



The Three Big Questions of Defense-Industrial Strategy Commercial or military, autarkic or globalized, public or private?

What are the industrial base issues that need to be considered in any defense strategy? In this age of austerity in military spending, we are hearing calls for bolder policies that would break with past practice, rewarding companies for taking risks, and punishing those that fail. We hear assertions that defense ministries should think seriously about what capabilities they want to preserve as economic constraints force choices in future force structure, and, ultimately, strategy. We should applaud these efforts to highlight industrial considerations in formulating strategy, for the question remains fresh. But in thinking about formulating public policies in this area, I believe that an overarching framework is more important. I recommend orienting on three dimensions, each of which encompasses a spectrum of potential defense-industrial policies.

The first is **civil-military integration**, which concerns how much the industrial resources on which any defense ministry relies should be commingled with civil technologies and a commercial business base. Should military programs consciously draw on commercial ideas, or be deliberately nurtured in isolation? The trend since the end of the Cold War has been toward a closer integration of defense and commercial industrial resources. A pure 'hot-house' approach is nearly impractical today, after all. Still, military and commercial technologies do not always naturally commingle, so substantial issues remain about exactly how any defense ministry can encourage—or simply resist impeding—the integration of civil with military industrial resources.

For us, this broad issue points to several specific questions for today:

- Should the Pentagon be concerned that hardware-oriented defense companies are *dis-integrating* themselves from information technology businesses? I am thinking here of Northrop Grumman's sale of TASC, L-3's spinoff of Engility, and the breakup of SAIC.
- Would a more thorough integration of defense and commercial aerospace strengthen the defense-industrial base, and should public policy encourage or discourage it? For example, how important to the *defense* industrial base are commercial satellite communications, space launchers, business aircraft, and trucks?
- What, if any, are the implications of the dust-up over Palantir versus the Army's Digital Command Ground System?
- And drawing on the [speech](#) by Textron Systems CEO Ellen Lord at the Atlantic Council in January 2014, I wonder whether the Pentagon is better served by industrial resources that are commingled in multi-industry firms, such as United Technologies and General Electric, or pure-players, like Lockheed Martin?

Our second issue is **interdependence**, which concerns how autarkic or globalized a nation should be in sourcing its weapons. Over the past twenty years, a substantially globalized industry has emerged from a fragmented collection of largely national structures. Autarky is not only out of fashion, it is also infeasible for all but the largest nations, and even the United States has affirmed a strategy that positions its industry in the global marketplace. Yet there remain substantial issues about how to balance a national industry's interdependence with the concurrent need of attending that country's security and economic objectives. Other than in nuclear matters, should the United States, as a matter of policy, still cultivate any segments of the defense-industrial base on an autarkic basis?

Again, I think of specific questions:

- Looking back over more than a dozen years of corporate and public policy initiatives to draw the industrial resources of North America and Europe together, what has it achieved and what is to come?
- Looking ahead to an era of austere defense budgets in the West, US and European companies are going to rely more heavily for their growth and profitability on exports to emerging-market countries. Is US public policy ready to accommodate—or even encourage—these imperatives?
- How great is the threat that global sources of supply will compromise or sabotage Western military technology as more and more of the upstream components and assemblies in our systems originate overseas?

The third issue is **capitalization**, or how much a nation's defense-industrial resources rely on public or private investment. While government ownership of defense-industrial resources has generally decreased since the end of the Cold War, the pace and depth of that evolution varies from one nation to the next, and the question of how defense-industrial resources are capitalized remains deeply complex. Even in a market like the United States, which has very little modern tradition of state ownership, the determination of its capitalization position is complicated by the fact that the Defense Department routinely makes substantial capital investments in companies to develop its acquisition programs. It also maintains a large, government-owned industrial base of depot maintenance and munitions facilities. For most ministries, the practical issues about capitalization have less to do with whether the government should make debt or equity investments in defense companies than with whether and how to share with private investors the risks associated with new projects, and with the disposition of the military's legacy of industrial assets.

With respect to this issue, still more questions come to mind:

- Does the Pentagon's *Better Buying Power* policy signal a meaningful change in acquisition practices over the extent to which it will continue to bear the financial risk of investments in dual-use programs? Can contracting practices accommodate the need for higher return to companies that have themselves borne risk in development without substantial government funding?

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- Can we consider United Launch Alliance and the Electric Boat-Newport News submarine partnership indicators of an industrial policy that recognizes the need in certain mature sectors for regulated monopolies, operating like utilities?
 - Will government continue to own and operate an entire industrial base for equipment maintenance and munitions production into the 21st century?
 - Are there certain niches of the defense-industrial base for which public ownership is the most efficient capitalization?

Commercial or military, autarkic or globalized, public or private? Smart stewardship of defense-industrial resources means addressing these issues strategically, and not as an artifact of decisions made program-by-program.