



# **The Butterfly Effect**

**By Kurt H. Hartwig**

## **Double Sales in 3-years? Think Again.**

Organic business growth is a top priority for CEOs and business owners, such as increased output, new industry acquisition, customer base expansion, or new product innovation. I've witness contract manufacturing (CM) companies declare an audacious goal of doubling sales in 3-years, with no how-to-plan. I am amazed that managers will just blurt-out such statements as, "We can get 60% from existing customers and 40% from new customers," with no creditable data to back the claim.

I admire their confidence and boldness; however, they live in fantasyland if they think the business will automatically double in 3-years, especially, when it took 20-years to reach sales of \$9,000,000. These managers only see the current state of the business, or its current capabilities.

*Just because the business has capacity to add a 2<sup>nd</sup> or 3<sup>rd</sup> shift or expand the facility, does not mean that business will double.*

In fact, when managers discuss capacity, they're generally speaking about machine-time, rather than employee-time. A business may have plenty of machine-capacity, but have employees stretched to the limit.

## **The Butterfly Effect**

As with all contract manufacturers (CMs), quoting is a key activity and necessary to business development. Quoting is time-consuming and strenuous—some customers want quotes-turned in 24-hours. This might be realistic with low dollar-value projects, but \$multi-million quote packages are very time-consuming and challenging to complete. Interestingly, this type of quote is most sought-after by CMs, since a WIN can quickly propel a business.

Unfortunately, as the **dollar amount** of a quote package goes up, the probability of a **win** goes down (Figure 1: The Butterfly Effect). This inverse relationship is very common with CMs because, as their capability level peaks, an OEM will perceive the CM as a risk—they will not tolerate or accept additional levels (Figure 1: The Line of Risk Intolerance). However, it is important to note there is always an inherent risk to outsourcing to CMs, and most OEMs are willing to absorb a certain amount—it all depends on the OEM and factors involved.

## Win Value Zone

Most CMs operate successfully in the Win Value Zone (Figure 1), where quote wins are common and customer account size is small dollar amounts—between \$50,000 and \$750,000. Their capabilities are average and subpar, and meet the minimum performance requirements set by OEMs.

*Industry rivals can easily duplicate capabilities and steal business from each other—there is no distinct value offering.*

This sameness allows OEMs to engage CMs into bid wars, where price-cuts and margin-erosion are the norms. However, if a CM operates in close proximity of an OEM customer, where product delivering is very low cost, then it would be hard for competing rivals to outbid.

## Lost Value Zone

Most CMs become frustrated and perplexed when they cannot win large, high-margin quote packages—they assume it is the **price** and the CFO returns to the BOMs and labor standards, searching and combing for any decrease in cost and time. However, if an OEM is confident the CM has the capabilities to handle the requirements of a large account, then price becomes less of an issue. Why? Very few CMs can successfully manage a \$2 million plus account, so it becomes a scarcity issue. Nonetheless, it is extremely rare that they will win a large quote package, which means these CMs also operate in the Lost Value Zone—OEMs do not perceive a CM as having any superior technological or manufacturing expertise to warrant a partnership. Therefore, it is realistic to state that **100% of CM sales** generate from the Win Value Zone.

## Average Value to Superior Value

Have you ever heard of a business stating they have a surplus of customer service, or they are tired of creating happy customers and don't need anymore? How ridiculous. Or is it? Today's OEM has expectations that far exceed what most CMs can offer. Within these priorities are new structural designs that incorporate business analytics and digital platforms for improved visibility, decision-making, and purchase. Skeptical CMs that define business as usual and remain passive, will find themselves struggling for new sales growth—if they haven't already done so. Acquisitions may help in the short-term, but even the acquired business must demonstrate a superior value proposition to win large, high-margin quote packages. Otherwise, the CM will remain in the Win Value Zone, where quote conversions and account size are well under \$1million.

*Figure 2 shows the answer to overcoming The Butterfly Effect, where CMs can make the leap from being perceived as average to superior—to win large, high-margin quote packages and boost sales to record-levels. The secret is to reduce risk to an acceptable level, so OEM confidence increase.*

It may be a surprise to some, but making the leap from average value zone to superior value zone is not rocket science (Figure 2). For example, what do you **expect to see and experience** when you walk into a Supermarket? If store A were dirty, messy, and smelly, would you stay and shop, or walkout? How about if store B were spotless, organized, and very clean, would you feel confident about shopping and spending money? Sure you would. Even if the prices were a little high, you would still purchase your groceries. Why? Because you've seen store A and do not feel confident buying from this grocer—to risky!

It is no different with relationships between OEMs and CMs. It is relatively easy for rival CMs to buy and have the same equipment and technology, but it is hard to duplicate and mirror outstanding service and superior housekeeping. Why? Employees may act differently each time they encounter a customer, and, for many reasons, a customer can perceive an employees' action differently any time they engage.

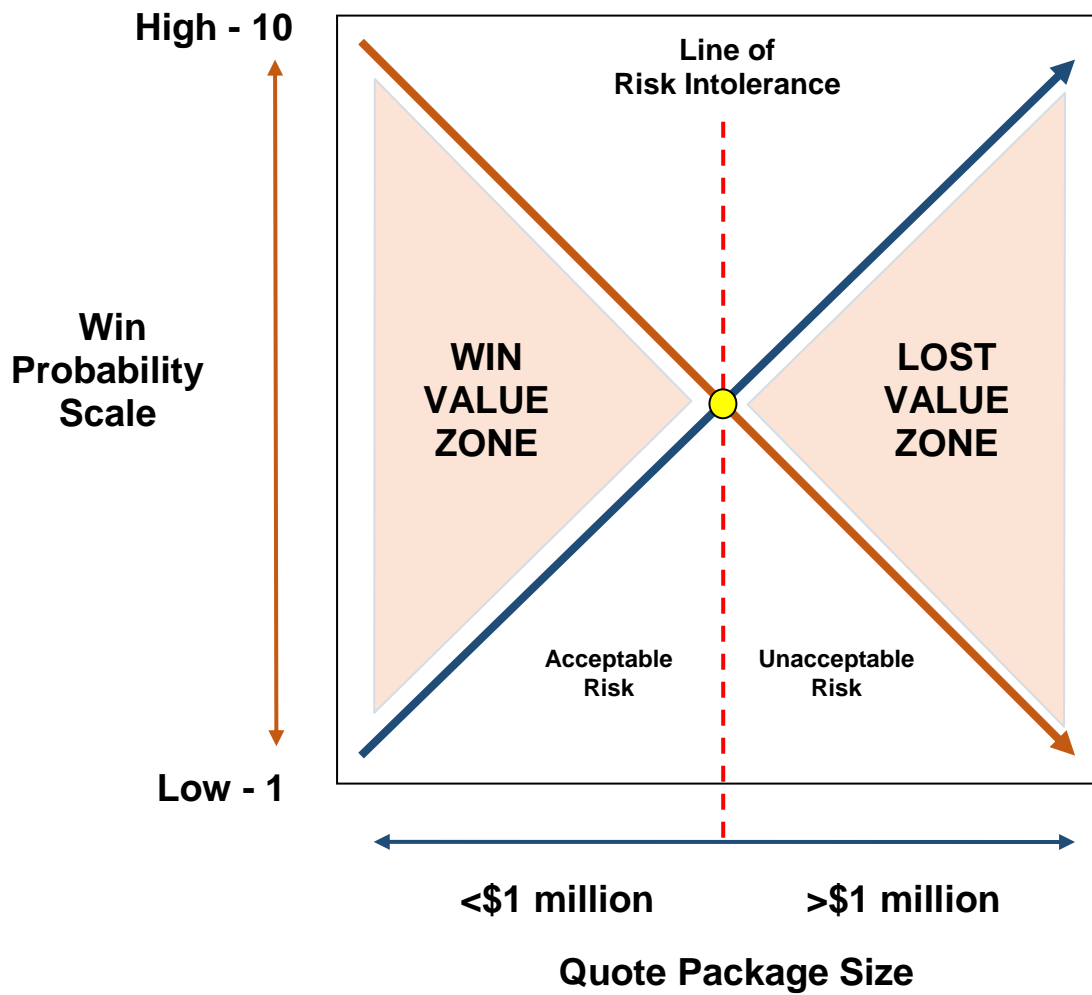
**Consider the ideals in table below:**

Facility condition and cleanliness	Reputation for solving complex problems
Adhere to agreed-upon schedules and prices	Attitude to customer requests and changes
Employees ability to be trusted	Employees sincerity to understand customers
Safe and secure work conditions	Image of being reliable and honest
Employee turnover rate	Employee attitudes to customer problems
Machines condition and cleanliness	Ability to keep promises
Employees courtesy and politeness	Employees appearance and demeanor
Facility climate and organization	Employees disposition and quick response

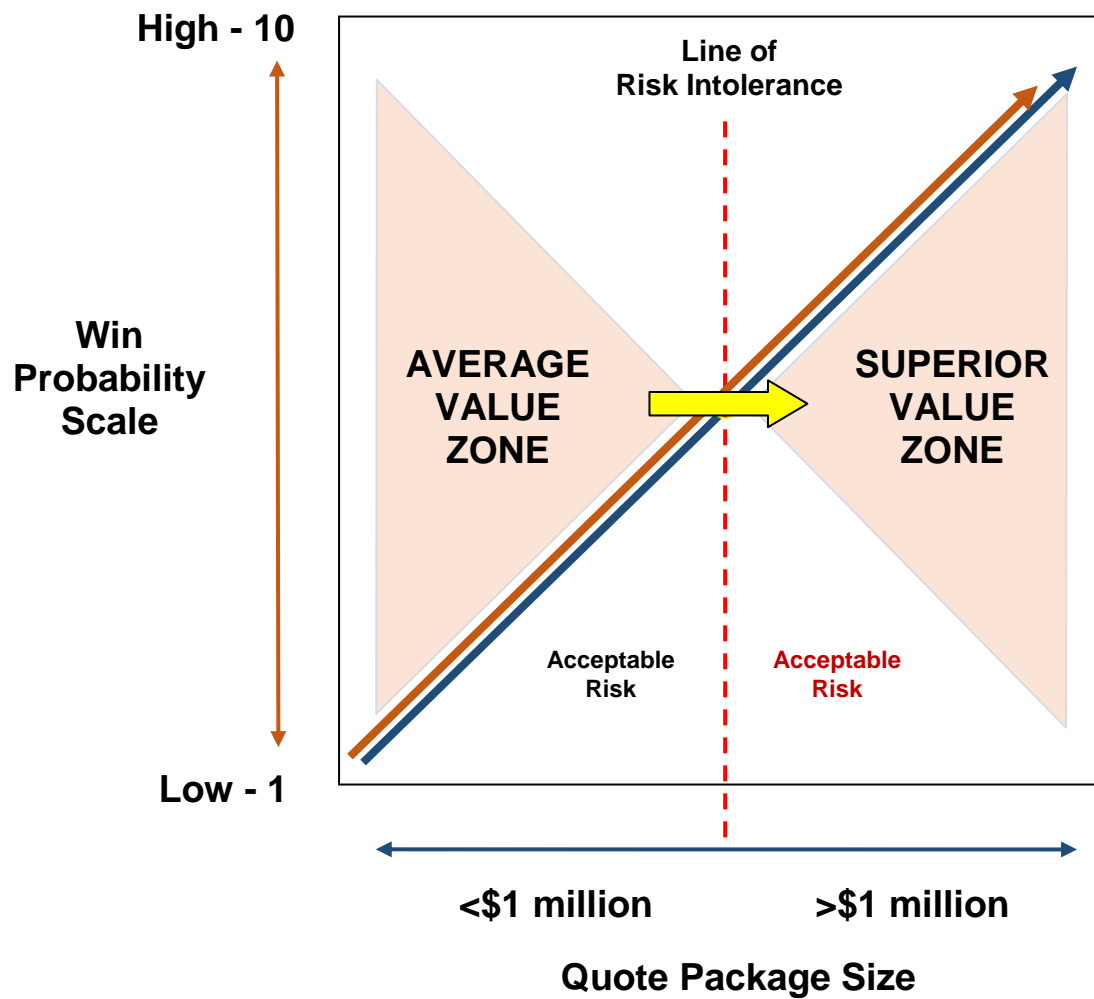
Would you say that your company delivers these ideals with superiority and consistency? When a prospect or customer visits and tours your facility, what will they experience? Do you know? Do you care? If you do not, it will definitely show and the business will remain in the average value zone, and the likelihood, or probability, of acquiring a \$multi-million account is zero.

Once a CM wins a larger quote package, and continues to win more with great success, their focus is no longer set on the average value zone. Low dollar quotes become less attractive—this is why the win probability arrow in Figure 2 rotates 90 degrees. Superior value zone CMs no longer expend time on small, slow growth opportunities, so they usually choose to no-bid—obviously, the win probability on these quote types is zero or very low.

OEM outsourcing to contract manufacturers is all about a continuing relationship. It is advantageous for both parties to define the criteria or ideals that are considered superior value. This has to be clearly stated at the strategy level; otherwise, CMs will determine and craft their own standards for business—in which, a lost proposition.



**Figure 1:** *The Butterfly Effect* (By Kurt H. Hartwig ©2018)



**Figure 2:** *The Butterfly Effect* (By Kurt H. Hartwig ©2018)