DOD WARNS DEFENCE PRIMES OF HIGH SUPPLIER PROFIT MARGINS

News / Manufacturer

The Pentagon's top acquisition office says first-tier subcontractors' **profit margins** for production programmes are about 7% higher on average than for the prime contractor, and this imbalance could be deterring major suppliers from bidding for new contracts as primes.

The revelation has spurred discussions between the **DOD** and the major primes about better controlling subcontractor prices and ensuring that "profitability is aligned with performance".

According to a new report from the office of acquisition, technology and logistics (AT&L), on average from 2001 to 2015, first-tier subcontract final margins for major **defence** production efforts average 16.3% compared to 9% for the prime contractor.

The margins are more balanced during the development phase, but major suppliers still earn 2.1% more at 8.3% compared to 6.2% for the primes.

The profit imbalance has come as a surprise to some prime contractors, according to acquisition chief Frank Kendall, who discussed the issue with reports after an acquisition forum in Washington

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“In some cases, I would say yes – they are surprised,” he says. “They’re not aware of what’s going on. We have access to data that they don’t necessarily have access to, and we have to protect the monetary nature of that data. We went to lengths in the report that was published yesterday to ensure we didn’t violate any proprietary constraints.”

Kendall says it is the head contractor's responsibility to “get good business deals,” but the department is discussing the issues with each of the primes.

Several important aircraft programmes, such as the Lockheed Martin F-35 and Boeing KC-46A, are about to enter higher rates of production and will likely come across the profit margins issue, but several long-standing production projects such as the Lockheed C-130J and Sikorsky UH-60 might also more closely examine their subcontractor costs.

"I’m engaged in discussions with each of the primes, and showing them the data and giving them the chance to reflect on it and we’ll work that as we go through our contracting processes,” says Kendall.

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