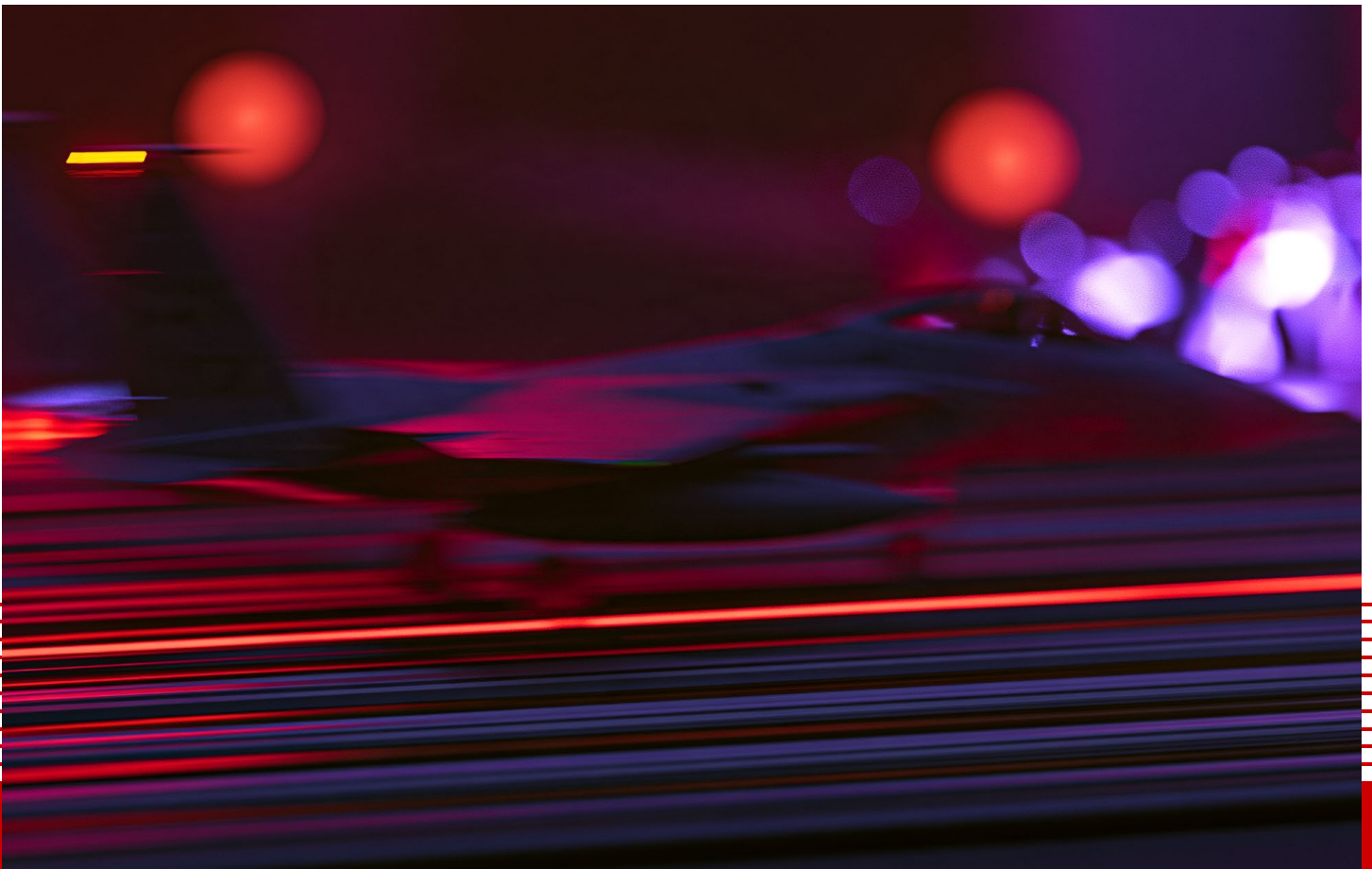




The State of Investment in Defense: Unlocking Growth

Executive Summary

By Michael Sion and Colin Leslie



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The State of Investment in Defense: Unlocking Growth

The United States operates the world's largest and most advanced defense sector. It supports an exceptionally capable military, produces nearly half of global defense exports,¹ and received almost \$900bn in government funding in 2025.² But the environment has changed: Global threats are growing,³ the gap between US defense requirements and budgets is accelerating, and demand for both conventional systems and new lower-cost capabilities is surging.⁴ Current acquisition, business, and investment models are increasingly out of step with security requirements.

Private sector investment is central to solving these challenges. Expanding production and driving rapid innovation require sustained investment—but key pockets of the defense sector struggle to attract it. It's not an overall shortage of capital, but a shortage of investable opportunities.

Barriers prevent capital from reaching areas that matter most: replenishing depleted stockpiles and moving new technologies from prototype to the field. Mixed market signals, capped returns, and risk aversion leave critical investments unrealized: unbuilt factories, unscaled technologies, and constrained supply chains.

In response to these challenges, the Aerospace Industries Association (AIA) asked Bain & Company to survey the current landscape, interview defense industrial base stakeholders, and seek views on ways to increase the private-investment levels needed to meet future security needs.

A health check for the defense investment ecosystem

Capital is not scarce in aggregate, and there is positive momentum. Across 50 interviews, investors, executives, and government leaders agreed: Defense is becoming more attractive for private investment. Strengthened demand signals, the need to replenish stockpiles, and the potential for acquisition reforms have spurred growing capital inflows⁵ and higher defense-company valuations and capital expenditures.⁶

Yet these trends do not represent structural change. Government defense spending, adjusted for inflation, has been flat since 2008,⁷ and higher interest rates and persistent inflation are further headwinds. Profit margins for defense companies are among the lowest of US large capital goods industries,⁸ reinvestment ratios for public defense companies trail commercial counterparts,⁹ and rapid scaling of new technologies remains difficult. As a result, earnings multiples for mature defense companies are similar to utilities: low risk, stable cash flows, and capped upside.¹⁰

These challenges jeopardize manufacturing capacity growth, higher valuations, and new-entrant momentum. Sustaining these outcomes requires consistently higher levels of company at-risk investment—and commensurate rewards to offset that risk. But alternative procurement approaches designed to do those things remain a tiny fraction of defense spending.¹¹

Private-investment gaps persist

Capital has flowed more readily to mature companies with programs of record and new entrants focused on early-stage development, particularly in segments like software and autonomy. The most critical gaps are in areas that represent systemic risks to capacity and scaled innovation, but have arguably lower visibility:

- **Funding for critical input production.** Reliance on imports for critical minerals represents a major risk to industrial resilience and production growth,¹² and refining capacity is also an acute exposure.¹³ Domestic mining and processing of critical minerals is capital-intensive, often globally uncompetitive, and long-cycle—a combination that deters private investment.
- **Technology transition funding.** The transition from prototype to production is a major financing gap: The top 100 venture- and PE-backed defense companies have raised \$118bn against only \$16bn in federal production commitments as of June 2026.¹⁴ For new entrants, this gap makes financing for their next phase of growth more difficult, and limited private-equity participation to date creates concerns about “exit infrastructure” for promising new entrants.
- **Financing for capacity growth and resilience in sub-tier manufacturing.** Many critical components and machines for manufacturing defense systems are in short supply at today’s production rates, let alone those anticipated in the future. Small suppliers also have less borrowing capacity.
- **Large company R&D and capex investments.** Today, most manufacturing capacity and advanced defense technology reside at large defense companies. But these companies invest approximately 2%–3% of revenue in company-funded R&D as well as capital expenditures—both below comparable industrial and technology sectors.¹⁵ Market conditions can deter greater at-risk R&D and capex investment in places where these assets are best leveraged.

At the root of these gaps are investments never made because expected returns don’t justify the risk. Traditional defense contracting caps profit margins and returns, which makes it hard to invest in higher-risk projects. This misalignment, along with buying friction and demand uncertainty, keeps capital on the sidelines.

How to encourage private investment

Our research with stakeholders identified six priorities to make defense investment growth more sustainable and deliver better, faster, lower cost capabilities for warfighters.

1. **Back clear priorities with funding.** Definitized munitions framework agreements, awards for worthy new entrants that send signals that risk-taking will be rewarded, and meaningful new company capacity and R&D commitments will all encourage increased investment.
2. **Link risk and reward.** When returns are fixed, so is the amount of investment, creating a structural cap on sustainable investment growth. Fit-for-purpose buying, contracting, and company incentives that align risk and reward can help address this challenge.

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3. **Reduce buying and selling friction.** Friction has a cost. It deters new entrants, raises the cost of capital, and reduces supplier agility. Increased use of flexible procurement pathways, clearly defined commercial buying processes, and faster company operating models can reduce friction.
4. **Grow market volumes.** Small markets are harder to invest in because low production volumes mean higher unit costs and limited benefits to scaling production. Increasing market volumes through international sales and dual-use products is likely to attract investment that benefits both domestic capacity growth and product affordability.
5. **Develop flexible sources of capital.** Traditional financing sources aren't always suited to the timelines and demand profile of defense. Flexible and fit-for-purpose fund structures aligned to defense timelines, and expanded flows to defense-oriented funds, can help fill the gap.
6. **Improve performance.** Suppliers must devote more time, energy, and resources to improving schedule, quality, and cost performance. New entrants should invest more in manufacturability to increase customer confidence.

Unlocking growth

Partnership between government, industry, and investors is key to achieving these goals. The defense investment gap will not close through enthusiasm alone. It will close when business-case conditions make private investment rational. That is a solvable problem—and when alignment is strong, the defense industrial base can deliver extraordinary outcomes.

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