

# Strategic Benefits of Using a Contract Manufacturer

by M. Amirul Karim

There are myriad strategic benefits to using a contract manufacturer. By outsourcing manufacturing, a supplement marketing firm does not have to worry about the great financial burden of acquiring and maintaining a plant, equipment and personnel, or the increasingly active government regulations and the general “headache” that is intertwined with a manufacturing plant. The primary strategic benefit of using a contract manufacturer is that it allows a marketing company to do what it does best: market and sell dietary supplements.

### Capital Resources

If you have been thinking of starting your own manufacturing facility, you might want to think twice. The first step in the planning of a manufacturing plant is to look at the finances. To establish a manufacturing site in today’s regulatory environment requires a facility that is spacious enough for product workflow and cleanliness, equipment that meets or exceeds good manufacturing practice (GMP) standards, and a highly trained workforce. It will likely take at least \$5 million for a modern manufacturing plant.

The manufacturing process involves the use of several auxiliary functions such as weighing, blending, mixing, wet-granulation, drying, inspection, polishing, coating and packaging. In addition to the primary manufacturing processes of encapsulating hard gelatin capsules and compressing tablets, the above steps are absolutely necessary to produce a product that is homogeneously uniform and ready for the consumer.

Finally, the actual systems and procedures for manufacturing solid dosage dietary supplements are very complex. The manufacturer is responsible for maintaining proper documentation of the batch records and formulating the product with the correct amount of excipients. Knowing which excipients to use and in what amount comes from experience. A common misconception is that a capsule of, for example, Ginkgo biloba, contains only Ginkgo biloba. That is nearly impossible. Many herbs, such as ginkgo, St. John’s wort or kava, lack flowability, which is vital to encapsulating or tableting these products.

The manufacturing process does not end with the actual finish of the product. With a skeptical public and recent media coverage of our industry, it is important to have strong quality control and quality assurance systems in place. This includes the use of analysis of the product to maintain efficacy and potency. These quality control measures tie into the upcoming government GMPs and the existing National Nutritional Foods Association (NNFA) GMPs. All of these auxiliary steps add up to an increasing overhead capital structure, which is very common in manufacturing businesses worldwide.

### GMPs & Government Regulation

The objectives of the GMPs are to provide the general public with unadulterated products, which are not misbranded and meet their respective label claims. In the dietary supplement industry, manufacturing operations are governed by food GMPs and enforced by local and state health departments. Although food GMPs require cleanliness of facility grounds and equipment, the proposed dietary supplement GMPs are far more comprehensive and are based on the more stringent drug GMPs. The NNFA GMP program is probably one of the most high-profile third-party certification programs. The NNFA GMP program includes the audit of systems and personnel, plant design and facility cleanliness, personnel

qualification and quality control systems including stability studies.

Once government dietary supplement GMPs are in place, the bar will have risen for the quality and efficacy of dietary supplements. Although NNFA GMPs are great guidelines for further ensuring that products are manufactured in controlled environments, most contract manufacturers are not NNFA GMP certified. There is only a handful of NNFA GMP certified companies. The U.S. dietary supplement industry is highly fragmented, with a small number of very large players, and a very large number of small players. Most of these companies use the services of a contract manufacturer. By utilizing an NNFA GMP certified contract manufacturer, consumer confidence is higher because the manufacturer uses quality systems and procedures.

### Core Competencies & Opportunity Cost

When considering entry into a new business, it is important to look at two things. What is the core competency of my organization? And what is the opportunity cost for entering this new business? For most supplement marketing companies, their core competencies are marketing and selling products, not manufacturing them. Their strength lies in creating brand awareness and increasing market share.

The opportunity cost is a fundamental economic idea that basically says that you must weigh how much of one thing you’re willing to sacrifice to gain another. To put this in context, if you were to spend \$5 million on a new manufacturing plant, would that be the best investment for your marketing firm? That is a lot of money, and could be used for a variety of advertising mediums including mass circulation magazine and network television advertisements. By spending the money on marketing and promotion rather than a manufacturing plant, a chain reaction begins. You increase the brand awareness of your product, thereby increasing sales, thereby increasing the amount of raw materials you purchase, giving you a quantity discount with your ingredient suppliers, thereby increasing your bottom line. The decision-maker of an organization must decide which is the better alternative with the capital in question.

It is a simple ideology to adhere to, which is not unique to our industry. Rather, many large corporations utilize the services of contract manufacturing and service firms. Apple Computer uses contract manufacturers to produce its personal computers, so it doesn’t tie up capital in unnecessary ventures. The former chairman of General Electric told his subordinates to be either the #1 or #2 contender in their particular business or discard it.

By utilizing the services of a contract manufacturer, a marketing firm is able to capitalize on its core competencies of marketing and selling dietary supplements. This allows the marketing company to operate leaner financially. By partnering with qualified contract manufacturers, a marketing firm also bolsters the consumer confidence of dietary supplement users, ensuring better quality control and systems. The strategic benefits are countless and result in all constituencies yielding better returns by focusing on their core strengths.

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