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# Key Priorities for Aerospace and Defense Compensation Committees

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PRINCIPAL

The aerospace and defense (A&D) industry is operating in an increasingly demanding environment, shaped in part by ongoing geopolitical tensions and heightened global security demands. Defense spending remains elevated, commercial aerospace continues its recovery, and companies are investing heavily in AI, autonomy, and advanced manufacturing. At the same time, challenges from supply chain constraints to labor availability persist, and the policy environment is placing greater emphasis on speed, readiness, and support for overall mission effectiveness.

For compensation committees, the implication is straightforward. The definition of strong management performance is evolving. The more difficult question is whether executive compensation programs are evolving with it.

Compensation structures in A&D tend to change gradually, while the business environment can shift much more quickly. That gap is where risk emerges. Not because plans are poorly designed, but because they may no longer fully reflect how value is actually created.

In this environment, compensation decisions also carry weight beyond financial outcomes, influencing how organizations prioritize, invest, and deliver on critical commitments. Against that backdrop, several priorities should be top of mind for A&D compensation committees.

## Aligning Incentives with How Value Is Actually Created

A&D companies operate in long-cycle, capital-intensive, and operationally complex environments. Value creation is shaped by factors such as how effectively they deliver on complex, long-term products and programs—often under tight production timelines, capital constraints, certification cycles, and aftermarket performance. It is not driven solely by near-term financial results.

Yet many compensation programs still lean heavily on relatively short-term or linear financial measures.

The core issue is rarely the structure of the plan itself. More often, it is whether:

- Performance metrics reflect the true drivers of value
- Goals are calibrated appropriately for the business cycle
- Payout curves differentiate meaningfully across levels of performance

In practice, the most effective programs are those that reflect how the business actually performs, not how performance appears in a simplified financial model.

For compensation committees, this means regularly pressure-testing whether the program aligns with the company's operating realities, not just whether it aligns with market practice.

## Reinforcing the Right Kind of Execution

In today's A&D environment, successful execution is becoming a more important differentiator. Increasingly, it means:

- Converting backlog into profitable delivery
- Improving production throughput
- Navigating supply chain constraints
- Hitting program milestones
- Deploying capital in ways that support readiness and resiliency

Recent Executive Branch policy developments and commentary reinforce this shift, including a suggestion that executive compensation at defense contractors could be capped at $5 million. While such policies stop short of prescribing specific compensation structures, they point towards potential constraints on executive incentive metrics, emphasizing measures around speed, operational readiness, and mission support. Companies should continue to monitor how this concept may evolve through future policy, regulation, or implementation guidance.

This raises an important question for compensation committees: Do incentive programs reinforce the behaviors that this environment demands?

For some companies, existing financial metrics may already capture these outcomes. For others, there may be a need to incorporate more explicit operational or milestone-based measures. The objective is not to replace financial discipline, but to ensure that the program reflects the full set of priorities the business is being asked to deliver against.

## Evolving Metrics to Reflect Strategic Priorities

One of the more subtle challenges facing compensation committees is how to evolve programs in step with strategy. Most incentive plans are built around what has historically driven performance.

But in A&D, the drivers of future value are increasingly tied to:

- AI and data capabilities
- Autonomy
- Digital engineering
- Advanced manufacturing

Some companies have begun to incorporate forward-looking or strategic measures to signal these priorities. The intent is not to chase trends, but to ensure that incentives remain aligned with where the business is going.

The challenge for committees is determining how far and how fast to move. We see this tension play out most clearly in how performance is defined and measured. There are two competing risks:

1. Evolving too slowly and failing to reflect meaningful shifts in strategy
2. Reacting too quickly to emerging themes that are not yet fully embedded in the business

The most effective approach is disciplined evolution—but in practice, it often requires accepting this difficult trade-off. Compensation programs should reinforce strategic priorities while maintaining clarity, focus, and line of sight to value creation.

## Resisting Overreliance on Market Norms

A&D companies operate under significant scrutiny from investors, proxy advisors, regulators, and, increasingly, policymakers. In that environment, there is a natural tendency to gravitate toward standardized compensation structures that are easy to defend. However, while external perspectives are important, over-reliance on them can lead to programs that are insufficiently aligned with the company’s strategy and operating model.

The most effective compensation programs are not those that most closely mirror the market. They are the ones deliberately designed to support how the company creates value while remaining clear and defensible to external stakeholders. This balance is particularly important in A&D, where companies often have diverse business portfolios, varying performance horizons, complex capital requirements, and evolving talent needs.

A standardized approach may simplify governance, but it rarely produces the best outcomes.

## Balancing Performance Alignment with Talent Realities

Compensation committees must also balance performance alignment with the need to attract and retain critical talent. The competitive landscape for talent in A&D is shifting, particularly as companies compete for expertise in rapidly advancing areas such as AI, software, and advanced engineering. In many cases, the relevant talent market extends beyond traditional A&D peers.

This creates tension:

- Maintaining a strong pay-for-performance orientation, while
- Ensuring compensation remains competitive and compelling for key talent segments

There is no single solution, but it reinforces the importance of viewing compensation holistically as a tool to support both performance and retention.

## Closing Thought

The A&D industry is not abandoning its long-cycle foundations, but new expectations around greater speed, technological advancement, and operational responsiveness are reshaping it.

For compensation committees, the challenge is not to redesign programs from scratch. It is to ensure that existing frameworks evolve in ways that reflect these realities. At their best, compensation programs do more than reward outcomes. They reinforce priorities, align leadership with strategy, and provide a clear signal about what success looks like.

In today’s environment, that signal carries real weight.

## About the Author

Stephen advises on executive compensation for public and private companies, including benchmarking, incentives, pay-for-performance, and proxy analysis/disclosure.

## About Pearl Meyer

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