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Guides to Practical Bookselling

Bookshop Finance

Cashflow

Contents

This Bookshop Finance Guide was originally written by Ric Jaques, Group Chief Accountant at STL, Carlisle. The BA and the Small Business Forum would like to thank Ric, STL and the BA Christian Bookselling Group for allowing us to adapt and make available this Guide to the general trade

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1. Introduction

A basic understanding of the financial issues affecting our shops and our businesses is vital if we are to continue to be effective in what we do - our very existence is threatened by ignoring the financial issues. We may get away with it in the good times, but it will store up problems when times get tough (and they do). These problems potentially have some very serious consequences.

2. The Problem

Why do businesses fail? A multitude of reasons…times and fashions change, technology moves on, competitors come and go….But the main reason that a business is forced to close is that it has run out of cash. It can't pay the next bill and someone, somewhere, is not prepared to go unpaid – so they do something about it! A business can easily be profitable – but run out of cash. Conversely –a business might make losses for a period of time but continue to operate – like Amazon – however, this is not sustainable for the longer term.

At some point, if you are not able to keep paying your bills, someone will do something about it. It might be your bank, your landlord, your staff, your key suppliers, Customs & Excise or the Inland Revenue. All of these people have been known in the past to get to that point where they run out of patience and try to recover their cash by 'force' – often leading to the business being closed, i.e. liquidated.

It may seem odd that a business can be making modest profits and yet run out of cash. But this is the case – it will be because cash is increasingly getting tied up in stock or fixtures, or because customers are not paying you quickly enough, or because of the seasonal variations of that profit. Long-term profits do not guarantee we will always have the cash at the right time to pay the bills.

3. Understanding What Makes Your Shop Profitable

Let us look at a fictional 'Profit and Loss' for a small independent bookseller:

For the year to 31 December

Sales	**84,302**
Cost of sales	-57,402
Gross Profit	**26,900**
Overheads	
Staff costs	15,230
Establishment costs	6,482
Equipment costs	245
Carriage, postage, phones etc	742
Travel costs	125

Finance costs	2,012
Depreciation	1,025
Other costs	129
Total Overheads	**25,990**
Net Profit	**910**

Now let us look briefly at the Balance Sheet for the shop

	31 Dec 04	31 Dec 03
Fixtures	12,205	4,702
Stock	27,312	22,109
Debtors	3,702	1,007
Cash	-9,596	4,102
Net Assets	21,418	27,218
Creditors	9,707	8,914
Net Current Assets	11,711	18,304
Net Assets	23,916	23,006
Reserves	23,916	23,006

Here we see a shop that is making a profit during the year, but their cash position has significantly worsened.

Cash has flowed out of the business, fixtures have been purchased, stocks have risen, money owed to the business has risen and all of these have eaten up the cash.

4. Understanding Important Elements of these Financial Issues

I want to concentrate now on a number of specific areas:

- ✓ **Sales**
- ✓ **Gross profit**
- ✓ **Overheads**
- ✓ **Cash flow control**
- ✓ **Stock control**

4.1 Sales

What affects your sales?

You will be far better qualified to answer this than I will but experience tells me that a whole host of things will impact your sales –

- The products
- Your customer service

- Promotions
- Marketing
- The weather
- Football/tennis/royal events/solar eclipses…….

So how can the finances help here?

The key is recording, and then learning from, the information on sales.

Analyse your sales – look for trends.

You need to be able to ask yourself questions like:

- Have I sold more or less audio/stationery this year?
- What if I moved/expanded my card rack?
- What is the most effective selling area in the shop?

The key to this sort of information is **till categories**.

You need to have the split between VAT-able and non-VAT-able goods, but split these further, for example:

- ✓ Books
- ✓ Stationery
- ✓ Audio
- ✓ Software
- ✓ Multi-Media
- ✓ Cards
- ✓ Gifts
- ✓ Miscellaneous Vat
- ✓ Book Tokens
- ✓ Gift Vouchers

By recording and then analysing these, you will start to understand what is happening to the sales in your shop. No longer – 'we sold more this year than last', now you can look at whether card sales in October to December were better or worse than last year.

Once you have such information, you can start to ask questions about 'WHY' something is up or down - did you do something to influence this? Is there something you can do gain because it was successful? (or avoid because it flopped!)

The more data on sales you have, over a few years (recorded on simple spreadsheets) the more questions you will be able to ask about your sales – and the more answers you will start to come up with.

4.2 Gross Profit

This is fundamental to the profitability of your shop! So what is it?

"The difference between what you sell a book for, and what you paid for it!"

Sales can increase until the cows come home, but if your gross profit stays the same or falls, it will hurt.

Learn to understand your shop's Gross Profit

- Regular stocktakes (at least two a year)
- Stocktake by till category (GP by category is very helpful, but extra work)
- Don't count dead stock – clearout before you count.

An accurate stocktake is the only way to find you actual gross profit. It will help to show you whether it is increasing, or decreasing. You will probably find that your GP (as a %) is higher in the Christmas run-in, as you sell more high-margin product – cards, calendars etc.

OK – so even if you understand your gross profit, how can you influence it? There are a number of areas that can be examined to see if you can improve your gross profit:

- **Discount received**
  Is this correct?

- **Discount given away**
  Are they entitled to discount?
  Are they earning it? (maybe time for a painful review!)
  Can you reduce it?
  Would extra discount actually generate extra GP (in £'s) eg Students?

- **Damages**
  Is your housekeeping good?
  Can your staff pack returns well?
  Do you always claim – and receive – your credit notes?

- **Returns**
  Did you return everything you could/?
  (or was it such a good offer you know you can sell it all?)
  Did you get the credit note and was it correct?

- **Theft**
  Have you taken all reasonable precautions?

- **Product mix**
  Do you and your staff appreciate the different gross margins on different types of product?

- **Small order surcharges**
  Can you avoid them?
  Can you pass them on to your customers?

- **Markdowns and write-offs**
  How can you minimise these?
  Are you learning from what you write off?
  Do you monitor the levels of these?

- **Buying decisions**
  Remember - Every item you buy will either be:
  - Sold
  - Returned (where possible)
  - Reduced / written off

4.3 Overheads

Some of the overheads faced by your shop will be fairly set in concrete (such as rent and rates). Others are fairly fixed, although you may be able to influence them a little (eg utility bills or bank charges). Others, such as staffing, marketing or investment in fixtures will be much more open to control and the decision making process – and that is where you come in!

The real skill of overhead management is to look at each area of expenditure and determine to what extent you have control over it. For all of those overheads where you have some influence, you need to see if your spending is being well controlled.

The areas of overhead control that are needed in your shop will vary widely. The list below is far from exhaustive, but may give a few pointers in some of these areas.

a. **Carriage / Postage**

Make sure you are using cost effective ways of moving product or posting orders. Royal Mail, UPS, others, may all be more effective depending on what you are sending out. The BA has a deal with DHL for returns parcels, so this may be worth looking at.

b. **Rates**

2005 sees another Rateable Value Revaluation – there will be many people trying to get your valuation re-evaluated – often on a no-win-no-fee basis. The BA has a recommended company who can help with valuations – call the BA on 020 7802 0802 for details on Ruddle Merz.

Whatever you do, always use a reputable/known firm. There is benefit in many people in one area working together – a local firm of surveyors may offer you a better deal if you get your whole block in together.

c. **Utilities**

There is room for savings here (costs are increasing significantly at the moment). And again, the BA has a utilities broker available to members, LSI Utilities Brokers, who will conduct a free audit for your on your utilities spending and recommend improved suppliers where feasible.

Consider having a water meter fitted.

Move suppliers for savings – but rely on recommendation – there are many suppliers and some of their service levels, billing etc are awful!

Care if moving phone rental away from BT – savings are there but there is some risk – and things like phone book entry, response rates to faults etc must be examined before moving.

d. **Rent Reviews and Dilapidations**

Always use a surveyor. Sometimes, a rent review may make it uneconomical to stay in your location, which is obviously bad news. Do not forget to build up some funds to pay for dilapidations on your lease.

e. **Bank and Credit Card Charges**

There may be some room to negotiate these – go to tender if need be, though your banking relationship is a key one – so proceed with caution – a good relationship with your bank could be very important at some point. The BA has a deal with Lloyds TSB Cardnet which has pretty competitive credit and debit card rates, so this is worth looking at.

f. **Staff Costs**

This is never easy in the book trade. We are characterised by low salaries and low staffing levels. Increases in minimum wage will continue to impact on our costs (another substantial rise is expected this autumn). We want to honour our staff with appropriate salaries, but it is not easy. However, they are your greatest asset, so treat them well!

g. **Marketing**

Balance needs to be exercised when it comes to spending on marketing - too little and people won't know you are there. But it can be a bottomless pit into which you throw money, with no real way of measuring the benefits.

Think carefully about how you spend money in this area. Work with what wholesalers and publishers provide as cost effectively as you can. Use local or other contacts as much as possible – and create relationships with local press and other traders.

4.4 Cash Flow

Remember, most businesses fail because they run out of cash. Let's look at some of the issues which affect your cash flow.

a. **Money Coming In**

Obviously, much of this comes through the till – cash, cheques and credit cards.

An obvious and simple thing is to keep it getting to the bank as often as possible – this may allow you to earn more (or pay less) interest – and is good for security!

Customers paying on account – late payment does not help you. You need to encourage prompt payment – you may even need to contemplate withdrawing credit for slow payers (the threat of this often does the trick!)

b. **Money Going Out**

Much of this is inevitable and you have little or no control over the timing of payments being due. Late payment to suppliers is not the solution and late payment of wages or rent never goes down well either.

So it is more a case of looking at what you can influence.

4.5 Stock Control

Probably your biggest tie-up of cash is your stock. It has been largely paid for, and sits on your shelves until a customer buys it, so care in this area can make a huge impact on your cash flow. We tread a delicate balance here – too much stock will tie up cash unnecessarily, but too little stock will reduce sales.

One way to measure your stock levels is to look at your shop's **stockturn**.

This is calculated as follows:

$$\text{Stockturn} = \frac{\text{Cost of sales}}{\text{average stock (at cost)}} \quad \begin{array}{l}\text{per your annual accounts} \\ \text{“ \quad “ \quad “ \quad “}\end{array}$$

This effectively tells you how many times in a year you will sell through your stock –so a stockturn of 4 means that you would sell the stock in your shop 4 times over during the course of a year.

The size and layout will have some impact on this, but to give you some benchmark to measure against, a small store should aim (but may just fall short) to have a stockturn of 3. Larger shops will be over 5.

You do have influence over the stock you hold. The following areas are worth thinking through for your shop:

a. Stock / buying budget
It is very important that you have a monthly target stock level – and that you monitor how you are doing compared to this budget – and a buying budget can be used off the back of this.

I would recommend at least two stocktakes a year – the only real way of knowing your stock value. (EPOS may help in this area).

b. Returns
As mentioned above, make sure all returns are made where possible.
Don't be tempted to hang on to stock unless you are convinced it will sell.

c. Ordering
Keep on top of your ordering, pendings etc and keep your dues lists tidied up – cancel them if you no longer want them.

d. Buying Special Offers

Think very carefully about offers like 'buy 10, get 1 free'. Sometimes these are great, but if you only sell 8 having got 10 plus 1, your gross profit % drops from 35% to 18.8%. You would have been better off paying for just the 8 (and help your cash flow as well.

To demonstrate:

Say the book is £10 – you get 35% discount.

If you buy and sell 8, you pay £52 and get £80 – Gross Profit = £28 (35%)

If you had bough 10 + 1 – you pay £65 and get £80 – Gross profit = £15 (18.8%)

You will need to liquidate the last 3 books for at least £13 to earn as much GP in £'s –and meanwhile your cash was tied up in stock.

So these are not always worth it.

e. Clearing Out Old Stock

The largest investment your business has (unless you own your building) will almost certainly be the stock on your shelves. Much of that stock will generate sales in the weeks and months ahead, but a small proportion of it will prove to be unsellable – at least at full price, and there comes a time when you need to move that stock on. Here are some of the main areas to think through.

Do you have a policy – detailing how often you will review stock with a view to clearing out old stock? It will vary depending on the type of product – theology will sell much more slowly than contemporary fiction.

Your policy should address how you make the decisions on whether to mark down a title to clear it. The better information you have, the more informed your decisions will be. You could think about using a date code on the pricing sticker so you know when a particular book was put on the shelf. Armed with that, you can tell if a book has just sat on a shelf for 18 months gathering dust. If it has, the chances are no-one is likely to buy it soon, so you are better off selling it on at a discounted price.

Regular sales and bargain sections will help to draw customers in, and are a great way of clearing out old stock.

Finally, try to keep a record of how much you are marking down stock – it is an important monitor over time of how effective your buying is, and may help to explain why your gross profit margin is changing over time.

5. Conclusion

There may be a lot here to digest for some readers – but remember that even the smallest step in the right direction will help you to manage your business more effectively.

Small booksellers need to get better at financial control – the more information we have about how our business works, the more we will be able to ask, and answer, questions on why we do things the way we do. This will inevitably lead on to the next step – asking can we do it more effectively?