

Perception and Profit:  
Understanding Commercial Military and Security Service Provision

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## **Perception and Profit**

### **Understanding Commercial Military and Security Service Provision**

#### **Executive Summary**

The forces of supply and demand have moved the areas of concern for many commentators from issues surrounding direct combat intervention towards security-related matters. Since the 'Arms to Africa' affair in 1998, a lack of engagement and understanding has ensured slow progress in the United Kingdom. The prospect of an adjournment debate in the House of Commons following the end of the Green Paper consultation period, and the possibility of a Government White Paper underlines the importance of early resolution of a number of matters. This discussion paper will raise two issues that the author feels are given scant attention by those engaged in the debate over Military and Security Companies (MSCs). Firstly, communication and mutual understanding between those engaged in the debate is currently not strong enough to enable its resolution in a manner that satisfies its stakeholders. Secondly, market forces have been ignored as powerful influences on the conduct of military and security service provision. These capabilities are no longer purely public goods.

Perception within the MSC debate varies widely. This reflects a broad spectrum of sentiment, in terms of depth, orientation and strength of opinion of MSCs themselves, their varied activities and reputations, and what, if anything, should be done to limit their activities. If the problem can be seen as one in which all interested parties have a desire for resolution, or at least progress towards it, then the basic themes of conflict resolution will ease and assist this progress.

This paper maintains that movement towards the conclusion of any debate must begin with each party to it examining in depth its own motivation, methods and desired outcome. Each must then study these same factors in respect of all the other stakeholders in the issue. This implies at least limited recognition, communication and honesty. Given these variables, a greater or lesser level of understanding can be reached. It is a short step from mutual comprehension to the establishment of common ground between parties. As trust and communication improve, pragmatic compromise becomes attractive, and leads the way towards at least partial resolution to the benefit of all those able to adopt a solution-oriented approach. It is the author's contention that all stakeholders in the MSC debate would benefit from an atmosphere of increased communication and understanding.

All those involved in the issue surrounding MSCs aspire to gain personal and/or organisational profit from it. Profit has economic, social and organisational meanings. This paper seeks to dispel the notion that profit is intrinsically evil, and suggests rather that it is the ultimate measure of organisational or individual success.

This paper will link commercial practice with the forces that shape the MSC market, via issues of brand, transparency and corporate activity, and will show how market forces and trends form a factor at least as important in the control of MSC activity as national and international legislation. In this context, it is designed to illustrate the importance of commercial indicators, trends and common practise when regulation is contemplated.

As a basis for discussion, this paper does not make any claim to academic rigour. In the main, it is based on theoretical concepts rather than empirical evidence, and it is hoped the

reader will find it more or less objective in its approach. The author has avoided entanglement in issues of definition, and has dropped the adjunct ‘Private’ from MSC, as it may be the source of some confusion if related to Public Limited Companies. The paper relies upon the author’s understanding of conflict resolution and of corporate and marketing strategy, and on his somewhat limited experience in these two fields. The author invites and welcomes dissent and discussion from all quarters.

### **Perception**

#### **The Stakeholders**

Those engaged in the debate over private military and security provision can largely be divided into three camps: activists, analysts and proponents. The activists seek to drive national and international political bodies into enacting legislation that will secure and enforce MSC conduct in line with a commonly understood human rights-based agenda. The analysts view MSCs as a phenomenon of increasing importance on the stage of international affairs, and study and comment upon their conduct and practice against a background of issues such as globalisation and interventionism. The proponents take a pragmatic or promotional view of the sector and ponder how non-state commercial actors can play a legitimate and positive role in international development.

Sitting apart from these three factions is the UK Government, under pressure to pass regulatory legislation on the sector, undecided as to its format, and unwilling to cripple or drive offshore a sector that may be of use in three areas: defence, foreign affairs and commerce.

#### **Communication**

Communication between stakeholders has been limited. Despite the worthy initiatives of International Alert, the British Red Cross and RUSI, such as the Wilton Park Conference in November 1999, and the publication of a large number of papers and pamphlets by activists and analysts, there has been little or no engagement between MSCs and other stakeholders. At Wilton Park, none of the 46 delegates represented the MSC sector. At the Tufts University conference in April 2001, again none of the 28 participants represented MSCs. The hearings of the House of Commons Foreign Affairs Select Committee took evidence earlier this month from witnesses: although there were a number of written submissions, MSCs were represented solely by Lieutenant Colonel Tim Spicer, a supplier of combat services.

The reasons for this lack of communication are numerous. Many parties do not wish to be seen participating in discussions marked by historical stereotype and sensationalism, both from the MSC arena, and from amongst the latter’s current or potential clients. International Alert’s latest publication, ‘Humanitarian Action and Private Security Companies’, is studded with references to a lack of information about MSC and NGO interaction. A cynic might suggest that aid agencies understand the concepts of client confidentiality and guilt by association only too well.

The expanding spheres of humanitarian and MSC activity have been in increasingly close contact since the late 1990s. There now exists a commercial niche market for humanitarian support activities that is being entered by various diversifying MSCs. The two sectors of endeavour must begin to communicate on a meaningful level, unmarked by

prejudice and polarisation, so that they achieve some mutual understanding and profit from each other's actions.

If a single cause of distrust can be identified, it is that of profit, the ultimate motive for commercial activity, and one that rests uneasily with those driven by humanitarian inspiration, who often lack understanding of business principles. Yet aid agencies themselves are driven by a desire for profit, albeit not purely in financial terms.

### **Profit**

To the economist the concept of profit is both simple and fundamental. It is the ultimate measure of financial success, and is understood in the following terms:

$$\text{Revenue} - \text{Cost} = \text{Profit}$$

Understanding this in commercial terms is easy enough. The 'bottom line' forms the bedrock of all commercial activity. For non-commercial organisations, those whose purpose is not to derive financial benefit for its shareholders, the concept of profit is less easy.

### **Organisational Profit**

All organisations have some form of purpose to their activities, usually to benefit their members or others. From family groups to residents' associations, congregations, political parties and multinational corporations, this sense of purpose is shared by the organisation's members and guides their actions. The table below illustrates the benefits or profits that direct the activities of a number of different organisations.

<b>Organisation</b>	<b>Activity</b>	<b>Benefit or Profit</b>
DFID	Assist developing countries. Give away money and goods. Manage successful contracts. Prevent or mitigate disasters. Develop infrastructure.	International goodwill and influence. Moral satisfaction. Increased budget allocation. Political satisfaction. Organisational growth.
OXFAM	Feed and water the needy. Prevent or mitigate famine. Promote OXFAM. Compete for activity. Compete for funding.	Decrease hunger. Grow organisational competence. Increased issue / brand awareness. Organisational growth. Increased funding and donations.
Ford Motors Ltd	Design cars. Build cars. Sell cars. Beat other manufacturers. Satisfy customers.	Intellectual property development. Increased brand equity. Increased shareholder profits. Increased market share. Increased customer loyalty.
The Family	Increase income. Procreation. Care for young, old and infirm. Asset acquisition. Grow influence.	Increased comfort. Bigger family. Longer life. Richer family. Societal advantage.

The organisational benefits and profits outlined above show that complete altruism is a very rare commodity. This conclusion is masked by the weight of factional public relations and promotional activity that is systemic to commercial or issue-based groupings. An increasing trend amongst many organisations is to measure profit in terms of the ‘triple bottom line’, of financial, environmental and social benefits of activity.

### Organisational Assets

Profit is generated by the coordinated action of an organisation’s assets. In general terms these can be divided into two areas, the tangible and intangible. The table below shows some of the assets of a commercial body:

<b>Tangible Assets</b>	<b>Intangible Assets</b>
Cash. Stock. Property. Employees.	Intellectual Property and Knowledge. Reputation. Goodwill. Brand Equity.

### Core Competencies

In addition to these common assets, each organisation will have specific abilities or core competencies tailored to its area of enterprise. In the world of MSCs things are no different, as is illustrated below:

<b>Company</b>	<b>Core Competency</b>
MPRI	High to Low-level Military Training. Military Facilities Management. Military and Security Personnel Management.
DynCorp	Military Logistics Management. Military and Security Personnel Management.
Armorgroup	Security Services and Training. Humanitarian Support Services.
Sandline International	Intervention Operations. Low-level Training.
Control Risks	Intelligence and Threat Assessment. Negotiation.
Brown and Root	Military Logistics. Military Facility Construction and Management.
Group 4	Guarding Services.

Although these core competencies may not have a great deal in common in practical terms, their effect is strengthened or dampened by stakeholder impressions of three issues:

Ability: Conceptual advantage – Technique, intellect, understanding, customer focus.

Capability: Physical advantage – Size, equipment, reach, speed, training.

Legitimacy: Moral Advantage – Reputation, transparency, history, ethical conduct.

### Transparency

A constant theme of the debate on MSCs is a desire by some stakeholders for increased corporate transparency. This aspiration has been enhanced following a number of recent international commercial collapses prompted by criminal corporate misgovernance. To many outsiders, the complex world of business agglomeration defies understanding. The mergers and acquisitions and parent and subsidiary companies that form an incomprehensible and bewildering maze to the uninformed seem to provide a perfect cover for underhand and immoral dealings.

The historical links between extractive industries in Africa, Central and South America and Central Asia and the military and security companies that have facilitated and protected their work add to the suspicions of malpractice in this part of the corporate jungle. Outsiders seem automatically to suspect the worst; in this they have a good deal of historical justification. The MSC sector must now work hard to dispel these suspicions if they are to enjoy improved stakeholder perceptions of legitimacy, and to derive increased commercial benefit from it.

MSCs are populated by former soldiers who have been brought up on a diet of ‘need to know’ information management. Their subjective approach to outsiders is by default one of secrecy, and in many instances their past and current activities, however legitimate, mark them out as targets for former enemies. Even smooth talking management consultants have difficulty in getting business from MSCs. Corporate transparency must not be perceived by MSCs as a factor that will impede the acquisition of profit, or compromise commercial secrecy and personal security, but rather as an indispensable element of image and brand that will boost marketing efforts.

Efforts to improve commercial transparency should focus on two areas: structure and method. For those MSCs listed on stock exchanges around the world, structural transparency is usually assured by the national investor protection regulations that are prerequisites for flotation. Company annual reports are freely available, and offer detailed but highly polished records of business activity. They also include the names, positions and often photographs of board members, alongside justifications of past performance and detailed financial analysis backed up by the signature of the company’s auditors. Details of subsidiary companies owned by the parent should be made clear, but will often not enjoy the same depth of detailed analysis and declaration. It is the privately owned MSCs that are much more reluctant to release information about their structure. They must be persuaded of the business advantages of transparency without compromising their right to commercial confidentiality. Customer power and market forces may be able to ensure this through the adoption of a transparency code that might include the following items:

- Identification of headquarters.
- Declaration of Board Members and their responsibilities.
- Declaration of Divisional activity.
- Declaration of subsidiary company ownership and interest.
- Declaration of shareholder profile.

Many of these details are declared to host nation governments in order to comply with corporate and taxation legislation, and often MSCs are obliged to trade under a different name by licensing and joint venture regulations in host countries, and lose much of their established brand equity in the process. Other companies choose to base themselves offshore in order to avoid scrutiny and taxation; they pay a price in terms of perceived lack of legitimacy. These issues are of great sensitivity to some private companies. They may face the danger either of physical attack and/or of hostile takeover. Huntingdon Life Sciences is a case in point.

Methodical transparency should be addressed by all MSCs, whether private or public. They should be able to publish their terms and conditions of employment and operating and quality assurance policies and open them to public scrutiny. These declarations need only be general statements of intent and acceptable practice, rather than specific details of company policy and of individual operations. If there is nothing to hide, then there is nothing to lose, and much to gain in terms of legitimacy, perception and reputation.

Competitive transparency must remain a separate issue. Details of contracts, customer relationships and current activity should remain privileged information – as it does in any other commercial sector. Client confidentiality policy should be left to the client: if he is worth working for in terms of risk to reputation, he may well prove unconcerned about publicity.

### Brand Equity

The links between legitimacy and the intangible assets of an MSC are clear, and can be expressed in terms of brand equity. Brand is of great importance to many different organisations, from family name to globally recognised trademark. Brands (and their care, maintenance and growth) build stakeholder awareness of product and service, maintain customer loyalty and are associated with perceptions of quality. They link past sound performance to current potential. The world's most recognised word is an expression of brand: 'Coke'.

MSCs need to build and exploit advantage from their intangible assets in order to increase their profits in the widest sense. In the face of scrutiny and scepticism they must increase stakeholder perception of their legitimacy. The building of a recognisable corporate identity is the first step. This will entail the design and promotion of a brand mark and its associations in line with corporate and marketing strategy objectives. The brand is then reinforced and developed in order to satisfy existing customers and attract new ones.

### Promotion

MSCs vary widely in their promotional policies. Those with something to hide do not promote themselves in conventional terms, but rely on word of mouth contact via the shadier elements of society. These are often companies formed around a single contract or deal, and

dissolve themselves at its conclusion, or change name to avoid association with failure, malpractice or unwanted scrutiny.

The larger the MSC, the more visible are its brands and activities, and the greater its promotional effort. Common advertising forms a small part of their current promotional activities, as much of their business is generated from governmental and trans-national contracts and spin-offs, as well as from encounter-initiated deals struck in the field. Potential service-contracting enterprises will see an MSC's activities while assessing or entering an area of operations, and will decide whether or not to procure its services. The establishment of an internationally recognised and trusted brand is key to attracting new business and securing supplementary and repeat contracts. MSCs that do not build their brand equity, and fail to promote their services with sufficient focus and vigour are intensely vulnerable to shifts in supply, demand and regulation.

MSCs most frequently offer their services through direct business-to-business marketing approaches to potential customers. Company representatives approach pre-selected potential clients and make their pitch. They generally offer tailored packages suitable for each individual client. This direct strategy offers MSCs many advantages: it is focussed, discrete, efficient, reinforces brand, and its outcome is easily measurable.

### Vulnerabilities

MSCs share a key vulnerability. Their specialised services attract significant scrutiny, both from sector specialists and from sensation-seeking international media. Indeed it may be judged that their seductive appeal to journalists and investigators is far greater than that enjoyed by the giant multinational corporations they often serve. For companies operating in the information-rich and presentationally aware developed nations, this has a significant shaping effect on their business.

Following potential client risk analysis, almost all MSCs will avoid clearly unethical business (while the remaining few will wish to hide it). Whether this avoidance is because of internal moral standards or on account of the danger of damage to image, brand and reputation depends much on the individuals involved, and in fact is unimportant. In an expanding and unfulfilled market, responsible and well-governed companies will endeavour to ensure their activities are clearly demarcated from even loosely questionable operations, and will thus turn away any opportunity that might endanger its reputation. In the MSC sector, long-term reputation, brand integrity and goodwill is always more important than short-term profit. Defensive public relations is a weapon of last resort, and rarely shores up damage caused by even unfounded allegations.

### Sector Expansion and Competition

The market for the services offered by MSCs is very fragmented. There are very few areas where companies compete directly with each other for business, save perhaps the area of US Government contracts concerning training and facilities construction and management, and for simple guarding services. This fragmentation has allowed MSCs to establish safe home or niche markets during the mid-to late 1990s. Since then, the service market has begun to consolidate and diversify simultaneously. There have been a number of acquisitions and mergers of small to medium enterprises, as well as entry into new areas of service provision and the expansion of MSCs' international presence.

Despite this, there remains little direct competition between the main players. Brand advantage and size help them secure contracts against the efforts of indigenous service providers. Security, defence and aerospace industries remain attractive options for investors who shy away from sluggish manufacturing and telecoms-related sectors. Existing undercapacity in the MSC sector combined with increased global perceptions of risk and insecurity indicate that further expansion in the medium term is likely.

Unfulfilled demand will encourage companies outside the current MSC sphere to diversify their activities into military and security service provision. New companies will continue to be formed to take advantage of gaps in the market.

Until this expansion matures, the real effects of competition will not be felt. Traditional models of competition entail falling prices and margins, as well as wider product or service availability. As competition intensifies, brand advantage becomes more significant, and the battle for solid market share begins in earnest. Skimming marketing policies will develop into those that penetrate the potential customer base more deeply, and easy profits will become harder to find. The critical factors for business success in the MSC sector are likely to be: size and reach, reputation, perceived legitimacy, and then cost and quality of service.

### Regulatory Objectives and the Market

Since the ‘Arms to Africa’ affair came to light in 1998, the MSC market has changed considerably. The demand for combat services has shrunk dramatically, and the types of contract that Executive Outcomes and Sandline International signed in the mid-to late 1990s are increasingly rare. The combat sector of the market forms a small and shrinking area of endeavour. Despite this it attracts a preponderant level of scrutiny and attention. This historical feature is based largely on stakeholder fears of human rights violations, and concerns around the exploitation of the natural resources of weak states by MSC-associated extractive companies.

The focus on combat operations disadvantages the majority of MSCs. In terms of earnings, employee numbers and activity, security companies and military/logistic outsourcers account for the lion’s share of the broad market. This sector will grow strongly in the medium term, and because of the wide range of activities undertaken and the growing demand for private security and business process outsourcing, there exist very few barriers to entry for new players and diversifying companies. This growth will be matched by the decline of the combat service provision niche market.

If the UK Government decides to propose legislation to Parliament, it will wish to secure the following objectives:

- Satisfy pressure for MSC regulation.
- Ensure national and international legal compliance by British MSCs.
- Increase government knowledge and understanding of British MSC activity.
- Enable UK MSCs to bid more easily for outsourced UK Government business.

A wisely regulated environment for MSCs is likely to have the following additional effects on a fragmented but expanding market:

- Assist in growing global perceptions of the legitimacy of UK MSCs.
- Attract new and diversifying MSCs to operate from the UK.
- Assist sector (and UK MSC market share) growth.
- Deter MSCs from operating offshore.

If UK legislation can support and encourage the growth of legitimate MSC activity based in Britain, this should help establish and reinforce international standards of conduct. The more available the services offered by reputable and licensed MSCs, the more widely they will be used, and the less easy the trading environment for disreputable organisations.

### **Conclusion**

Legitimacy and thus legal and moral conduct is key to the commercial success of MSCs. This offers activists and those with a human rights-based agenda key leverage and influence over MSCs. If MSCs and active stakeholders are to derive mutual benefit and satisfaction, then they must build trust and understanding through communication. MSCs should facilitate this by increasing their structural and methodological transparency, and thereby gaining both trust and business. In return, stakeholders should adopt a pragmatic approach to profit, conclude that commercial endeavour is not bad by default, and reconcile themselves to their own non-financial profit orientation.

The potential for legislation to shape the emerging MSC market in the interests of all stakeholders should not be missed. The opportunity currently confronting the UK Government must satisfy activist suspicions and encourage increased legitimate business for British companies.

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