

Dollar Shift: The Iraq War and the Changing Face of Pentagon Contracting

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It's a bit early to start feeling sorry for Lockheed Martin, Boeing, and Northrop Grumman. The nation's "Big Three" weapons contractors split \$49.7 billion in Pentagon contracts in fiscal year 2004, according to new data from the Department of Defense. But that's a slight decline from the \$50.3 billion the three firms divvied up in FY 2003, a surprising development for a year in which overall Pentagon contracts grew by nearly 10%. The Big Three's share of major Pentagon contracts (defined as all contracts for goods of services worth over \$25,000 each) dropped from 24% in FY 2003 to 21.6% in FY 2004.

Who were the big winners in 2004? The lion's share of the growth in military contracts went to companies involved in supplying the Iraq war in one form or another. For example, despite continuing controversies over cost overruns and questionable accounting practices for its work in Iraq, Halliburton saw its contracts more than double from 2003 to 2004, from \$3.9 billion to \$8 billion (see Tables I and II, below). The company's \$8 billion in awards for 2004 is more than *16 times* the roughly \$500 million in Pentagon awards it received in FY 2002. With Pentagon contracts increasing by roughly \$22 billion overall, this means that almost one out of every five dollars of increased Pentagon contract dollars from 2003 to 2004 went to one company, Halliburton.

A list of the top ten contractors measured by the largest percentage increase in awards from 2003 to 2004 bears out the impact that the war in Iraq -- and to a lesser degree, the war in Afghanistan and increased deployments justified as part of the "global war on terrorism" -- have had on the companies that supply the Pentagon with goods and services. Counting Halliburton, nine of the ten fastest growing firms have clear connections to rebuilding, logistics, or war fighting related to the U.S. occupation of Iraq (see Table II, below).

Fastest Growing Pentagon Contractors:

Despite all of the problems in getting the work done – or perhaps because of it – reconstruction contractors continue to reap huge benefits from their presence in Iraq. In addition to Halliburton, three other rebuilding firms were among the top ten fastest growing Pentagon contractors in 2004: Bechtel (91%), Contrack International (59%), and the Fluor Corporation (58%). Given the chaos that reigns in large parts of the country, some times money isn't enough: Contrack pulled out of Iraq rebuilding work in December 2004, citing high security costs.

Logistics has also been a lucrative specialty. The fastest growing firm, AP Moller Gruppen (up 167% from 2003 to 2004), owns Maersk, a shipping company which has been contracted to run cargo ships to and from the Persian Gulf to carry ammunition and tanks to the region. Another key logistics supplier among the top ten is NV Koninklijke Nederlandsche, a holding company that owns Royal Dutch Shell, a major oil company that supplies fuel to the Pentagon, a commodity that is in higher demand in war-time. Halliburton is actually a "mixed" case, drawing funds from rebuilding and logistics work. A substantial part of Halliburton's revenues flow from its LOGCAP contract with the U.S. Army (Logistics Civil Augmentation Program), a multi-year arrangement which involves supplying meals, building facilities, maintaining vehicles, and generally serving as the Army's "on-call" logistics arm for major overseas deployments.

Firms involved in supplying equipment to U.S. forces in Iraq have also done extremely well. Alliant Tech Lake City, which operates a small arms ammunition facility for the U.S. Army, saw its contracts grow by 157% from 2003 to 2004. Renco, which owns AM General, the producer of Humvees for use in Iraq and around the globe, increased its Pentagon revenue stream by 92%. And Oshkosh truck saw its Department of Defense contracts grow by 57%.

Fastest Growing Contractors by Dollar Amount:

An analysis based on the largest *dollar amounts* of increased contracts shows a slightly different picture, but Iraq-related contractors still dominate. Rebuilding/logistics firms Halliburton, Bechtel, and Royal Dutch Shell come in at numbers one, three and seven on the list, while equipment suppliers Renco and Oshkosh Truck are sixth and ninth, respectively. General Dynamics, which comes in second measured in increased contracts by dollar amounts, is a major military vehicle producer as a result of its role in producing the M-1 tank.

Air Transport, Health Care Companies Thrive:

Two other categories of firms that have benefited from a combination of the Pentagon's growing interest in privatization and the needs of a wartime military are air transport firms and health care companies. North American Airlines (\$961 million) and Fedex (\$953 million) each garnered almost \$1 billion in Pentagon awards in FY 2004 for transporting goods and personnel for the military; and three health care firms, Humana

(\$2.4 billion), Health Net (\$1.9 billion), and Triwest Health Care Associates (\$1.3 billion) were among the Pentagon's top 25 contractors for 2004.

Long-term Occupation Will Force Tradeoffs Within the Pentagon Budget:

One of the largest line items in the \$82 billion supplemental package that President Bush forwarded to Capitol Hill on February 14th is "\$12 billion to repair or replace tanks, helicopters, or other weaponry damaged or destroyed in Iraq" (Eric Schmitt, "Bush Seeks \$81.9 Billion, Mostly for Forces in Iraq," New York Times, February 15, 2005). This is a hefty sum, particularly during a year when the Pentagon's regular procurement budget is being held flat, at \$78 billion. If the U.S. occupation of Iraq continues for several more years at anything approaching current force levels, it could force tradeoffs within the Pentagon budget. It would not be a "guns versus guns" tradeoff per se, but rather "guns versus occupation," with big ticket weapons system with little relevance to current conflicts feeling the greatest budget pressure. This tradeoff would add steam to the commitment made in an internal Pentagon memo earlier this year which called for "stretchouts" or early termination of programs like the F-22 combat aircraft, the C-130J transport plane, the V-22 Osprey, and the Virginia-class submarine.

At a time when there is little "give" on the domestic side of the budget, these battles within the Pentagon budget could be joined quite sharply. Simply separating war costs from the regular Pentagon budget in "emergency" supplemental appropriations will not be enough to hold off the tradeoffs to come, given the larger budgetary context. With budget deficits running at over \$400 billion per year, not counting the costs of the President's plan for the partial privatization of Social Security or the burgeoning costs of the Medicare prescription drug plan, there will be little room for maneuver within the overall federal budget.

Don't expect Lockheed Martin and Boeing to start lobbying for an early exit from Iraq any time soon, but, contrary to the popular myth that war -- in any form -- is uniformly positive for the arms industry, a prolonged stay could hurt the interests of manufacturers of big ticket systems in favor of companies involved in logistics, rebuilding, and equipment supplies directly related to sustaining the occupation of Iraq. Ironically, this could bring the Pentagon spending debate full circle.

The Bush administration took office promising to revamp U.S. strategy and discard weapons that were “Cold War relics” with no clear mission with respect to the new security threats on the horizon, but the surge in support for military spending in the wake of the 9/11 attacks allowed the administration and the Congress to postpone those choices for the most part.

The growing friction between war costs and big ticket procurement offers an opportunity to revisit that discussion and make sure that the Pentagon is buying only weapons that are efficient, effective, and necessary for a period when catastrophic terrorism and the spread of nuclear weapons are the two biggest threats facing the nation and the world.

TABLE I
TOP TEN PENTAGON CONTRACTORS 2004
(Dollars in Millions)

RANK 2004	COMPANY NAME	2003	2004	% INCREASE
1	Lockheed Martin Corporation	21,900	20,700	-5%
2	Boeing Company	17,300	17,100	-1%
3	Northrop Grumman Corporation	11,100	11,900	7%
4	General Dynamics Corporation	8,200	9,600	17%
5	Raytheon Company	7,900	8,500	7%
6	Halliburton Company	3,900	8,000	105%
7	United Technologies Corporation	4,500	5,100	13%
8	Science Applications International Corp.	2,600	2,500	-3%
9	Computer Sciences Corporation	2,500	2,400	-4%
10	Humana Inc. ¹	2,400	2,400	0%

TABLE II
TOP TEN PENTAGON CONTRACTORS WITH THE
LARGEST PERCENTAGE INCREASES
(Dollars in Millions)

COMPANY NAME	2003	2004	PERCENTAGE INCREASE
AP Moller Gruppen ²	2,389	6,387	167%
Alliant Lake City, Small Caliber ³	271	428	157%
Halliburton	3,920	7,996	103%
Electronic Data Systems Corp	772	1,538	99%
NV Koninklijke Nederlandsche ⁴	545	1,070	96%
Renco Group ⁵	575	1,107	92%
Bechtel	910	1,742	91%
Contrack International, Inc. ⁶	206	329	59%
Flour Corporation ⁷	347	549	58%
Oshkosh Truck	649	1,024	57%

TABLE III
TOP TEN PENTAGON CONTRACTORS WITH THE LARGEST DOLLAR
INCREASES
(Dollars in Millions)

COMPANY NAME	2003	2004	AMOUNT INCREASE
Halliburton	3,930	7,996	4,076
General Dynamics	8,235	9,563	1,328
Bechtel	910	1,742	831
Electronic Data Systems, Inc	772	1,538	766
Raytheon	7,915	8,472	557
Renco Group	575	1,107	532
NV Koninklijke Nederlandsche	545	1,070	525
United Technologies Corp	4,547	5,056	509
Oshkosh Truck ⁸	649	1,024	375
ITT Industries, Inc.	1,234	1,539	305

Sources:

“100 Companies Receiving The Largest Dollar Volume Of Prime Contract Awards - Fiscal Year 2004,” <http://www.dior.whs.mil/peidhome/procstat/p01/fy2004/top100.htm> and “100 Companies Receiving The Largest Dollar Volume Of Prime Contract Awards - Fiscal Year 2003,” <http://www.dior.whs.mil/peidhome/procstat/p01/fy2003/top100.htm> and analysis by the authors.

¹ A Louisville, Kentucky-based company contracted with the Department of Defense to provide healthcare to military personnel based in the southern United States and Puerto Rico.

² Owns Maersk Lines, a shipping company contracted by the Department of Defense to operate eight cargo ships capable of carrying ammunition and tanks into the Persian Gulf in August 2002.

³ This Army-owned company is operated by Alliant Techsystems, and is the only entity in the United States capable of producing a large volume of small-caliber ammunition. (*National Defense Magazine*, September 2004).

⁴ Owns Shell Petroleum.

⁵ Owns AM General LLC of South Bend, Ind., which makes the Army’s Humvees.

⁶ In December 2004, Contrack International Inc. pulled out of reconstruction efforts in Iraq, after winning twelve major reconstruction contracts, including one to help rebuild transportation in Iraq, citing rising costs of security.

⁷ Reconstruction contractor.

⁸ Builds military trucks.