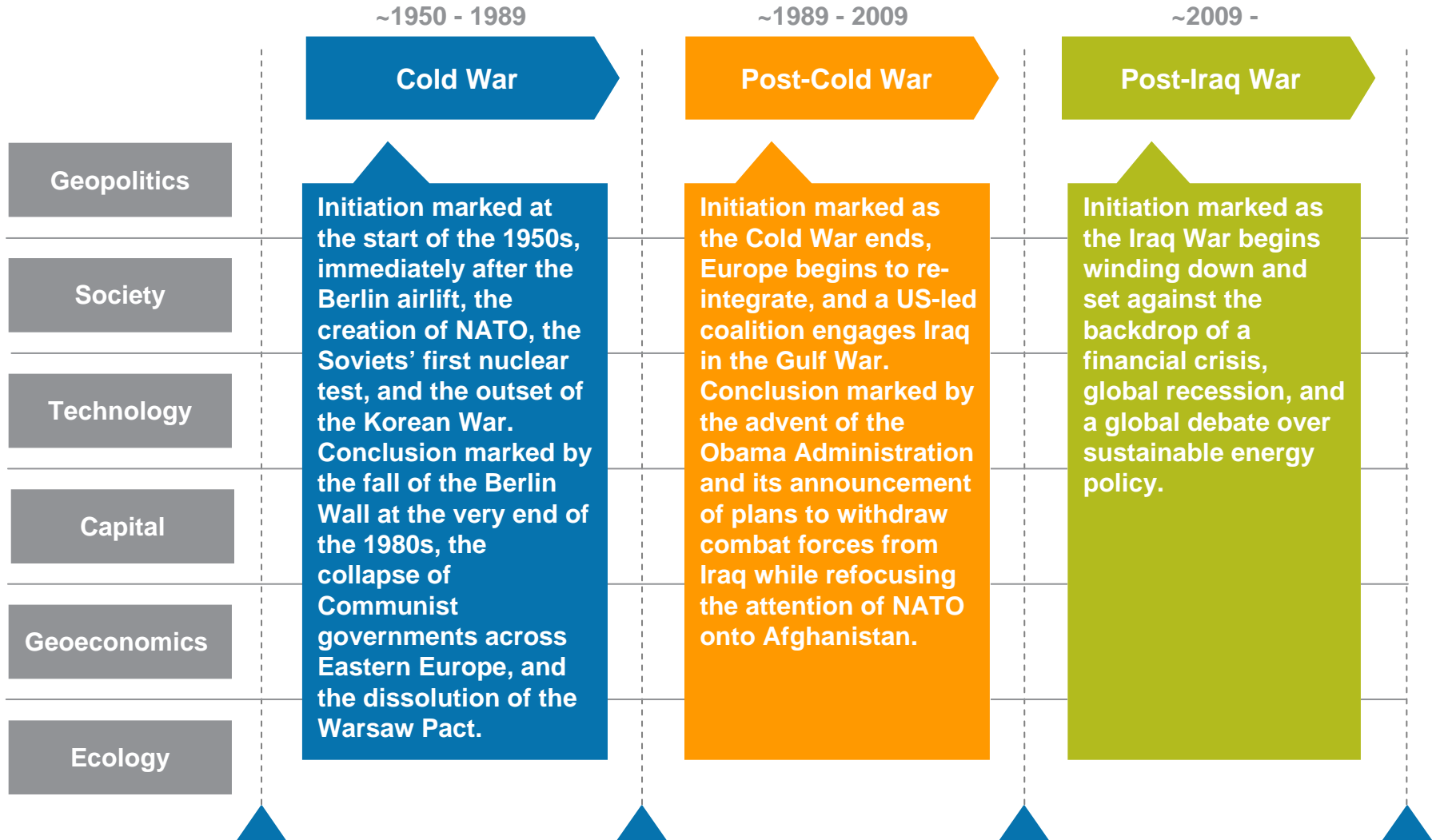
“Defense-21” Landscape: Macroscopic Dimensions

Six macroscopic dimensions of the strategic landscape characterize the key drivers of change affecting the defense industry



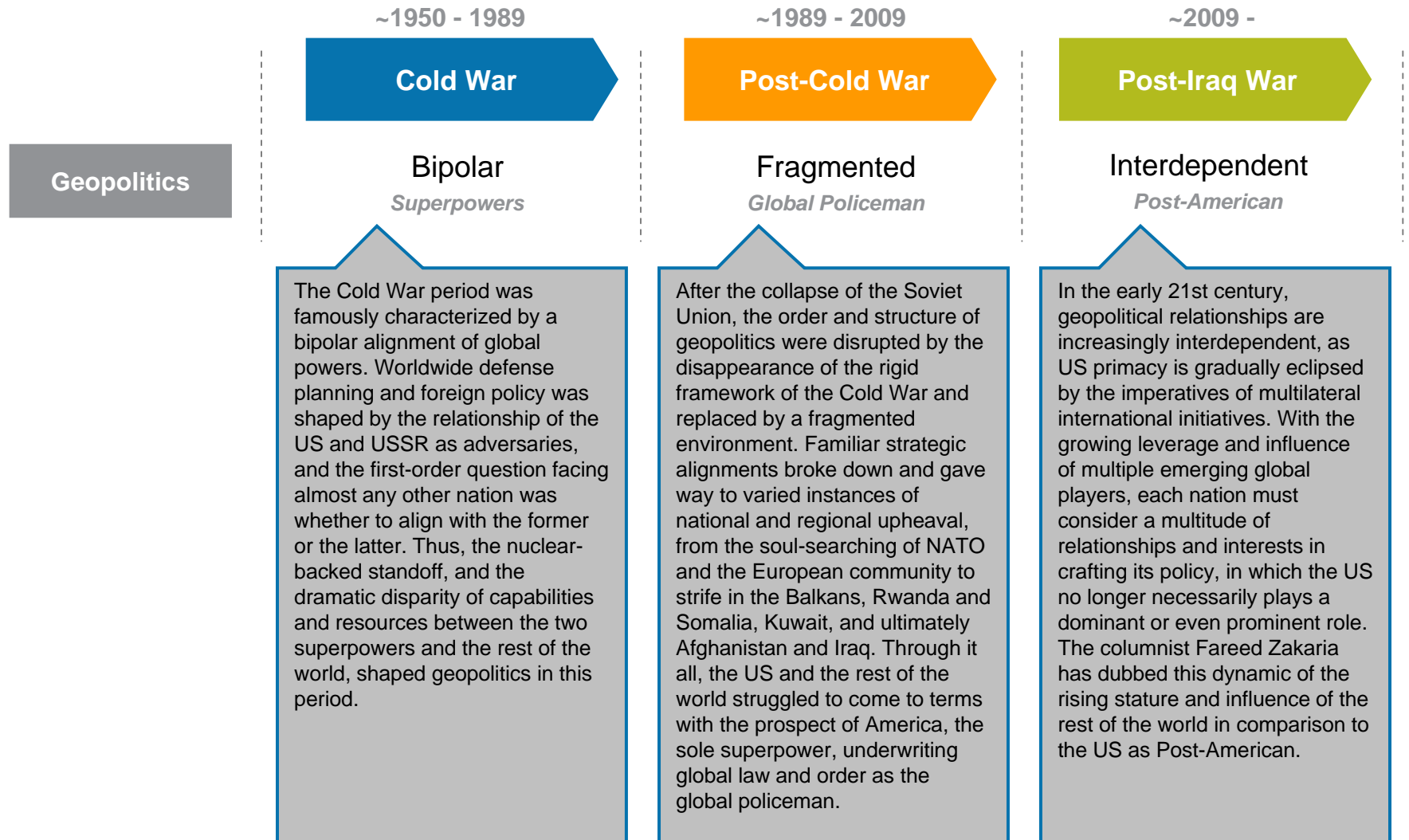
“Defense-21” Landscape: Historical Eras

Three historical eras, beginning with the onset of the Cold War and culminating in the contemporary, post-Iraq War era, mark the inflection of landscape trends



“Defense-21” Landscape: Geopolitics

We are entering a “post-American” world in which radical interdependence of nations will reshape the allocation and exercise of power



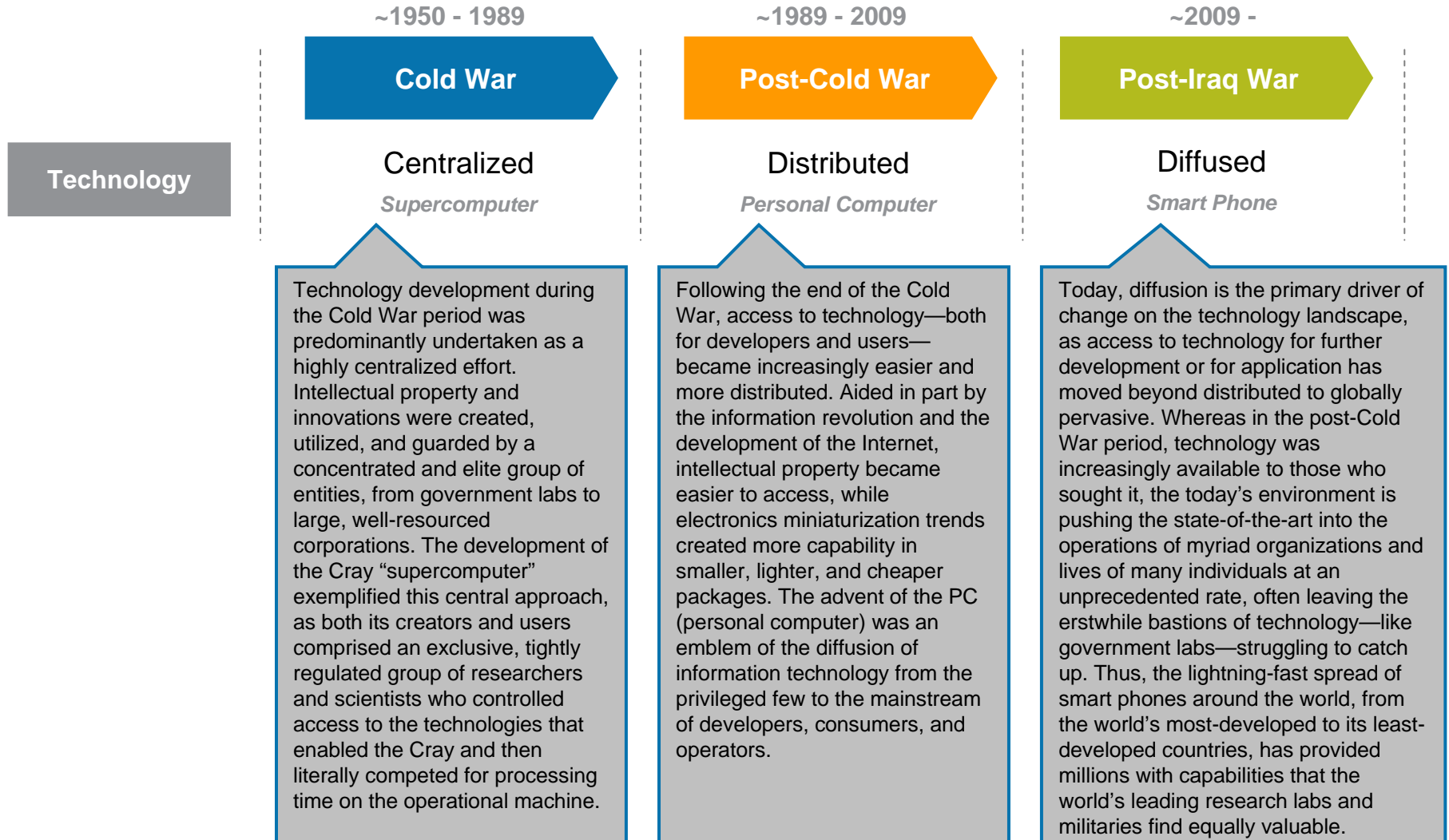
“Defense-21” Landscape: Society

Fueling interdependence will be the formation of personal relationships within global communities that transcend traditional national and tribal identities



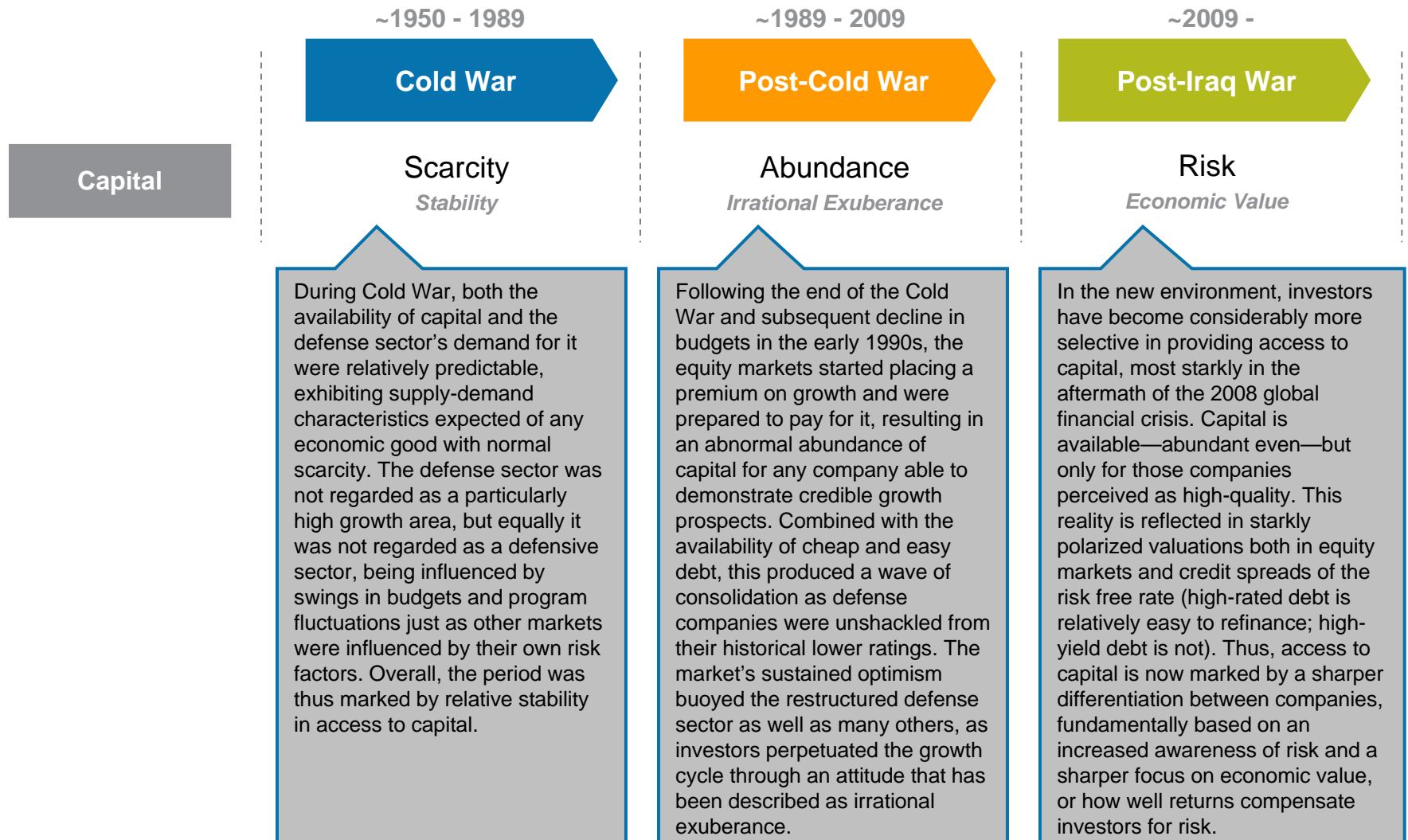
“Defense-21” Landscape: Technology

An unprecedented diffusion of advanced technologies will shape the character of security threats and the ever faster pace and open venues of industrial innovation



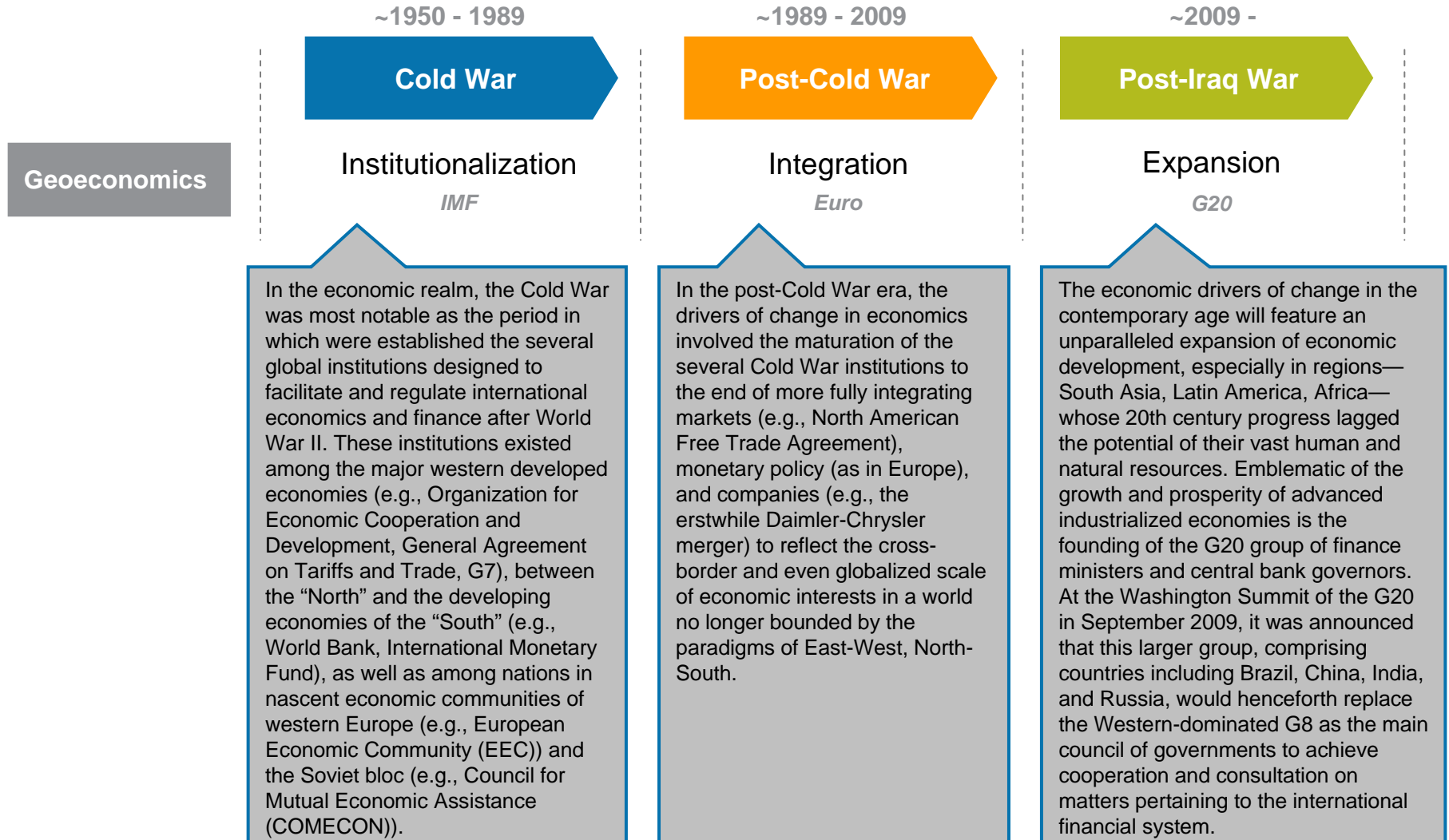
“Defense-21” Landscape: Capital

While access to technology is expanding, access to abundant capital will be tempered by the watchword risk



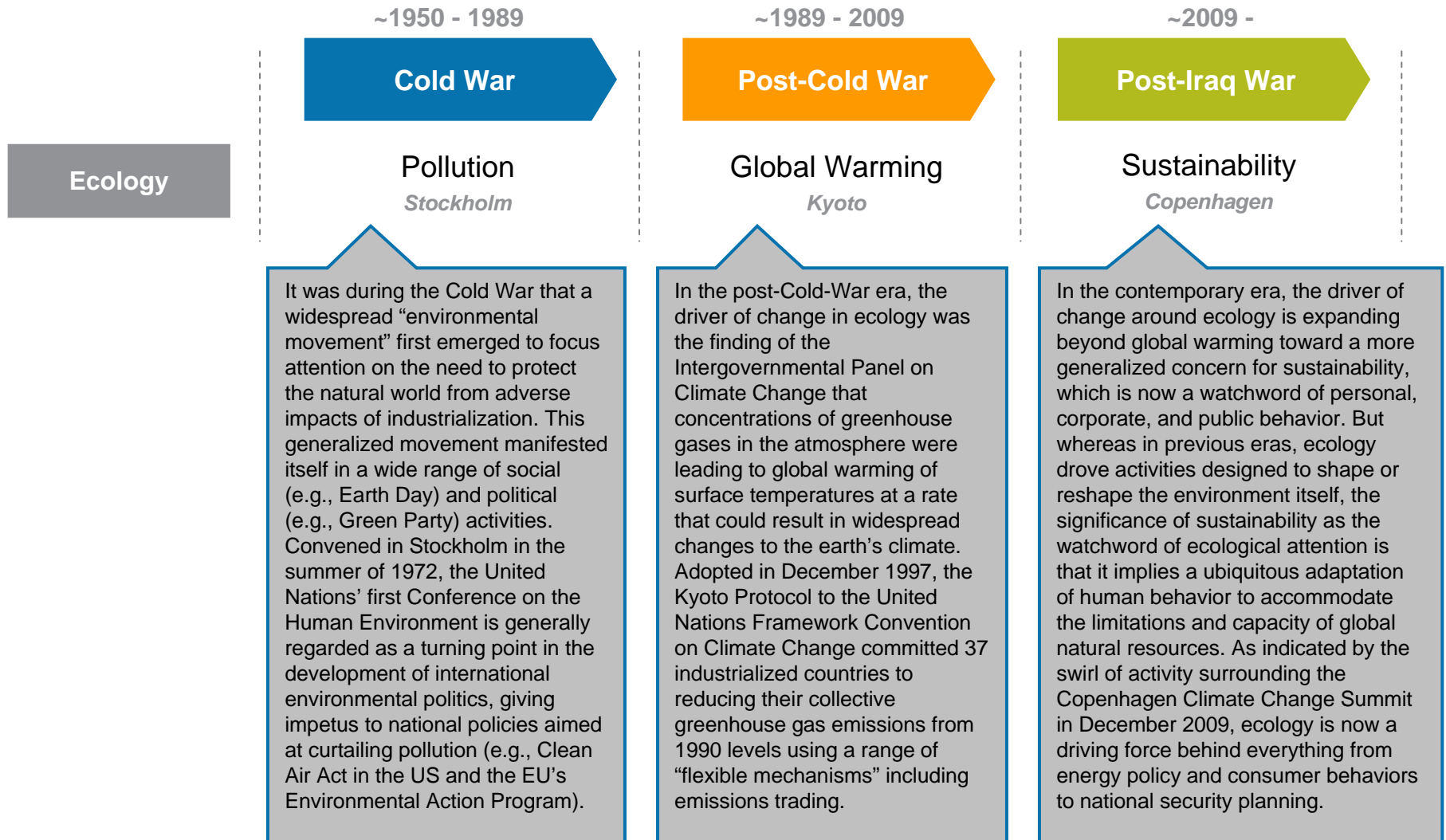
“Defense-21” Landscape: Goeconomics

The locus of economic growth will move outside the West, followed by a dramatic expansion of middle-class prosperity in those regions



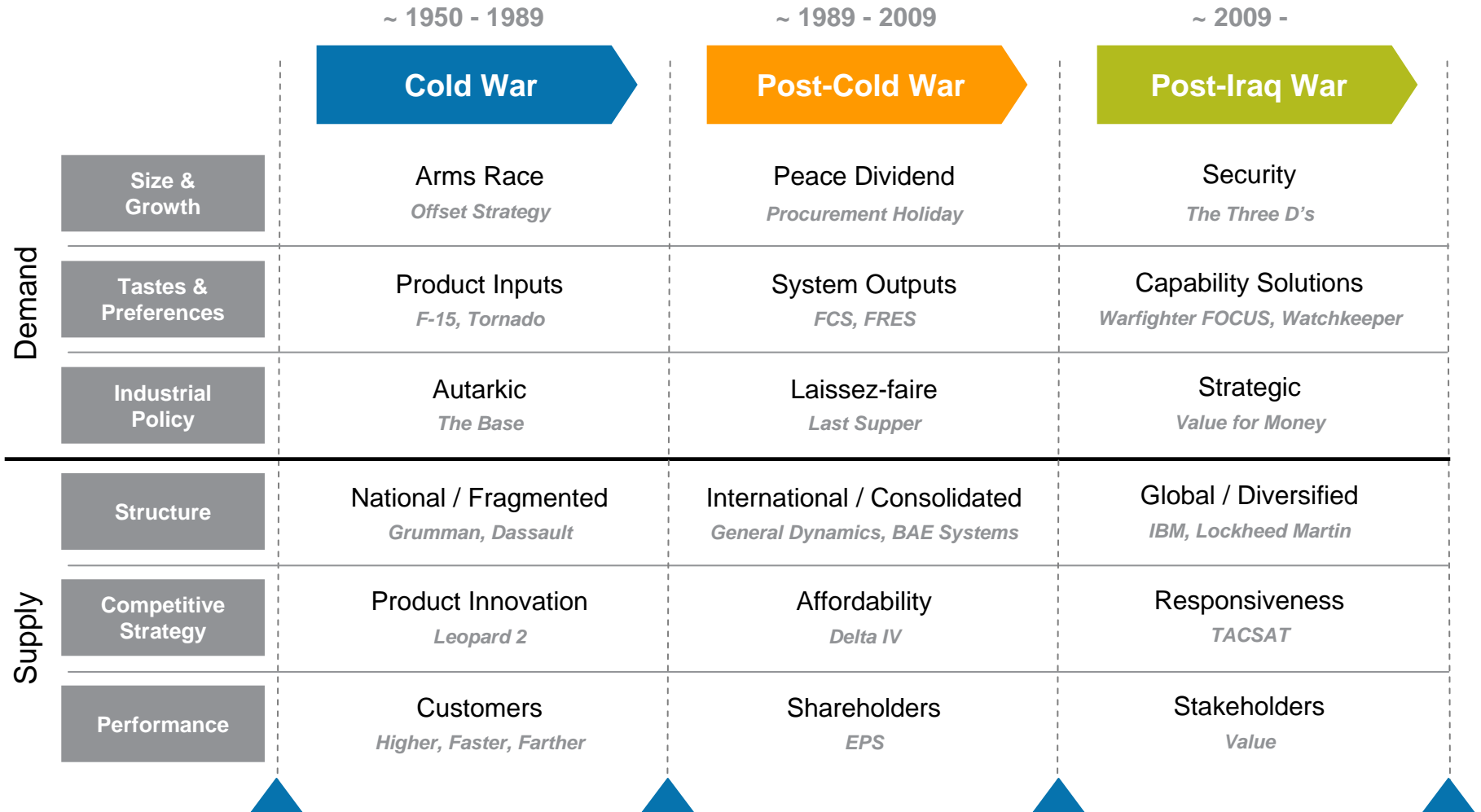
“Defense-21” Landscape: Ecology

Economic growth will be juxtaposed against sustainability, the new and ubiquitous test of responsibility toward the human ecology



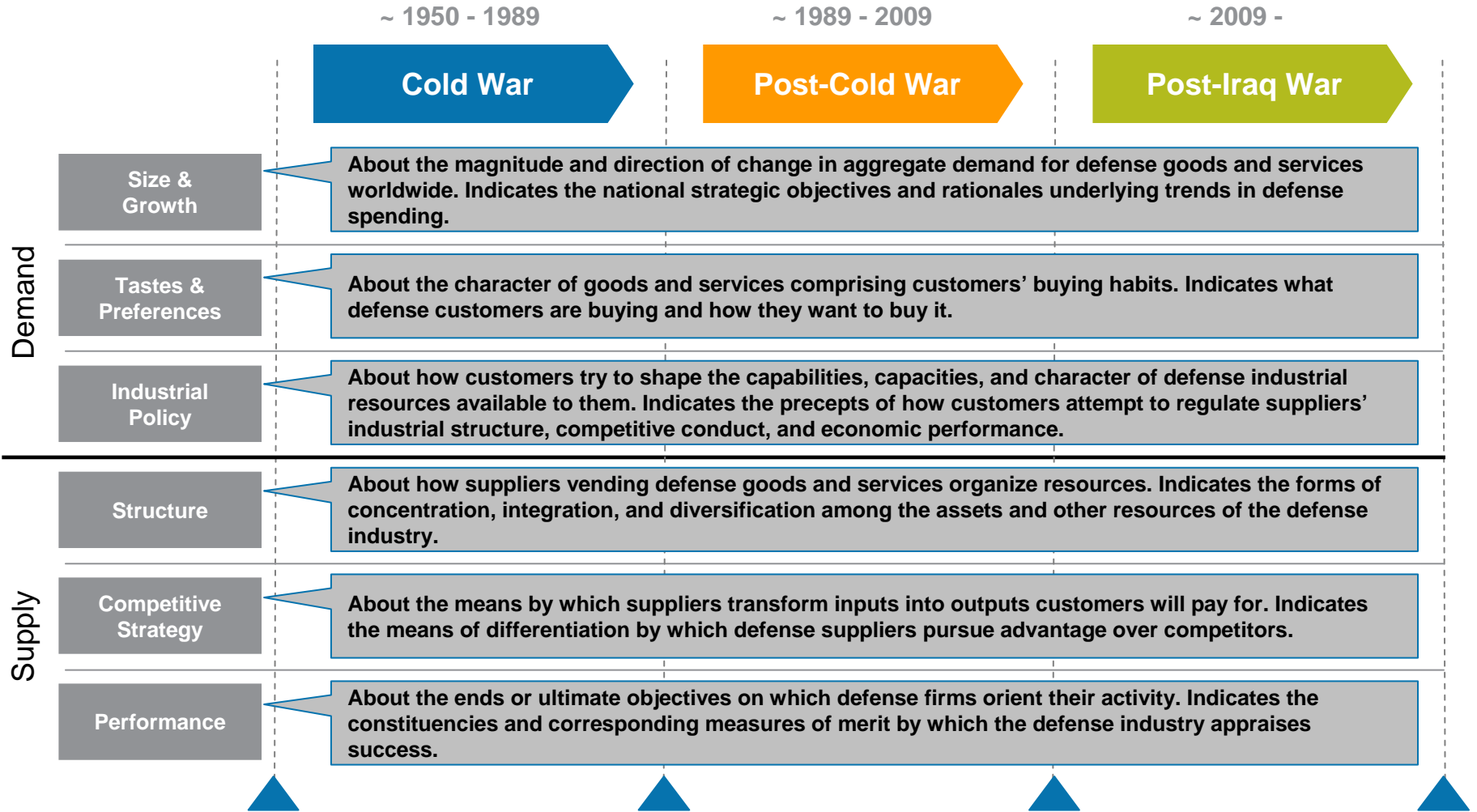
“Defense-21” Market: Overview

Inflection in the dynamics of the defense market in the 21st century is indicated by captions of the key drivers and iconic emblems of change over time



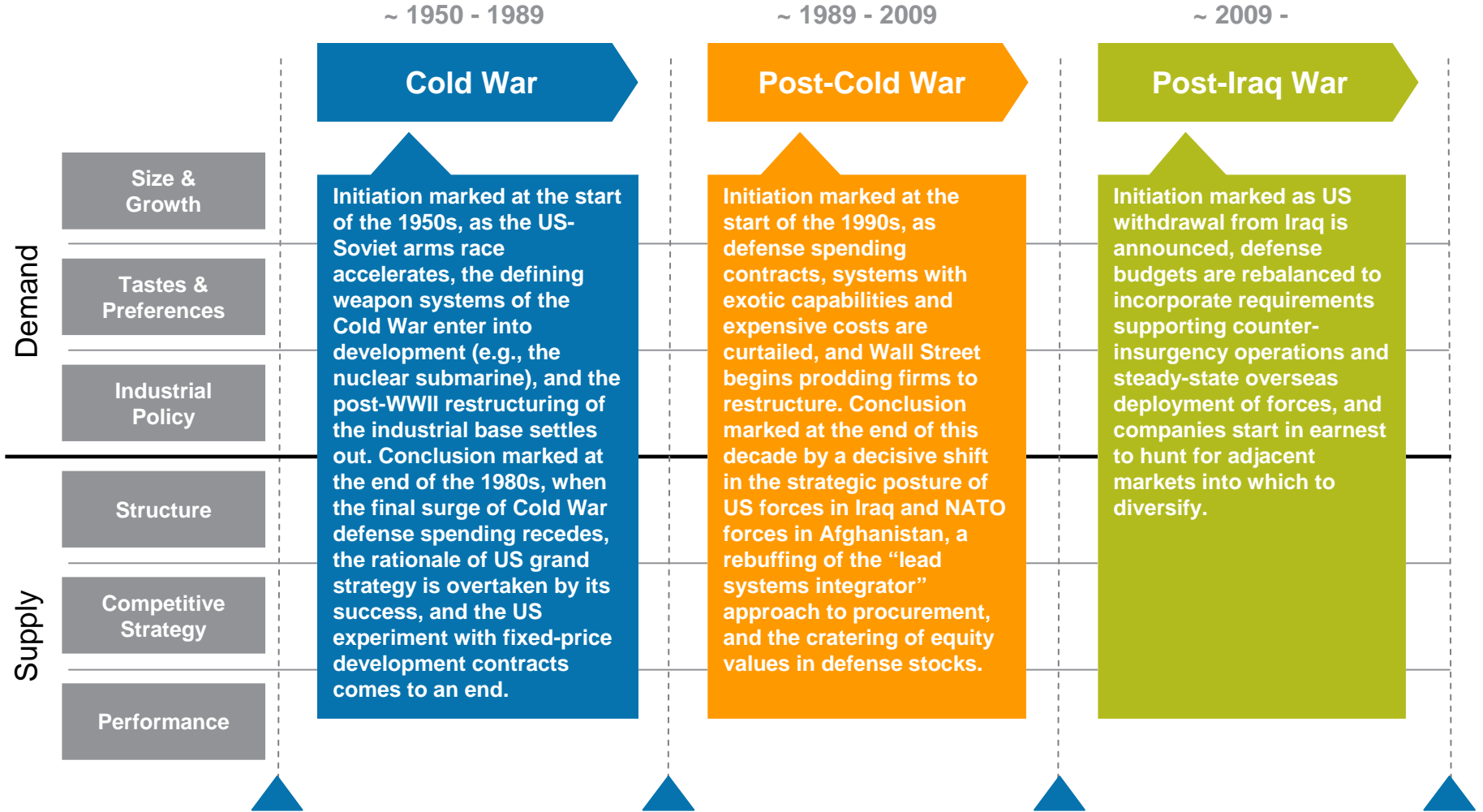
“Defense-21” Market: Dimensions of Demand and Supply

Three dimensions of demand and three of supply characterize the key drivers of change in the 21st century dynamics of the market



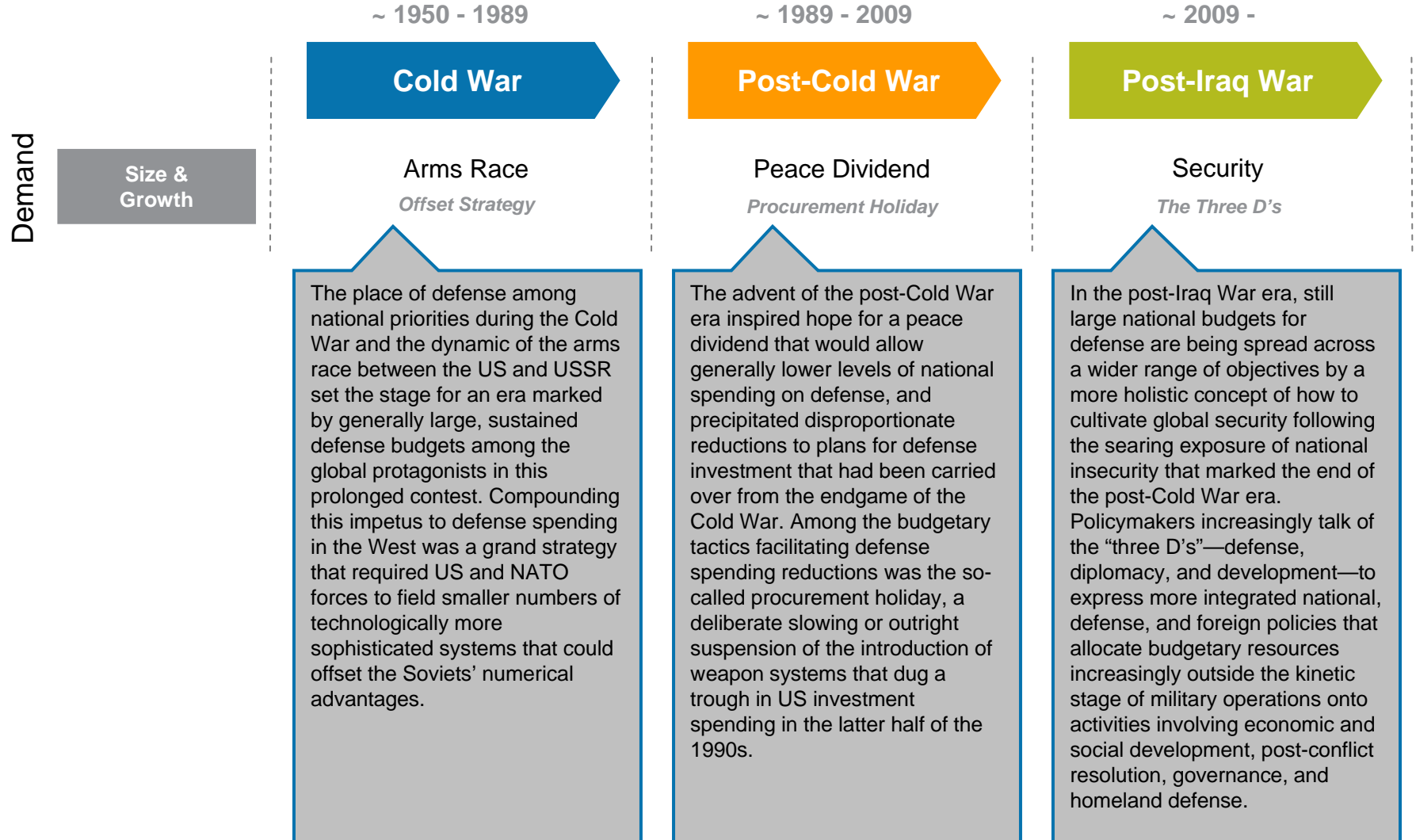
“Defense-21” Market: Historical Eras

Three historical eras, beginning with the onset of the Cold War and culminating in the contemporary, post-Iraq War era, mark the inflection of market dynamics



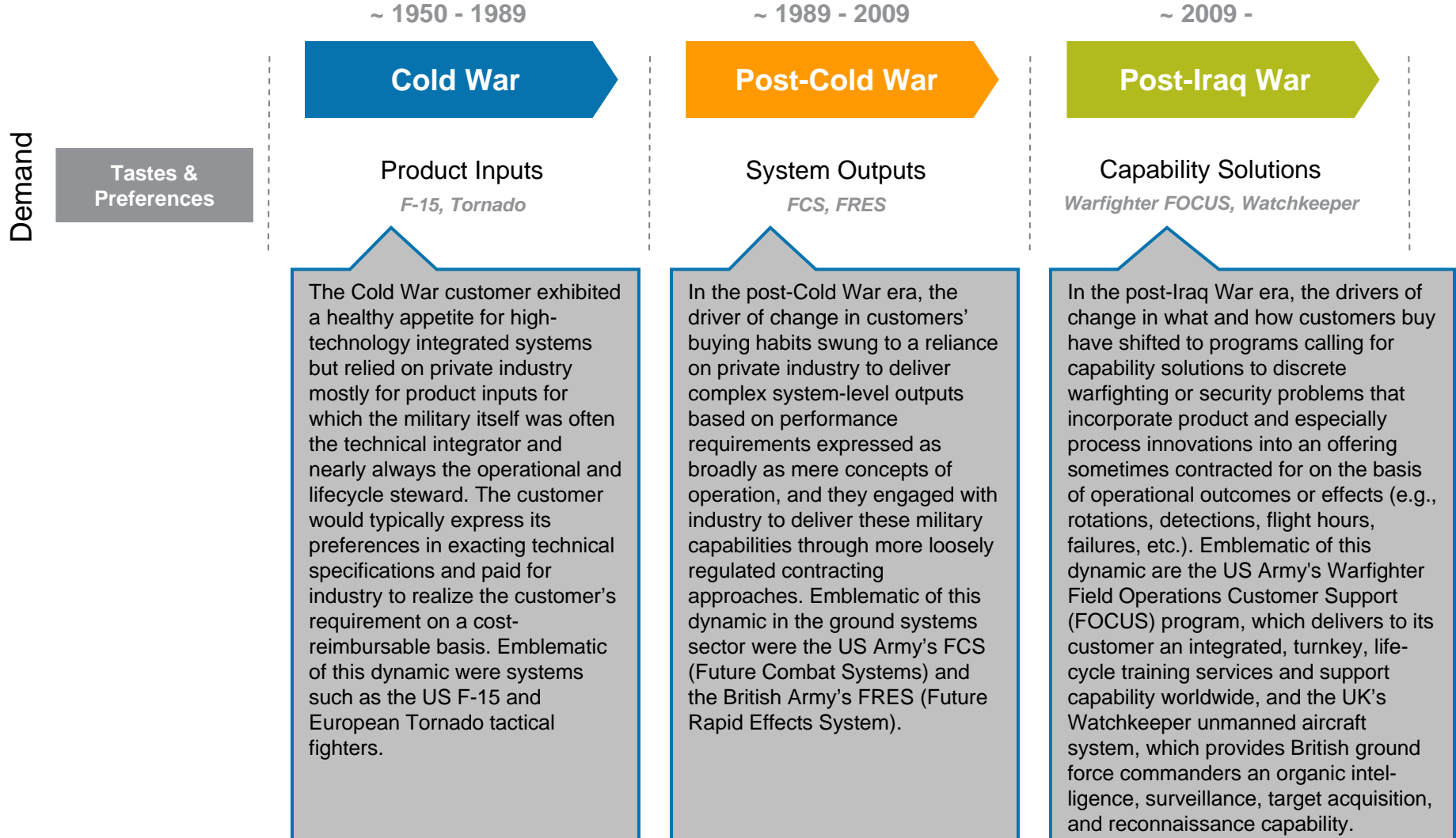
“Defense-21” Market Demand: Size & Growth

The end of high growth in the “kinetics” of defense will be somewhat offset by a more expansive concept of defense encompassing diplomacy and development



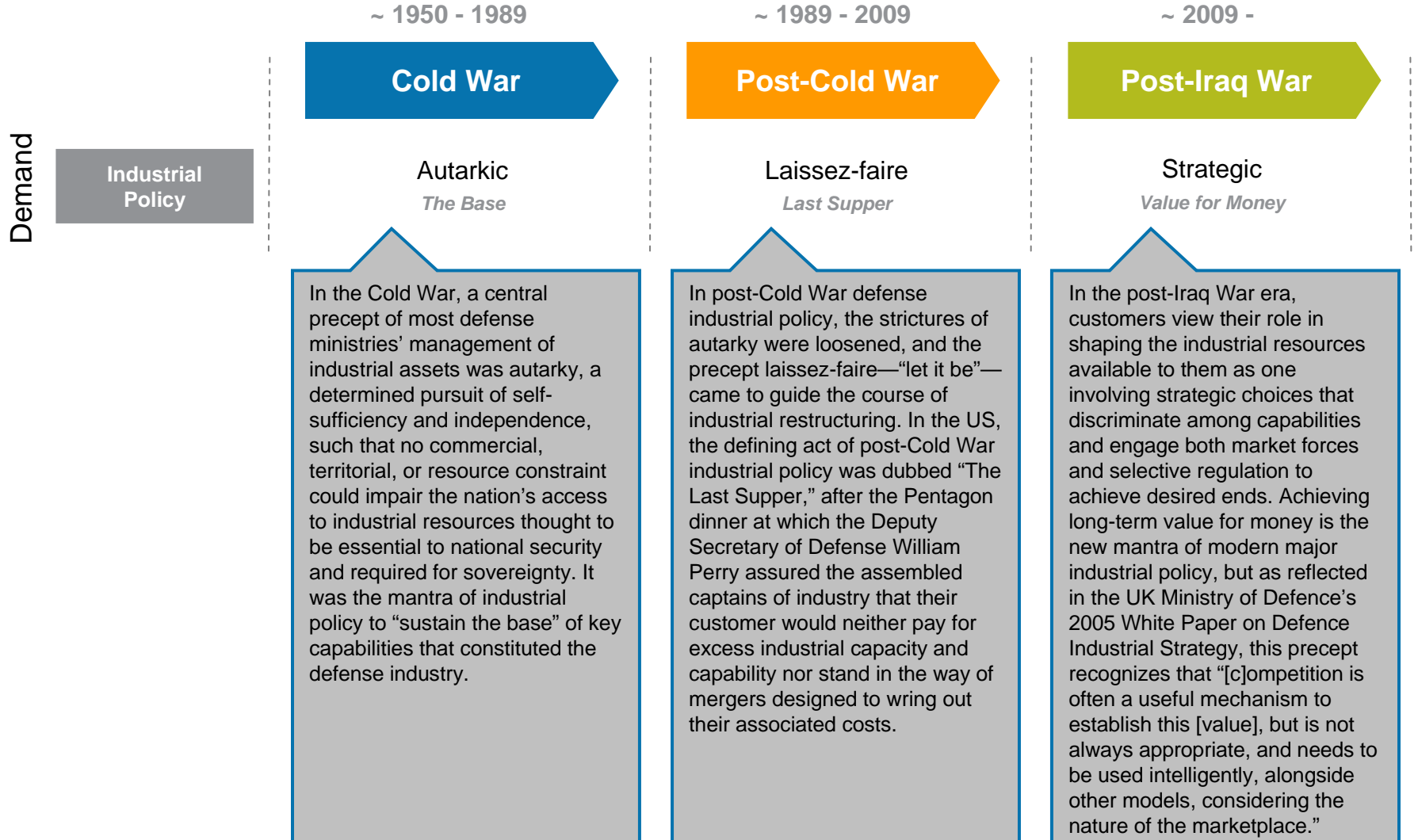
“Defense-21” Market Demand: Tastes & Preferences

Customers’ buying habits are shifting toward capability solutions that involve delivery of moderate-complexity products through large-scale services platforms



“Defense-21” Market Demand: Industrial Policy

Defense industrial policy will selectively forgo short-term expedience in order to protect strategic capabilities and capacities over the long-term



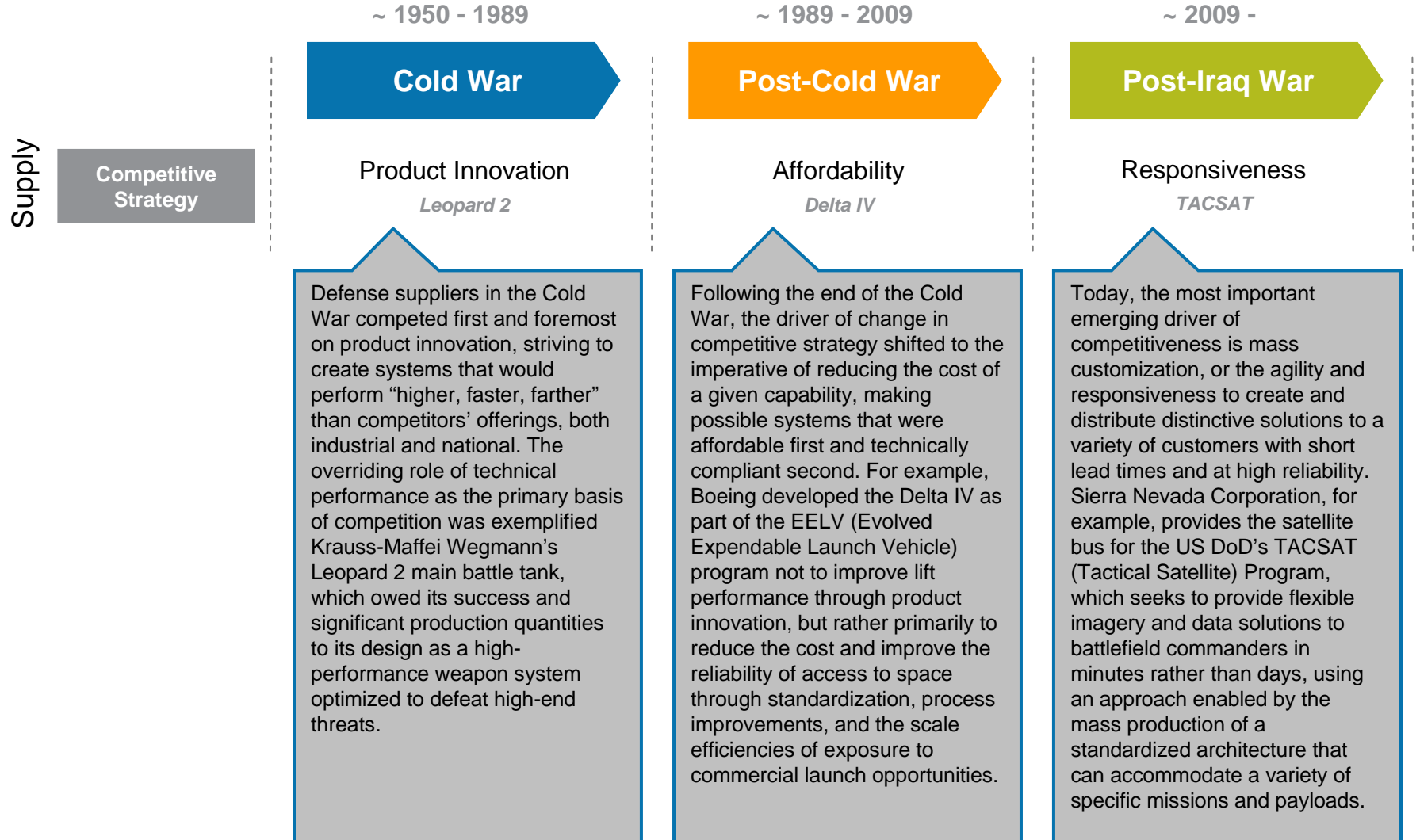
“Defense-21” Market Supply: Structure

The post-Iraq War inflection is marked by the emergence of an industrial structure that favors firms with a global footing and diversified market exposure



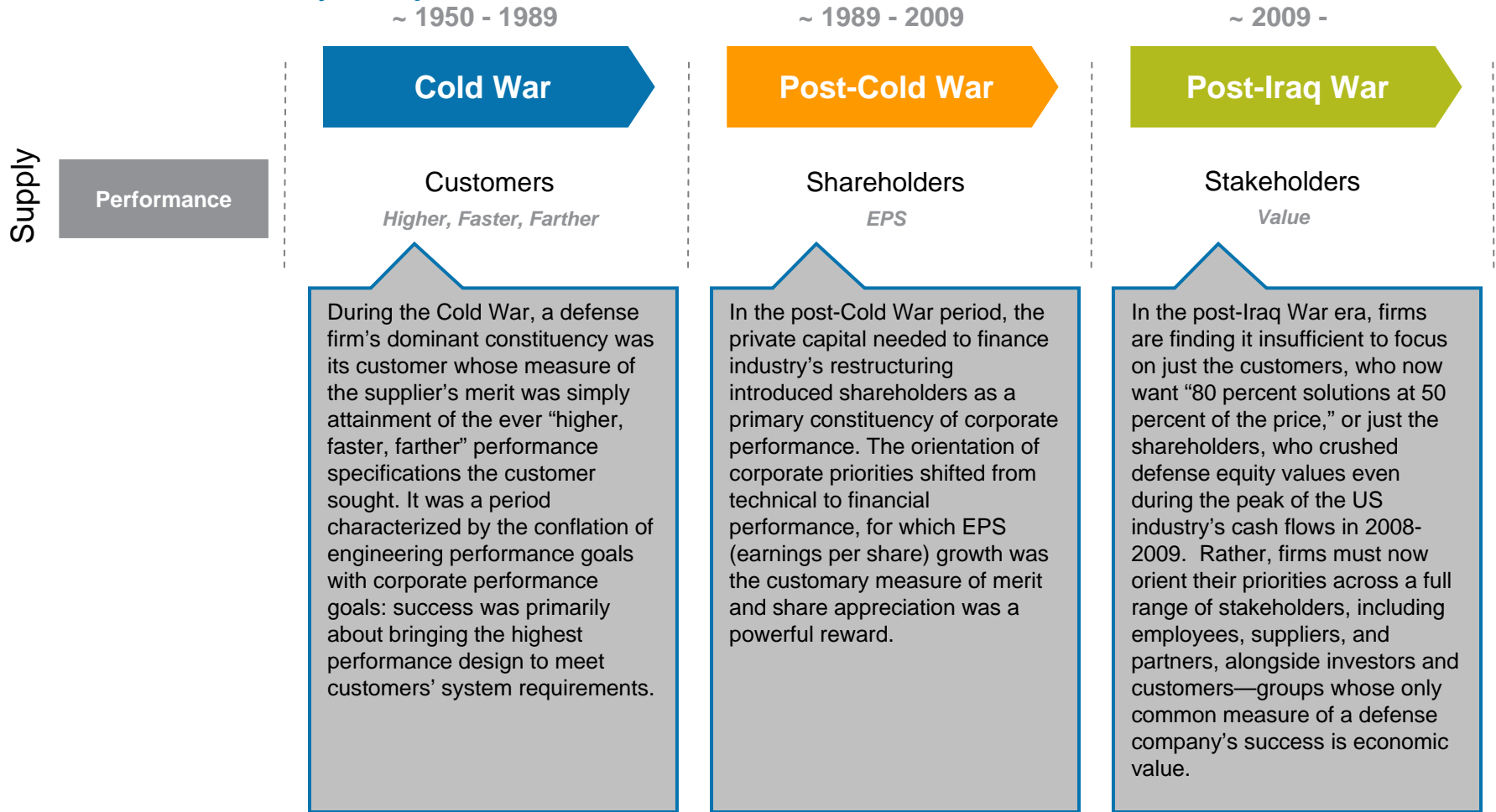
“Defense-21” Market Supply: Competitive Strategy

The change driving competitive advantage is responsiveness, a competence attracting entry from firms employing non-traditional business models



“Defense-21” Market Supply: Performance

Executives will need to focus on satisfying the interests of a still wider array of stakeholders beyond just customers and shareholders



“Defense-21”: Implications

The enterprise adjusts its strategic posture to changes in the environment by its choices about Participation, Offering, Proposition, and Structure

1 Participation

What customer markets do we address?

- By geography (local, regional, national, international, global)
- By economic sector (military, civil, state/local, commercial)
- By domain (sea, air, ground, space, cyber)
- By product (structures, propulsion, electronics, weapons, systems)
- By lifecycle (S&T, product development, production, support)

2 Offering

What do customers buy from us?

- Inputs (subsystems or labor)
- Outputs (a system or discrete service)
- Solutions (capability or outcomes)

3 Proposition

Why do customers buy from us?

- Best cost
- Most responsive
- Best performance
- Best value

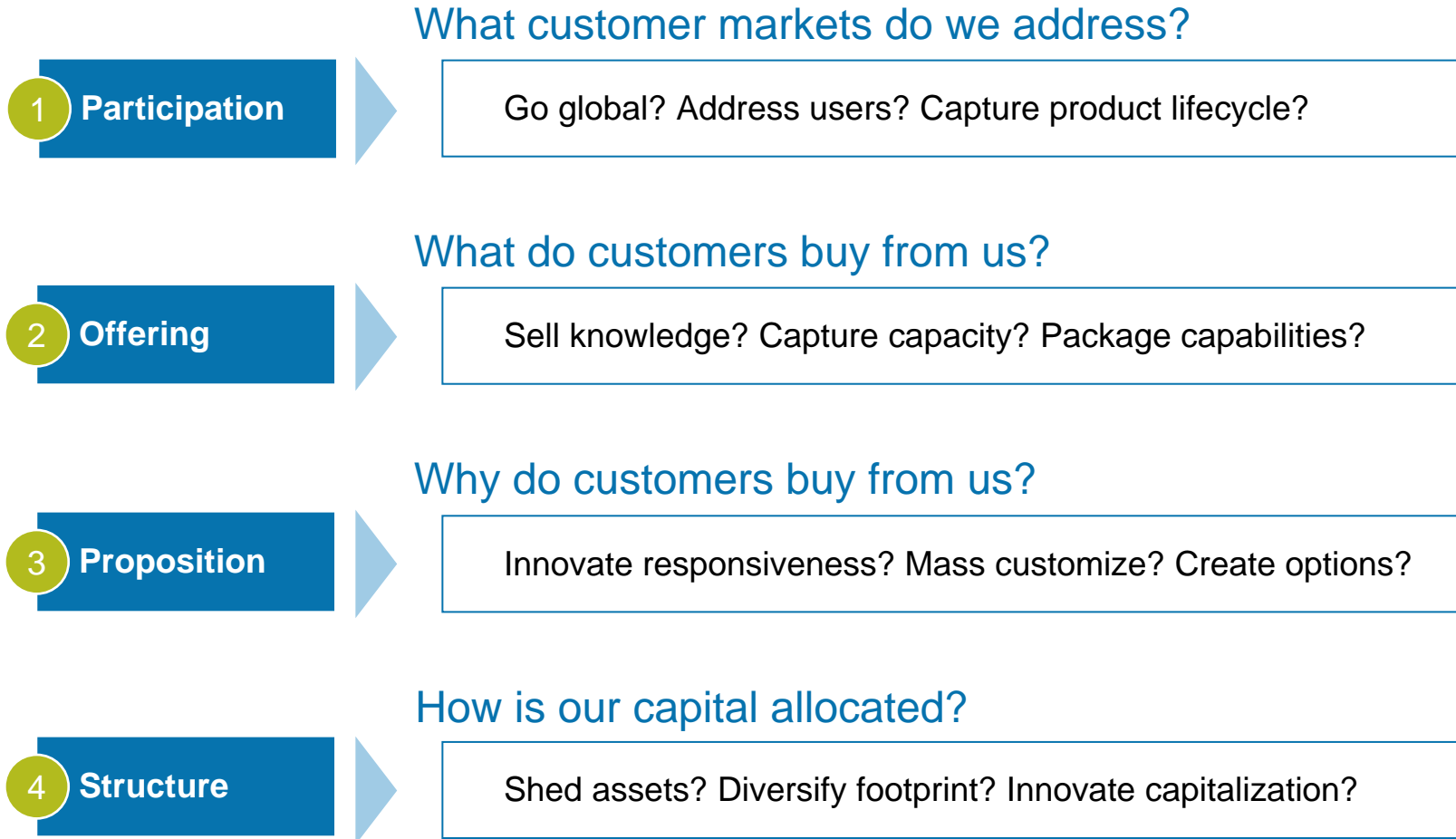
4 Structure

How is our capital allocated?

- Scale (concentration)
- Scope (diversification)
- Depth (integration)

“Defense-21”: Conclusion

The implications of these changes should prompt a reconsideration of the key tenets of strategic posture in defense companies





Steven Grundman

Vice President

Director, Aerospace & Defense Consulting

(617) 425-3168

sgrundman@crai.com