

Charlotte Regional Partnership: Defense Sector

Defense companies hope boon continues

Firms that rely on federal contracts have their fingers crossed

By Cameron Steele, The Charlotte Observer

Saturday, Jul. 25, 2009

Intepoint LLC is an example of how defense contracts can help a company grow.

The Charlotte company makes software that creates a virtual model for how a single event – such as a terrorist attack, power outage or computer virus – can affect a city. Government contracts have helped Intepoint grow from a one-man show in 2003 to a business with 10 employees and counting. More than 90 percent of the company's contracts have been for top secret agencies within the Defense Department.

That government relationship has increased Intepoint's revenue by 25 percent to 30 percent every year since 2003. But Mark Armstrong, Intepoint's chief executive and founder, said those government contracts were all granted under the Bush administration and he doesn't know what to expect in the future.

Despite recent contracts, Charlotte defense companies say they're not sure whether the trend will continue.

The continuing wars in Iraq and Afghanistan have prevented major defense cuts.

As President Obama and Congress finalize the federal budget, companies are keeping their fingers crossed.

“There's going to be a lot of pressure inside the budget; some of the decisions that had been fairly easy ... will now be tough,” said Bill Lennox, senior vice president of Washington operations for Goodrich Corp., a Fortune 500 aerospace company based in Charlotte that makes airplane parts and supplies for the defense and airline industries.

Federal law requires U.S. military supplies to be made in America, giving a boost to domestic plants – from major corporations to small operations – as some commercial manufacturing has migrated to other countries in recent years.

And the recession hasn't left much of a mark on the defense industry, while other Charlotte sectors such as banking have been on the chopping block.

But under priorities outlined in April by Defense Secretary Robert Gates, the Pentagon is focusing more spending on weapons needed to fight the insurgencies it faces in places such as Afghanistan. That means less of an appetite for the big weapons used to fight conventional wars, such as giant warships, expensive fighter jets and hulking Army vehicles. The Pentagon is expected to give further details on its future strategy this summer.

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Defense firms are still trying to figure out the long-term impact of the changes in defense spending.

A target for growth

Defense and security companies have been a target for the Charlotte Regional Partnership, the region's business recruitment group, and for N.C. state officials, who held a meeting in Raleigh this month to push businesses to compete for military and defense contracts to stimulate economic growth. Companies in Charlotte and 16 nearby counties last year secured more than 1,800 contracts with the Defense Department – 200 more than in 2007 and almost four times as many as in 2000 – worth more than \$540 million, according to data from the partnership.

There are 551 defense contractors in Mecklenburg County – from uniform manufacturers to helicopter engine builders to computer software programmers – that have won more than 3,000 government contracts totaling more than \$2.6 billion for the past eight years, according to partnership data.

Obama has set aside about \$534 billion for the 2010 defense budget, which is about 2.1 percent higher than the 2009 budget after inflation. And costs for special-operations programs and the increasing number of the armed forces, which had been paid through supplemental appropriations, will now be included in the regular budget.

David Swenson, partnership vice president, said Charlotte defense companies will flourish because the government will still want to give projects to companies with immediate, skilled labor – such as Goodrich and General Dynamics, which has an armament and technical products division in Charlotte.

But until the 2010 budget is finalized, Intepoint and other defense companies – large and small – operate in limbo, hoping for continued Defense Department business even as the government looks at the bottom line for cost. That's a bigger risk as competition for contracts increases because the supplemental budget will probably be cut, Lennox said.

“We may be in a pretty good position, but then...we may be in trouble because the budget is going to shrink,” said Armstrong, who plans to commercialize his software program if he begins to lose defense contracts.

Watching Washington

The Defense Department issued more than \$3.6 billion in contracts to N.C. companies last year, up 22 percent from 2007. Those deals, though, usually end up somewhere other than Charlotte. In the past eight years, less than 13 percent of contracts won by N.C. and S.C. companies went to Charlotte-area businesses, according to data from the regional partnership.

The partnership is trying to change that as a way to reverse climbing unemployment and office closures that have shaken the area's once-sturdy business foundation.



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“The opportunities are there with defense spending the way it's been for the last number of years,” Swenson said. “Since the recession, (the defense industry) is not less of a priority; it's more.”

This week, Goodrich reported second-quarter revenues of \$177 million – up from just under \$170 million in the first quarter but down 5.1percent from the same period in 2008. The decrease came as sales dipped 8 percent to \$1.7 billion. But defense sales – which make up 27percent of total sales – rose 11 percent.

Lennox said he expects his company to come out on top when the 2010 budget is finalized because it specializes in the areas that Obama has prioritized: helicopter manufacturing and intelligence surveillance reconnaissance, which is a way to discover information about an enemy through passive observation.

Goodrich employs about 400 people in the Charlotte area and has only had to lay off a small number of commercial workers, Lennox said.

General Dynamics' Armament and Technical Products division in Charlotte has also avoided layoffs.

Gail Warner, the senior director of communications for the armament division, said rather than firing people, both Charlotte plants are hiring.

Since January, General Dynamics' armament division has secured more than \$495 million in defense contracts. Most of these are extensions on existing contracts under the Bush administration, but Warner isn't worried about business dropping off when the 2010 final budget comes out. She said General Dynamics plans to adjust its priorities according to what Washington wants.

But for smaller companies such as Intepoint that don't have the funds or manpower to adjust on a dime, the new budget may force them to turn to commercial customers to help fill the void. But without the made-in-America requirement for those contracts, companies would be less immune to the lingering recession. Still, Armstrong thinks Intepoint's software – once designed for commercial use – will help the company to reduce reliance on government business.

Last year, Intepoint secured a contract with Wachovia to help the bank test some of its own computer programs.

“I'm hopeful, because agencies outside the DoD are also beginning to be interested in our software,” Armstrong said.

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