

**Outline of Secretary Winter's Remarks to Bear Sterns Defense and Aerospace Conference**  
**31 May 2006**  
**Ritz Carlton, Arlington, VA**

Challenges in running the Department of the Navy

- **The challenge of executing today's operations while preparing for the future.**
  - o Today, we are involved in a long war, the war on terror, a war we cannot lose
  - o Future is very uncertain – need to prepare for a wide spectrum of scenarios
- **This requires a broad naval transformation – so broad that it is changing our relationship with the industrial base.**

History

- **Industry has been with us through other periods of change**
  - o **Those who changed with us did well**
  - o During WWII the Nation needed responsive production
    - Industry accepted a shift from commercial to defense production
    - Industry was production oriented; government role was development focused
      - Industry produced: Combatants, Liberty Ships, B-17s and 29s, tanks
      - Government development included: Radar, sonar, proximity fuses
    - Numbers counted in this war of attrition
    - We targeted production, transportation, and access to raw materials
  - o Cold War activity was a major change from WWII: industry emphasis shifted from production to system development
    - SLBMs, nuclear powered aircraft carriers, Aegis, etc. were capabilities that largely came out of industry
      - Nuclear weapons were one of the few examples that did not transition to industry
    - Industry learned to make its money on system development
  - o The end of the Cold War further accelerated the movement from quantity production as the expectations of a “peace dividend” eroded our investment accounts
  - o Transformation of the DoD started with this administration, before 9-11, is likely to be accelerated, both by GWOT and budget pressure and will have a significant impact on industry.

## Trends and transformation

- This is **not the first time we have transformed**
  - o Examples of previous transformations include the transformation from Battleship centric fleets to Carrier Based Aviation focused fleets; the transformation from conventional to nuclear powered submarines; the introductions of Submarine Launched Ballistic Missiles and Tomahawk Cruise Missiles; and use of GPS.
- **Our emphasis is force transformation**
  - o **Hardware transformation is only a means to that end**
  - o **Industry is understandably focused on delivering the hardware aspect of transformation**
  - o An example: We are in the midst of transforming the fleet from a “Blue Water” centric force to one which can fight and win in Blue, Green and Brown waters. This requires us to develop new capabilities to address the Green and Brown water challenges. It requires us to invest in Riverine forces and the LCS.
    - Much of the focus is on LCS – the hardware part of the transformation
    - The Department has a much broader challenge of transforming personnel systems, sensors, weapons, CONOPS and IT systems for this new regime.
  - o Another example: The Marine Corps is well into the process of transforming to distributed operations.
    - The industry hardware play in this transformation will focus initially around MV-22
    - But the transformation is much larger than hardware; we are well on our way to executing distributed operations in Iraq and Afghanistan, well before we deploy MV-22
- **Again, the transformation is much larger than hardware. At the end of this transformation, we will have fewer systems, smaller quantities, but much more capability when compared to the latter part of the last century**

The forcing function: Looming budget pressures

- **The budget will continue to get tighter; the amount available for procurement will get tighter; we must deal with real cost issues**
- More and more of the DoD budget is going into personnel and O&M. This will continue after GWOT further pressurizing investment accounts.
- Today, much of the acquisition program funding is focused on recapitalization of the fleet in the wake of the hiatus taken after the build up in the 1980s and the drawdown in the wake of the peace dividend.

**What needs to happen to accommodate transformation?**

- **What are the implications of transformation on industry in the current budget environment?**
  - o **Four themes hardware producers need to accommodate**
    - Systems must be capable of supporting the transformation mission
      - LCS – shallow water
    - Reduced manning is vital
      - As personnel costs drive total cost, value of reducing crew size achieves similar importance to acquisition system cost reduction
    - Logistics must be simplified
      - Common elements, reduced numbers of models/series
      - JSF example
    - Open Architecture is paramount
      - Allows rapid upgrade of systems to the latest technologies
      - Allow for continuing competition of the best ideas/capabilities

- We cannot repeat the mistakes of the “peace dividend” years
  - o After the Berlin Wall fell, challenge was to fulfill the expectation of the Peace Dividend
    - To accommodate this, cutbacks in investment mandated unachievable reliance on COTS and Dual Use hardware – satellite example
    - Expected cost savings were not realized
  - o Industry consolidation
    - Achieved consolidation but not rationalization of the defense industry
    - Hoped-for savings limited; budget pressure on the system continues
- On the positive side, development of advanced technologies has been a real boon
  - o For example, the advances in micro-electronics and IT-at-large have greatly benefited the community
    - But, this has major implications to DoD and naval system development – we no longer control the pace and focus of developments that are critical to our future success.

Closing thoughts – changes need to be made

- **We want companies to be successful and supported by Wall Street**
- **A different set of business models are required for today’s environment**
  - o There will always be a need for those companies that produce hardware
    - But low rate of production, high performance systems will be the norm
    - Dictates a different approach - need to look for efficiencies beyond economic order quantities
  - o Hardware to software businesses must re-examine their models – It is the responsibility of companies to define the models; we can assist
- **An aligned, concerted effort is required by all players to make this work**
  - o Department of the Navy – stabilize requirements/acquisition
  - o Contractors – increase effectiveness and efficiencies of an acquisition process refocused to high quality, low production rates

## **Consequences of not adapting**

If we don't adapt to this new situation, we will reach a critical point – Winter's corollary to Augustine's principal

- Costs of systems are rapidly increasing
  - The budget squeeze – Zero or negative growth in out year funding
  - Augustine – one plane by 2054

*Law Number XVI: In the year 2054, the entire defense budget will purchase just one aircraft. This aircraft will have to be shared by the Air Force and Navy 3-1/2 days each per week except for leap year, when it will be made available to the Marines for the extra day.*

- If something doesn't give, we will hit one ship well before 2054.