Defense Conversion, Myth or Mystery?

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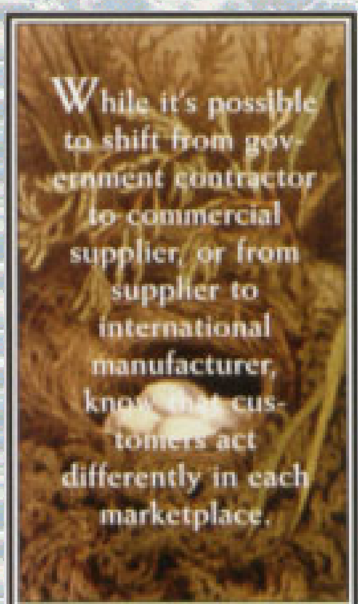

Defense Conversion, Myth or Mystery? ***Text***
By John M. Collard

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John M. Collard

THE transitions from a defense-oriented to a peacetime economy, and from regional to worldwide trade are forcing basic changes in commercial and public sectors. These changes are generating intense "battles" for those who want to increase payoffs by using better management practices. Unlike war battles; however, which can be won by brute force, these can be won only by sure-minded approaches.

During the last decade, defense-oriented businesses flourished. Many did so even while using unsound business principles. The Pentagon spent 60 cents of every dollar in the Mid-Atlantic, the Northeast, and the West, but the days of high defense spending are over; the days of defense conversion are here. By 1997, conversion will have touched some 2.6 million people and companies. The combined effect of reduced defense spending and the increased need to convert defense-oriented business to other markets has forced most companies to adjust.

While it's possible to shift from government contractor to commercial supplier, or from supplier to international manufacturer, it's important to be aware that customers respond differently in each marketplace. Their motivation and timing are different from what you might be used to. You may not be able to penetrate new markets unless you understand this first. Trying to generate sales in new markets with old strategies may not work.

In federal competitive procurements, the trend is toward commodity-based solutions. Where personnel are part of that solution, the trend is toward lower fees. If your marketing efforts are geared to building relationships first, your competition will have the contract while you're still warming up to the procurement officer. In this market, you'll have to think about pricing to win, then work aggressively later to cut costs or negotiate adjustments.

On the other hand, commercial buyers look for cost-effective (usually, fixed-price) solutions that operate in, and complement existing investments. Internationally, environments are "productized," but the bottom line is who you know, or don't know, that counts.

Typically, you may find yourself steering your company into one of three major markets. To enter them, you'll have to posture your company differently in each to win business.

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The Federal Market

Two markets are open in the government contracting sector. There are government set-asides, targeted primarily for small and disadvantaged businesses. Here, the government buys from a qualified seller. Set-aside programs are limited to those who can participate. The key is to get there first. In this market, you'll find constantly-changing players, all of whom vying for contracts ranging from $10,000 to $10 million. This market is somewhat easy to enter since the government introduced the "up-to-5-percentminority" set-aside program for federal procurements.

Larger federal contracts are obtained through competitive bids. This is a highly-structured process. Competition is scattered among major manufacturers and service providers, established systems integrators, and even small businesses. Moreover, this market has a second tier of competitors: subcontractors who "bundle" services to win contracts and become part of larger teams.

The low bidder always wins in this market, but the low bidder may not always have the lowest price. Today, contracts go to the "lowest evaluated bidder," or one who offers the most value for the price. Plan for long lead times, reams of paperwork, and rock-bottom pricing in the somewhat flat new acquisitions market. Businesses go fishing for deals in this market in ranges of $5 million to $100+ million to $1 billion.

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The Commercial Market

Most businesses look to the economically unrestrained commercial marketplace for new opportunities. But here, sellers approach buyers at will and are subject to their whims. While profits are usually higher and relationships ensure future stability for service-oriented companies, buyers are fickle. You may have what the buyer needs, but he may decide he doesn't like your tie. Also, a competitor may have a similar, yet inferior product, but because he has had the potential buyer on the golf course for the past three weekends and has talked about everything except the product, that product looks better to the buyer. Good relationships mean everything in this market, although they are maintenance intensive. The commercial market has project- and results-oriented customers. Performance under pressure is the key to survival.

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The International Market

While the U.S. welcomes foreign competition, some countries limit entry. Their tactics often range from burdensome import duties and competition-limiting treaties, to competing against local government-subsidized bids. And, don't be surprised at paying "entry" fees through a power structure that includes a distributor who may be controlled by the King's nephew.

Perhaps the best way to penetrate the international market is through a local presence. Countries like to keep their currency local and limit the export of profits. They favor companies that invest in their economy. Ford and Honda proved this point with their worldwide plants. Still, entering this market can be done from afar, particularly by demonstrated willingness to learn or adapt to new cultural and business practices, plus legal and financing mechanisms. Use local contacts and enter into joint ventures to develop proposals and/or technologies and transfer the latter as well.

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What Does It Take?

What does it take to win business in new markets? In set-aside contracting, the work must be done by a small, disadvantaged business. While the government procurement cycle is structured to be fair to all, the commercial market is driven by solutions, products, and services that fill needs in a specific time frame. Foreign buyers are commercial in nature, yet they favor their own suppliers, unless what they need can only be bought abroad. They may go outside their own borders for a short time seeking technology transfers because many technologies can be replicated.

Do your homework before you head for the boardroom. Determine first whether your company has the skills, services, or products that are, or could be, in demand in foreign markets. Precisely identify the potential new markets, and from them, identify the one or two that hold the highest potential for success. Finally, take a rifle shot approach at your new-found customer. If you've learned the characteristics and adapted to the business-style of your target market, the chances are you'll hit your mark. But always aim well. You seldom get a second chance. Know your strengths and exploit your competition's weaknesses. Do your products and services beat the competition in terms of technology, design, or cost? you'll also be limited by the size of your company's resources; therefore, tackle only one or two market niches at a time.

Above all, throw assumptions out and watch for subtle nuances — new markets bring new personalities, customs, and business traditions to the table — and create and welcome opportunities to demonstrate your willingness to adapt.

But remember, too, when you reach for new business, protect as well the market share you've already earned. In the battle for new opportunities, new sales, and higher income, your competition is waiting for you to leave this flank exposed.

John M. Collard is president of Strategic Management Partners, Inc., Annapolis, MD, and is a Certified Turnaround Professional. His firm specializes in valuation enhancement, corporate renewal, defense conversion, strategic repositioning, transition management, and equity capital investing. He is past chairman of The Turnaround Management Association, an advisor to President Clinton's National Economic Council, President Yeltsin's Bankruptcy Law Reform Delegation, World Bank, EBRD, investor groups and business leaders around the world.

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Contact Information

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John M. Collard, Chairman
Strategic Management Partners, Inc.
522 Horn Point Drive
Annapolis, Maryland [MD] 21403
Voice 410-263-9100 Facsimile 410-263-6094 E-Mail Strategist@aol.com

We serve as experts for comment or quote, please contact us at **410-263-9100**

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