How the Orphan Product Placement Program Works

qualitycontrolcorp

The strategic value of traditional outsourcing

Why do companies outsource? According to executives surveyed recently by the Outsourcing Institute, the top two reasons on their list were: 1) to reduce and control operating costs; or 2) to improve company focus (See Exhibit 1). A company's ability to focus on its core competencies – those activities which differentiate one company from others and provide the greatest strategic value – and outsource other activities can have a positive effect on the bottom line. Through strategic outsourcing, firms can focus management time, manufacturing space and equipment on new products, services and marketing decisions that provide a competitive edge and stronger profit margins.

Exhibit 1

Top 10 Reasons Companies Outsource

1. *Reduce and control operating costs*
2. *Improve company focus*
3. *Gain access to world-class capabilities*
4. *Free internal resources for other purposes*
5. *Resources are not available internally*
6. *Accelerate reengineering benefits*
7. *Function difficult to manage/out of control*
8. *Make capital funds available*
9. *Share risks*
10. *Cash infusion*

Source: Survey of current and potential outsourcing end-users, The Outsourcing Institute Membership, 1998.

Most companies have traditionally looked at outsourcing as designing a product and passing it on to a contract manufacturer for production. The contract manufacturer has invested in production equipment and resources that would be expensive to duplicate. This supplier is depended upon to have best-in-class capabilities to produce the product more efficiently and improve its time to market.

This all makes perfect sense, but there are other "less traditional" outsourcing methods that companies are now considering. This White Paper describes how companies are leveraging their skills and resources for increased profitability through one such non-typical outsourcing means – the Orphan Product Placement Program.

Core Competency versus Orphan Product – Tips to identification

The McKinsey Quarterly previously featured an article entitled "Make versus buy: Strategic outsourcing"* that suggests if a company can perform an activity "cheaper, better, in a more timely fashion, or with some unique capability" then it is a core competency and should be kept in-house. The orphan concept focuses on what the article describes as a peripheral activity. These activities, though proprietary, do not offer a competitive advantage and would be better assigned to an outside partner.

* Used with special permission from the McKinsey Quarterly, 1995, Number 1.

Situations that can uncover orphan candidates include:

- Product lines with declining sales for two or more years
- Product lines less profitable than others
- Services that absorb significant resources without favorable returns
- Manufacturing floor space is needed
- Labor force reductions
- Company undergoing organizational change
- Manufacturing plant closing or relocating

A purchasing manager at a major OEM defines a core competency as an area where "we have to be the best and we'll invest in the resources to be the best." Products or services not demanding the proper attention or resources to make it cost effectively are prime orphan candidates.

A midwest manufacturer of hydraulic products found orphan candidates by studying sales trends. A handful of products had experienced at least two years of declining sales. These products had evolved through their life cycle and had reached their phase-out stage. The only opportunity that remained was an aftermarket that would need to be served for several more years. Unfortunately, these product lines were consuming valuable manufacturing space and management resources. By outsourcing production of these orphans, the manufacturer could realize benefits such as increased floor space for new product manufacturing.

The steps one should take to outsource the orphan operations should not be taken lightly. As with traditional outsourcing, choosing the right partner is as important as taking that first step to isolate non-core activities.

Keys to finding the right partner for your orphan product

Most manufacturers have a database of suppliers segmented by the services they offer. The establishment of a trusting relationship takes time so many manufacturers are trimming their supplier rosters. As one outsourcing manager at a major agricultural and industrial equipment manufacturer stated, "We are in the supplier reduction business." That's why it is so important for original equipment manufacturers to establish "single-source" relationships with contract manufacturers.

A true, single-source partner for industrial equipment manufacturers would offer:

- Integrated project management teams comprised of engineering, manufacturing, quality assurance and materials. This approach ensures all aspects of a manufacturer's project is monitored and pre-set milestones are reached.
- Complete control of ancillary services such as heat treating and plating. Controlling critical heat treating operations enables the contract manufacturer to maintain the consistency of material performance as demanded by customer specifications.
- Manufacturing systems created to fit the project, not the other way around. The contract manufacturer's obligation is to improve the product's value and, wherever possible, reduce the associated costs of manufacturing the product or offering the service.

Other qualities of a single-source partner have become standard expectations. These include Just-In-Time delivery and the willingness to invest in the latest production equipment to ensure the highest quality product is being manufactured for its customer.

What to look for in an outsourcing partner

In order to take advantage of the potential that outsourcing provides, manufacturers should consider the following:

1. Readiness assessment: A candid review of all operational activities.
2. Review existing book of business: Using a defined criteria, determine what percentage of existing activities could and perhaps should be outsourced to maximize the return on investment level for these functions.
3. Bring culture along: Through a series of informal and formal dialogs across the organization, prepare people for the likely integration of outsourcing. Emphasis should be placed upon freeing individuals to grow in new and productive directions by the removal of habitual tasks.
4. Identify qualified candidates: Experience will count for a lot, as many will attempt to "talk the talk" without having any reference for having successfully "walked the walk."
5. Beta test fit: Isolate several candidates/tasks for outsourcing. Then begin the process of working through the cultural and operational dynamics involved with integrating outsourcing.
6. Production level manufacturing: On a real-time basis, ensure that production level manufacturing is achieved, which meets or exceeds prior quality levels, and yet remains within the boundaries established for speed and margin considerations.
7. Performance metrics: Real-time measurement of activities along with process enhancements to identify, isolate and eliminate triggers to sub-par performance.
8. Ongoing monitoring: Experience shows that real-time monitoring of activities will be the bare minimum standard for measurement, both internally and among strategic partners. Access to such information should be available across both organizations and may involve the integration of computer systems.
9. Cross-functional team exposure: Regular site involvement from both the OEM and contract manufacturer to share the benefits experienced by the process as well as to address changes which will enhance future results. This step is essential to building lifetime bridges.
10. Acknowledgements and rewards for exceptional successes: Clearly gains are envisioned to be realized from this process and a percentage of the gain should be shared among the work groups who meet or exceed the expectations of the plan.

How does the Orphan Product Placement Program from QCC work?

Quality Control Corp developed its Orphan Product Placement Program to assist manufacturers in identifying and outsourcing production or services no longer essential to a company's growth. Figuratively referred to as orphans, these "unwanted" operations cannot be abandoned since they are part of your offering and important to maintaining customer loyalty.

The program includes a confidential On-Site Orphan Product Analysis, which is an evaluation service conducted by Quality Control Corp at your facility. The site visit includes an in-depth look at your manufacturing processes and a review of your sales forecasts, product specifications, marketing strategies, quality procedures and requirements, work instructions and more. Approximately two weeks after the audit, you'll receive a detailed report summarizing our observations and confirming or denying that you have an orphan product. If an orphan exists, the report may include a detailed proposal for adoption or other suggestions if it does not fit well with QCC's capabilities.

The best case scenario is that you will have found a home for your orphan products or services and streamlined your organization to focus on its core competencies.

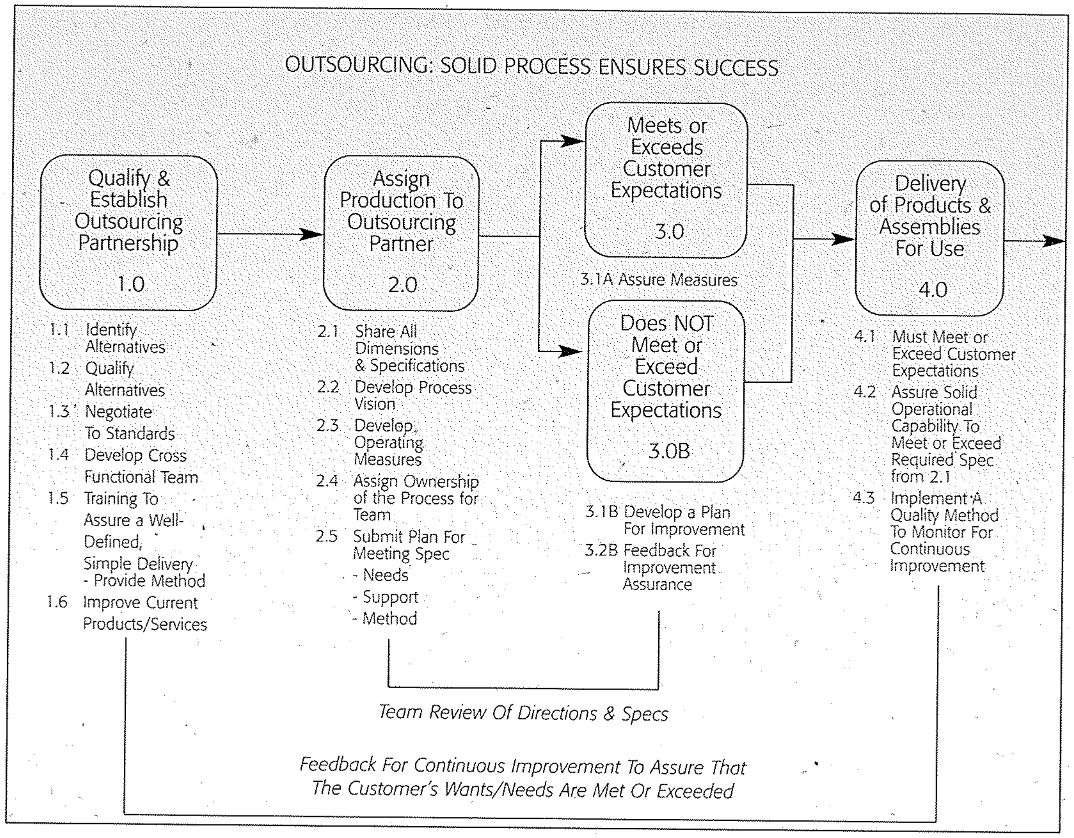
A quick review of the process to outsource an orphan product

Once a candidate for an orphaning initiative is identified, a quick review of its impact on other dimensions of the organization is undertaken. First, manufacturers should examine the impact the elimination of this product or product line will have on space, labor, overhead allocation, throughput or capital utilization.

Next, determine which suppliers offer single-source capabilities for the orphan product or service. Candidates should have at least 10 years of work history handling these types of relationships. Interview candidates to determine interest level. Key items to review include units produced, status of prints and specifications, and any unique circumstances which might affect production projections.

To be most effective, complete the interview process within 35 to 45 days of the outsourcing decision. This prevents deliberations from languishing. Subsequently, serious negotiations on price and transfer structure are undertaken. It is not uncommon for work in progress, inventory, finished goods inventory as well as equipment and material supplier lists to be included in the transfer.

Best practice methods suggest that in addition to ongoing dialog among both parties, a formal session should be held approximately 12 months after the transfer has been completed. This session permits both parties to jointly benefit from the knowledge and experience gained during the transfer. Such a session highlights the pluses as well as determines the changes that might be beneficial in future efforts.



How other companies have discovered an orphan product and how they benefited from outsourcing

Orphan products often come about during periods of organizational change. Products or services once manufactured or provided to meet the needs of the moment are no longer practical. The purchasing manager of a hydraulic power systems and components manufacturer saw two key benefits to outsourcing an orphan product: manufacturing floor space and engineering support could be allocated for new product initiatives paralleling the company's core strategies. The orphan product was a low volume part carrying a high degree of overhead. Outsourcing the orphan was simply financially advantageous.

The orphan concept does not only apply to the adoption of products that have declining sales and an installed customer base to support. Take for example a large industrial equipment and components manufacturer involved with service parts fulfillment. Through an on-site orphan audit, it was determined that significant resources were being invested in service parts fulfillment. Resources, such as facilities, systems, personnel and finished component inventory, were diverting the OEM's attention away from its core business strategy – to design and manufacture new products that are of a relatively short product life.

The fulfillment program – though not a core activity – was necessary to serve an installed customer base. Abandonment of the service could be detrimental to future opportunities with loyal customers. With an orphan program relating to this service part initiative, the OEM had three options:

1. Depend on an outsource partner to provide service parts directly to a service parts facility. Activity at this level could begin with parts and volumes that fit with existing manufacturing capabilities and expand to the management of a supply base providing all required parts to support established parts service policies.
2. In addition to the above activity, the partner would manage the shipment of parts directly to customers.
3. The outsource partner would assume full-service part fulfillment responsibility, including financial responsibility for finished goods inventory.

Each option allowed the OEM to invest its resources more wisely and effectively exploit its unique capabilities. Many other orphan examples exist. It just takes a willingness on a company's part to find them.

Summary

Several forces are pressuring companies to focus on those competencies that will drive growth. Downsized work forces. Earnings targets. Technology advancements. Only with the proper allocation of resources can companies continue to compete and think toward the future. A strategic outsourcing partnership for orphan products is an option that can help companies establish the focus that their core competencies demand.

About Quality Control Corp

Quality Control Corp is a contract manufacturer of high precision machine components and assemblies for several niche applications, including aerospace, diesel fuel systems, air tools and fluid power. Its capabilities include full-service machining and assembly along with complete control of ancillary services such as heat treating and plating. Located in Chicago, the company has more than 120,000 square feet of production capacity in four facilities and over 250 employees.

qualitycontrolcorp

7315 West Wilson Avenue
Chicago, Illinois 60706

Telephone: (708) 887-5400
Fax: (708) 887-5009
E-mail: info@qccorp.com
Web: www.qccorp.com