

# *Outsourcing Manufacturing*

Including 7 Critical Pitfalls To Avoid



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# OUTSOURCING MANUFACTURING

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# OUTSOURCING MANUFACTURING

## Contents

<u>Prelude</u>	.....	4
<u>Intro to Outsourcing Manufacturing</u>	.....	5
<u>Long Road to Benefits</u>	.....	6
<u>Why Outsource?</u>	.....	7
<u>History</u>	.....	8
<u>Disadvantages of Outsourcing</u>	.....	9
<u>7 Common Outsourcing Problems (Pitfalls)</u>	.....	10
<u>Outsourcing Advantages</u>	.....	11
<u>5 Main Reasons for Outsourcing</u>	.....	13
<u>How to Ensure Outsourcing Quality</u>	.....	14
<u>How to Find a Suitable Contract Manufacturer</u>	.....	15
<u>Fragile Foreign Relations</u>	.....	16
<u>DIY Outsourcing</u>	.....	17
<u>Why Hire A Consultant?</u>	.....	18

## **To Those Who Fuel This Outsourcing Revolution**

Inventors, Designers, Entrepreneurs, Builders, Creators of things people want and need; each an artist in their own right, turning ideas into valuable products; Companies that produce or distribute parts and products to the world. We support you. You see potential and opportunity; see a need and solve it with a product. Your inspirations and inventions make the world a better place. We honor you.

We hope to help you through this revolution in manufacturing called outsourcing.

The revolution surges on and awaits your profitable participation.

## Introduction to Outsourcing

*"No man is an island."* – John Donne 1624

The Internet era has done so much for us with respect to the advent of breaking down borders, preceded by trade agreements between countries. It is fundamental modern management knowledge that no man is an island, no department is an island within a company. If a department in a company can perform a task better and cheaper than another, only a foolish company would ignore the cost savings of assigning the task to the more efficient department.

We're all in this together and we can work together for greater profit for all. Why should a company function as an island cut off from the world, when some other place could produce some or all of what's needed better, cheaper, faster, or all of the above?

### **Globalization**

With the globalization of everything from services like computer programming to hard goods like product manufacturing, it is difficult to tell whether the product or service you order is actually made or performed on domestic soil. Software companies like Apple and Microsoft have many offshore facilities full of programmers for their apps, and many domestic manufactures are actually domestic companies with overseas plants, while others are outsourcers that do not have their own factory. The latter two look internationally to leverage foreign territories that have lower costs, and in some cases consider the foreign factories to be almost a part of their company due to the integral purpose.

One company cannot be all things; each has a specialty. The production of a new part or product may not be that specialty, either for financial reasons, equipment reasons, manpower reasons, quality control reasons, or any other reason. Often they must seek a partnership in order to produce what is needed economically and with high quality.

### **Partner Up For Mutual Success**

Rather than sacrificing something like the cost or quality of goods in a way that might tarnish your company or product's name, or the time to market, it makes sense to partner up with another company that can more quickly and effectively produce what is needed.

Finding the best partner for your project(s) takes substantial work and the traditional rules of business do not apply. One must first and foremost understand that western companies operate differently than those overseas. In China for example, the supply chain can involve many different companies that work together in often informal relationships that would boggle the mind of the typical western executive.

Nonetheless, it behooves most companies to outsource manufacturing of certain stages or entire production in order to:

- Focus resources on core business
- Minimize tooling costs
- Control manpower
- Eliminate training overhead
- Produce with better quality
- Quicken production

## Long Road

As one embarks on the string of arduous tasks associated with finding and contracting with a custom manufacturer overseas, they typically discover that it takes approximately 12 months from the beginning of their investigation to successfully outsource manufacturing of a part or product. In that amount of time, the opportunity to bring the part or product to market may be gone.

There are a lot of steps, functions, and pitfalls to investigate, negotiate, and avoid. There are many hurdles to creatively circumvent before a company acquires a basic set of capabilities for outsourcing, such as, but not limited to, the expertise to evaluate a supplier's ability to meet requirements; independently test prototypes before production; create samples; and fulfill the necessary logistical activities such as arranging the transportation and freight brokering.

Outsourced custom manufacturing can give companies a competitive edge; but with language barriers, cultural differences, fluctuating exchange rates, laws, taxes, trade restrictions, and trust issues, finding suitable contract manufacturers can become an arduous task.

The road to outsourcing manufacturing is long and winding, and the road signs are usually not well illuminated. Choosing an experienced partner with well-established relationships overseas can make the experience both more profitable and more fulfilling.

### **Benefits**

If you reduce your expenses by outsourcing, and if your sales remain the same, you'll have more money to spend on marketing, debt reduction, research and development, headquarters salaries and other areas that can help improve your bottom line.

Savings can be derived from lower labor costs, less expensive tooling, shorter set-up times, and lower raw material inventory. However, no savings can offset the risk to your reputation if the quality of your product suffers as a result of outsourced supply. It is therefore imperative that your outsourcing partner take very seriously their position of responsibility with regards the quality of your product. Only a partner with experience and well established relationships can be expected to perform to a high standard when there a problem occurs, as they inevitably do.

## WHY OUTSOURCE MANUFACTURING?

What would drive one to send something they could do themselves out to someone else? Just because you *could* do something if you sunk enough money and time into it, doesn't make it a good business decision. Executives know that usually delegating is the better way and that surrounding themselves with experts in their respective fields is more productive, profitable, and leads to progress in the long run. Likewise, since no company is an island, it may make sense at some point to outsource some things.

Most people attribute the outsourced manufacturing savings to labor costs which are reduced through wages, payroll taxes, benefits and shared expenses, and even by alleviating union problems. Let's examine some other reasons why a company might outsource manufacturing.

### **Organizational Reasons**

- Enhance effectiveness by focusing on what you do best
- Increase flexibility to meet changing business conditions
- Transform the organization
- Increase share-holder value

### **Customer Reasons**

- Demand for products and technologies
- Economical changes
- Increase value, customer satisfaction

### **Improvement Reasons**

- Improve operating performance
- Expertise acquisition
- Technological improvement
- Improve management and control

A company may want to maintain or lower its current price levels to become more lean and mean, or because something in the business landscape changed. Lowering labor, operating, and overhead costs through outsourcing allows a company to reach such pricing goals. Extra profit can be used in many ways, including ability to take market share from competitors, or re-invest to increase sales. In some cases, outsourcing enables companies to lower prices *and* still increase profit margins.

### **How They Do It Cheaper**

Offshore manufacturing can be calculated to be less expensive due to either or all of lower costs of labor, education, material, resources, real estate, and plant costs. With almost everything being more expensive in America, there are plenty of areas in which overseas countries save money to produce less expensive goods.

## **AMERICAN HISTORY OF OUTSOURCING MANUFACTURING**

Manufacturing represented 30% of American GDP in 1950; but inflation and unions drove plant material and labor costs up to a point in the 1960's when U.S. offshore programs like the "Twin-plant programs" with Mexico were born. It was less expensive to send parts there to be assembled and then shipped back into the US. By 1965, manufacturing accounted for 53 percent of the American economy, but by 2009 it only amounted to 11% of GDP.

In the grand scheme of economics, this manufacturing decline is not a bad statistic. When progress happens things work themselves out, so when companies grow stronger due to outsourcing manufacturing, and domestic factory jobs are lost, people do other things to service the stronger companies and other companies are formed and more jobs are created. Some companies' very existence, and the wellbeing of their employees, depends solely on the ability to outsource production. Without outsourcing, those jobs would not be, their companies would not exist, the money they make would not be spent, and the local economy would suffer because of it.

With proper supervision, off shore companies can maintain product quality and safety while reducing costs.

## DISADVANTAGES OF OUTSOURCING MANUFACTURING

At times, legitimate manufacturing companies may use unscrupulous tactics or misinformation to convince you to take advantage of their services. Therefore, it is vitally important to research any potential vendor or agency before you use their services or products. In fact you should go over the entire process and all parties involved right up until the product shipment is received.

Despite the realization that outsourcing is unpopular with the American public, domestic companies flock in droves to have their goods manufactured overseas.

Manufacturers and individuals in foreign countries will often agree to everything to avoid embarrassment, so those who outsource to them have to check and re-check everything at every step of the process. You'll need engineers and quality control personnel to inspect the goods prior to shipment so that a disaster doesn't occur, like the million toys recalled by Mattel in 2007.

There have been FDA concerns and health and safety issues related to other products.

Overseas business partners may not be operating legally or may be finding ways of getting around the regulations, so you'll need to independently test all products to ensure that they meet specifications.

Government regulation is often poorly enforced.

In overseas countries there is much corruption in government (and business), and in the agencies that deal with the government.

There are so many foreign rules that western executives must learn, not to mention domestic rules that apply and must be adhered to.

Outsourcing has many pitfalls and domestic companies would be wise to make themselves aware of what can go wrong and what steps should be considered to lessen the gravity of problems that arise.

## **SEVEN COMMON PROBLEMS (*PITFALLS*) WHEN OUTSOURCING MANUFACTURING**

Every element of outsourcing is not applicable in every situation. Every relationship is different depending on the way the participants co-operate. Excellent agreements are essential, however, things can go wrong with your outsourcing on both sides of the relationship. A new relationship with a contract manufacturer will require a completely new set of management techniques.

### **Communication Costs**

It is common for companies to ignore or underestimate the long distance and higher expenses for communication when working with contract manufacturers.

### **Inadequate Governance**

Domestic companies agree that after their first outsourcing venture they truly should have had an in-house steering committee to oversee the work of the contract manufacturer. This doesn't require new personnel, just calculate a certain percentage of the working time of the employees on the team to be devoted to smoothing the outsourcing process and relationship, over and above their regular duties.

### **Loss Of Control**

Your technical staff's know-how, and the documents they produce are going to be handled by another company, the contract manufacturer, who is independent and has its own interests, profitability concerns, and morals which might be different than yours.

### **Business Growth**

Your dependency on the supplier might grow in time so you need a plan in place to be able to continue your business in case you hire a consultant or a sub-contractor to handle the relationship, or bring the production back in-house.

### **In-house Resistance**

The participation and buy-in of the existing in-house team is crucial so that their know-how will be transferred to the suppliers. It might be wise to have each team member read this document in preparation for the new way of conducting business.

### **Dynamic of Costs**

Salaries and other operating costs in growing countries have been increasing steadily. Be prepared to renegotiate an agreement down the line and to follow market indicators in raw materials and labor rates.

### **Sly and Unfair Suppliers**

Contract manufacturers or their representatives could exploit their superior experience in outsourcing and manipulate unsuspecting companies. Unscrupulous businesspeople exist in all countries, but are much more difficult to hold to account when they are overseas. The laws, when enforced, often favor the local.

## **ADVANTAGES OF OUTSOURCING MANUFACTURING**

Despite precautionary warnings and a few instances of outsourcing gone wrong, by and large those who outsource their production enjoy peaceful, profitable relationships with their suppliers. The advantages often outweigh the pitfalls especially when you are guided by an outsourcing firm with experience to match their dedication to making the process seamless.

### **Competitive Pricing**

The most important justification for the companies who contract to outside factories is lower cost of goods. If domestic companies don't overspend on the treacherous research phase, and don't fall prey to an unscrupulous overseas manufacturer, and don't involve themselves in logistics headaches, they stand to gain competitive advantages through lower prices or even better service.

### **Improving Company's Focus**

Companies that outsource can concentrate on their core business, while production is taken care of by experts. So often outsourcing is the way to a greater focus on a company's core capabilities.

### **Leverage**

Experience

Contract manufacturers have already made investments in technology, methodology, and people, and their previous experience in the field with other clients who have had similar demands is a valuable asset to be leveraged.

### **Investment**

Whatever savings a buyer realizes by outsourcing manufacturing can be leveraged to be invested in another way.

### **Freeing Up Resources**

By contracting manufacturing operations to an outside company, the buyer can redirect employees to other more profitable activities. Labor costs are also maximized when outsourcing results in reduction in set-ups and shop floor time management processes.

### **Non-critical Business Functions**

Outsourcing is the way to decrease the investments which have to be made in adjoining business activities.

### **Better Technology**

It is most likely that the contractor to whom you outsource will have better technology geared toward the production of whatever you need, because it's the mainstay of their business. They tend to have the best pertinent equipment because of, and to suit, their specialization. This specialization frees up resources for investment in more core functions within a firm.

## **Shared Risks**

Companies that choose outsourcing can soon become more dynamic and flexible to meet changes in the economy. Investment risks made by a company in different fields are enormous. Markets, competition, laws, financial terms and technology are changing very fast. It is very difficult to stay abreast of the changes. When one outsources, the risks are divided between several companies. By sharing investments, the risks for one company decrease.

## **Improvement of Production and Reduction of Delays**

More products or components are processed outside the company in a shorter time while the company's resources are pointed to its other critical activities. The contracts stipulate the delivery terms for the products or components and this way any delays become the contractor's responsibility and possible loss. All parts of an outsourcing project can be closely followed. Some outsourcing firms will take on the additional role of a local distributor, stocking product domestically that can be delivered just-in-time, as if the manufacturing location of the product were domestic rather than overseas.

## **Additional Profits for Employees**

When any part of production is outsourced, the productivity and efficiency of employees and management generally increase. The employees will be focused on the activities where they have the necessary skill set, and their self-esteem will increase, coinciding with their increased production. The major benefits can be registered not only in what relates to decreased cost of goods, but also in the employees' perceptions of the company. Better usage of employees and resources leads to better usage by the employees of the facilities and resources, which often leads to more profit being shared with employees in various ways.

## **Better Inventory Management**

Any problems with respect to the availability of inventory can be resolved with the components or products arriving just-in-time. Less money is tied up in inventory. An outsourcing firm often will have enough breadth in its current agreements with suppliers to be able to accommodate smaller domestic manufacturers with smaller part requirements, making it feasible for them to take advantage of outsourcing in spite of their limited size and market penetration.

## FIVE MAIN REASONS FOR OUTSOURCING

Even in short term contracts, a confident relationship can be developed with the suppliers. There are many scenarios in contract manufacturing wherein regular companies rely on other manufacturers that can assist them on a mutually profitable basis.

### **Specialized Work**

Some products and processes are just too specialized and are more expensive or risky to manufacture in-house, especially if either a specific knowledge or a machinery upgrade is necessary. A specialist can deliver a higher quality product, usually faster, and often cheaper.

### **Insufficient Capacities**

Outsourcing is a solution in case of insufficient industrial capacities where serious suppliers are necessary. This allows an optimized allocation of machinery or manpower at a cost that can be lower and which the buyer can afford. The company that outsources may sell off some machinery that is no longer needed, or may use outsourcing instead of having to purchase new machinery.

Once outsourced, capacities can vary according to demand and business cycles; orders can be reduced or increased, and the buyer can ask the suppliers to manufacture the products according to their own schedule.

### **Cheaper Supply**

When the supplier's prices are lower than the buyer's internal costs of doing their own production, the savings can be considerable. Costs related to quality control of raw materials and finished goods are included in this savings, as well as control of the delivered product.

### **Key Activities**

Thanks to outsourcing, attention can be oriented toward key activities. An increased excellence in other departments can be expected, such as new product development.

## HOW TO ENSURE QUALITY OF OUTSOURCING

Ensure that expectations are well documented and well conveyed to the contractor. Having quality procedures in place for raw materials, safety standards, shipping, and receiving will ensure that the material and production output comply with the standards that you and your customers demand.

There are certified agents that can visit potential factories on your behalf. This is one more thing a company has to consider, and another reason why trying to enter into contract manufacturing alone is both frustrating and risky.

Quality can be affected by the combination of advanced technologies used in equipment and quality control, employee training, and advanced processes and procedures which address improved manufacturing and cost effectiveness.

Look for well-developed Quality Systems certified to ISO 9001 at a minimum. A buyer will need the support of those system performance standards, and monitoring and evaluation of many critical processes and quality objectives, looking for areas of possible improvement.

Nobody wants RMA handling, defective parts sorting, and other quality failures to become a large portion or focus of business. Practice avoidance of this aspect of business with sound QC.

Coordinate with the factory's quality control department to develop the QC process, including a final checklist for QC inspection purposes. The system must be successful in exposing potential problems early on, when solutions are easily and cheaply implemented.

## HOW TO FIND A SUITABLE CONTRACT MANUFACTURER

Have a list of must-haves and nice-to-haves and questions prepared related to your project to better qualify potential partners.

### **Common Relationships**

Who do you know that makes parts or products? Ask everyone you know or do business with about their products, because a very good way to locate a partner to make your product is through a common relationship. You may be working with an organization that has an established relationship with a trusted manufacturing partner and you may get a referral, or an introduction. LinkedIn.com is great for this kind of networking where everybody knows somebody who is somehow related to what they need.

### **Word-of-Mouth Networking**

Let your current word-of-mouth network know what you need. They are usually more than willing to volunteer information that may lead to a few solid leads. Talk to those in your contact list who have direct contact with potential manufacturers.

### **Professional Organizations**

Expand your network directly through online and offline organizations you can join, like forums and associations, or the Chamber of Commerce, and other business networking events. When you meet other networking professionals and tell them about your organization, pay close attention as they tell you about their products, core capacities, and current projects. Often, you can meet some great like-minded people that could become potential partners or refer you to others.

### **Niche and Industry Trade Groups**

Don't be afraid to find potential manufacturing partners through niche and industry trade groups, trade associations, and industry-specific conferences. User groups and related consultant reseller groups are also great places to meet niche providers. Sign up for industry mailing lists for newsletters and blogs, as these subject matter experts may showcase the work of potential partners.

### **Vendor Web Sites**

A potential partner's website is a good source of information, but not always the proof you seek. Once you receive a referral or find a lead on the web, read everything you can find about them on the Web.

## **ESTABLISHING AND MAINTAINING CONTRACT MANUFACTURERS' RELATIONSHIPS**

Establish *guanxi*. In China, establishing business relationships is much more than surface-level networking. China's cultural customs are deeply rooted in its history, and even though they are so technologically advanced, and their economy is growing so large, China is slow at building relationships. A small-business operator from the United States can ruin a potential relationship with a Chinese factory from the very start by not following specific customs.

Did you know it is regarded as impolite to neglect to offer a business card? Here's a tip on business etiquette: Always use both hands to present a business card to a Chinese person. When accepting a card, examine it carefully for at least 10 seconds so that they are comfortable that you paid attention to them or perhaps their credentials.

## DIY OUTSOURCING MANUFACTURING

To work directly with manufacturers, you would have to properly

- research and analyze the outsourcing possibilities;
- search for offshore manufacturing that suits your product;
- evaluate manufacturer's production capabilities, history, credentials and overall production quality;
- obtain a sample to inspect before agreeing to a contract;
- investigate costs;
- discover possible time frames;
- research and analyze shipping and logistics for dependability and cost;
- become knowledgeable in importing and exporting regulations between countries;
- understand customs, insurance, tariffs and taxes;
- visit the final candidates for an on-site inspection.

The right sourcing partner is the most critical component in any outsourcing strategy. Companies' needs should be matched with the appropriate manufacturing facility, and an agreement where both sides win has to be negotiated.

### **Cost of Doing Your Own Research**

Understand how your lowest total cost of production can be met by manufacturing companies. Sure there's the labor savings, but there's also considerations like freight, engineering support, travel, and logistics. Each has to be investigated, and it costs money to do so. If you do it yourself, when all of the expensive and time consuming research and analysis is considered, the first time manufacturing is outsourced will be expensive because there's such a learning curve and so much time, and research on the venture to be done. After a possible strategy is determined, and a few possible suppliers identified, traveling overseas to visit the factory and arrange details is very necessary, time consuming, and expensive. If it is necessary to obtain a visa to enter the foreign country, more time and money has to be spent, and then a non-direct flight to China, for example, will take 24 hours or more.

## WHY CONSULTANTS?

Contract manufacturing consultants provide negotiation, communication, and oversight for all aspects of a relationship in coordination with the factory.

With a consultant, you avoid huge expenses for searching out a viable outsource. More companies who try to enter into outsourcing on their own, without the help of an experienced consultant, have to spend more for researching, development, marketing, and launching. Without leveraging the experience and wealth of information already learned by a trustworthy consultant, they are prone to all of the disadvantages of predatory manufacturers overseas and the cost of their products will be higher.

### **Business Relations Leadership**

The buying company must maintain control of the relationship with the factory. If the outsourcing relationship progresses and the amount of outsourced work increases, unscrupulous consultants might takeover leadership in the buyer's business relations with the contractor. In time, some of these relations may be managed by the consultant, and communication will not reach the buying company.

**Con-Tech Custom Manufacturing** conducts a detailed study of their client's requirements, including such areas as product samples and/or drawings, volume and frequency of orders, and budget to match the client's specific requirements with the most appropriate factory. They can provide details which may include samples or photos of similar products produced by the factory. Of the utmost concern will be the level of production quality achieved by the manufacturer, and evidence based on experience of its reliability and consistency over time. Product pricing will also be a necessary component of the recommendation.

### **Taking Your Order for Contract Manufacturing**

The client supplies product, packaging, and ordering information such as: drawings (CAD files, if possible), product specifications, and/or samples, volume/order frequency, as well as labeling and packaging details.

### **Con-Tech's Role**

- Introduce a manufacturer who can meet your needs.
- Coordinate all details involved in the development of approved samples.
- After an average time of 5 – 10 working days, Contech will quote tooling cost, if required, and price quotations of the finished products.
- Upon acceptance of our quotation by the customer, samples, prototypes or trial orders will commence promptly.
- After the client gives final approval of samples, a Purchase Order/Sales Contract, including packing and shipping date requirements will be issued.
- Upon receipt of approved Purchase Order, production will proceed. There is no need to, but clients are welcome to send their engineers overseas for quality assurance.
- Con-Tech Custom Manufacturing will provide shipping details and, if required, oversight of shipment from loading to receipt of order.

Avoid the massive learning curve, lengthy time to research, and all of the [pitfalls](#) of trying to find a manufacturer overseas by yourself. There are sharks in those waters.

**Take Their Word for It -**  
CDF Corporation said,

"We tried finding a manufacturer in China ourselves but we eventually just gave up - too much hassle, too much uncertainty. Working with Con-Tech Custom Manufacturing was a breath of fresh air."

**Call Con-Tech Custom Manufacturing in New Orleans.**

They match your needs with the right custom manufacturers and often get back to you with a custom manufacturing proposal within 24 hours!  
Call Contech Custom Manufacturing now in New Orleans at 504-523-4785.