The Capital Will Leave Quietly

Why the acquisition reckoning misses the number that decides it

By COL (Ret.) John Cavedo | 360 Enterprises LLC | 18 June 2026

For the first time in a generation, venture-backed technology firms are treating the Pentagon as a serious customer. Ukraine, autonomy, and renewed great power competition put defense back on the table for capital that spent two decades avoiding it. The policy machine has noticed. Commercial-first is the new default, portfolios are replacing programs, and the language coming out of the building finally sounds like it understands speed.

I have spent the better part of two years in the rooms where the other side of that decision actually gets made. Board rooms, founder conversations, private equity partners deciding whether to commit. I sat in those rooms after thirty years in the Army, the last as the JLTV project manager, and six years running a defense manufacturer as its CEO. I am now a limited partner in a venture fund with five years of capital calls in front of me, so I am tied to the same arithmetic the founders are. I did not take that risk for index-fund returns.

Here is what I learned. The capital is not deciding whether the mission matters. It is deciding whether the math closes. And the reform debate, for all its energy, is fixed on the wrong variable.

Two entities, one misread

The Department keeps collapsing two very different things into one idea, and the confusion is expensive.

A venture fund and a venture-backed company do not make money the same way. The company makes money the way any business does, by selling a product at a margin. The fund makes money exactly once, at the exit, when a company is acquired or goes public. Until that moment the fund has earned nothing. Not from revenue, not from profit, not from dividends. A fund holds twenty or thirty companies. Most return little. One or two have to carry the entire portfolio at three to ten times the capital put in. Those one or two breakouts are the whole game.

That structure has a consequence the building rarely follows to its conclusion. A breakout exit only happens when a company has high margins, or the credible promise of them, because margin is what builds enterprise value, enterprise value is what sets the exit price, and the exit is the only thing the limited partners ever see. Suppress the margin and you have not trimmed a little profit off the top. You have removed the reason the capital showed up.

This is where the current reform model has a blind spot it does not know it has. The model is built on a sound instinct: let private capital fund development, then compete for the output. The trouble is the chosen instrument. Recurring fixed-price production competition is, by design, a margin-compression engine. It is supposed to be. So a venture-backed firm can do everything the new system asks. Win the capability shoot-off. Win the recurring production award. Deliver at scale. And still never produce the margin an exit requires. What it ends up with is a government revenue stream, which is not what its capital structure was built to deliver. The contract is necessary. It is not sufficient. Winning production at a price the government is comfortable with is not the same as generating a venture return, and the people writing the checks know the difference even when the people writing the requirements do not.

The math that makes it a no-bid

None of this is emotional. It is numbers, and the numbers are not hard to run.

Take a notional unmanned ground vehicle. Six hundred units over six years, ten million dollars of company money invested up front before a contract exists. Set the unit cost at three hundred thousand dollars with a ten percent margin, which is normal across the defense industrial base. Risk-adjust for a realistic eighteen percent combined probability of both winning the award and the program staying funded, discount it like any investor would, and the net present value comes out around negative eight million dollars. That is a no-bid. Not because the firm lacks patriotism. Because the project loses money.

Now solve it in reverse. To drag that same program to a barely positive net present value and an internal rate of return that just clears a venture hurdle, the unit cost has to rise to roughly four hundred thirty-four thousand dollars at a forty-one percent margin. The government will not pay that, and I would not expect it to. But that is the point. The honest number sits in a range the system treats as profiteering. Defense industrial base net margins average about six percent. Commercial technology runs four to seven times that. Apple clears thirty-eight on an iPhone. The math does not bend because we wrote a smarter acquisition strategy on top of it.

Underneath the math is something harder to fix than a pricing formula, because it is not written down anywhere. The Department values low visible margin over high real efficiency. A company that charges a hundred dollars, spends ninety-five, and earns five percent looks reasonable. A company that charges ninety-five, spends sixty, and earns thirty-seven percent looks like it is getting away with something, even though it is cheaper for the taxpayer and more capable. That instinct is not in the regulation. It lives in the heads of cost estimators, program offices, and contracting officers who were taught that thin margins are virtuous and fat ones are suspect. You can publish every industrial strategy you want. If the value system in the building still equates low margin with integrity, the most efficient, best-capitalized firms will read the room and walk. They already do.

This is the part the affordability process gets backwards. Per unit price targets are built to stretch a budget, and they are blind to how industry decides. They assume instant recovery of research and development, they assume a blink-of-an-eye time horizon, and they ignore the probability math entirely. The result is a target that looks responsible on a government spreadsheet and pencils as a loss on an industry one. Fewer firms bid. Competition thins. The very outcome the target was meant to protect, a healthy supplier base, is the one it erodes.

The clock nobody is pricing

Suppose the building fixes all of it. Suppose margins are allowed to breathe, the demand signals arrive, and the model works the way its authors intend. There is still one variable nobody is putting a number on, and it may be the one that matters most.

Time.

The reforms on the table are real, and the people driving them are serious. But this transformation did not arrive as a shock to the system. It arrived as the agenda of one administration, on its terms, on its calendar, and it is welded to that administration. That is the difference between this moment and an actual Sputnik. Sputnik produced a durable, bipartisan settlement. The institutions it created are still standing almost seventy years later because the consensus outlived every president who came after. Reform that lives by executive energy dies the same way. Two years to a midterm. Lose both chambers and the agenda stalls. Lose the White House in the next cycle and the successor unwinds it, the way every administration now unwinds the last one out of something close to spite. The acquisition system does not even have to absorb this reform the slow way, through process and precedent and habit. An election can simply reverse it.

Put that next to the capital, and the two problems turn out to be the same problem. Venture funds invest on a five to seven year horizon to reach an exit. The policy that would permit exit-grade margins is good for, at best, two to four years before it faces an electorate. So the multi-year demand signal that the reform model treats as its fix is not actually credible. No serious fund commits capital to an exit that lands after the policy enabling it may already have been repealed. A multi-year commitment from an administration that could lose Congress in two years is not a commitment. It is a forecast, and capital does not price forecasts at face value.

Margin and durability are one question wearing two faces: whether a short-horizon political system can make a long-horizon promise that private capital will believe. Right now it cannot, and no contracting vehicle solves that. Only a settlement that survives a change of party does.

What it would take

I am not arguing against the transformation. I am arguing for finishing it, and finishing it means naming the variables the current debate skips.

Compete for the output of private investment, yes. But pay margins that produce exits, not just revenue, which means rebuilding what the building considers a fair return for fast-cycle, high-risk work. Build a demand signal with enough bipartisan and statutory weight that it can outlive an election, because a signal that cannot is just noise to the people it is meant to persuade. And do both before the window the reformers correctly identified closes the way it has closed before.

The firms DoD finally attracted will not stage a revolt if none of this happens. That is the trap. They will not write angry op-eds or rage against the acquisition machine. They will look at the margin, look at the clock, and quietly redirect their capital to markets where the math closes and the rules hold still long enough to plan around. Energy. Logistics. Consumer technology. Places with better-aligned capital structures and no election risk baked into the business case.

Not loudly. Just quietly. And we will be left wondering why the prototypes were so promising and the production never came.