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Key Takeaways From the Pentagon's National Defense Industrial Strategy

On January 11, the Department of Defense (DoD) released its first-ever National Defense Industrial Strategy (NDIS). The NDIS offers “a strategic vision to coordinate and prioritize actions to build a modernized defense industrial ecosystem that is fully aligned” with the National Defense Strategy. The NDIS emphasizes four long-term strategic priorities: (i) building resilient supply chains, (ii) securing workforce readiness, (iii) enabling flexible acquisition, and (iv) promoting economic deterrence.

Part I of this Client Alert provides a summary of the key actions identified by the DoD as necessary in order to achieve those strategic priorities. Part II puts those actions in context, highlighting the areas likely to be of most interest to industry participants.

Part I: Summary of Strategic Priorities Identified by the NDIS

1. Building Resilient Supply Chains

Priority Defined: *The ability to securely produce the products, services, and technologies needed now and in the future, at speed, at scale, and at cost. Resilient supply chains are those able to withstand, fight through, and recover quickly from disruption.*

Core Topics and Actions Identified:

Capacity	<ul style="list-style-type: none"> ▪ Incentivize industry to improve resilience by investing in extra capacity ▪ Establish public-private partnerships, risk-sharing mechanisms, and technology-sharing structures to jointly fund and develop spare production capacity
Inventory	<ul style="list-style-type: none"> ▪ Manage inventory and stockpile planning to decrease near-term risk <ul style="list-style-type: none"> > <i>DoD's stockpiles act as shock absorbers for the supply chain, insulating it from unexpected demand spikes and disruption. The war in Ukraine has spotlighted gaps in national stockpiles and has underscored the challenges inherent in replenishing them.</i>
Domestic Production	<ul style="list-style-type: none"> ▪ Continue and expand support for domestic production and promote accelerator programs to foster innovation ▪ Deploy innovative funding mechanisms to revitalize the network of government-owned industrial facilities for the production and sustainment of equipment where manufacturing by the private sector is not economical
Supplier Base	<ul style="list-style-type: none"> ▪ Diversify the supplier base through expanding its relationships with companies and industries that are not traditionally part of the defense ecosystem; mitigate barriers to entry, including cybersecurity costs <ul style="list-style-type: none"> > <i>NDIS notes that the DIU's efforts have been particularly successful in fostering collaboration between established contractors and nontraditional companies to accelerate the development and production of emerging technologies</i>
Supply Chain Visibility	<ul style="list-style-type: none"> ▪ Leverage data analytics to (i) improve sub-tier supply chain visibility, (ii) identify and minimize strategic supply chain risks, and (iii) manage disruptions proactively <ul style="list-style-type: none"> > <i>NDIS acknowledges that, as the defense supply chain has become more global, prime contractors have increasingly lost sight of their own sub-tier supply chains and face a growing risk of sourcing resources from potential adversaries</i>
Production Diplomacy	<ul style="list-style-type: none"> ▪ Engage allies and partners to expand global defense production and increase supply chain resilience <ul style="list-style-type: none"> > <i>NDIS cites U.S.-led international initiatives to expand ammunition production in response to Russia's invasion of Ukraine as an example of effective production diplomacy</i>
Foreign Military Sales	<ul style="list-style-type: none"> ▪ Take steps to improve the Foreign Military Sales (FMS) process <ul style="list-style-type: none"> > <i>Close coordination with allies and partners is a central premise of the U.S. National Defense Strategy – to this end, NDIS indicates an intent to accelerate the responsiveness of the FMS system to better meet the global capability requirements of U.S. allies</i>
Cybersecurity	<ul style="list-style-type: none"> ▪ Take steps to enhance industrial cybersecurity <ul style="list-style-type: none"> > <i>This effort will be guided by the DoD Cyber Strategy (released September 2023)</i>

2. Securing Workforce Readiness

Priority Defined: *Building a skilled and sufficiently staffed workforce that is diverse and representative of America. Today's labor market lacks sufficient workers with the right skills to meet domestic production and sustainment demand, directly impacting military readiness.*

Core Topics and Actions Identified:

<p>Skills Adaptability</p>	<ul style="list-style-type: none"> ▪ Prepare the workforce for technological change through upskilling and re-skilling programs <ul style="list-style-type: none"> > <i>NDIS cites workforce requirements of nuclear submarine production as an example of one of the most acute skill shortages facing the defense industrial base today; an adaptable workforce should have re-skilling programs and adequate incentives in place to address that shortage</i>
<p>Skills Applicability</p>	<ul style="list-style-type: none"> ▪ Continue to invest in institutions and programs that address current and forecasted skills gaps in defense-related manufacturing and STEM jobs <ul style="list-style-type: none"> > <i>NDIS cites Manufacturing USA (MFG USA) as an example of effective collaboration between DoD and private sector companies, universities, community colleges, and other educational groups</i>
<p>Training Access</p>	<ul style="list-style-type: none"> ▪ Increase access to apprenticeship and internship programs <ul style="list-style-type: none"> > <i>NDIS cites the Naval Fleet Readiness Center as an example of an on-the-job training and apprenticeship program that develops highly skilled, Navy-oriented, U.S. Department of Labor-certified workers</i>
<p>Narrative</p>	<ul style="list-style-type: none"> ▪ Reframe the narrative around industrial careers, including by partnering with high schools and higher education to challenge the stigma associated with trade occupations <ul style="list-style-type: none"> > <i>NDIS cites initiatives by AIM Photonics to partner with colleges to offer an Advanced Manufacturing & Integrated Photonics Technician Certificate program</i>
<p>Workforce Breadth</p>	<ul style="list-style-type: none"> ▪ Expand the scope of recruiting efforts, with a particular focus on communities that are underrepresented in the industrial workforce today <ul style="list-style-type: none"> > <i>NDIS cites DoD's engagement with Historically Black Colleges and Universities as a positive step in investing in enhanced workforce breadth</i>



3. Enabling Flexible Acquisition

Priority Defined: Acquisition strategies that achieve dynamic capabilities, while balancing (i) efficiency, (ii) maintainability, (iii) customization, and (iv) standardization across defense platforms and support systems. Successful acquisition strategies should result in reduced development times, reduced costs, and increased scalability. Properly executed, flexible acquisition will allow DoD to scale production of priority assets quickly and adjust the production mix to achieve and maintain an enduring advantage during conflict.

Core Topics and Actions Identified:

Interoperability	<ul style="list-style-type: none"> ▪ Promote open architecture and adopt industry standards and incentives for interoperability and exportability; consider exportability <i>during</i> system design rather than post-production <ul style="list-style-type: none"> > <i>Interoperability serves both to strengthen ties with allies and partners, and to reduce barriers to non-traditional suppliers by simplifying product development and integration, making it functionally easier and less expensive for these suppliers to participate in the defense ecosystem</i>
Managed Scope	<ul style="list-style-type: none"> ▪ Strengthen requirements process to curb “scope creep” ▪ Implement policies aimed at incremental development and virtual modeling methodologies with fewer physical prototypes <ul style="list-style-type: none"> > <i>Process should focus on ensuring that proper engineering analysis is conducted, and resource trade-offs are made, before programs enter their manufacturing phases</i>
COTS Technology	<ul style="list-style-type: none"> ▪ Embrace commercial-off-the-shelf (COTS) solutions where appropriate <ul style="list-style-type: none"> > <i>COTS can drive faster procurement cycles, accelerate the pace of innovation, deliver better cost-effectiveness, and provide a natural avenue for expansion of the supplier base</i>
IP Access	<ul style="list-style-type: none"> ▪ Use modular open systems approaches (MOSA) and mitigate IP restrictions on proprietary components by negotiating specialized license agreements <ul style="list-style-type: none"> > <i>For example, the open architecture of Bell-Textron’s V-280 Valor has been credited in playing a role with the company’s successful FLRAA bid</i>
Contracting Strategies	<ul style="list-style-type: none"> ▪ Work with Congress to modify contract authorities to align with present defense production priorities; seek contract types that enable rapid and iterative delivery of capabilities <ul style="list-style-type: none"> > <i>The SDA’s Proliferated Warfighter Space Architecture is one example of this; Replicator, depending on its implementation, may be another</i>
Acquisition Reform	<ul style="list-style-type: none"> ▪ Orient DoD’s acquisition policy for aggressive expansion of production capacity <ul style="list-style-type: none"> > <i>Increased use of multiyear procurement (MYP) should be used to create sustained demand signals that will promote investment into the capacity of the industrial base</i>
Regulatory Framework	<ul style="list-style-type: none"> ▪ Lay the groundwork for legal and regulatory conditions <i>today</i> to ensure proper mobilization authorities in the future <ul style="list-style-type: none"> > <i>‘Mobilization authorities’ refer to the legal and regulatory mechanisms that enable the U.S. to rapidly expand, reconfigure, and draw upon the defense industrial ecosystem in times of crisis</i>

4. Promoting Economic Deterrence

Priority Defined: *Fair and effective market mechanisms that support a resilient defense industrial ecosystem among the U.S. and close international allies and partners and contribute to economic security and integrated deterrence. Credible threat of reduced access to U.S. markets, technologies, and innovations will inform the cost-benefit calculus of potential aggressors.*

Core Topics and Actions Identified:

<p>Formal Economic Security Agreements</p>	<ul style="list-style-type: none"> ▪ Work with other federal executive departments to ensure the maintenance of economic and national security alliances <ul style="list-style-type: none"> > <i>Efforts should focus on leveraging existing bilateral and multilateral relationships, such as NATO, AUKUS, and the NTIB, and on sourcing from countries that are geopolitical allies (“friend-shoring”) to reduce reliance on potentially adversarial or unstable nations for critical defense and strategic materials.</i>
<p>Interoperability Standards</p>	<ul style="list-style-type: none"> ▪ Work in concert with the State Department and the Department of Commerce to promote interoperability standards between U.S. forces and those of our allies and partners, with the goal of making systems modular, upgradable, and maintainable by vendors and entities other than the original manufacturer <ul style="list-style-type: none"> > <i>Interoperability among allies and partners also increases FMS opportunities.</i>
<p>Technology Alliances</p>	<ul style="list-style-type: none"> ▪ Work with other federal executive departments and with Congress to generate new mechanisms for sharing technologies and applications with our allies and partners
<p>Enforcement</p>	<ul style="list-style-type: none"> ▪ Work with applicable agencies to strengthen enforcement against (i) adversarial ownership (i.e., protecting critical U.S. assets from ownership by commercial entities controlled by adversarial nations) and (ii) cyber attacks against entities involved in the maintenance of our national defense
<p>Supply Chain Visibility</p>	<ul style="list-style-type: none"> ▪ Work to ensure that the materiel required for national defense is not sourced from adversaries <ul style="list-style-type: none"> > <i>This topic runs parallel to the NDIS’ discussion on upstream visibility in support of its ‘Resilient Supply Chains’ pillar – while the discussion on upstream visibility in the context of supply chain resilience focused primarily on leveraging data analytics more effectively, the actions raised in the context of ‘Economic Deterrence’ focus on regulatory levers and strengthening America’s prohibited sourcing policy</i>



Part II: Takeaways for Industry Participants

The NDIS joins other strategic planning-focused policy documents from the DoD, including the National Security Strategy, the National Defense Strategy, the Nuclear Posture Review, and the Missile Defense Review. While the NDIS articulates a thorough strategic vision for the American defense industrial base, standing alone it offers little in the way of concrete guidance to industry participants. In a January press briefing introducing the NDIS, Assistant Secretary of Defense Laura Taylor-Kale stated:

“We are finalizing a detailed classified implementation plan with near-term, measurable actions and metrics to gauge progress. [...] While the detailed implementation plan will be classified, I commit to publishing, in the coming months, an unclassified overview of the implementation plan.”

Our team looks forward to reviewing the unclassified overview of the implementation plan when it becomes available. Until then, Part II of this Client Alert aims to help bridge the gap between vision and execution by putting the NDIS in context and providing industry participants with actionable insights on some of its key themes.

Several recurring concepts underpin the NDIS as a whole and arise repeatedly across the document’s four core strategic priorities. Among these are: (i) enhanced cooperation with U.S. allies and partners, (ii) increased emphasis on commercial technologies and nontraditional suppliers, and (iii) an emphasis on remedying – or at least acknowledging – some of the challenges faced by small- and medium-sized contractors.

1. The Role of Allies and Partners

Few themes receive more attention than the positive role that U.S. allies and partners can play in successfully executing on the strategic vision outlined in the NDIS. Variations of the phrase “allies and partners” appear 66 times in the 59-page document. Of the four long-term strategic priorities identified in the NDIS, three rely extensively on cooperation with U.S. allies and partners. Streamlining the FMS process and effectively leveraging “production diplomacy” are key levers in the NDIS framework for building **Resilient Supply Chains**. An emphasis on interoperability and designing for export are central to the framework’s **Flexible Acquisition** pillar. Platform interoperability again arises in the context of the strategy’s **Economic Deterrence** pillar, alongside discussion on ‘friend-shoring’ and sharing key technologies.

In a sector historically defined by domestic or regional champions and regulatory skepticism of cross-border transactions, the NDIS’ emphasis on fostering a *global* industrial base suggests a positive step towards encouraging more cross-border M&A, joint venture, and strategic partnership activity. This is a particularly welcome signal for smaller suppliers that stand to benefit most from economies of scale, market access, and manufacturing muscle on both sides of the Atlantic. Agreements like AUKUS, as well as recent transatlantic collaboration on JVs for munitions manufacturing in support of Ukraine, are encouraging developments.

2. The Role of Non-Traditional Suppliers and Commercial Technology

The NDIS similarly emphasizes DoD’s embrace of a broader supplier ecosystem, signaling opportunity for manufacturing and technology companies that have not historically done business with the Pentagon. In its discussion on **Resilient Supply Chains**, the NDIS explicitly advocates for promoting accelerator programs, mitigating barriers to entry, and expanding its relationships with companies and industries that have not traditionally been part of the defense ecosystem. The actions called for in support of enabling **Flexible Acquisition** touch on similar themes, with the NDIS explicitly emphasizing the cost-effectiveness of COTS solutions and the importance of rapid, iterative development and deployment of capabilities.

From the perspective of industry participants, DoD’s growing comfort with leveraging commercial solutions and trusting non-traditional partners will continue to create new opportunities for companies both inside and outside of the defense ecosystem today. For defense-oriented companies exploring a potential sale or capital raise, DoD’s evolving posture is likely to open the aperture of potential acquirors and investors, as barriers that have historically been associated with doing business with the Pentagon become easier to navigate. While concrete demand signals from the Pentagon will ultimately be required to drive investment, the NDIS sets the right tone and lays the groundwork for improving collaboration between Silicon Valley, the traditional defense industrial base, and investors.

3. Recognition of Disproportionate Challenges Faced by Small and Medium-Sized Contractors

The NDIS identifies several systemic challenges that DoD must overcome in order to execute on its vision of supporting a more agile and robust defense industrial base. While some of these challenges are global in scope (e.g., combatting adversaries' anticompetitive trade practices and shoring up global supply chains), others are directly related to the immediate hurdles faced by small- and medium-sized businesses seeking to contribute to the American defense ecosystem. These include:

- **Fragility of the Supplier Ecosystem:** The NDIS acknowledges that sub-tier suppliers often operate on narrower margins, making them more susceptible to cyclic demand and shifts in defense budgets. This affects their ability to remain in the defense market, with potentially outsized downstream consequences for defense industrial capacity.
- **DoD's Position as a Monopsony Buyer:** The NDIS further acknowledges the fact that low-volume buying patterns, lengthy periods between modernization, and over-customized design specifications have combined to make DoD an unattractive customer. This is especially true for prospective new entrants that lack the infrastructure and experience of more traditional defense primes. The issues articulated here echo some of the challenges set forth in DoD's Small Business Strategy (released January 2023).
- **Absence of Predictable Demand Signals:** Budget uncertainty, fiscal year spending constraints, and political factors have adversely impacted DoD's ability to provide clear demand signals. Continuing resolutions compound on these challenges by prohibiting new program starts and disrupting recruiting. Industry will follow the demand signals that flow from specific resource allocations, and – despite encouraging rhetoric – to date these demand signals have been limited.

While each of these challenges in theory applies to large primes in equal measure, small businesses are particularly vulnerable when it comes to having cash on hand to cover operating expenses in a constrained budgetary environment. They generally have a higher cost of capital than their larger counterparts and do not have the same opportunities to raise capital quickly to navigate unexpected pauses in contract funding arising from budgetary constraints. Although the NDIS does not advocate for broad acquisition reform or new legislation, DoD's explicit recognition of these challenges in the NDIS is a positive step for innovative, growth-stage companies seeking to enter the defense ecosystem.





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