

Guideposts of Defense Industry Change

By **Steven Grundman**

COMMENTARY

THE MESSY WITHDRAWAL OF U.S.

combat forces from Afghanistan heightens attention to the milestone that is this month's 20th anniversary of al-Qaida's attack on New York and Washington.

The events of Sept. 11, 2001, reshaped nearly every dimension of U.S. national security posture, including the defense industry. An industrial sector poised to spearhead then-Defense Secretary Donald Rumsfeld's "transformation" to dissuade the rise of a peer competitor was, after 9/11, refocused onto counterinsurgency, homeland security and nation-building. And while the end of Operation Iraqi Freedom in August 2010 might have allowed industry to slew its capabilities back to the agenda of peer competition, enactment in that very same month of the Budget Control Act of 2011 stunted for another decade the resources and managerial attention required to fully enact that strategy.

"WAVES OF CHANGE CAN SUDDENLY CULMINATE IN AN INFLECTION THAT DISRUPTS THE CAREFULLY CRAFTED STRATEGIC POSTURES OF COMPANIES AS WELL AS NATIONS."

With the Pentagon now free of the constraints of the Budget Control Act and focused squarely on peer competition in the Asia-Pacific region, corporate strategists should be trying to gain clarity about a profound change now building in the business of defense.

As Richard Rumelt, professor emeritus at the University of California-Los Angeles, observes in his book *Good Strategy/Bad Strategy*: "The challenge is not forecasting but understanding [that] . . . [o]ut of the myriad shifts and adjustments that occur each year, some are clues to the presence of a substantial wave of change and, once assembled into a pattern, point to the fundamental forces at work. The evidence lies in plain sight, waiting for you to read its deeper meanings."

But where to look for the evidence? Rumelt cites five guideposts to anticipating waves of industry-wide change, in three of which I recognize some forces already buffeting the defense industry.

RISING FIXED COSTS

The simplest indicator of an imminent transition is when fixed costs, especially product-development costs, begin rising rapidly, Rumelt contends. For example, the transition in aircraft propulsion from piston to jet engines in the late 1940s rapidly winnowed a multitude of players down to the three we know still today—GE, Pratt & Whitney and Rolls-Royce. The formation in 2020 of Raytheon Technologies is a leading indicator that sustained competitive advantage in

defense prime contracting now requires a super-size balance sheet to keep up with the product-development bets being made by companies with more than \$100 billion of enterprise value or deep-pocketed investors backing them.

GOVERNMENT POLICY

A transition instigated by changes in government policy, especially deregulation, is a second guidepost that is also apparent today. Rumelt references the deregulation of air transport beginning in the late 1970s, which brought intense price competition to an airline industry accustomed to differentiating on service. Current Pentagon acquisition strategies are aiming to separate development from production, which would fundamentally challenge the business model on which prime contracting is staked. The best known example of this is former Air Force acquisition executive Will Roper's concept for developing and building a "Century Series" gen-



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eration of air dominance fighters. But no less an encrusted acquisition system than the U.S. Army's has revamped its thrice-canceled program to replace the Bradley M-2 with an acquisition strategy that envisions a fresh open competition, rather than a downselect, at each phase of the program's development.

ATTRACTOR STATE

A third guidepost in view today concerns what Rumelt calls the attractor state, which "describes how the industry 'should' work . . . [to meet] the needs and demands of buyers as efficiently as possible." To illustrate the power of an attractor state, Rumelt recounts the late-1990s rise of Cisco Systems to dominance in internetworking by its response to customers' demand for "IP everywhere," a standard that rendered incumbents' proprietary networks obsolete. Vice Chairman of the Joint Chiefs of Staff Gen. John Hyten's oft-cited expectations for Joint All-Domain Command and Control (JADC2) is the defense customer's articulation of an attractor state for battle-management networking if there ever was one.

This month's Afghanistan milestone should serve as a timely reminder of how waves of change can suddenly culminate in an inflection that disrupts the carefully crafted strategic postures of companies as well as nations.

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