

MEMORANDUM

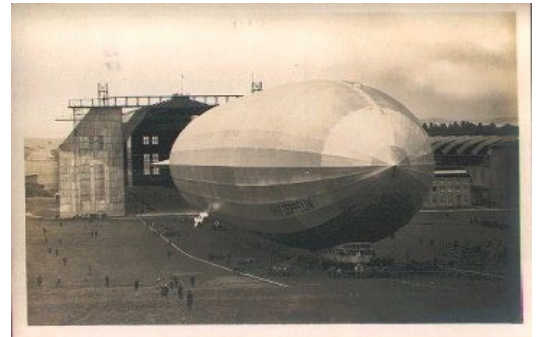
TO: Our Referral Partners (First Issues Chris Ebert Company)

FROM: David Schwartz

Dateline Friedrichshafen Germany, May 1940,

Zeppelin Aircraft Co. Closes – lack of suppliers

Contrary to public opinion, the crash of the Hindenburg in 1937 was not reason for the Zeppelin Aircraft Company closing its doors. Actually, they ran out of suppliers. In order to meet market demand and pricing against the new Taiwanese Blimps, the Zeppelin Aircraft Company pushed their Tier One and Tier Two suppliers to the brink. By May of 1940, there were no suppliers left.



The Duralumin Company - Duralumin got its name from the material for the rigid structure in Zeppelins. Duralumin was the largest of all suppliers to The Zeppelin Aircraft Company. Their business was somewhat different from yours with unique practices and jargon. However, your common business goal is to generate cash. In the last two years, we have worked with 4 companies where both the working capital demand was too high, the margins were low and risks were greater than the potential rewards.

It is not all about profit! It is cash - a direct relation between Working Capital required and Profits.

$$\text{Working Capital} = \begin{matrix} + \text{Inventory} \\ + \text{Accounts Receivable} \\ - \text{Accounts Payable} \end{matrix} \times \text{Margins}$$

This formula results on your **Return on Investment**. Seeking competitive advantage? This relationship creates the opportunity to find strategic and actionable strategies. Low Working Capital requirements results in more Margin flexibility. Higher Margins provides more Working Capital flexibility.

Cash Potential is a direct relationship between Working Capital employed and Margin. When you use cash from high and growing working capital, you **must** achieve meaningful margins to insure your viability. All businesses are driven by this relationship. Manufacturing, product or project distribution, and typically are Working Capital intensive businesses requiring higher margins. **MORE?** While retail and food manufacturing and some service businesses the daily turnover of inventory and low A/R days are the true game breakers

What was the Duralumin Return?

+ Accounts Receivable	80 Days
+ Inventory	3.6 Turns
-Accounts Payable	49 Days
Total Working Capital	
Margin	12.4%

Return on Working Capital

Duralumin - their money goes out long before it comes in! Zeppelin Company paid Accounts Receivable (A/R) 80 days by after Duralumin's parts shipment. However, DURA Accounts Payable (A/P) averaged 49 days from the production starting point.

Inventory - increases the demand for cash. The Zeppelin Co demanded Duraalumin carry a meaningful finished goods inventory in case they have a spike in demand DURA have a production problem. Further Zeppelin dictated specific material suppliers who demand payment faster than the typical A/P..

For each \$1 M in revenue, using the model above, DURA are obligated to fund \$800K in working capital. Do the margins cover the cost of Capital?

Margins - The Tier 2's margin is negotiated, renegotiated and then dictated by the customer. The Zeppelin Company drove DURA to commodity pricing, close to costs and ignored their technical contribution.

Risk, suppliers and their vendors typically have more risks than rewards. Exhibit 2 is an example of what actually happens.

How Does this Happen?

Accounts Payable

Inventory

Accounts Payable

Margins

Risk

You're the Companies Professional Advisor. How do you bid to the food or other retail industries? These operating questions will help you evaluate the company's performance.

If you have a question about this or you'd like to privately evaluate one of your clients, just call. Fresh from the risk of Crashing, Jacquard Associates needs a new client and a new country.