

Preparing for a Deep Defense Drawdown: The Defense Drawdown Working Group (DDWG) and the "Cost-Capped" Methodology

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Background

The Budget Control Act of 2011 (enacted in August 2011) mandated caps on national security and domestic spending (BCA caps) totaling \$1 trillion over 10 years and created a sequester mechanism imposing another \$1.2 trillion over 9 years if triggered (on 2 January 2013) by Congress' failure to reach a bipartisan solution (via a "super committee" process) by the end of 2011 or a "grand bargain" compromise. The total bill for the Department of Defense (DoD) is \$487B in FY2012-2021 and \$475B in FY2013-2021. This would bring the defense budget top line from its post-9/11 peak of \$735B (in constant FY2013 dollars) to \$510B, which is a 31% decline and comparable to past drawdowns of 33-43%.

Convinced that DoD faced the almost certain prospect of a defense drawdown much deeper than the approximately 9% reduction imposed by the BCA caps, Kim Wincup and Clark Murdock, both CSIS senior advisers, formed the Defense Drawdown working group (DDWG), consisting of approximately 30 leading defense and budgeting analysts (see Appendix A for a list of participants). Murdock, who had been intensely working on defense budget issues since September 2011 when CSIS hosted a daylong conference on Defense in an Age of Austerity,¹ formed a Defense Drawdown (DD) study team consisting of Kelley Saylor and Ryan Crotty, both CSIS research associates, and himself. The principal purpose of the DDWG is to provide feedback on charts, briefs, and draft text produced by the DD study team. The intent of this self-funded effort was to address both *how* a deep defense drawdown should be conducted and provide a set of recommendations on *what* decisions DoD should make as it implements a significant reduction in defense spending.

Starting on 25 January 2012, the DDWG has met almost monthly and provided feedback to a wide range of DD study team products, ranging from lessons learned from past drawdowns to a depiction of

¹ See Clark A. Murdock, Kelley Saylor, and Kevin Kallmyer, "Defense in an Age of Austerity: Conference Proceedings, Presentations, and Key Takeaways," Center for Strategic and International Studies, October 2011, http://csis.org/files/publication/111121_Murdock_DefenseAusterity_WEB.pdf.

security environment from now until 2020+. (See Appendix B for a list of DDWG meetings and the issues discussed). In May 2012, CSIS released an interim report² proposing a methodological approach to preparing for a deep defense drawdown in an effort to inform DoD analysts and policymakers that, if they were planning for the BCA sequester cuts, which they adamantly insist they are not, this is how they might do it.

While helpful across the range of DD study team products, feedback from the DDWG has been critical in shaping the evolution of the study team's methodological approach for preparing for a deep defense drawdown. The factors driving the study team's redefinition of its methodological approach were twofold: (1) the growing realization of the magnitude of the resource challenges facing the Department; and (2) lessons learned from the study team's initial efforts to execute the methodological approach as was formulated in January 2012 (when the DDWG first met) and then detailed in its May 2012 interim report. As discussed in more detail in a companion piece to this paper, "The Defense Budget's Double Whammy: Drawing Down While Hollowing Out from Within,"³ the defense budget is being "hollowed out from within" by internal cost inflation even as it faces downward pressure on its top line. It's not just fewer dollars for defense, it's also a weakening defense dollar in terms of how much military capability can be purchased with each dollar. Although several organizations have documented the growth in Pentagon costs – including GAO (acquisition costs), CBO (O&M costs), and the Defense Business Board (costs of military compensation and health benefits) – the aggregate impact of these streams of inflationary costs upon the defense budget have not been well understood, much less internalized, either inside or outside the Pentagon. If these inflationary trends, which have persisted since 2001, continue at the same pace until 2021, there will be no funds available for modernization (that is, RDT&E and procurement) by 2020. These are startling findings, to be sure, but those defense policy analysts we have consulted (both in and outside of the DDWG) have confirmed the thrust of the DD study team's analysis.

The combined effect of a declining defense budget top line and the aggregate impact of internal cost inflation pose a zero-sum tradeoff between modernization and end-strength. We calculate that restoring modernization's share of the defense budget to 32% (the level of effort in the FY2001 budget)

² Clark A. Murdock, Ryan A. Crotty, and Kelley Sayler, "Planning for a Deep Defense Drawdown: A Proposed Methodological Approach," Center for Strategic and International Studies, May 2012, http://csis.org/files/publication/120522_DD_Interim_Report.pdf.

³ Clark A. Murdock, Kelley Sayler, and Ryan A. Crotty, "The Defense Budget's Double Whammy: Drawing Down While Hollowing Out from Within," Center for Strategic and International Studies, October 2012, <http://csis.org/program/defense-drawdown-working-group>.

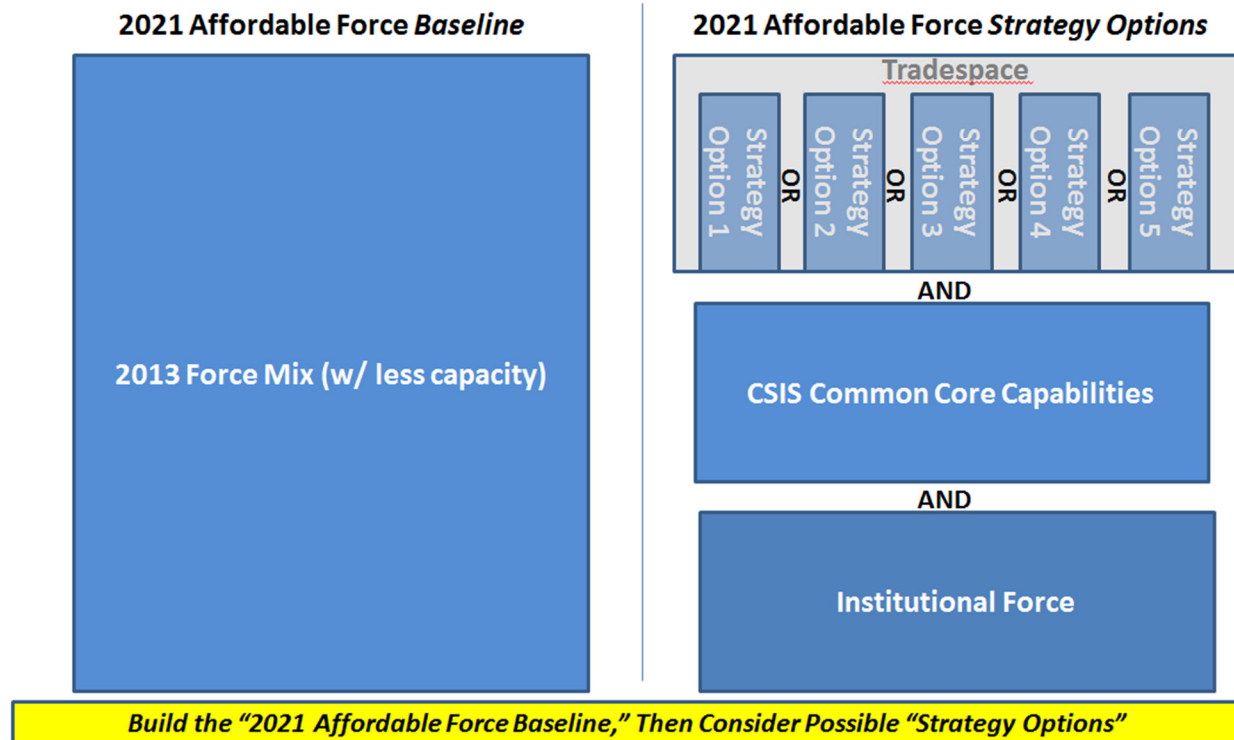
would require cutting end-strength by 455,000 active-duty personnel. Talk about tough tradeoffs! Since the resource challenges facing DoD are much more severe than is generally recognized, our recommended approach for coping with them is dramatically different from those being employed currently in the policy community and DoD; however, desperate times often require drastic solutions.

Conceptual Underpinnings of the Cost-Capped Approach

The logic is straightforward:

1. Decide first what DoD can afford to spend on people and weapons.
2. Using the resource limits (for people, equipment and readiness) of the "2021 Affordable Force," define the "2021 Affordable Force Baseline," which is essentially today's force under 2021 resource caps.
3. As the first step in constructing strategically-driven alternatives ("Strategy Options") to the 2021 Affordable Force Baseline, define the support infrastructure that any future military will need to produce military capabilities, or, as Title X expresses it, to man, train and equip the force. We call this the "Institutional Force."
4. Then define the "Common Core Capabilities (CCC)," both qualitatively (the kinds of capabilities) and quantitatively (the minimum amount or capacity of a particular type of capability), that any 2021 military needs to cope with the challenges of the 2021 security environment (e.g., the minimal capability needed for offensive counterterrorism and homeland defense). (See Chart 1)
5. "On top of" (so to speak) the Institutional Force and CCC, construct a set of alternative force mix options that represent alternative strategies (e.g., an Asian-Pacific emphasis) for the 2021 Affordable Force.

Building the Affordable Force 2021 Baseline and Strategy Options



This is the decision package for DoD's senior leadership – today's force structure under 2021 cost caps (the "2021 Affordable Force Baseline Option") and a set of cost-capped strategy options (the "2021 Affordable Force Strategy Options"). While the cost-capped approach is sequential and transparent in nature, executing it will take discipline and guts, particularly from the Secretary. Four guiding principles are applicable:

- **It's cost caps; the harder the better.** In the early years of the Rumsfeld era, the Pentagon said that the planning cycle was "cost-informed" and the programming cycle was "cost-constrained." In terms of the annual budget cycle, the two processes were merged into a single PBD (program budget decision) process that typically ended in a last-minute, fairly-arbitrary "cut drill" that often cut procurement at the expense of personnel and O&M. The result? A lot of "broken glass" at the beginning of each execution year consisting of insufficiently or erratically funded programs. As Congress has done with many acquisition programs experiencing cost overruns,

costs must be "capped" if internal cost inflation is to be brought under control. If the tradeoff becomes less of anything (people, weapons, etc.) versus better business processes, perhaps the Pentagon's dysfunctional incentive structure (when it comes to non-operational matters) will change.

- **National security ends must be commensurate with DoD means.** The cost-capped approach attempts to close the gap between ends and means by suppressing the appetite for expansive strategic objectives through limiting the nation's ends to the resources available – that is, keeping them inside the Affordable Force box.
 - As several commentators have noted, U.S. strategy statements are often statements about aspirations, goals, and objectives, not how the U.S. should achieve them. Strategy formulation is about ends, ways, and means. The first principle for success should be that one's ends must be achievable with one's means, so that good strategy – the "ways" – has a chance to succeed.
 - Putting resource constraints first as hard caps on our strategic choices should help curb the all-too-American inclination to solve problems and be all things to all people (see the role of "indispensable nation" and the COCOM demands needed to fill that role). This is about formulating a sustainable strategy, one that is economically and politically affordable. Those who want a more activist foreign policy or a bigger U.S. global role should bear the burden of coming up with the resources to pay for it.
- **Take savings-through-better processes after they have been earned and at the back end of the process.** The Pentagon, as well as legions of defense analysts, have known for decades that DoD has to "change the way it does business" in order to free up dollars for buying military capability. The push for defense efficiency reforms can be traced back to at least to the mid-1980s with the Packard Commission proposals for reform of defense acquisition processes (which were incorporated in the Goldwater-Nichols Act of 1986). Since then, DoD has had defense reform initiatives, the revolution in business affairs, and defense business transformation, even as internal cost growth persisted. Defense Secretary Gates announced in January 2011 that the services had found \$100B in overhead reductions and that OSD had found \$54B in efficiency savings and freezes on civilian pay and hiring. Secretary Panetta tacked on another \$60B in claimed efficiency savings in Jan 2012. Given decades of internal cost growth, defense planning predicated on the "negative funding wedges" made possible by as yet to be

achieved efficiencies is an exercise in self-delusion.⁴ To be sure, there are savings to be had through efficiency initiatives and better business processes, but, in a return to basics, they need to be earned before they can be counted.

- **In this cost-capped world, the principal source of modernization dollars is reductions in end-strength.** We estimated that each 100,000 reduction in active duty forces from today's force level will save DoD \$147B in FY2017-FY2024. In our illustrative example, the 2021 Affordable Force Baseline would need to be a smaller force (shrinking from 1.32 million active duty personnel in FY2017 to 0.854M in FY2021), to preserve a level of modernization (defined as percentage of the DoD budget) that is the same as that of the last pre-9/11 force. This is the 2021 Affordable Force Baseline.

In the 2021 Affordable Force Baseline, we have identified how many people, how much readiness (in terms of dollars available under the total cost cap) and how much modernization DoD will get in FY2021. These are the inputs that DoD uses when it "buys" capabilities. Rather than ask "how much is enough," we have asked first "how much can be spent." Only after we have determined how much we can spend, much like any prudent- and frugally-minded household, can we turn to strategy.

A methodology for bringing supply (as defined by the Affordable Force) and demand (as defined by the defense implications of the 2021 Security Environment) into balance.

At first, two parallel processes:

- Supply:
 - Step S-1: Define the Affordable Force Baseline:
 - Project the topline over the planning period
 - In this case, the BCA-mandated cuts over FY2012-21
 - Project the internal sources of cost inflation that are crowding out modernization dollars
 - Trade end-strength to "buy back" sufficient investment dollars to achieve the desired level of modernization, in this case equivalent to the pre-2001 level

⁴ The belief that significant savings can be gained without making tough tradeoff decisions is a persistent one. In a recent (8/15/12) *Fortune* interview, Republican presidential candidate Mitt Romney said that he believes "we will find enormous opportunities for efficiency and cost savings in the military" and that he would use those savings to buy back 100,000 of the military personnel being cut to meet the BCA caps.

- This is the generic 2021 Affordable Force Baseline, which we would currently define as having 845K in active duty manpower and \$167B (in FY2013 constant dollars) for modernization (RDT&E and procurement)
- Demand:
 - Step D-1: "Paint a picture" of the multi-dimensional demand for military capabilities.
 - Vet draft with experienced SMEs and revise until satisfied that most of the experts agree with most of the depiction of the 2024 Security Environment.
 - A "living document" that should be revisited regularly (not just every four years)
 - Step D-2: Identify the Implications for Defense
 - Starts the process of converting the demand for military capabilities into the metrics used on the supply side
 - Step D-3: Identify a Common Core of Capabilities (including the minimum essential capacities) needed for any 2021 Force
 - This establishes a demand-centric statement of the minimal military capabilities needed to address 2021 security challenges and opportunities.
 - The Common Core of Capabilities (CCCs) would be defined as the minimum level provided in each of DoD's primary missions and key enablers.
 - Our initial list of Primary Missions includes the following:
 - Counterterrorism (black and white SOF)
 - Homeland defense (steady-state and surge)
 - Project power (How much is a critical issue) in an A2/AD environment
 - Safe, secure, reliable and effective nuclear deterrent
 - Key Enablers
 - ISR (strategic and tactical)
 - Assured C3, including superior cyber and space capabilities
 - Innovation Account: the level of effort, defined as the percentage of the budget (perhaps 25% below historical levels) devoted to this function. Providing an Innovation Account enable the United States to force the pace of military innovation, shape the evolution of warfare, and maintain its technological superiority. This is the floor for spending on RDT&E for any 2021 Force strategic option.

- Balancing Supply and Demand:
 - Step S/D-1: Decide how much of the 2021 Affordable Force should be allocated to the Institutional Force:
 - The Institutional Force is the percentage of the defense budget that funds the institutions of DoD (the military services, OSD, the Joint Staff, the defense agencies, etc.) whose combined activities produce the capabilities employed by the Joint Force Commander.
 - Estimates of how much of the defense budget pays for the "force providers" vary considerably, although usually in the range of 30-35%. For illustrative purposes, let's assume that it is 32%, which means that the Institutional Force will consume about 30% of the active duty manpower, since more civilians and contractors are involved in these infrastructure functions and 35% of the modernization dollars (or \$182B in FY2013 dollars).
 - Step S/D-2: Determine the size of the "discretionary capabilities trade space"
 - Iterate between the demand-centric Common Core Capabilities (CCC) statement (Step D-3) and the supply-driven Affordable Force Baseline (Step S-1)
 - If the initial CCC requirement is unaffordable, because it crowds out too many modernization dollars (or even worse, exceeds the total funds available for the 2021 Affordable Force capabilities), adjust downward the CCC level of effort:
 - Today, we often refer to a full-spectrum force as one that has capabilities that are robust across the full range of conflict. We often imply that our vision of the force is one that is fully capable across the spectrum of conflict. While the cost-capped 2021 Affordable Force Baseline and Strategy Options may all have capabilities that can be applied to any contingency, it will be transparently clear that our capacity varies widely across the spectrum of conflict. This increased awareness of our capability and capacity shortfalls comes with a cost, however, since our potential adversaries will also be aware of strengths and weaknesses. This is both unavoidable and prudent -- better to do this "net assessment" in the pre-conflict virtual competition than on the battlefield.
 - After taking out the "wedges" for the Institutional Force and the CCCs, the residual is the trade space for buying capabilities tailored for each strategic option:

- In a sense, this is the level of "discretionary defense dollars" available for alternative mixes (to the 2021 Affordable Force Baseline, which is the "discretionary capabilities tradespace" within which the strategic options have to "fit." Different mixes of personnel, modernization and readiness are likely parts of each alternative.
- Step S/D-3: Develop a roster of 4-5 alternative 2021 Affordable Force Strategy Options with associated force mixes to allocate the \$XXX billion (see Step S/D-2) available for making capability tradeoffs (beyond those capabilities already provided via the CCC). Each "Strategy Option" would represent different strategies and priorities for how DoD should spend its scarce capabilities dollars in 2021.
 - Our initial list of alternative 2021 forces include the following:
 - 2021 Affordable Force Baseline (today's force mix under 2021 cost caps)
 - Asia-Pacific emphasis
 - Middle East emphasis
 - Homeland Defense Centric
 - Kinetic Strike – Emphasis on hard power, warfighting capabilities
 - Global Pol-Econ-Mil (PEM) Competition
 - Other?

A Separate, Parallel Cost-Reduction Initiative to "buy back" space for discretionary defense spending

True savings – that is, savings that can be "banked" and then used to buy capability – are very important. For \$25B, DoD can buy XXXX end-strength equivalent (number of active-duty personnel) or YYYY equipment equivalent (half a helicopter, a quarter of a Global Hawk) or ZZZZ force structure equivalent (a quarter of a BCT; a fully-trained SOF squad, etc.). The downward pressure on the defense budget topline is likely to persist for at least a decade or so, in part because the Budget Control Act mandates a budgetary decline out to FY2021. Reducing the cost of how DoD does business is one of the few sources of additional funds to "buy" people and equipment and train them. Everyone agrees, we should save money, whether through defense reform, defense transformation, efficiency initiatives or better buying power.

DoD's problem is that they usually claim the savings in advance and then spend them before they are actually achieved. Too often, the size of the claimed savings (see the January 2012 *Defense Budget Priorities and Choices*) is the gap between the overall savings target (see the BCA caps) and the savings gained from actual cuts (e.g., Army and Marine force reductions). As discussed previously, these claimed savings take the form of "negative funding wedges" that are "spent" in advance, often to

prevent having to take deeper actual cuts. The result is a broken budget in the execution year, because too many programs and activities are underfunded.

Bankable savings are generated when organizations stop doing something (and lay off the people engaged in that activity) or stop buying something (and put the money in the bank). Efficiency initiatives in the public sector often do not result in bankable savings because government organizations don't lay off people since it's all too easy to give them something else to do and it's all too hard to separate them. It's also hard to stop buying things because there are numerous vested interests with sufficient political clout to prevent it.

The Secretary needs a separate, independent, and empowered cost-reduction office, whose job it is identify ways in which the organizational components of the Institutional Force and Operational Force can reduce costs and generate bankable savings. They would be responsible for setting cost-reduction targets and then validating that the savings have actually been achieved (and "banked" for reallocation). This DoD Cost Reduction Office would also determine when an organization could "spend" the savings. As part of the end game for the annual budget submission, the Cost Reduction Office would release its year-end allocation of earned savings that could be used for additional capabilities. Although the force providers would be tempted to use the last-minute "plus ups" for avoiding end-of-cycle cuts, the use of these cost-reduction savings would be strictly for adding more funds to the 2021 Affordable Force discretionary capability spending.

Next Steps for Deep Defense Drawdown Study

- We have developed a common template for assessing alternative 2021 Affordable Force strategy options. It has the following elements:
 - Capabilities: those emphasized and those de-emphasized
 - Posture: those emphasized and those de-emphasized
 - Missions: those emphasized and those de-emphasized
 - Risks: Makes explicit the areas in which greater risk is being accepted
 - Implications for National Security Strategy
 - For example, instead of relying upon a broad array of "shaping" tools (e.g., forward presence, mil-to-mil contacts, combined exercises, BPC, etc.) the Kinetic Force would rely upon war-fighting capabilities, a credible "reputation for action," and coercive diplomacy as the principle means of influencing the behavior of other states.
 - Implications for Defense Strategy

- For example, a DoD optimized for a Global PEM Competition would be a smaller Defense Department as defense dollars are diverted to AID, Commerce, State, etc. to resource these chronically under-funded instruments of national power.
- We are currently operationalizing (that is, defining and costing in terms of force structure) the concepts of the Institutional Force and Common Core Capabilities. The Defense Drawdown working group will review them and provide feedback at the 24 October meeting.
- Once the discretionary defense spending tradespace has been determined, the DD study team will develop a set of strategic options and their associated cost-capped force structures and present them, along with the 2021 Affordable Force Baseline option, to the DDWG on 13 November.
 - At this point, the DD study team will start vetting its initial findings with defense analysts in the policy community and selected interlocutors in DoD.
- The DD study team will integrate its analysis and recommendations into a final "vetting brief" that will be used to communicate its findings to relevant DoD and policy communities. This vetting brief will be a living document that will be revised as it is disseminated. It will be reviewed by the DD working group on 18 December.
- Based on the brief and other supporting work, the DD study team will draft a final report, which will be released in mid-January 2013.

Purpose and Targeted Audience of DD Study Initiative

The goal of this unfunded project has been fairly consistent from the start:

- Provide a straightforward, transparent, and disciplined methodological approach for how DoD could plan for a deep defense drawdown.

When the DD study team realized the severity of DoD's internal cost inflation problem, an additional goal was added:

- Raise awareness in DoD and the policy community of the extent to which the defense budget was being "hollowed out" from within by the aggregate impact of its inflationary streams of activity.

The impact of the double whammy of topline reductions and the weaker defense dollar made it clear that the mantra was not "doing more with less" or even "doing the same with less" – it was really "doing less with much less." This led the DD study team to develop a more stringent "cost-capped" approach that first determined what the nation was willing to spend (that is, the 2021 Affordable Force) and then built the force from the bottom up (Institutional Force + Common Core Capabilities + Strategy Option). Underlying this approach is the conviction that during an age of austerity, it is critical to begin by identifying first what the nation can afford to spend on defense and then identifying those capabilities that, either for the Institutional or the Operational Force, are must-have capabilities.

The targeted audience, of course, is senior-level officials in the Department of Defense. It is their decisions that will determine how well the Department copes with severe resource challenges. In our companion piece ("The Defense Budget's Double Whammy"), we make the case for urgency and change; in this paper, we lay out one approach for how to do it. In our final report, we will provide the recommendations that flowed from our application of the cost-capped methodological approach.

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APPENDIX A: DEFENSE DRAWDOWN WORKING GROUP PARTICIPANTS

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APPENDIX B: DEFENSE DRAWDOWN WORKING GROUP SCHEDULE

Although the initial round of spending cuts mandated by the Budget Control Act of 2011 will not require a fundamental change in the nation's defense strategy, as articulated in the 2010 Quadrennial Defense Review, cuts substantially beyond this level will likely force DoD to examine the growing disconnect between strategy and resources. To help facilitate the long-range planning needed to address this misalignment, the Defense Drawdown Working Group, co-chaired by senior advisers Clark Murdock and Kim Wincup, convenes approximately 30 leading defense and budgeting analysts to provide feedback on charts, briefs, and draft text produced primarily by the CSIS study team.

Session 1: Overview of CSIS Approach & Assessment of DoD's Strategic Review

25 January, 0800-0930, Basement Conference Room C (B1C), CSIS

DDWG will provide feedback on the Murdock-Wincup brief and discuss the 5 January DoD rollout of the Defense Strategic Guidance.

Session 2: Best Practices for Managing the Defense Drawdown

7 March, 0830-1000, Basement Conference Room C (B1C), CSIS

DDWG will discuss a CSIS brief (lessons learned from past drawdowns & recommended design principles) and a commissioned brief on how DoD should address the management challenges facing them.

Session 3: Critical Factors Determining the Shape and Size of the Future Force

5 April, 0800-1000, Fourth Floor Conference Room (B1C), CSIS

DDWG will provide feedback to a CSIS brief and a commissioned brief that first identifies, and then establishes priorities between, the principal determinants for both defining the qualitative nature and the relative quantities of the capabilities needed by the 2020+ U.S. military.

Session 4: Interim Report Methodology & Future Security Environment

9 May, 0800-1000, Fourth Floor Conference Room (4CR), CSIS

DDWG will provide feedback on the CSIS interim report draft outline on how the defense drawdown should be conducted, receive a short brief on baselining the current drawdown and discuss (if time permits) a CSIS brief on the context in which future military missions are likely to be executed.

Session 5: Must-have Capabilities for the 2024 Force

18 July, 0800-1000, Fourth Floor Conference Room (4CR), CSIS

DDWG will discuss today's high-leverage capabilities and, based upon the future security environment and likely evolution of warfare, identify additional "must have" capabilities that will be required to cope with future challenges.

Session 6: Portfolio Rebalancing Exercise

14 August, 0900-1600, Basement Conference Room C (B1B/C), CSIS

DDWG will participate in a portfolio rebalancing exercise utilizing a Center for Strategic and Budgetary Assessments (CSBA) costing tool. Participants will be divided into two teams, and each team will be asked to rebalance DoD's portfolio of capabilities (i.e. investing in new capabilities and divesting of capabilities no longer needed) in a reduced budget environment, noting where they must deviate from current strategic guidance.

Session 7: Revised Methodological Approach

25 September, 0800-1000, Fourth Floor Conference Room (4CR), CSIS

DDWG will discuss the revised methodological approach for how DoD should prepare for sequestration, as well as updates of both the supply and demand functions of the methodology.

Session 8: Identifying the Common Core of Capabilities & Building the 2021 Affordable Force

24 October, 0800-1000, Fourth Floor Conference Room (4CR), CSIS

DDWG will provide feedback on CSIS and commissioned briefs identifying the common core of capabilities and will additionally discuss methods for costing the institutional force.

Session 9: Roster of Alternative 2021 Force Mixes

13 November, 0800-1000, Basement Conference Room C (B1C), CSIS

DDWG will discuss the CSIS roster of 4-5 alternative 2021 force mixes, each of which will represent a different strategy for how DoD should spend its operational capability dollars in 2021.

Session 10: Final Brief Vetting

18 December, 0800-1000, Fourth Floor Conference Room (4CR), CSIS

DDWG will provide feedback on the final vetting brief.