

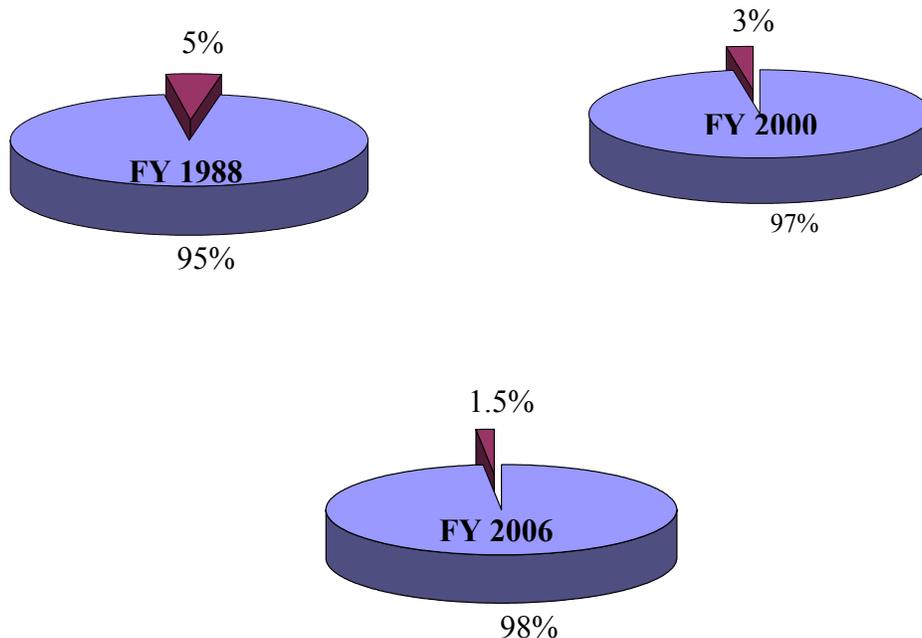
April 19, 2005

**NATIONAL SECURITY
AND
THE AMERICAN SHIPBUILDING INDUSTRIAL BASE**

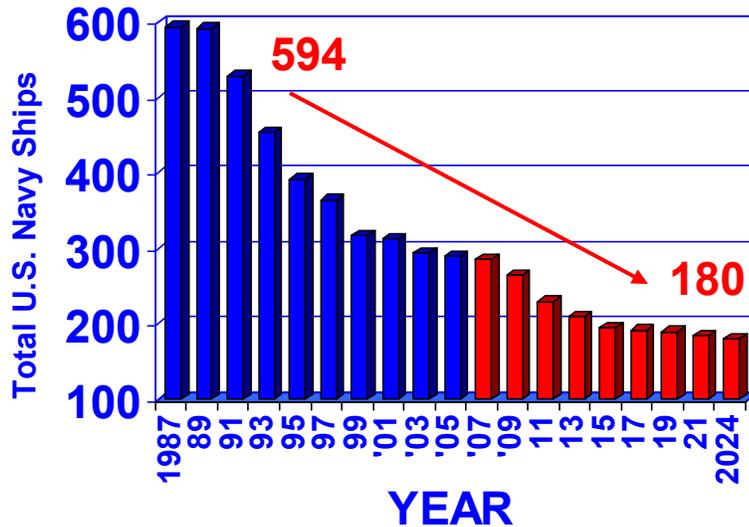
Naval Shipbuilding Budgets:

For more than a decade, the Department of Defense has been procuring the fewest number of naval ships since 1932. Annual naval ship production has averaged six ships a year. The fiscal year 06 budget calls for the procurement of just four new ships and is \$3.2 billion below the dollars appropriated for naval shipbuilding in FY05. Since 2001, the DOD budget has increased 28% (excluding supplementals) while the naval ship procurement budget has decreased by 33%. These low production rates have caused our naval fleet to contract to just 288 ships – a fleet that is 22 ships below the 310-ship minimum fleet requirement identified in the 2001 Quadrennial Defense Review. The fleet will continue to shrink to fewer than 200 ships by 2015.

Naval Ship Construction Compared to Entire DOD Budget

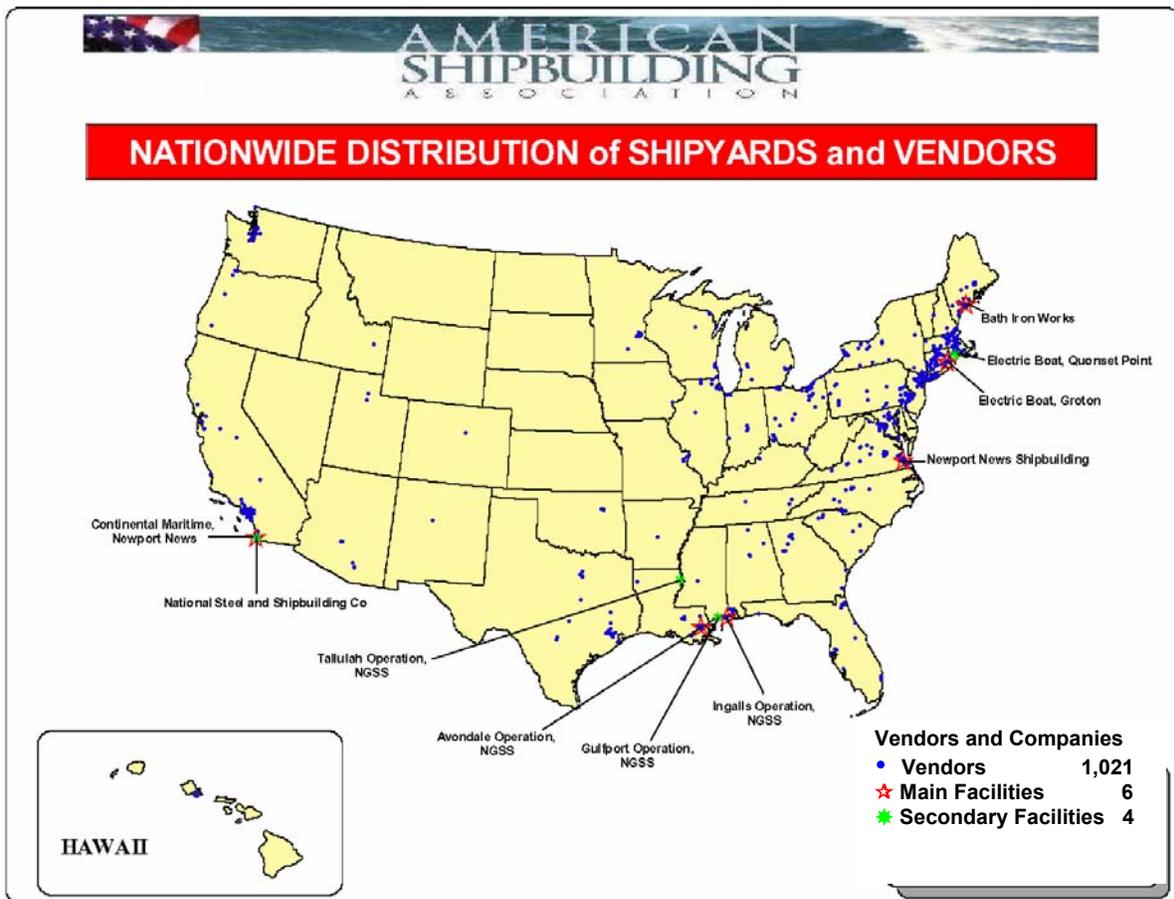


FLEET WATCH Decline of the U.S. Naval Fleet



Impact on Industrial Base and Unit Prices of Ships:

Persistently low production rates combined with consistently changing production profiles and schedules has taken a devastating toll on the shipbuilding industrial base, and is driving up the unit cost of ships. The United States has only two sources for its major naval ships, and for a majority of major ship systems and components there is only one source.



The U.S. shipbuilding industry employs approximately 350,000 people. The core defense shipbuilding industrial base is comprised of six major shipyards, owned by two corporations, and thousands of companies that manufacture major ship systems and components. Of the six major shipyards: Electric Boat of General Dynamics and Newport News Shipbuilding of Northrop Grumman build nuclear submarines and Newport News is the sole builder of nuclear aircraft carriers; Bath Iron Works of General Dynamics and Ingalls of Northrop Grumman build surface combatants; Avondale of Northrop Grumman and National Steel and Shipbuilding Company of General Dynamics build auxiliary ships; and Avondale, NASSCO and Ingalls build amphibious ships. The closure of any of these shipyards will lead to a single shipyard source for certain types of naval ships.

For many critical ship systems and components, there is only one remaining U.S. manufacturer in business today. For example, 80% of the Virginia Class submarine component manufacturers are sole source. Production rates are not high enough to sustain more than one company, and the companies left are struggling to stay in the business because of low production rates for all classes of naval ships.

Since 1991, the major shipyards have cut their engineering and production work force by 24,000 and 120,000 jobs have been lost throughout the manufacturing supplier base. It is estimated that the shipyards will be forced to reduce their workforce by another 13,000 between now and the

end of 2009 and that an estimated 58,000 people will be displaced in the supplier base. Shipyards and critical manufacturers face potential closure.

The DOD practice of cutting the number of ships planned to be procured and delaying construction schedules has caused major disruptions throughout the industry and caused unit prices to rise. Because there is no certainty in naval shipbuilding budgets and programs, the private sector is not able to plan its workload efficiently, size its workforce to match a stable workload, or have confidence with respect to facility and technology investments.

Consistently Changing Naval Budgets:

There has been no stability in naval shipbuilding programs over the past decade. The situation has worsened with recent budgets. The below comparison of the FY05 FYDP and the FY06 FYDP demonstrates the volatility in all shipbuilding programs. Ship prices are based on a certain quantity of ships of a class to be bought over a specified time period. Reductions in the number of ships of a class and in production schedules result in higher costs for all ships.

Navy’s FY-06 Shipbuilding Plan
(Compared to President’s FY-05 budget request)

	FY 05	FY 06	FY 07	FY 08	FY 09	FY 10	FY 11	FYDP
CVN-21	0	0	1 0	0 1	0	0	1 0	2 1
SSN-774	1	1	1	1	2 1	2 1	2 1	6
CG(X)	0	0	0	0	0	0	0 1	0 1
DDG-51	3	0	0	0	0	0	0	0
DD(X)	1 0	0	2 1	2 1	3 1	2 1	2 1	11 5
LCS	1	2 1	1 2	3	6 5	5	5	22 21
LPD-17	1	1	1	1 0	1 0	1 0	1 0	6 2
LHA(R)	0	0	0 1	1 0	0	1	0	2
T-AKE	2	2 1	1	0 1	0	0	0	3
T-AOE(X)	0	0	0	0	2 1	2 1	0 2	4
MPF(F)	0	0	1 0	0	2 1	2 1	2	7 4
TOTAL	9 8	6 4	8 7	9 7	17 9	15 10	12	68 49

This budget comparison highlights the magnitude of change:

- CVN-21 Aircraft Carrier – Construction start delayed one year
- SSN-774 Submarine – Production of 2 subs a year postponed
- DDX Surface Combatant - # of ships cut from 11 to 5, and Navy wants to sole source the DDX and future surface combatants.
- T-AKE Combat Logistics Ship – one ship cut from the FY06 budget

Is America Secure without the capability to Design and Build Warships?

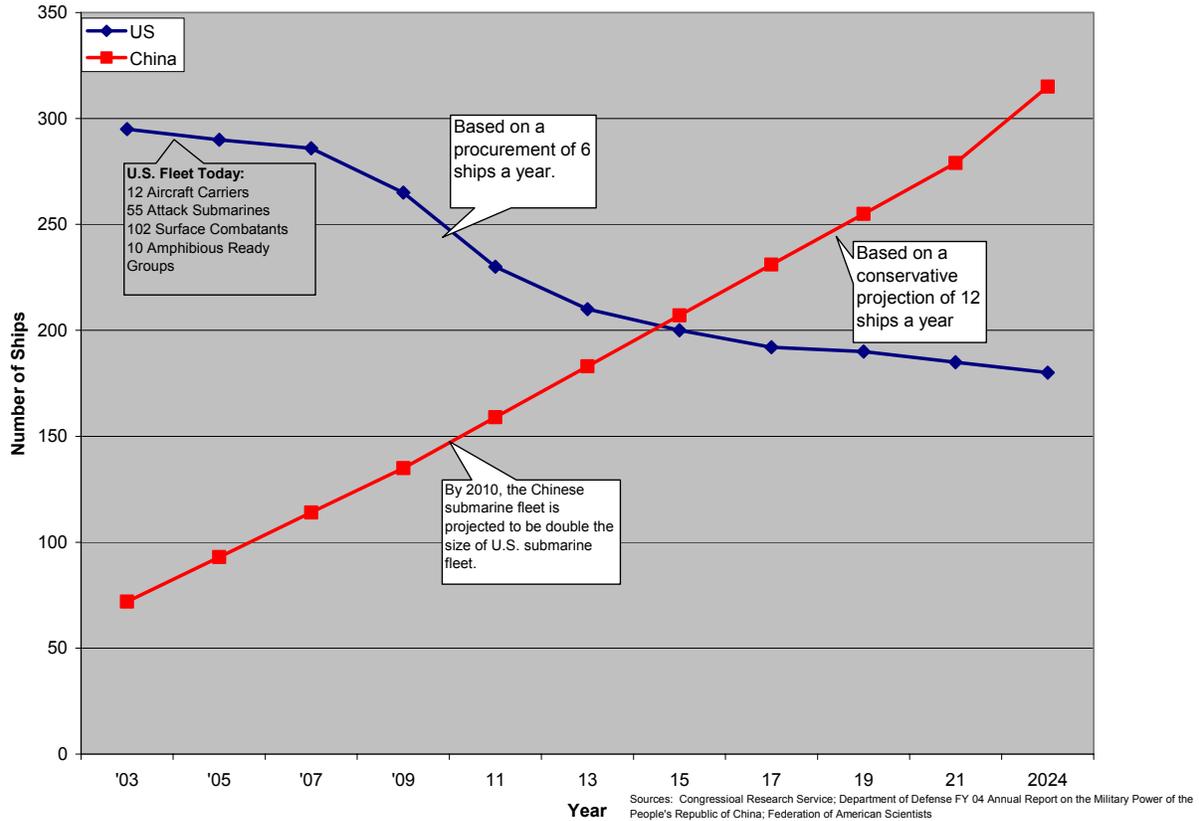
We should learn from Great Britain. The once mighty sea power nation took an extended holiday in naval ship construction, and lost most of her industrial base. Today, Great Britain is trying to build a nuclear submarine, but has lost the engineering know how. We are sending our engineers to England to help retrain them in the art of nuclear submarine design and construction. No new submarine is being designed in the U.S. today, which threatens our future engineering capability. Who will train us?

China's Growing Naval Fleet and Shipbuilding Industry:

DOD states that numbers do not matter, that it is capability that matters. Granted, the naval ships we build are the most capable in the world, but no matter how capable a ship is, it cannot be in two places simultaneously. Numbers and capability are both important in warfare. As the Chief of Naval Operations has stated on numerous occasions: "Numbers have a quality all their own."

While the U.S. is allowing our force projection naval fleet to decline, China is investing in building a blue water Navy to challenge the U.S. in the future, according to defense and intelligence experts. China's naval buildup began with China buying submarines and surface combatants from Russia. Now China, after years of investing in her indigenous shipbuilding industry, is building advanced submarines, surface combatants, and amphibious ships. If the U.S. allows our submarine fleet to shrink to 33 submarines, which is the projection based on the current build to retirement rate, China's submarine fleet will be twice the size of ours by 2010. If China expands her naval fleet by 12 ships a year, China's Navy will surpass that of the United States in 2015. While China's ships are not as capable as those of the U.S., the submarines and surface ships being built by China are advancing quickly in technology and capability. China is building a new class of conventional submarines, the Yuan Class. This class is a follow-on to its Song Class of diesel electric submarines. It also has nuclear submarines bought from Russia. It has begun construction of a new class of destroyers as a follow-on to its LUHAI Class. This new class is believed to match the air defense capability of the DDG-51 class.

Do Numbers Matter? China's Naval Fleet Overtakes U.S. by 2015



Conclusion:

Decisions made on the Navy's shipbuilding budget this year and over the next few years, will determine the physical capacity and the size of the shipbuilding skilled engineering and production workforce of the United States. If China continues to expand her naval fleet, it will take the industry this country has today, at a minimum, to match this emerging threat. If the industry is reduced further, the U.S. will have to reconstitute the industry if it is to counter this emerging threat. Reconstitution of facilities and the skilled workforce will be extremely costly and will take almost a decade.

Attached is the industry's recommendation to Congress on addressing the biggest shortfalls in the FY06 shipbuilding budget in an effort to stabilize the shipbuilding base and contain program costs.