

Defense Update

COVID is over, back to work: what 80% progress payment rates mean for FCF

Industry Overview

Progress payment rate back to 80% from COVID era 90%

On May 8th, 2023, the Department of Defense (DoD) announced that the progress payment rate would revert back to 80% after being temporarily raised to 90% in the wake of the COVID-19 pandemic. The temporary increase had been in place since March 2020.

However, the DoD is maintaining the 95% rate for small businesses (consistent with the March 2020 raise) for the time being. The announcement also notes that existing contracts will retain the higher 90% rate for the life of the contract and the reversion to pre-COVID rates will apply to new contracts, task orders, and delivery orders.

Reversion of progress rate could drag on FCF of primes

By using progress payments, the DoD reimburses the contract for a fixed percentage of the costs incurred by the contractor, with the balance being paid upon completion of the contract. During the pandemic, increasing the progress payment rate helped improve contractor's cash flows and provided support throughout the supply chain. To that point, we believe the reversion to the lower progress payment rate will likely be a headwind to the cash flows of the defense primes on future contracts.

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