



# STRATEGIC ASSESSMENT OF DEFENSE SECTOR SERVICE COMPANIES

*Findings from Pilot Study*



Department of Commerce

TIP strategies  
AUSTIN • SEATTLE



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## ABOUT THIS WORK

Washington State's military and defense sector provides tens of thousands of jobs and contributes billions of dollars to the economy annually. The state is home to over 1,500 businesses supporting and supplying military and national security missions both globally and locally at many of the critical assets safeguarding our national security, from armed forces installations to homeland security assets around the state. While the military and defense sector's economic importance has long been touted, little is known about the state's defense contracting base. Given planned reductions in defense spending at the national level, a solid understanding of these firms was needed.

To address this need, the Washington State Department of Commerce (Commerce) applied for and was awarded a \$4.3 million grant from the US Department of Defense (DOD), Office of Economic Adjustment (OEA). The primary objective of the grant, titled "Washington State, Military & Defense Sector, Industry Adjustment Analysis and Strategy," was to:

1. Assess and forecast the statewide economic impact of Washington's defense industry, and
2. Craft a plan to mitigate the potential catastrophic impact of federal defense budget cuts and sequestration on a region, which has become increasingly dependent on military and defense contracts.

This document outlines findings from the Defense Services Supply Chain Pilot Program, one of several pilot projects funded under the OEA grant. The primary focus of this work was to create and test a viable economic diversification strategy specific to the defense services supply chain in the state (which includes firms offering a range of services such as specialized defense engineering, industrial design, software development, and management consulting).

Potential participants were identified by Commerce based on a number of factors, including their reliance on defense spending (defined as deriving 40 percent or more from annual revenues from DOD contracting), the industry represented (to ensure a mix of business types), and their geographic location. Five companies participated in the pilot; a sixth company started the strategic assessment, but did not complete the process. Information gathered throughout the pilot will be used to prepare agency funding requests and help private organizations clarify their role in supporting the defense sector. In addition, lessons learned from the pilot will inform the development of a statewide strategy to support the future of this important sector.

# 1: EXECUTIVE SUMMARY

There is no question—a substantial change in federal defense spending would create a challenge for a number of states, including Washington. A well-formulated response to these cuts has the potential to minimize economic disruption while potentially opening the door to new opportunities. With these objectives in mind, Commerce, in collaboration with the Washington Military Alliance (WMA), initiated a pilot project to assess the strategic response of service supply chain companies to reductions in federal defense spending. Centering this effort on professional service firms within the defense supply chain is a logical target, given the size and scope of this activity in the state. Defense services firms include a range of high-wage jobs and encompass companies engaged in providing specialized engineering, design, software development, and consulting services.

To conduct the pilot, Commerce engaged Kepner-Tregoe, a global management consulting firm based in Princeton, New Jersey, and TIP Strategies, an economic development consulting firm with offices in Austin and Seattle. The work was funded as one component of a \$4.3 million grant from the DOD designed to help retain, grow, and diversify the state's defense and military sector. This white paper was created using information gathered from strategic assessment and top management strategy sessions conducted with the pilot companies. It describes the challenges faced by the companies through individual case studies as well as cross-company observations and best practices. Findings from this work are intended to serve not just the five participating companies, but to assist other defense supply chain companies across the state as they adjust to an uncertain business environment that includes possible reduced DOD spending.

## OVERVIEW

The pilot project was conducted in three phases. The initial phase consisted of identifying appropriate companies. Potential participants were identified by Commerce's military and defense sector program based on criteria that included:

- Demonstrated reliance on DOD contracting (defined as firms deriving 40% or more of business revenue from a DOD contract[s] or subcontract[s]).
- Demonstrated or imminent loss of at least 5% of sales and/or production due to reduced DOD expenditures.
- Willingness to provide 24 months of *historical* sales, production, and employment data.
- Willingness to provide 24 months of *projected* sales, production, and employment data.
- Willingness to serve as a case study participant.
- Willingness to allow the inclusion of select data in public documents (descriptive information, but not confidential disclosures).
- Willingness of senior management to participate in a two-day executive session.

### SPECIAL THANKS

The Washington State Department of Commerce acknowledges the contributions of the five companies that participated in the pilot project. The analysis could not have been conducted had it not been for participants' willingness to open their firms up to the management review and their commitment to the process. Names of the participating companies are held in confidence to protect the information compiled as part of the assessment process, which included sensitive financial data, information on the current and future customer base, as well as the unique value proposition these firms offer to clients and any trade secrets they were built upon. The participants' willingness to share this information openly during the strategy sessions with the consulting team was instrumental in the development of this work. The consulting team and Commerce are grateful for their contributions to this effort and to the industry across the state.

## STRATEGIC ASSESSMENT OF DEFENSE SECTOR SERVICE COMPANIES

The five companies that completed the pilot include a software and logistics firm, a marine engineering and services firm, an ocean safety training and consulting firm, a construction and design build firm, and an IT and logistics support firm.

Once the participants were selected, Kepner-Tregoe conducted a strategic assessment of each firm. The assessment followed the consulting firm's well-established approach for honing business strategy, which has been used by private businesses, public agencies, and nonprofits around the world for more than four decades. In light of the constraints of the pilot, Kepner-Tregoe's approach focused on core elements of the process, with the goal of assessing each firm's current strategic posture and understanding their capacity for diversification.

The companies participating in the pilot submitted a descriptive data set to inform the consulting team of the current state of each business, including data showing the impact of reduced DOD spending. Each company then had a two-day strategic assessment session attended by top management and facilitated by senior Kepner-Tregoe strategy consultants.

Management consulting services paid for by the grant included:

- an assessment of each pilot company's current strategic situation,
- an assessment of company response to the challenges of reduced DOD spending,
- company preparedness to respond using strategic best practices, and
- an action plan to move forward, with assigned responsibility

The final stage of the pilot consisted of documenting the results of the assessment, preparing case studies of the individual companies, and synthesizing lessons learned and best practices. This document represents the culmination of those tasks.

## FINDINGS

The Defense Services Supply Chain Pilot Program has been very well received by participating companies. Commerce obtained positive feedback from virtually all of the firms at the conclusion of the program. The work of the selected management consultant, Kepner-Tregoe, has shed light on which strategies might be best suited to assist companies in diversifying and the resources that are likely to be required. The ultimate value in the pilot program is taking this understanding and translating the findings to the preparation of a statewide implementation plan on a larger scale.

The following findings emerged from this work:

- *Provided benefit to participants.* Based on feedback from pilot companies, the program was highly valuable because it provided them with expertise they would not have been able to secure independently. The program allowed decision makers within each business to focus on and address larger strategic issues outside of daily operations. The companies that participated in the pilot project built an understanding of the key decisions that will shape their business, the actions needed to start creating a viable business future, and initial responsibility assignments to start down the path. A key element of the statewide strategy should be to explore funding options to extend and expand on this program and others conducted as part of the OEA grant.

## STRATEGIC ASSESSMENT OF DEFENSE SECTOR SERVICE COMPANIES

- *Yielded insight for statewide implementation.* The pilot program tested potential interventions on a small scale, which provided valuable lessons for the design of larger scale program and ultimately a statewide diversification strategy. This work identified challenges to existing operations and decisions that must be made to diversify revenue. These challenges and decisions, now documented, provide valuable lessons that will be shared with businesses on a statewide level. Carrying these findings forward and leveraging the insights and resources compiled will maximize the return on investment from these and other grant-funded activities.
- *Revealed lack of existing business strategy.* None of the assessed companies had completed a structured approach to formulating their forward-looking business strategy. There were notable gaps in:
  - Assessing the external business environment and internal business capabilities
  - Defining the intended future scope of products/services—what should be pursued and what should not
  - Evaluating possible business diversification alternatives
  - Establishing strategic business emphasis and mix
  - Strategically focused implementation planning
- *Exposed deficiencies in firms' organizational structures.* There were frequent gaps among pilot companies in the strategic governance structure (who participates in the decisions that will shape the company's future.) Without clear lines of decision-making, crucial strategic choices may be made or implemented poorly. Findings from the pilot companies suggest that setting aside sufficient time for business strategy planning is an essential step. Firms should be encouraged to allocate time for top management to remove themselves from day-to-day operations for this purpose and to seek out organizations (public and private) with strategic planning expertise to assist in this effort as needed.
- *Revealed challenges in formulating a business development strategy.* A major challenge for all of the assessed companies is instituting a business development function that is effective in the non-DOD commercial sector. The business development practices and approaches that were once successful at winning DOD contracts often have little traction in the commercial market. Findings from the pilot suggest this issue stems from a lack of understanding of how to approach the commercial market, as well as an overall lack of business development expertise at the staff level. Strategies for addressing this challenge include helping firms build relationships with organizations in traditional business development channels (such as chambers of commerce and trade associations) and coordinating the work of the Department of Commerce Sector Leads to help defense firms identify opportunities for diversifying into one or more of the state's target sectors.
- *Confirmed the absence of an existing export strategy.* None of the companies had an active effort in searching for international business, and previous experience with international customers was minimal. Accessing foreign markets and navigating an often-complicated export process presents a barrier for most firms, particularly for defense-related products and services, which are subject to additional constraints. Helping firms to explore these avenues of untapped business should be a focus of the industry adjustment strategy. Commerce has a very successful and long-standing International Trade promotion division. This group should be leveraged to benefit services firms in the military and defense sector.

## STRATEGIC ASSESSMENT OF DEFENSE SECTOR SERVICE COMPANIES

- *Demonstrated the need for enhanced skills and expertise among company employees.* In service companies, such as those included in the pilot program, human resource assets play a key role in competitiveness. Therefore, company recruiting, training, and human performance management are critical to success. Findings from other grant-funded activities, including the state analysis and outreach tasks, should be used to design effective strategies to assist companies in finding qualified employees, develop required capabilities, and retain them when workloads change. This strategy would extend beyond Commerce and include a broad range of partners at the state, regional, and local level.
- *Affirmed the need for continued support.* As part of the OEA grant work, Commerce’s military and defense sector program has been conducting efforts to support the defense contractor community and mitigate the impacts of defense spending cuts on contractors. It is crucial for this work to continue. The staff that runs these programs has an established network of individual businesses and the efforts have been well regarded. A Defense Business Development Manager has been hired with a strong background in federal contracting and workforce development to provide support and guidance to contractors statewide. A plan of work has been developed that will provide individualized technical assistance on a wide range of topics including strategic market research, business development and diversification, and international trade. Ensuring the future of these activities will be paramount to the diversification strategy’s success.

The approach to this phase of the grant—creating diversification strategies for specific companies—offers a number of advantages. Lessons learned from the pilot program will help shape the state-level response and suggest areas for further evaluation. Information gathered throughout this phase will be used to inform agency funding requests and help private organizations clarify their role in supporting the military and defense sector in the state. In summary, this phase has provided a clear understanding of the outcomes of the pilot initiative, a compilation of potential solutions gleaned from the process, and recommendations to enhance the state’s ability to implement a response to changes in the defense-contracting environment.

## ABOUT THIS REPORT

The remainder of the report further describes the pilot and presents detailed findings from the strategic assessment, as well as recommendations for supporting this vital sector of the Washington State economy. Chapter 2 provides additional information about the company selection process and outlines the Kepner-Tregoe strategy model. Chapter 3 outlines Kepner-Tregoe’s observations based on the application of that model to pilot companies. It presents a graphic illustration of each firm’s assessed performance relative to optimal performance and provides summary observations and recommendations with regard to those findings. Chapter 4 presents a strategic framework for future business support efforts based on the results of the pilot project and the experience of the consulting team in conducting economic and management strategy work. Pilot company case summaries are presented in Appendix A.

A Resource Roadmap was provided as a separate deliverable. The Roadmap is intended to provide guidance, document the available support system, and assist in developing a diversification strategy for similar contractors across the state that are heavily dependent on defense spending—ultimately in an effort to mitigate their exposure to federal budget reductions. Resources included in the Roadmap represent a comprehensive collection of the tools and programs most relevant to military and defense services supply chain companies. Additional details about the Roadmap are provided in Appendix B.



## 2: PROJECT APPROACH

The consulting team’s approach included: 1) selection of pilot companies within the Washington defense services supply chain; 2) application of the Kepner-Tregoe strategy formulation logic to assess the pilot companies’ strategic response to decreased DOD funding; 3) development of case studies based on the assessment of each pilot company, and 4); summarization of lessons learned and recommendations of best practices for Washington State companies facing similar challenges. In addition, TIP Strategies compiled an inventory of resources to assist Washington State companies in making the transition to less dependence on DOD contracts. An overview of this Resource Roadmap, published separately, is provided in Appendix B.

### COMPANY SELECTION & REQUIREMENTS

The five companies that participated in the pilot program were identified by Commerce and the consulting team. Company selection was based on criteria that included:

- Demonstrated reliance on DOD contracting (defined as firms deriving 40% or more of business revenue from a DOD contract[s] or subcontract[s]).
- Demonstrated or imminent loss of at least 5% of sales and/or production due to reduced DOD expenditures.
- Willingness to provide 24 months of *historical* sales, production, and employment data.
- Willingness to provide 24 months of *projected* sales, production, and employment data.
- Willingness to serve as a case study participant.
- Willingness to allow the inclusion of select data in public documents (descriptive information, but not confidential disclosures).
- Willingness of senior management to participate in a 2-day executive session.

| FIGURE 1. PILOT COMPANY KEY |                                 |
|-----------------------------|---------------------------------|
| <b>A</b>                    | Software and Logistics          |
| <b>B</b>                    | Marine Engineering and Services |
| <b>C</b>                    | Safety Training and Consulting  |
| <b>D</b>                    | Construction and Design Build   |
| <b>E</b>                    | IT and Logistics Support        |

The five companies in the assessment include software and logistics firm, a marine engineering and services firm, an ocean safety training and consulting firm, a construction and design build firm, and an IT and logistics support firm. To maintain confidentiality, companies were assigned a letter (A through E) in place of their corporate name. Figure provides a key showing the letter name assigned and the industry of each participating company.

The companies participating in the pilot submitted a descriptive data set to inform the consulting team of the current state of each business. Sensitive company data was kept strictly confidential, subject to a non-disclosure agreement. Each company then had a two-day strategic top management assessment session, facilitated by senior Kepner-Tregoe strategy consultants.

## STRATEGIC ASSESSMENT OF DEFENSE SECTOR SERVICE COMPANIES

Examples of the information discussed during the session include:

- What are the products and/or services your organization (business, division, function) offers?
- What products or product groups have you considered but rejected? Why?
- What product groupings or categories do you use to describe your current product range?
- Who are your major customers or customer groups?
- Which customers or customer groups have you considered but rejected? Why?
- What are the routes for your products and/or services to market? Who are the major players in the chain to the end user?
- Who are your major end users or end user groups?
- What customer groupings or categories do you use to describe your current customer range?
- What major geographic markets do you serve?
- Which other geographic markets have you considered but rejected? Why?
- What geographical groupings or categories do you use to describe your current geographical markets?
- What capabilities are essential to your organization (e.g. product technology, production process, sales methods, raw materials, etc.)?
- How do you measure growth and return for your overall organization?
- What has been your organization's performance to date?
- What expectations have you had, and do you now have, for performance?
- How do these expectations compare with performance of competitors and industry averages?
- How do you measure performance of profit/revenue and cost centers?
- What is the organization structure?
- What recent organization structure changes (reorganization, addition, or deletion of units) have taken place?

The outputs of that session included an understanding of the key decisions that will shape the businesses, actions needed to start creating a viable business future, and initial responsibility assignments to start down the path.

## STRATEGIC ASSESSMENT LOGIC

To conduct a strategic assessment of pilot companies in the defense industry service supply sector in Washington, Kepner-Tregoe applied its established model of strategy formulation<sup>1</sup> as follows:

1. A strategic assessment questionnaire was developed using the Kepner-Tregoe strategy framework.
2. The questionnaire was distributed in advance to the leadership of each company in the assessment.

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<sup>1</sup>*Top Management Strategy*, Benjamin Tregoe and John Zimmerman, 1980.

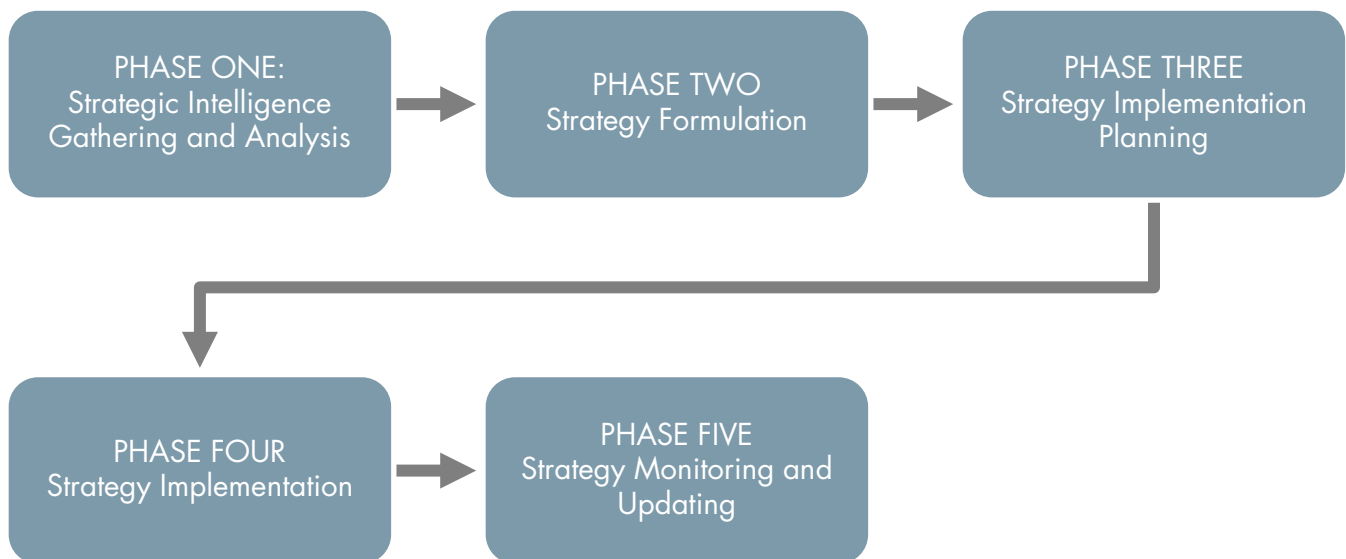
## STRATEGIC ASSESSMENT OF DEFENSE SECTOR SERVICE COMPANIES

3. Returned questionnaires were reviewed by Kepner-Tregoe to shape the structure of the pilot workshops scheduled for each of the companies.
4. Inputs from each company were developed into a presentation for the pilot workshops.
5. A presentation depicting the Kepner-Tregoe strategic assessment was developed for each pilot workshop.
6. Five 1-2 day pilot workshops were scheduled for the companies to be assessed.
7. Interactive workshops with pilot companies were conducted between April 25 and May 11, 2016, in the offices Commerce.
8. Workshop discussions were documented and shared, confidentially, with each of the assessed companies.
9. The company case studies and overall findings and recommendations herein are based on all of the above.

Kepner-Tregoe has a long history in the field of business strategy derived from the research of one of its founders, Dr. Benjamin B. Tregoe. Dr. Tregoe, a pioneer in the development of management logic for decision making, problem solving, and issue management,<sup>2</sup> was struck by the realization that the senior executives with whom he worked were seldom able to discuss strategic business choices in more than a cursory fashion. Tregoe conducted research with more than 100 US and international companies as the foundation for the Kepner-Tregoe approach to formulating business strategy.

The Kepner-Tregoe approach has been used successfully by hundreds of companies, big and small (as well as a wide array of public and not-for-profit organizations) to shape their strategies in the United States and around the world. It is at the core of the strategic assessment conducted with pilot companies in this project.

A representative project flow is illustrated by the following diagram:



<sup>2</sup> *The Rational Manager*, Dr. Charles H Kepner and Dr. Benjamin B. Tregoe, 1965.

## STRATEGIC ASSESSMENT OF DEFENSE SECTOR SERVICE COMPANIES

Completion of this process through Phase 3 would typically occur over four to six months and would require full engagement of the top management team over an extended period. To accommodate the constraints of the pilot, an abbreviated assessment was used by the Kepner-Tregoe team. This abbreviated approach focused the assessment of pilot companies on some fundamental considerations in Phase 1 with the bulk of the assessments focused on the elements of Phase 2.

The focused approach, used to shape the strategy questionnaire and the pilot company workshops, was comprised of the following basic elements for each company:

- 1.** Strategic Intelligence Gathering and Analysis
  - a.** Revenue and Profit History and Forecast
  - b.** External Environment
  - c.** Internal Environment
- 2.** Basic Beliefs and Values
- 3.** Strategic Horizon
- 4.** Intended Product/Service Scope
- 5.** Intended Market/Customer Scope
- 6.** Thrust for New Business
- 7.** Product-Service/Market Emphasis and Mix
- 8.** Key Capability Investments
- 9.** Measures of Success
  - a.** Growth and Return
  - b.** Non-financial
- 10.** Critical Issues

The company workshops, conducted by senior Kepner-Tregoe consultants, asked representatives of the top management team for each pilot company to engage in the critical questions underlying each of these basic elements. The workshop discussions were documented real time, in the context of the Kepner-Tregoe strategy logic, and subsequently shared back with the leadership of each pilot company team.

Results from the strategic assessment and top management strategy sessions, including case studies outlining challenges faced by each of the pilot companies, cross-company observations, and best practice recommendations, are provided in the following sections.

### 3: STRATEGIC ASSESSMENT

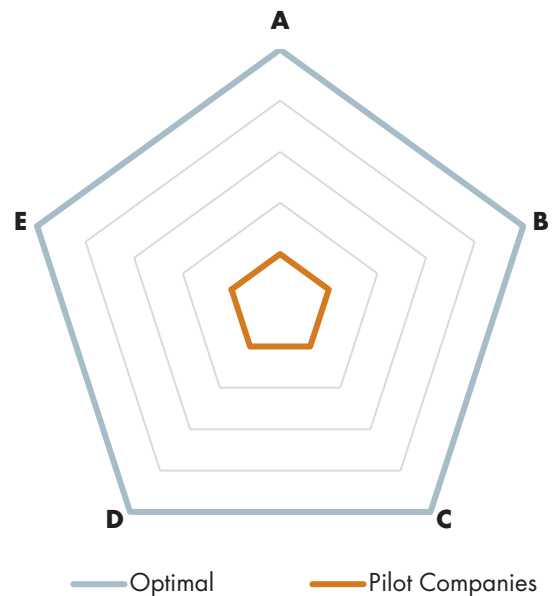
Responding to an advance request for strategic information, the assessed companies provided data on their revenue and profit history and forecast. This information was used to assess the company in a number of strategic areas. Findings from this assessment are outlined below, followed by observations and recommendations arising from the review process.

#### KEY ASSESSMENT ELEMENTS

Companies were assessed across multiple characteristics, including revenues and profit, market scope, approach to new business development, the role of corporate values in decision-making, and the indicators used to measure success. Significant findings from each element of the assessment are provided on the following pages and include “radar” charts showing the performance of the five companies with regard to each element. To maintain confidentiality, each company was assigned a letter (A through E), which is used in place of the corporate name throughout this section and in the companion case studies presented in Appendix A. Figure 1 (page 6) provides a key connecting the assigned letter to the industry of each company.

Figure 2 provides a sample of the radar chart and scale upon which each figure is based. In each case, the blue border indicates the optimal value for the element—that is, if each company performed optimally, its assessment score would align with the outside blue border. The performance of the pilot companies is shown by the orange line, depicting different levels of performance for each company according to the index for that element. Each chart includes a scale showing how participants’ performance was evaluated and the text and numeric value assigned to each level. The scale used varied slightly depending on the element, with “1” reflecting the lowest level of performance across all elements.

FIGURE 2. SAMPLE ASSESSMENT ELEMENT



SCALE: SAMPLE ASSESSMENT ELEMENT

|  | Value  | Scale |
|--|--------|-------|
| Statement of optimal performance for element | ↑<br>↓ | 5     |
| ...  |        | 4     |
| ...  |        | 3     |
| ...  |        | 2     |
| Statement of minimal performance for element |        | 1     |

**COMPANIES FACE REVENUE CHALLENGES**

As expected, none of the companies is in an optimal position (robust revenue growth and consistent profitability), as illustrated in Figure 3.

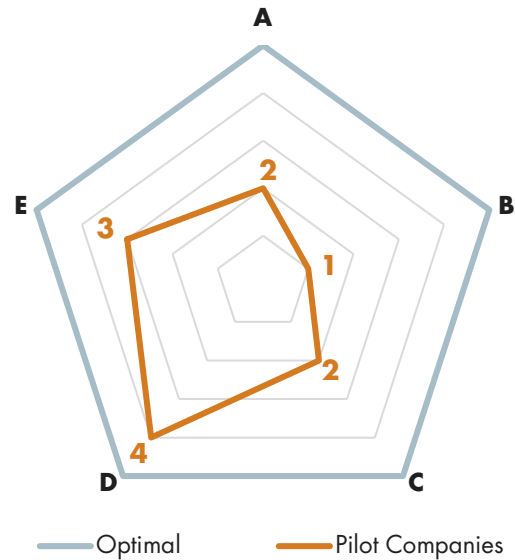
As described in the accompanying case studies, the companies face a particular set of challenges, including:

- One company lost a Navy contract that made up more than half of its business, forcing a decline in staffing and increased pressure to break even.
- One company finds its legacy business struggling to win US government contracts as the procurement cycle is less predictable and more extended.
- One company has experienced strong revenue growth, but is constrained by capital limits and sharp competition in potential markets.
- One company has seen recent revenue driven by non-repeatable material sales, while looking to increase revenues and profits to benefit a widespread stakeholder base.

In pilot workshops, the relationship between strategic decisions and financial results was emphasized. While every company requires certain levels of revenue growth and return, in every case it is decisions about the strategic nature and direction of the organization that ultimately produce revenue and profit.

The central question of this assessment is what strategic shaping decisions can be made by companies affected by DOD spending reduction to improve their future sustainability as measured by continued streams of revenue at an acceptable level of profit.

**FIGURE 3. REVENUE AND PROFIT ASSESSMENT**



*SCALE: REVENUE AND PROFIT*

|                                    | Value      | Scale |
|------------------------------------|------------|-------|
| Robust growth and profit           | Optimal    | 5     |
| Sustainable growth and profit      | Sustain    | 4     |
| Limited growth, constrained profit | Limited    | 3     |
| Revenue decline, press on profit   | Stress     | 2     |
| Company survival at risk           | Endangered | 1     |

**LITTLE FORMAL ASSESSMENT OF EXTERNAL ENVIRONMENT**

Leadership assessment of trends in the external environment is an essential element of any useful business strategy. As there is no reliable data about the business’s future, it is the responsibility of top management to discuss and agree on the trends in the external environment that will affect the future of their business.

Following the pilot workshops, the assessment of the External Environment provided by company leaders was evaluated using the scale shown in Figure 4.

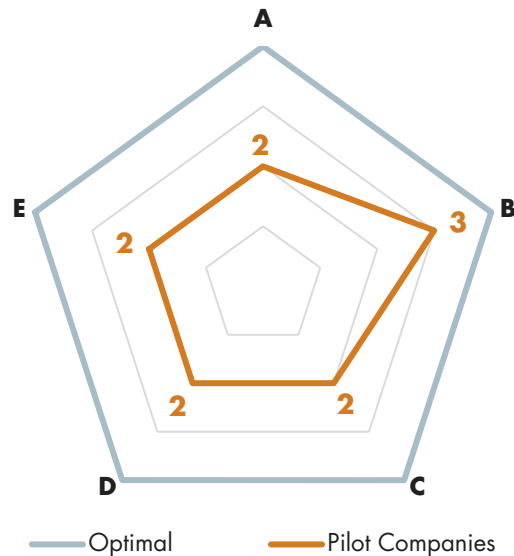
While the future cannot be predicted with any certainty, the top management team of a company should certainly have a shared view about what in the external environment should be considered in shaping strategy. In pilot workshops with company leadership, it was apparent that none had conducted extensive formal reviews of the external environment resulting in robust assumptions on which strategic decisions could be based.

Most of the companies had given thought to the downward trend of federal spending and competition, with several articulating developments within the contracting system upon which they depend. One company had taken action to affect decision making in the federal purchasing environment, although it is unclear whether that action has yet had any positive impact.

In an optimal approach, Kepner-Tregoe would expect to see the top management team of each organization undertake a thorough review of the trends in the external environment surrounding their company, taking into account such considerations as changes in technology and the industry environment, competitive trends, customer trends, and the requirements for business success.

As data about the future can be suggestive but not definitive, it is incumbent upon the top management team to conduct this discussion with awareness that certain judgments are necessary and that those agreed upon judgments should be shared by team members and documented as assumptions. It is most useful if the implications to the company of those assumptions are specifically drawn and documented, improving subsequent strategic decision-making.

**FIGURE 4. EXTERNAL ENVIRONMENT ASSESSMENT**



*SCALE: EXTERNAL ENVIRONMENT*

|  | Value         | Scale |
|--|---------------|-------|
| Formal, documented assumptions resulting from top team consensus | Optimal       | 4     |
| Detailed assessment of key trends                                | Knowledgeable | 3     |
| Awareness of some trends   | Aware         | 2     |
| No consideration in decision making                              | Unaware       | 1     |

**DISCIPLINE NEEDED IN ASSESSING INTERNAL ENVIRONMENT**

Just as top management assessment of the external environment is essential, disciplined consideration of the internal environment is a necessary precursor to effective strategic decision making.

While it can be difficult to develop an objective view of company strengths, weaknesses, capabilities and vulnerabilities, every company strategy should begin with understanding where it really is before charting where it should go.

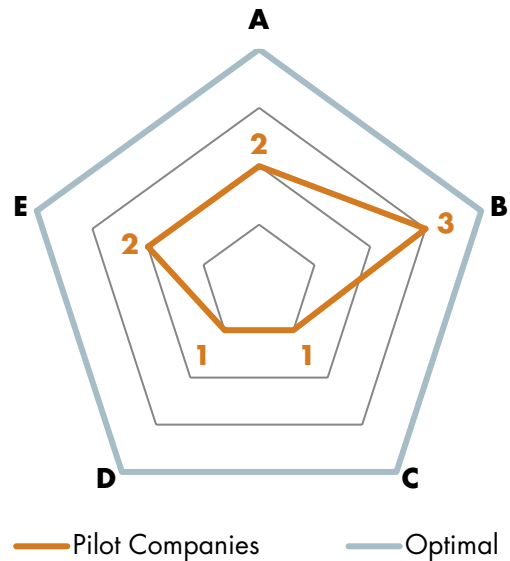
Following the pilot workshops, the assessment of the strategic Internal Environment provided by company leaders was evaluated using the scale shown in Figure 5.

It can be particularly difficult for a senior leadership team to conduct a clear-eyed review of its own internal environment. There may be biases related to organization position or perspective, or the influence of founders, owners and other stakeholders may be acute.

In pilot workshops with company leadership, it was apparent that each of the companies had given thought to and was aware, to some extent, of critical factors in their internal environment. During the assessment, no evidence was found that any comprehensive reviews had been conducted or that implications for strategic decision-making had been drawn and documented. In each case, the top teams concluded that they would need to undertake one or more improvements in their understanding and management of their internal environments.

In schools of strategic thinking that have emerged since the 1980 publication of *Top Management Strategy*, some have maintained that the only foundation for setting strategic direction is the set of competencies, or key capabilities, of the company and how they are arrayed against opportunities and threats. Kepner-Tregoe believes that key capabilities may be one foundation for strategic choices, but may also be an element of implementing strategy based on other foundational choices. In any event, the capabilities of any company are not fixed in stone, but may be added to or reshaped by top management as determined by strategic opportunity and available funds.

**FIGURE 5. INTERNAL ENVIRONMENT ASSESSMENT**



SCALE: INTERNAL ENVIRONMENT

|   | Value         | Scale |
|---|---------------|-------|
| Comprehensive review of company and documented current status | Optimal       | 4     |
| Leadership review of key elements                             | Knowledgeable | 3     |
| Awareness of some elements                                    | Aware         | 2     |
| No consideration in decision making                           | Unaware       | 1     |



**BELIEFS/VALUES NOT CONSISTENT GUIDE TO DECISIONS**

In strategic decision-making, beliefs and values are brought to bear that influence the alternatives considered and the directions chosen.

Those beliefs and values should be made explicit—discussed, agreed to, documented, and used—by the top management team with responsibility for the business. Basic beliefs are a critical expression of the nature of the organization, the people who lead it, the customers and communities they serve, and the people who work there.

To assess the basic beliefs discussed during our sessions with the pilot companies, Kepner-Tregoe applied the scale shown in Figure 6.

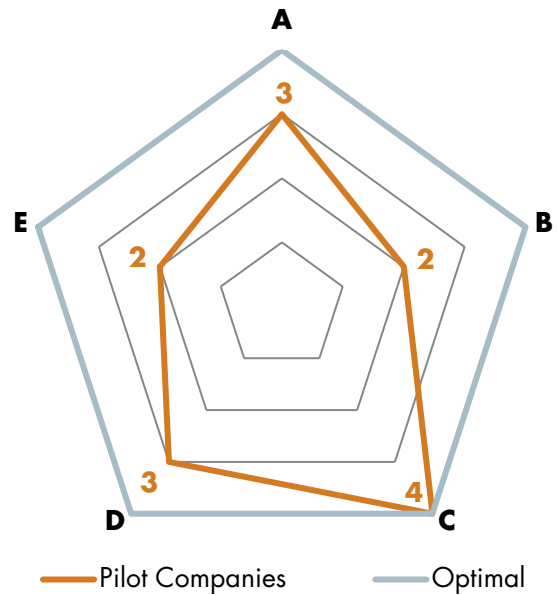
In each case, the pilot company leaders we worked with were able to articulate beliefs and values important to them and their organizations. In only one case did we find those basic beliefs stated in a form that clearly reflected full top management team consideration and communication with all relevant stakeholders.

There is considerable utility in the explicit use of basic beliefs in company decision making. In the normal course of business, leaders, managers, and employees are guided to pursue high value activity, sharing a sense of purpose that aligns their work with the larger world. When challenges occur, such as product failures or unethical conduct, basic beliefs provide a sound foundation for critical decision-making.

Arriving at internal consensus can be challenging. To be useful, statements of basic belief should avoid bromides and platitudes, concentrating instead on meaningful construction of statements that truly express what the organization values.

This often requires time, discussion and many drafts to develop beliefs that express what is needed. By the time the internal process is completed, there should be little need for wallet cards or posters, as the company leaders will have absorbed and will demonstrate through use their commitment to the company’s basic beliefs.

**FIGURE 6. BASIC BELIEFS/VALUES ASSESSMENT**



*SCALE: BASIC BELIEFS/VALUES*

|  | Value      | Scale |
|--|------------|-------|
| Comprehensive review, consensus, communication, use in decision making | Optimal    | 4     |
| Explicit, brought to bear in leader decisions                          | Informing  | 3     |
| Implicit, tacit influence on decisions                                 | Contingent | 2     |
| No consideration in decision making                                    | Unaware    | 1     |

**MOST PRODUCT-SERVICE SCOPE DECISIONS NOT STRUCTURED**

One of the most important decisions a company makes is what to provide and what not to provide. Or, in other words, what is the product-service scope.

For a single product company in its early stages, it is a simple choice to find the first paying customer and then find more paying customers.

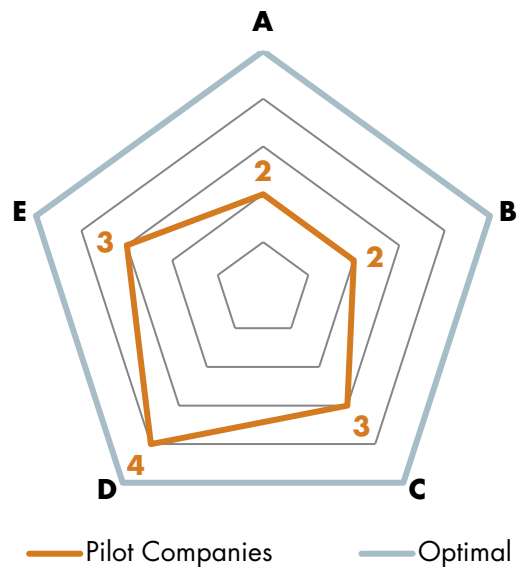
But as companies grow in size and complexity, they are increasingly faced with choices about what to provide, what should fit within their product-service scope, and what should remain outside.

Working with information provided in advance by the pilot companies and subsequent session discussions, Kepner-Tregoe applied the scale shown in Figure 7 to assess their decisions about product-service scope.

Like many others, the product-service scope for the pilot companies was seldom the result of explicit choices about what to develop and/or what to avoid. The scope was often the legacy of a company’s history, or sometimes expressed an inherent conflict between pursuing one set of opportunities over another.

The absence of explicit choices on product-service scope leads to two sources of wastage and failure. The first concern with an inadequately defined product-service scope is that the company is unlikely to achieve its fundamental objectives if it has failed to define what it wishes to provide as a product and/or service. That, in turn, can provide opportunities outside the intended product-service scope of the company—sometimes called “blue birds”—the ability to compete for company time, attention, and resources.

**FIGURE 7. PRODUCT-SERVICE SCOPE ASSESSMENT**



*SCALE: PRODUCT-SERVICE SCOPE*

|  | Value       | Scale |
|--|-------------|-------|
| Explicit strategic scope used to guide business priority decisions | Optimal     | 5     |
| Scope explicitly determined as part of strategic decision making   | Intentional | 4     |
| Legacy scope, not the result of proactive choices                  | Informing   | 3     |
| Clear conflicts in stated scope                                    | Diverting   | 2     |
| No consideration in decision making                                | Uniformed   | 1     |

MARKET SCOPE DECISIONS LEGACIES OR IN CONFLICT

It should go without saying that pursuing a new course of business requires intense focus. In moving from one revenue-producing product-service line to another, there are myriad decisions that must be made and implemented. Each choice opens the possibility of new risks, which must be managed proactively to achieve business success.

Companies seeking to change their product-service scope, such as those involved in this assessment, should exercise considerable discipline in establishing that scope as an explicit guide to decision making.

In defining the strategic “space” in which a company operates, the second key dimension is the scope of its market—who is served and who is not served as an explicit choice. Market scope may be based on understanding customer needs, geography, or some combination of the two.

The companies chosen for this assessment were generally focused on a single market—the United States Department of Defense—and must now select other markets to diversify successfully.

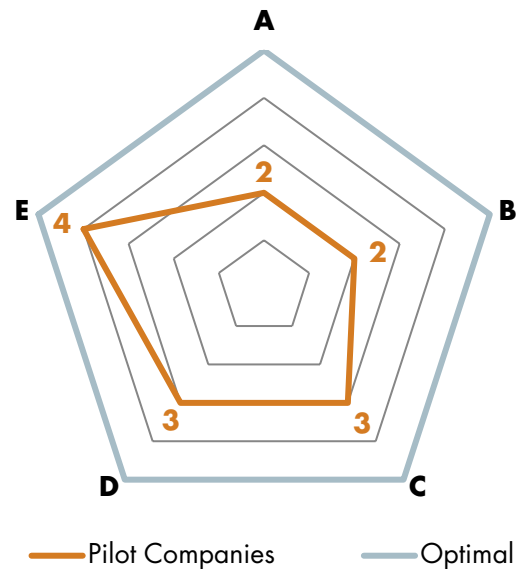
Working with information provided in advance by the pilot companies and subsequent session discussions, Kepner-Tregoe applied the scale shown in Figure 8 to assess their decisions about customer-market scope.

As noted above, at the time of the assessment, the customer-market scope for the assessed companies

was most often the result of legacy choices to serve the DOD. In some instances, loss of contracts or uncertainty about future contract awards directed the attention of the company to other potential markets. Approaches to pursuing opportunities with the DOD, such as contracts awarded through the DOD procurement process might be partly or wholly inappropriate in pursuit of other, non-DOD opportunities.

Although it is a priority of the state of Washington that companies in the defense services supply chain seek export opportunities to diversify their revenue streams, this assessment found that the subject companies had given little attention to selling outside of the United States. In one case, a core service was considered as a possible business development opportunity, but the complexities of meeting US Homeland Security requirements raised logistical barriers and costs to an impractical level. Other companies found that their current DOD customers favor local presence and, accordingly, limit their scope of operations to the continental US.

FIGURE 8. CUSTOMER-MARKET SCOPE ASSESSMENT



SCALE: CUSTOMER-MARKET SCOPE

|  | Value       | Scale |
|--|-------------|-------|
| Explicit strategic scope used to guide business priority decisions | Optimal     | 5     |
| Scope explicitly determined as part of strategic decision making   | Intentional | 4     |
| Legacy scope, not the result of proactive choices                  | Informing   | 3     |
| Clear conflicts in stated scope                                    | Diverting   | 2     |
| No consideration in decision making                                | Uninformed  | 1     |

**THRUST FOR NEW BUSINESS UNCLEAR OR IN CONFLICT**

Opening new markets, that is, deciding to change the existing customer-market scope, often requires even more discipline than changing the product-service scope. The familiar purchasing requirements and the procedures developed to meet those requirements are unlikely to fit well with the requirements of non-DOD customers. An entirely new set of customer needs might be in play, requiring new capabilities in customer contact, value propositions, proposal development, and contract management.

Structuring the pursuit of new customers and markets may be the most critical, and difficult, set of tasks the assessed companies must face. Even beginning with clear decisions about its intended customer-market scope, building the process and team to ensure success entails managing critical decisions and multiple possibilities for risk.

As it faces the future, the most critical question any company faces is its choice of thrust for new business.

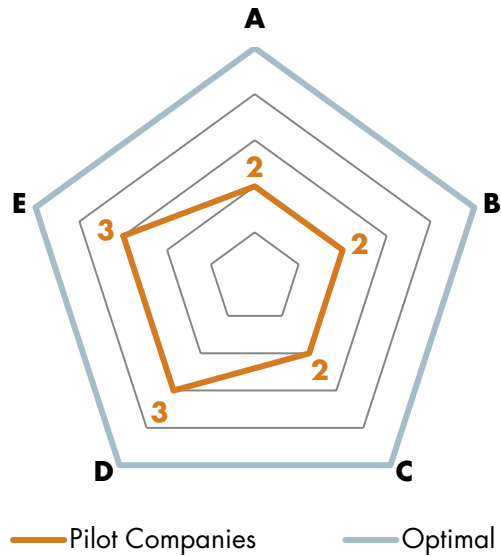
Choosing a strategic business thrust provides primary definition of which opportunities will be pursued, which should be avoided, and how company time, attention, and resources should be allocated.

Decisions about product, service, customer, and market development—the nature and direction of the company—should be guided by an explicitly chosen thrust for new business.

Working with information provided in advance by the pilot companies and subsequent session discussions, Kepner-Tregoe applied the scale shown in Figure 9 to assess their decisions about their strategic thrust for new business.

At the time of the assessment, none of the companies had made an explicit choice about the direction of its new business thrust. Each company had given some thought to what its priorities for business development should be, but not in a way that linked product-service, customer-market, and capability decisions.

**FIGURE 9. THRUST FOR NEW BUSINESS ASSESSMENT**



*SCALE: THRUST FOR NEW BUSINESS*

|   | Value       | Scale |
|---|-------------|-------|
| Top team consensus on directional thrust for new business used to guide business priority decisions | Optimal     | 5     |
| Thrust for new business explicitly chosen, some application to business priority decisions          | Intentional | 4     |
| Legacy direction, not the result of proactive choices   | Informing   | 3     |
| Clear conflicts in stated thrust for new business   | Diverting   | 2     |
| No consideration in decision making   | Uninformed  | 1     |

## STRATEGIC ASSESSMENT OF DEFENSE SECTOR SERVICE COMPANIES

A clear business thrust serves critical communication needs within and outside a company.

Internally, the business development thrust shapes priorities from marketing and sales to product development and performance management. It provides a quick reference check for the use of any company resources, defining what should and should not be pursued. It is the “bright line” for decision-making.

Externally, the business development thrust, properly articulated, provides a clear basis for explaining to customers, markets, and other stakeholders what the purpose of the company is and where the company is going. It can be particularly powerful when introducing the company to those who might have little prior knowledge or relationship.

### PRODUCT MARKET EMPHASIS AND MIX NOT SHAPED BY STRATEGY

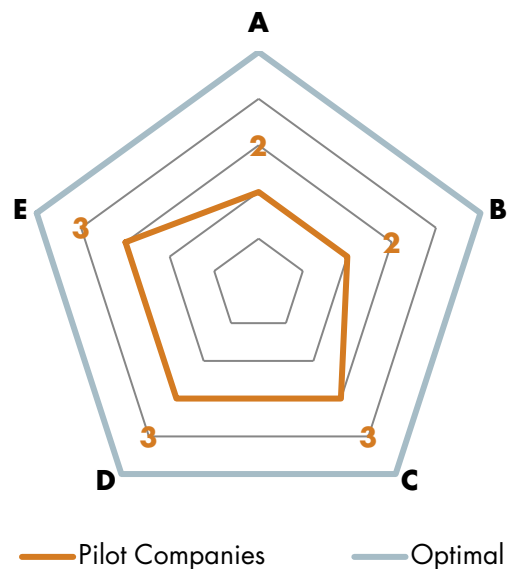
The first dimension of business strategy is defined by the choices a company makes about its product-market emphasis and mix, providing the roadmap for strategy implementation. The revenue a company collects is determined by the second dimension: which of its products/services is purchased by which of its customers/markets and in what volumes. Both of these dimensions are influenced by the company’s current capabilities, which comprises the third dimension.

When considering what products and services to pursue with which customers and in which markets, a company should have a clear idea of its strategic priorities. Looking forward, a company should have a clear map of where it is moving, where it is sustaining current efforts, and where it is intentionally phasing down.

Working with information provided in advance by the pilot companies and subsequent session discussions, Kepner-Tregoe applied the scale shown in Figure 10 to assess their decisions about product market emphasis and mix.

At the time of the assessment, none of the companies had made explicit choices about their product-market emphasis and mix. While all had provided information about the relative size of their current service lines and customers/markets, as well as their judgment of trends, the explicit priorities and tradeoffs had not been mapped.

**FIGURE 10. PRODUCT MARKET EMPHASIS AND MIX ASSESSMENT**



*SCALE: PRODUCT MARKET EMPHASIS AND MIX*

|  | Value       | Scale |
|--|-------------|-------|
| Prioritization based on intentional business development thrust, clear tradeoffs | Optimal     | 5     |
| Some explicit prioritization, some application to business priority decisions    | Intentional | 4     |
| Legacy emphasis and mix, not the result of proactive choices                     | Informing   | 3     |
| Conflicting priorities and/or lack of prioritization                             | Unfocused   | 2     |
| No consideration in decision making  | Uninformed  | 1     |

## STRATEGIC ASSESSMENT OF DEFENSE SECTOR SERVICE COMPANIES

Once strategic decisions about product-service scope, customer-market scope, and thrust for new business have been made, the foundation is set for establishing priorities for what products-services are directed to which markets. These priorities will necessarily involve tradeoffs between different business objectives, such as between profitability and growth, consistently applied to all possible product/market pairings.

The map of product market emphasis and mix should address both the current pattern of priorities and the future, desired strategic priorities. Thus, areas of strategic growth and development can be emphasized, while identifying other areas that might receive decreased future emphasis. This, in turn, can be used to define key change projects and company budgets and to calculate future revenue and profit levels.

### CAPABILITY INVESTMENTS PARTLY SHAPED BY STRATEGY

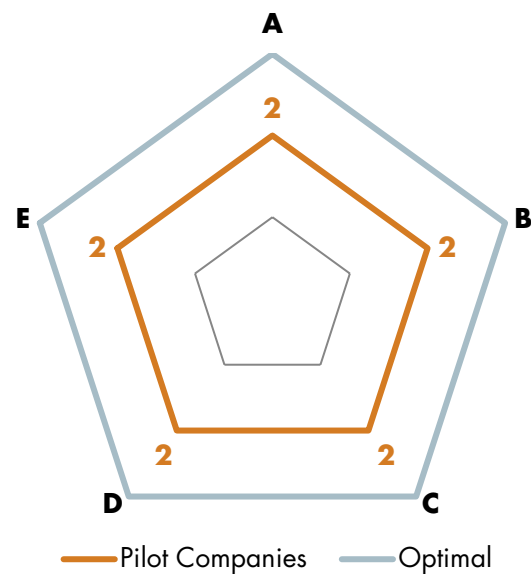
A company may base its choices about strategy on what its current capabilities are (the third dimension of strategy) or it may reshape its capabilities to carry out its chosen strategic direction. In any event, the company must understand its capabilities and how they will be deployed and managed to achieve strategic success.

Working with information provided in advance by the pilot companies and subsequent session discussions, Kepner-Tregoe applied the scale shown in Figure 11 to assess their decisions about capability investments to support their strategies.

In each case, the companies in the assessment had considered the capability changes required to advance their future business thrust, even if those choices were not explicitly guided by a specific set of choices on business strategy.

In service companies, such as those included in this assessment, capabilities are often centered in the knowledge and skills of their employees along with the tools that employees use. Accordingly, company recruiting, training, and human performance management are often critical to success. Turning on an employee is characteristically different from turning on a machine, putting a high premium on clear communication of company purpose and direction translated to specific, person-level expectations for performance and effective feedback.

**FIGURE 11. CAPABILITY INVESTMENTS ASSESSMENT**



*SCALE: CAPABILITY INVESTMENTS*

|   | Value          | Scale |
|---|----------------|-------|
| Capability investments guided by strategy       | Optimal        | 3     |
| Capability investments consistent with strategy | Intentional    | 2     |
| No priorities for capability investments        | Non-supporting | 1     |

## STRATEGIC ASSESSMENT OF DEFENSE SECTOR SERVICE COMPANIES

In addition, service companies often emphasize issue resolution methods that enable employees to effectively address customer concerns as well as work collaboratively with internal colleagues. In a world of project-based work, consistent project management methods can provide the structure that service delivery sometimes lacks.

The capability dimension of strategy is often a key driver of service company costs, particularly personnel costs. In pursuing strategic differentiation, service companies should be particularly careful to develop project plans and budgets that support chosen opportunities with effective, well-focused teams.

### INDICATORS CHOSEN TO MONITOR STRATEGY

Business success is usually indicated by numbers, most typically growth in revenue and some measure of return. But as these are lagging measures of after-the-fact results, leading indicators are useful when expanding (or at least changing) strategic scope.

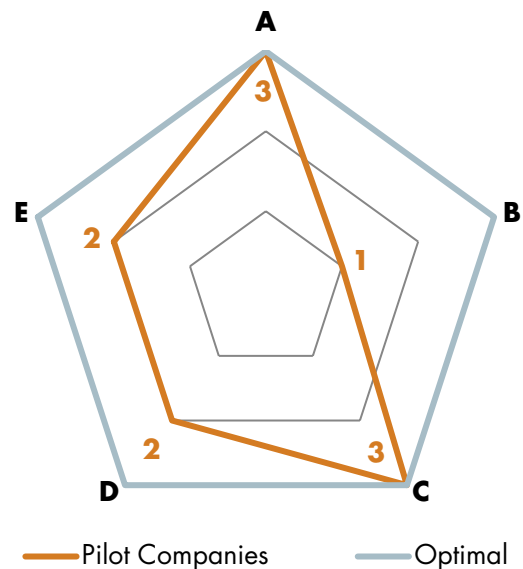
Indicators of strategic success will often drive financial measures such as growth and return, or can be monitored independently. For example, a company seeking to expand its service scope might measure its talent acquisition process to achieve that expansion without a formal link to financials.

Working with information provided in advance by the pilot companies and subsequent session discussions, Kepner-Tregoe applied the scale shown in Figure 12 to assess their decisions about indicators chosen to monitor their strategies.

Primary measures of strategic performance often include sales by product, service, and market; shifts in product/market emphasis; rate of new product introduction or innovation; penetration of new consumer or geographic markets; and successful withdrawal from de-emphasized products and markets. In addition, companies may wish to track competitive developments, customer and employee feedback, and process performance.

For the most part, the assessed companies focused on measures of internal performance, such as number of contracts in the pipeline, capacity utilization, and activities leading to contract wins. Appropriately, the non-financial indicators chosen by the companies were specific to the nature of the strategic performances they are aiming to achieve.

**FIGURE 12. SUCCESS INDICATORS ASSESSMENT**



*SCALE: SUCCESS INDICATORS*

|   | Value       | Scale |
|---|-------------|-------|
| Indicators chosen to measure strategic progress | Optimal     | 3     |
| Indicators consistent with strategic direction  | Intentional | 2     |
| Indicators unrelated to strategy                | Unrelated   | 1     |

## STRATEGIC ASSESSMENT OF DEFENSE SECTOR SERVICE COMPANIES

It is often the case that well-established measures of financial performance are not necessarily suited to managing day-to-day company performance. The necessity of reporting financials on a consistent basis is oriented toward a smooth pattern of information rather than the frequent deviations and discrepancies that are typical in real-world performance.

Given the often-flexible nature of service definition, companies such as those included in the assessment can often benefit by adopting alternative indicators of performance, including measures of outcomes/results, timing/schedule, or costs. It should go without saying that, whatever indicators are chosen, indicator definitions are clear, data collection is disciplined and timely, and reports are designed to prompt effective action.

## RECOMMENDATIONS & OBSERVATIONS

The observations and recommendations that follow are based on the Kepner-Tregoe assessment of pilot company responses.

**OBSERVATION:** In the pilot companies, there were frequent gaps in the strategic governance structure (who participates in the decisions that will shape the company's future). Without clear lines of decision-making, crucial strategic choices may be made or implemented poorly.

**RECOMMENDATION:** Provide training/organizational development in the nature and practice of strategic decision-making. To be most effective, training should be:

- Focused on the top management team;
- Oriented toward clarifying the nature of, and accountability for, strategic decisions; and
- Delivered via training/company-specific facilitation.

**OBSERVATION:** The pilot companies experienced major challenges when attempting to establish business development functions oriented toward commercial business beyond their traditional markets. Diversification beyond the DOD will be problematic without effective commercial business development functions.

**RECOMMENDATION:** Provide up-to-date information on attractive potential non-DOD customers and markets and provide assistance in designing and organizing individual company business development functions. This information should be:

- Compiled from existing sources.
- Oriented to highlighting sustained and emerging market needs.
- Supplemented by training/capability development in establishing commercially focused business development process/functions.

**OBSERVATION:** Due largely to business legacy/tradition issues, the pilot companies showed significant gaps in setting forth the intended current and future scope of their products and services. In turn, this clouded decision making about where to invest company time, attention, and resources.



## STRATEGIC ASSESSMENT OF DEFENSE SECTOR SERVICE COMPANIES

**RECOMMENDATION:** Each company seeking to diversify beyond the defense services supply chain should re-examine and understand the original intent of their legacy products and services as well as new and emerging market needs. Considerations for this reevaluation include:

- Product/service, revenue and contract history;
- Shifts in DOD requirements and practices; and
- Potential extensions/applications of company services/capabilities outside the DOD.

**OBSERVATION:** The pilot companies found it difficult to make sound decisions on diversification alternatives. This led to use of scarce resources on unsuitable projects, reducing the likelihood of successful diversification.

**RECOMMENDATION:** Companies should be trained in criteria-based decision making to evaluate diversification alternatives. Training should:

- Be coordinated with company governance and decision making;
- Utilize consistent logic; and
- Incorporate data based decision-making.

**OBSERVATION:** There were significant gaps in the pilot companies' understanding of their external and internal business environments. Decisions on diversification and expansion should not be made without a clear understanding of competition, industry, and market trends, as well as an acute understanding of company strengths, weaknesses, and capabilities.

**RECOMMENDATION:** Commerce should provide comprehensive information and reports on the emerging external business environment along with services to help companies assess their own strengths and weaknesses. Useful business services and intelligence would include:

- Industry trends;
- Growth areas and emerging business opportunities;
- Census of competitive companies;
- Consulting services to support individual company internal assessments; and
- Best practices regarding information that drives strategic decision-making (i.e., an understanding of the types of information required and the value of measuring and tracking this data).

## 4: STRATEGY FRAMEWORK

Findings from Kepner-Tregoe’s strategic assessment coupled with the consulting teams’ experience working with a wide variety of firms were used to outline a strategic framework for private organizations in response to declining DOD contracts or revenue streams. This framework is intended to help focus investment decisions should a major change in funding occur. It is supported by a Resource Roadmap which provides contact information for a variety of state, regional, and local organizations that can assist defense contractors in both responding to downsizing and enhancing their business generally. Additional information about the Resource Roadmap, which was published separately, is provided as Appendix B.

### STRATEGY: FOCUS ON RELATIONSHIP BUILDING

**OBSERVATION:** The pilot companies have not built expertise or relationships in industries outside of the military and defense sector. Establishing a business development path that is efficient and effective for these services firms is essential for their ongoing health.

**RECOMMENDATION:** Commerce’s sector lead program should be leveraged to support defense services firms in the state. The program has been innovative and very successful. The program has established a team of industry experts within Commerce who have a deep understanding of several industries that drive the state’s economy as well as a strong network of businesses and experts within and outside the state that are leveraged for business retention, expansion, and recruitment efforts. The industries that the sector leads program covers are all exceptional business development targets for the defense services firms in the state such as aerospace, life science, military, maritime, and ICT (information and communication technology). These industry experts can and should assist the defense services firms by:

- Using the sector leads to educate military and services firms about the industries that drive the state economy outside of the military and defense sector.
- Using the sector leads to identify and promote businesses development opportunities for defense-related firms in each sector. This work can be facilitated through Commerce’s technical assistance program.
- Using the Resource Roadmap and Commerce-maintained websites to help connect firms with first-point-of-contact organizations including:
  - State-level resources beyond Commerce;

#### “NO WRONG DOOR”

In recent years, various types of business assistance programs have focused on instituting “no wrong door” policies. These policies recognize the complex nature of many service delivery systems can be overwhelming for customers. With this protocol in place, customers can enter the system at any point. Service providers work together to find appropriate assistance, with the first point-of-contact having primary responsibility for coordinating the initial response and providing direction. Diversification assistance programs should aim to operate with this protocol in place. Successful policies require close collaboration across agencies and cross-training and coordinated resource management within individual agencies.

## STRATEGIC ASSESSMENT OF DEFENSE SECTOR SERVICE COMPANIES

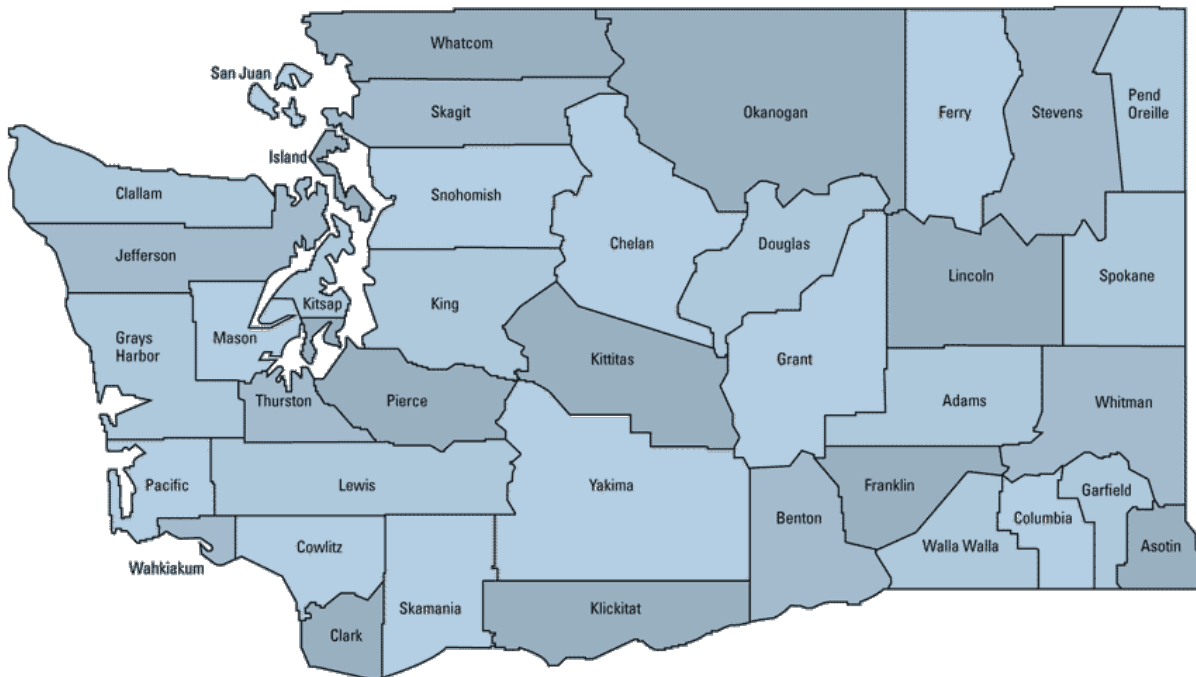
- Relevant trade associations and networking organizations, including those that support the state’s target sectors (e.g., Washington Biotech & Biomedical Association, Washington Aerospace Partnership, Washington Technology Industry Association); and
- Local Associate Development Organizations (ADOs).

## STRATEGY: CONNECT FIRMS TO TECHNICAL EXPERTISE

**OBSERVATION:** Defense services firms that participated in the pilot expressed their need for expert assistance in diversifying their customer base and strengthening their long-term outlook. The management consultation identified specific actions that each company should take to move ahead with the work to diversify their revenue base. Examples of these recommended actions included better defining corporate governance structures, formalizing and enhancing business development processes, and reevaluating product/market priorities. This pilot program has been very well received by participating companies and each company has committed to taking this work forward. Maintaining connections with these firms can provide a valuable “laboratory” for understanding the pilot’s long-term effectiveness. In addition, the challenges and decision framework identified through this work could form the basis for conducting additional pilot projects to address specific aspects of the diversification process.

### FIGURE 13. ASSOCIATE DEVELOPMENT ORGANIZATIONS

Each of the state’s 39 counties is represented by an ADO that furthers the county's or region's economic development goals. These ADOs are funded in part by Commerce, and their performance and expertise is critical to growing the economy and building communities statewide. A list of ADOs by county is provided on the Commerce website.



## STRATEGIC ASSESSMENT OF DEFENSE SECTOR SERVICE COMPANIES

**RECOMMENDATION:** Commerce should maintain connections with the five pilot companies to measure their success and continue to learn from and document their experiences. In addition, Commerce should continue the pilot program model of serving individual companies and sharing the information gathered with the broader business community.

- Check in with pilot companies every quarter to learn what strategic steps they have taken, what successes have resulted, what difficulties they have experienced, and what additional support they may require.
- Share the information gathered with other services businesses in the state so they can continue to learn and benefit from the experiences of these five companies.
- Identify continued funding to conduct a second stage of pilot company support. This work would take the companies through an even more detailed strategy session based on the work that has already taken place.
- Identify resources within the state and grant opportunities to support additional pilot projects.
- Dedicate staff to seek out pilot opportunities, oversee their execution, share lessons learned, and track long-term benefits received by participants.
- Based on findings from the initial pilot and any follow-up, design programs that bring needed expertise to defense contractors on a regular basis. The Back Streets Boston initiative (see box), while aimed at manufacturing and industrial companies, is an example of a program that delivers tailored expertise at regular intervals in locations that facilitate access for small- and medium-sized establishments.

### BACK STREETS BOSTON

Launched by former mayor Thomas Menino in 2001, Back Streets Boston provides support services for the more than 4,000 small and mid-size light industrial and commercial businesses operating within the city's boundaries. Housed in the Boston Redevelopment Authority, the Back Streets program offers services to protect industrial land through planning and zoning, identify opportunities for industrial expansion and development, identify transit and infrastructure improvements, and identify public realm improvements. Program staff recently started holding office hours in three of the city's major industrial areas to make it easier for businesses to access these services.

## STRATEGY: HELP IDENTIFY NEW MARKETS AND CUSTOMERS

For businesses, potential responses to defense industry downsizing are essentially focused on some combination of finding new markets or securing new customers. Either approach touches on a variety of programs and services such as export promotion, procurement, technology commercialization, process improvement, and skills training. For service companies, two areas are emphasized: international trade and procurement.

**OBSERVATION [INTERNATIONAL TRADE]:** Pilot company participants were asked about their experience with international customers and if any of them had considered foreign markets as an options or opportunity. None of the companies had an active effort in searching for international business and previous experience with international customers was minimal.

### RECOMMENDATION [INTERNATIONAL TRADE]:

International business and trade opportunities for services companies can be limited depending on the type of service provided and the level of expertise within the company. However, where appropriate, they can provide an important opportunity for diversifying a company's revenue base. Exploring these avenues of untapped business should be a focus of the industry adjustment strategy. Commerce has a very successful and long-standing international trade division. This group should be leveraged to benefit services firms in the military and defense sector in multiple ways, including:

- Directing the international trade division staff to educate defense services firms about how to conduct business with international companies to diversify their customer base one-on-one and in seminar/workshop settings.
- Supporting an international trade mission specifically for Washington's military and defense sector targeting countries and trade shows where products and services would be best received.
- Building expertise in the international trade division on specific international requirements in military and defense goods and services (e.g. ITAR), so they can be a resources on this topic to Washington State companies.
- Obtaining support for expanding Commerce's trade activities using Virginia's Going Global Defense Initiative as a model. (See box.)

**OBSERVATION [PROCUREMENT]:** Service sector firms in the state that work with the military and defense sector benefit greatly from the existing technical assistance programs provided by Commerce through the OEA grant. The staff that runs these programs has a strong business network and the efforts are well regarded. The state's program is designed to work in concert with the Washington State Procurement Technical Assistance Center (PTAC) and help mitigate gaps in PTAC coverage in the Seattle area. (The closest PTAC offices outside of Seattle are in the cities of Everett and Kent).

**RECOMMENDATION [PROCUREMENT]:** The technical assistance that has been provided through Commerce in the military and defense sector should continue and expand, and stay in alignment with the efforts of the PTAC program.

- A dedicated staff member has been funded under the OEA grant. This position should continue to be supported by other resources after grant funding expires. The budget should also be increased to include additional staff.
- The military and defense sector program should coordinate and manage future pilot programs and workshops/education events that have been listed in this document.
- Continue the partnership with PTAC to serve companies with technical support needs.

### GOING GLOBAL DEFENSE INITIATIVE

Virginia's Going Global Defense Initiative (GGDI) helps the state's defense-related companies diversify into new international markets. Now in its third year of federal funding, the program has assisted more than 300 companies, with 230 companies finding new international customers in the program's first two years of operation. GGDI offers a range of technical assistance, including market research, export training seminars and videos, and website translation and search engine optimization services to help participants target foreign markets. In addition, the program assists firms with export compliance, including guidance on completing a Commodities Jurisdiction Analysis and submitting the required paperwork to the Department of State in compliance with International Traffic in Arms Regulations (ITAR). GGDI is housed within the Virginia Economic Development Partnership's International Trade Program, which features a staff of 20 and global representation in more than 50 countries.

### STRATEGY: SUPPORT TRAINING NEEDS

**OBSERVATION:** In service companies, such as those included in the pilot program, capabilities are often centered in the knowledge and skills of their employees along with the tools that employees use. Accordingly, company recruiting, training, and human performance management are often critical to success. A lack of business development expertise, generally and with regard to the commercial market, was identified as a common issue.

**RECOMMENDATION:** A dedicated business development effort is at the core of any diversification strategy. Helping defense services firms strengthen this function should be a priority. While Commerce could play an important role in this aspect of the diversification strategy, relevant industry associations, military, and defense support organizations should be leveraged to expand the effort's reach. Examples of approaches for addressing this issue could include:

- Helping connect firms with the appropriate expertise, including public organizations and private firms that can help build in-house capacity in marketing and procurement activities, as well as traditional business channels (such as chambers and trade associations).
- Hosting training events (seminars, workshops, webinars) focused on business development tools and techniques in the commercial market.
- Coordinating the work of the Commerce Sector Lead Program to identify opportunities for defense contractors to diversify into the commercial market within the target industries. Based on this work, conduct trade shows to help firms access commercial markets in relevant industry sectors.
- Communicating to firms the importance of building in-house expertise and a creating a business-development-focused culture among all personnel.

### STRATEGY: PLAN FOR LONG-TERM SUPPORT AND OUTREACH

**OBSERVATION:** Significant lessons and themes were identified during the pilot program. This information has been incredibly valuable to the pilot companies that participated in the program but in isolation will only benefit the individual company. The take-aways of this program must be shared to the broader community of service businesses supporting the military and defense sector across the state to meet the ultimate intention of the pilot program.

**RECOMMENDATION:** A dedicated, organized, and ongoing effort to share best practices, resources, and lessons learned from this pilot program, other pilot programs that have been completed under the overall OEA grant, and future pilot projects is essential to supporting and diversifying the customer base of businesses that are dependent on the military and defense sector.

Several mechanisms for transmitting this information have been identified and described in detail below. It is important to note that much of this work will be conducted by Commerce's military and defense sector program as well as the Washington Military Alliance; but the work to effectively broadcast and share the information will require the engagement of a network of organizations throughout the state.

## STRATEGIC ASSESSMENT OF DEFENSE SECTOR SERVICE COMPANIES

- Military and Defense Services Industry Diversification Summit. Commerce, in partnership with the WMA, should host an annual military and defense summit. This event will provide a forum for business experts to present the latest in management consulting expertise so that services businesses can consider new approaches to their business plans and operations. In addition, this event should promote and highlight the valuable set of organizations and initiatives in the state that are available to these businesses to support their ongoing success in diversification.
- No-cost webinars. Commerce should host a no-cost series of webinars to build the skills and assist in the diversification of services providers. Topics would include business development, marketing, human resources and training, financing, and lean management processes. The content and presentations would be prepared and given by partner organizations, such as those identified in the Resources Roadmap. (See Appendix A for additional information about the Roadmap.
- Public Sector/Large Institution Services Contracting Forum. Commerce and the WMA should hold a Public Sector/Large Institution Services Contracting Forum. This event would bring together multiple large private and public sector institutions (e.g. county governments, city governments, hospitals, manufacturers, colleges, and universities) that require service contracts and those service firms that depend on the military and defense sector. The forum would be an opportunity for the large institutions to inform services companies about what is required to work with them and secure contracts as well as introduce the large institutions to services companies across the state.

## APPENDIX A: PILOT COMPANY CASE STUDIES

### PILOT COMPANY A | *Software & Logistics*



The company, a software and logistics firm, expects revenue to be flat over the forecast period, but its owner has mandated a doubling of company profit.

The legacy business, upon which the company was founded, is heavily dependent on DOD spending for maintenance support, particularly by the US Navy. A prior effort at strategic diversification led to the development of a business unit focused on software development and IT that has had success in federal civilian contracts. The software/IT business unit has grown to constitute about 75 percent of company revenue.

The company has been particularly affected by disruptions in the federal budget process, including shutdown, sequester, and delays in federal RFP releases and awards. The competitive environment is made more difficult by larger contractors pursuing smaller business and the requirement that company offices be collocated with DOD facilities.

The company maintains a start-up attitude despite having a business track record of more than three decades. Efforts at diversification through business development have considered many alternatives, but historically, the selection of opportunities has been lacking. One participant noted that the company “has a pathological inability to say ‘no,’” frequently considering alternatives that are costly in time, resources, and management attention.

Company beliefs and values, shaped by its founder, focus on customers, employees, and delivering value. When downsizing was required due to the loss of a contract, senior leaders received employee feedback on the process that “you did it the right way.”

Company leaders chose a three-year strategic horizon.

The company’s current product and service scope is largely defined as the legacy business, the emergence of the software development business, and the lack of success in prior business development initiatives.

The current company market/customer scope is largely defined by the legacy business and its success in pursuit of particular civilian government and commercial RFPs in which it was able to demonstrate its value offering.

The focus of the company product-service/market emphasis and mix is divided among continued development of the legacy DOD business, expansion into federal civilian agencies, and development of commercial opportunities.

Looking ahead, the top management team sees the need to invest in key capabilities related to business development, governance, project management, and recruiting. To gauge its strategic progress with leading indicators, the company will track non-DOD contracts, the run rate of proposals, mean time between existing customer contacts, the increase in direct FTE, and new hire referrals.

To address strategic critical issues at the top management level, Company A articulated projects aimed at clearly defining the company governance structure, improving the federal and commercial business development process, refining product-service and/or market priorities (including reviews with top stakeholders), developing required staff



capabilities, and establishing a process for tracking and reporting leading strategic indicators. Each of these critical issue projects will be led by a member of the top management team and will be reviewed periodically at meetings of senior management.

### PILOT COMPANY B | *Marine Engineering & Services*



After a marked decline in revenue over the past three years, Company B, a marine engineering and services firm, forecasts a 30 percent increase in revenue and a significant increase in profit. In the course of the revenue reductions, the company selected some projects to keep people working even if at a low profit.

Company revenue has been adversely affected by reductions in spending by key federal clients, a change in GSA contracting procedures, instability in the federal budget, and increasing complexity in the federal procurement process. With some competitors consolidating, the company sees the need to better differentiate itself. Tightening industry and regulatory standards are expected worldwide.

Poor performance by key personnel, weak internal strategic decision-making, and inadequate cost management during the recession are continuing causes of concern. Whereas the company has a long business history working successfully with the federal government, there is internal concern about unclear direction and different styles of project management.

Basic company beliefs and values are focused on customers, building long-term relationships with stakeholders, and building knowledge to support innovation. The company selected a five-year strategic horizon.

The company product-service scope is defined largely by its legacy business and success in specialized applications/structures. Its market scope is defined by its existing set of mainly prime customers; excludes largely unknown, smaller scale entities; and confines its activities to the United States.

The desired thrust for new business includes providing a single product/service to multiple customers and providing multiple products/services to multiple customers. One participant noted that the company had taken on many types of projects in the past, without sufficient focus.

The company articulated a large number of possible product-service/market possibilities going forward, in keeping with its previous history and emerging possibilities. After further review, it was determined that the company should prioritize optimizing its contract with a large customer and deploy current capabilities in existing and new markets.

In reviewing which of its capabilities to advance, the company placed its priority on improving sales, developing consistent project management methods, and advancing R&D into new technologies.

Top management at the company determined that the strategic critical issues it should address include developing a strategy for retaining its large existing contract, replacing key staff, integrating marketing and sales in the company budget, and developing two new product/market pursuit strategies. Each of these projects will be led by a member of the top management team and progress will be reviewed at senior management meetings.

### PILOT COMPANY C | *Safety Training & Consulting*



Loss of a major contract cut the revenues of the company, an ocean safety training and consulting firm, by more than half, requiring a staffing decrease and placing increased pressure on overhead expenses.

The company's core commercial service operates near break-even, putting future company viability at risk. Advisory services have not yet been firmly established as a substantial source of revenue, whether for commercial clients or in litigation support.

The company helps clients, including US military services, commercial entities, and individuals, meet safety requirements set by a branch of the federal government. It has seen increasing competition, in both direct and indirect (online) forms. In addition to loss of a federal contract, the company has been adversely affected by the slump in the oil and gas industry.

The company seeks to serve its mission by employing highly competent people, with delivery of some services requiring as many as eight different skilled practitioners. The staffing decrease, aging of incumbent staff, and reduced availability of appropriate new hires has strained the ability of the company to meet client schedules at acceptable levels of revenue and profit.

The company emphasizes a strong set of basic beliefs and values focused on helping its customers operate safely in risky environments through enhanced capability and competence. The company believes that its character and values are communicated through the experience of customers, resulting in a strong, earned reputation in its field.

For the purposes of considering future strategy, the company chose a relatively short, one- to two-year horizon. This reflects the significant challenges that must be overcome in the short term to ensure future viability.

The current company product-service scope is heavily influenced by the loss of its major government contract, with the remaining services less able to support needed staff and other overhead. The core service is staffed as noted above, with advisory services heavily dependent on the knowledge, skills, and availability of the company founder.

The company customer/market scope is defined primarily by commercial and government segments at significant scale on the West Coast of the United States. The company does not pursue some smaller scale markets or opportunities on the East Coast and Gulf Coast, but sees the possibility for worldwide expansion in a particular segment.

In its thrust for new business, the company has attempted to balance its unique technical capabilities, deep understanding of its customer base, and value-adding differentiation with ensuring it is a low-cost provider. Looking forward, the company hopes to be able to provide multiple services to multiple customers

In considering its future product/market emphasis and mix, the company is aware that the largest part of its offering depends on helping customers meet the requirements of a branch of the US government. It is the company's intention to enhance the core offering as more organized demand for its safety programs emerges in a consolidating segment and as it pursues increased emphasis on customer-tailored training.

## STRATEGIC ASSESSMENT OF DEFENSE SECTOR SERVICE COMPANIES

To support its strategy, the company will focus its key capability investments on marketing and sales, as well as developing its pipeline of key human resources to deliver its core service.

The company will implement a mechanism for tracking capacity enrollments one month in advance of the start of each course and the number of sales opportunities (“at bats”) for its key service as leading indicators of strategic success. The company uses year-over-year revenue growth and profit as a percent of revenue as overall financial measures.

At the senior management level of critical strategic issues, the company decided to focus on developing projects to improve the hiring pipeline of qualified people, improve its approach to customer service, develop a strategy of increased loading of its key service, and increase the number of business development opportunities. Leadership of each of these is assigned to a member of the top management team and will be followed up regularly.

### PILOT COMPANY D | *Construction & Design Build*



Company D, a construction and design build firm, forecast its revenue to double through the end of 2016, along with a continued trend of increasing profit. This follows a doubling of revenue over the previous period, during which the company shifted its focus to the federal construction market.

Facing “graduation” from the Small Business Administration 8(a) loan program, the company is aware that it must advance a sustainable approach to developing business opportunities. The company is cautious about managing its growth, given its bonding limits, the availability of experienced people, and what it views as its optimal project size and location. Cash flow, a concern in the past, has come under more effective control.

The company sees a number of factors affecting its external environment. These include: 1) increasing material and labor costs, 2) fewer sole source projects, 3) the potential for state and local work to be more competitive than federal contracts, 4) the commercial market being very different from its current market and 5) the potential to compete against competitors bidding at cost. The company believes it has little visibility outside of its existing market segments and must work to build its brand, but the company sees more growth in segments it does not believe it can effectively serve at present.

In considering its internal environment, the company believes it could become more effective pursuing work outside its existing comfort zone and obtaining repeat work based on good performance. In a growing market, it is challenged to manage travel and per diem costs, find qualified workers, and recruit competent general managers that fit the company culture at an acceptable cost.

The company’s basic beliefs and values are focused on a culture supportive of clients and employees, delivering solutions done right the first time, and persistence. The company emphasizes good communications, externally and internally, with a commitment to integrity in everything it does.

Company D established its strategic horizon as three years, corresponding to its graduation from the SBA 8(a) program.

## STRATEGIC ASSESSMENT OF DEFENSE SECTOR SERVICE COMPANIES

The company defines its current product-service scope largely by the capabilities it deploys in federal projects. Its intended customer/market scope includes federal government, general contractors, walk in traffic, and local business and municipalities, while excluding state and residential projects. Its geographic scope is limited to the states of Washington, Oregon, Montana, and California.

The desired thrust for new business for the company is providing multiple services to multiple customers.

The company anticipates that its product/market mix and priorities will be driven by increasing existing services to two key market segments. It will review several other possibilities based on past and possible future performance, seeking to ensure that each opportunity is consistently reviewed with rigor.

To advance the key capabilities required to advance its strategy, the company will place continuing emphasis on developing internal and external communication, selecting strategic partnerships, [verb] project management excellence, and improving estimating and contract management methods.

To measure strategic progress, the company will track improved marketing capability, its ability to better understand customer needs/purchasing behavior, sales activity, and talent acquisition.

The company team determined that the critical issues the company must address are developing a short-term staffing plan, developing the strategic measures described above and implementing a tracking/reporting process, creating and implementing a non-federal business development process, clarifying its product/market priorities, and defining its market strategy. Each of these is assigned as a project for members of the top management team, with ongoing progress reporting toward their completion no later than the end of 2016.

### PILOT COMPANY E | *IT & Logistics Support*



Company E, an IT and logistics support firm, expects a recent sharp increase in revenue and profit to stabilize, with contraction or leveling in future years. It is targeting a 5-10% revenue increase in future years. The company is one subsidiary of a complex holding company, with slightly more than 10% of its revenue derived from Washington State.

In its external environment, the company sees shrinking government budgets, contract consolidation, and the labor market becoming very competitive for key people. As a relatively small entity, the company believes it must align with prime contractors, particularly where low price is a requirement for success.

In reviewing its internal environment, the company believes it has strengths as a flat organization with good processes and little bureaucracy and enjoys a high level of trust and self-management. It views its weaknesses as 1) difficulty in targeting resources on high-value opportunities, 2) the requirement to absorb corporate overhead, 3) the absence of an overall corporate strategy and the need for a better definition of company strategy, and 4) little sharing of knowledge across the corporation.

The company's basic beliefs and values are focused on broad shareholder interest over the long term, advanced career opportunities for community members, and a commitment to effective contract execution. The company chose a five-year strategic horizon.

## STRATEGIC ASSESSMENT OF DEFENSE SECTOR SERVICE COMPANIES

The current company product-service scope is defined by service capabilities in IT, logistics, repair/maintenance, and administrative support. The company product-service scope excludes other lower-value services and specific products.

The current company customer-market scope consists primarily of federal defense and civilian agencies. The scope excludes non-federal customers, with geographic markets determined by location of existing offices and facilities.

The desired thrust for new business for the company is multiple products/services to multiple customers. It believes it should not attempt to be the lowest cost provider or value differentiator.

The highest product/market emphasis and mix priorities for the company are focused on delivering existing services to existing customers. The company also anticipates expanding into other extended markets by introducing existing services. The company will explore some other possibilities and accept some business opportunistically (with no active pursuit.)

In an effort to carry its strategy forward, the company intends to expand its business development capabilities. Specific investments include obtaining better knowledge of end-user needs and contracting requirements, pursuing targeted (buyer-specific) business development hiring, increasing software development capabilities, and developing internal software tools.

To measure its strategic progress with leading indicators, the company will track the number of prime contractor relationships, win rates within its sales funnel, and the stability of its backlog.

The company determined that the projects it must complete to address its strategic critical issues are: creation of business development process and metrics, establishment of monthly strategic management cycle, improvement of "bid/no bid" decision process, development of enterprise knowledge sharing process, continuance of business strategy process with senior team; and acquisition of talent for senior business development positions. Each of these is to be led by a member of the top management team, and all are to be completed no later than the middle of October 2016.

## APPENDIX B: ABOUT THE RESOURCE ROAD MAP

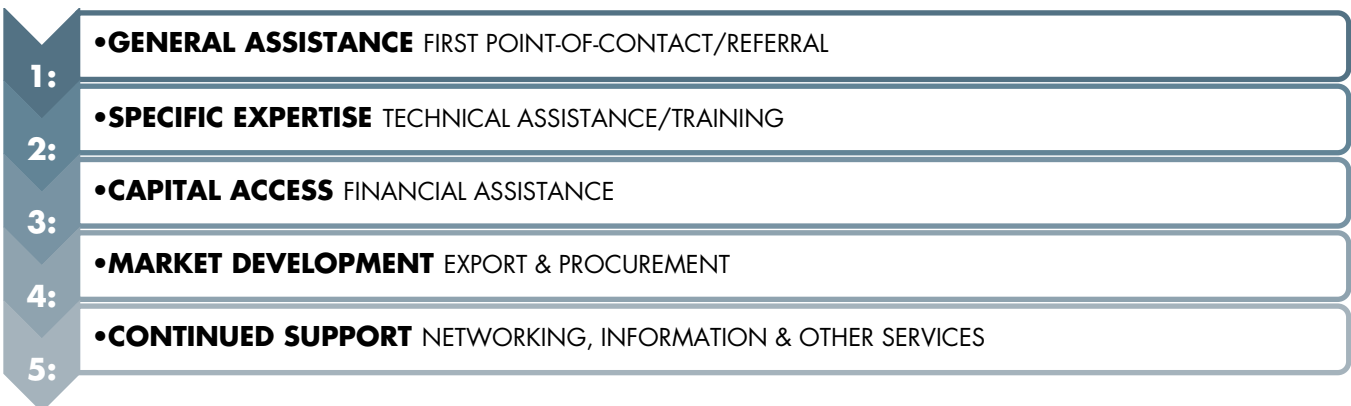
As part of this work, TIP Strategies provided a Resource Roadmap. This business tool, published under separate cover, represents a compilation of available resources to support contractors within the Washington State military and defense sector. These resources are based on the findings, identified needs, and best practices captured during the pilot project, which assessed five Washington defense services supply chain contractors’ tolerance to potential reductions in defense spending.

The Roadmap is intended to provide guidance, document the available support system, and assist in developing a diversification strategy for similar contractors across the state that are heavily dependent on defense spending—ultimately in an effort to mitigate their exposure to federal budget reductions. Resources included in the document represent a comprehensive collection of the tools and programs most relevant to military and defense services supply chain companies. The focus of this effort was on compiling resources offered at the local, regional, or state level; however, in some cases, pertinent national-level organizations are also included.

The Roadmap is organized by resource type as defined by the five categories outlined below. For each organization, the document provides contact information and a “clickable” link to their website.

1. **FIRST POINT-OF-CONTACT/REFERRAL:** These organizations represent important points-of-contact for referral to various business assistance and may also provide direct counsel on a variety of business-oriented topics at little or no cost to the client. Most organizations offer varying combinations of programs and services including but not limited to business retention and expansion, workforce enhancement, entrepreneurial development, incentives, financial assistance, research, data, and site selection. For this resource type, the focus was on identifying the “front door” for assistance. At the local level, Associate Development Organizations (ADOs) are listed as the primary starting point given their lead role in economic development. Other local-level economic development organizations are highlighted in later sections. At the state level, emphasis was placed on identifying agencies that play essential business support roles. Finally, a number of nonprofit organizations, including trade and professional associations, also provide a good foundation for understanding available resources.

FIGURE 14. ROADMAP OVERVIEW



## STRATEGIC ASSESSMENT OF DEFENSE SECTOR SERVICE COMPANIES

- 2. TECHNICAL ASSISTANCE/TRAINING:** Organizations in this category provide in-depth one-on-one or group advisement, training, and/or coaching on specific topics including but not limited to: strategic planning, operations, accounting, sales, and marketing. These are usually provided at little or no cost to the participant. Included in this group are entrepreneurship initiatives (including business incubator and accelerator services), small business development centers (SBDCs), and various business coaching organizations.
- 3. FINANCIAL ASSISTANCE:** These organizations provide guidance on available funding sources, assistance in applying for and obtaining funding, and/or direct funding for qualifying projects and/or companies. Select organizations also offer mentoring and coaching as a part of their services. US Small Business Administration loan programs are a key component of these services.
- 4. EXPORT & PROCUREMENT:** This category includes organizations that help businesses access new markets and customers. Procurement-related resources assist companies doing business within the government marketplace, including but not limited to: applying for and fulfilling government contracts, determining government products and service needs, bidding, marketing and other services. The state's network of Procurement Technical Assistance Centers (PTACs), which offer an array of technical assistance services specific to government contracting, comprise the majority of programs in this category. Export-related resources help companies market and sell their products internationally. These programs are typically government-funded and include activities undertaken by Commerce and the US Small Business Administration.
- 5. NETWORKING, INFORMATION, & OTHER:** This category captures organizations that facilitate access to professional networking opportunities (such as chambers of commerce) and/or economic and demographic data (such as regional planning organizations). It also serves as a catchall for any additional resources not classifiable elsewhere. Given the large number of chambers of commerce in the state, these organizations are integrated into the Roadmap via a directory maintained by the Commerce executives.