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Auto bankruptcies could weaken defense

Suppliers serve both industries

By Chad Halcom

Bankruptcy restructuring and supplier consolidation for **General Motors Corp**. and **Chrysler L.L.C**. could disrupt the supply chains of some defense contractors — particularly makers of trucks and smaller vehicles, local industry leaders and analysts said.

Up to half of the companies represented in the membership of the **National Defense Industrial Association Michigan** chapter could be automotive suppliers or manufacturers in other industry segments that recently diversified into the defense industry, said Paul Curtis, NDIA-Michigan president.

As of this spring, NDIA-Michigan has 2,016 individual members from at least 70 different companies. That's compared with around 1,600 people from 35-40 different companies two years ago, Curtis estimated.

Most of the new members are suppliers, manufacturers, service industries and specialty companies that recently branched out into defense work, he said.

But since at least a portion of the 1,400-plus GM suppliers and hundreds more doing business with Chrysler likely won't see their contracts carry over to the new companies that emerge from bankruptcy, the question now becomes how many defense contractors' suppliers may be lost.

Kenneth Dalto, president of Farmington Hills-based **Kenneth J. Dalto Associates** and consultant to the automotive supplier industry, said he expects to see significant defense fallout from the GM and Chrysler restructuring.

“Within a year or two after this (restructuring) is complete, probably a third or more of all companies in the manufacturing supply chain are either going to be gone — as in out of business — or they're going to be severely undercapitalized,” he said. “That would have to affect the defense industry to some degree, because there are serious crossovers.”

For their part, Sterling Heights-based **General Dynamics Land Systems** and **BAE**

Systems, which is consolidating the Heavy Brigade Combat Team division of its U.S. Combat Systems in Sterling Heights, both said they expect supply chain fallout to be minimal.

BAE media relations manager Steve Field said the company's senior supply chain managers report “things look good” in terms of few intersections with its own supply chain, but it will continue to monitor the automotive situation.

“BAE Systems has a long and diverse list of suppliers, including many other defense manufacturers,” he said in a statement. “Our company is ... constantly evaluating our suppliers to ensure our continued performance, taking several steps to mitigate risk in our supply chain.”

Karl Oskoian, manager of communications and public affairs for GDLS in Sterling Heights, said the company sees relatively few intersections between its own supply chains and those of GM or Chrysler, and the few places that could be impacted, such as steel production, already have “excess (manufacturing) capacity,” so the company can easily use other sources.

GDLS was formerly Chrysler Defense before Falls Church, Va.-based General Dynamics bought it in 1982. Virtually all steel used in the defense industry production of Mine Resistant Ambush Protected vehicles came from the U.S. operations of **ArcelorMittal S.A**., said Loren Thompson, COO of Arlington, Va.-based **The Lexington Institute** and a defense industry analyst.

Thompson expects to submit an industry article for publication shortly on the importance of strong domestic manufacturing to U.S. national security. He contends that allowing manufacturers to implode could entangle the Department of Defense with foreign companies that acquire the companies' assets.

“There's a reason why the company that makes the Humvee is called AM General,” he said, referring to its previous ownership by the former American Motors Corp. “But Washington hasn't been managed or represented well by people of industry for decades. It's run mainly by lawyers and people who don't really understand this point.”

He adds, however, that he expects defense contractors will see less impact on tanks or other treaded vehicles than on military trucks and wheeled vehicles, which use domestic automotive components. Echoing that point was Arthur Sirilla, associate director of operations for the Tacom Contracting Center at the **U.S. Army Tacom Life Cycle Management Command** in Warren.

“It's kind of going to depend on which products and commodities we buy,” he said. “For tanks and treaded combat vehicles, there's probably not going to be as much overlap.”

Troy-based automotive supplier **ArvinMeritor Inc**. appeared to derive slightly more than 3 percent or $150 million of its roughly $4.8 billion annual sales in its

Commercial Vehicle Systems division. It employs 525 of its roughly 17,000 employees on military vehicle systems — just over 3 percent.

In fact, BAE is a slightly larger consumer of its CVS products than GM, according to an industry report the company prepared last year. ArvinMeritor contributes components to the Family of Medium Tactical Vehicles fleet of military trucks, a group of defense contracts awarded by Tacom.

GM and Chrysler together accounted for about 15 percent of the company's total $7.2 billion in revenue for 2008, according to an industry presentation the company gave last year. But Krista Sohm, senior director of corporate communications at ArvinMeritor, said the company does not expect the OEM bankruptcies to jeopardize its ability to execute defense contracts.

“We anticipate, in particular, that the impact of GM bankruptcy on (commercial vehicle) revenues would be nearly a nonevent,” she said.

Dalto said he expects the heaviest impact would be on companies that are currently straddling the two industries, particularly if they did not push aggressively enough to expand their defense component in years past.

A “golden opportunity” existed during the closing years of the Bush administration that may have passed with the change of administrations and defense priorities, he said — those who started diversifying only recently may be too late to survive the loss of automotive contracts.

But Curtis insists the opportunities to diversity continue.

“It's going to be getting tougher, probably, but there are still plenty of new opportunities there,” he said. “With the (Joint Light Tactical Vehicle) coming, MRAP (ATVs) and other opportunities, there will continue to be contracts awarded and plenty of supplier need.”

But Ed Walker, president and CEO of **W Industries** in Detroit, said his company is fortunate to have diversified into defense five years ago. W Industries, with 400 employees and $82 million in revenue last year, makes shipping container systems to transport automotive components between suppliers and OEMs, as well as structural components of MRAPs and other defense vehicles.

Today, he estimates the automotive sector comprises 15 percent of all sales, compared with 35 percent defense. Ford is his sole automotive customer today, so he faces no exposure from the bankruptcies.

“I think we were very fortunate to have moved over to defense when we did, because it's a very different climate now. A whole lot of automotive suppliers knocking on a lot of prime contractors' doors, that means the prime (defense contractors) have more control over prices,” he said. “It's still a good market, but there's a new kind of pressure on it.”