Business Learning By Dan

Understanding Our Members' Businesses: Manufacturing and the Circulation of Capital

By Dan Topf*, CPT

"I don't know what's going on!"

Recently, a friend invited me to join a meeting of the Practical Farmers of Iowa. Being an Iowa farm-boy, I thought I would tag along to learn about sustainable farming practices. What I saw at the Wallace Farm near Keystone, IA surprised me. I was surprised to see the "circulation of capital" playing out before my eyes. Then, I realized that the circulation of capital model can help ASTD members in knowing what's going on in their companies. Really, it did.

You see, farming requires capital. All businesses require capital. Further, farmers need their capital to move quickly. I noticed lots of money goes out to suppliers, machinery stores, veterinarians, farm stores, bankers, and other stakeholders. Then time passes, and finally the farmer sells crops, cattle, chickens, or other produce and gets paid. Think about it the next time you're at the Farmer's Market – How long has that vendor been spending money to produce that loaf of bread or jar of jam?

Many of our ASTD members' businesses produce tangible products (Pella Corporation, Vermeer, Pioneer Hi-Bred, Firestone, Kemin, and many more). When we view business as a circulation of the capital, we can then see how training and performance contribute to its movement. Let me explain.

In general, the circulation of capital works like this (see figure A). A business starts and end with cash. So, capital (a. k. a. money) starts moving when the business uses cash to buy raw materials from a supplier. Then, the company applies labor to the raw material to produce a finished product. These finished goods are sold to a customer, who pays the company to complete the circulation. From cash to cash, as shown in the figure:

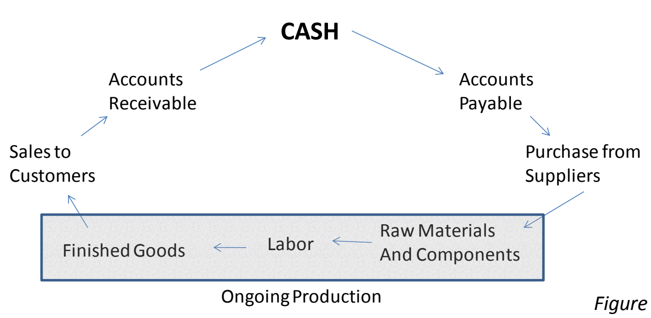

Figure A

Let's take a look at a local example. Pella Corporation manufactures "quality windows and doors for new construction, remodeling and replacement applications." Let's see. Cash leaves the company to purchase wood, vinyl, and other component parts from suppliers which are kept in inventory. Next, Pella employees (labor) saw the wood, prepare the materials, fabricate and assemble the windows and doors. The finished products are placed in Pella showrooms and in home centers for customers to buy. A customer places an order and takes delivery, and pays their bill. Thus, the circuit is complete, young Jedi.

The circuit is a broader notion than the value stream. A value stream (or value chain) typically starts with the supplier and ends with finished goods. The circuit of capital includes the necessary steps of accounts *payable* (the time it takes the **company** to pay for raw materials and components) and accounts *receivable* (the time it takes the **customer** to pay for finished goods delivered). For some companies, the time from purchase of materials and payment for delivery of finished products can be months, or even years! When the company's capital is tied up for that long, it makes the operation VERY expensive. Capital comes to your company with 'strings attached' in the form of interest for borrowed money or returns to shareholders for invested money. If your circuit is slow, it takes more capital to keep things running, adding to costs and risks. (How costly? Send me an email and I'll explain the Cost of Capital for your company! DanTopf@MDI-Learning.com.)

The idea is to have more cash coming in than going out during a given period of time. So, this circuit needs to move as quickly as possible (With a 'given' that customers are willing to pay more than it costs to produce your product!). Some companies take months to complete the circuit. Others take a few days. How long does it take for your company? How can training and development speed things up? How can training and development reduce the need for capital in the first place?

The answers to these questions start with a reading of the overall business goals and objectives. Then, we can strategically apply training and development to further these goals. Sounds difficult, but it's really pretty straightforward. Consider these applications of Training and Development to improving the circulation of capital:

> For further reading:
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> "Finance for Managers. Your Mentor and Guide to doing Business Effectively." HBS Press. 2002
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> "Telling Training's Story: Evaluation Made Simple, Credible, and Effective." Robert Brinkerhoff. Berrett-Koehler. 2006
>
> www.bizzia.com and search "Working Capital."

Element of the Circuit of Capital	Value to Your Business	Role for Training and Development
Accounts Payable	Materials and components are generally paid for after delivery. How **long** after delivery? Generally, a longer payment term frees capital to be used for other things during	Train purchasers and supply managers to maximize their performance to free up capital for other uses. Train for much more than negotiating prices, but integrating supply management with engineering, design, manufacturing, and marketing to minimize

	that time.	capital requirements in purchasing. Train employees to reduce Working Capital.
Suppliers	Many firms have preferred suppliers for their materials and component parts to ensure consistent quality and pricing (among other things).	Train employees in continuous improvement practices to minimize waste and truly partner with suppliers. Teach leaders to think systemically across your supply network and across your value stream to pinpoint areas of waste and/or inefficiency.
Raw Materials and Component Parts	Businesses keep an inventory on hand so that production starts as needed.	Train in inventory management and lean practices. Every dollar of inventory purchased and not used, or purchased too soon, is a dollar that can't be used for something else. Teach the circuit of capital in your continuous improvement courses to provide business context.
Labor	Your most valuable asset is your people, and people provide the value-added that makes your products desirable.	Train in consistent procedures and continuous improvement practices. Teach employees to innovate. Teach employees how their work differentiates your product in the market and allows for good profit margins. Teach how accelerating a process can accelerate the circuit.
Finished Goods	A well-stocked store or a quick turnaround on an order increases the likelihood for profitable sales and repeat business.	Teach continuous improvement procedures and tactics to quickly sell inventory. Train employees in enterprise software tools to minimize production to inventory to maximize production to customer order.
Accounts Receivable	Generally, customers have a bit of time to pay for their purchases after delivery. However, sometimes they pay late, slowing down the circuit.	Train employees in consistent contracting and payment terms policies. Teach employees how to tighten procedures and improve accuracy in billing. Train employees in new billing systems and software to speed up collections.

A model like the Circuit of Capital can be very helpful. It provides you a framework for positioning training and development to deliver real business value. Your executives are focused on getting this circuit moving as quickly as possible, and your training and development activities can be the essential ingredients for achieving business success. By positioning training and development to deliver on accelerating the circuit of capital will bring your team immediate credibility. Good luck. See you at the Farmers Market.

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