independent booksellers FORUM

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Guides to Practical Bookselling

Stock and Margin Management

Stock Levels, Buying, Dead Stock and Margin Management

Written and Presented by Harry Wainwright of Oldfield Park Bookshop for the Small Business Forum, 21st June 2005.

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STOCK AND MARGIN MANAGEMENT

A Brief Introduction

I have been a bookseller for 20 years, starting in an independent bookshop in Dublin in 1985, and joining Waterstone's in Dublin three years later. Having managed Milsom Street Waterstone's in Bath for six years, and the South West Region for five, I opened the Oldfield Park Bookshop in Bath in 2002.

We are trading out of 600 sq.ft., with stock at retail of £80,000. Turnover this year will be £270,000 in the shop, plus £50,000 from schools. Setting up as an independent has been the best move I have ever made, and it would take a great deal to change my mind, and return to chain bookselling.

Independent booksellers have big advantages over chains. We are so close to our customers that we give a phenomenal level of service. Our stock can change responsively, and is not beholden to head office deals, and we can offer a stunning ordering service. I passionately believe that these strengths will work even more in our favour – if we play to them – because the chains will come under even more pressure to deliver more from less.

Relating this to stock…

Shortly after opening, there was the heady excitement of sales running ahead of the (modest) business plan. I remember telephoning Patrick Neale in Chipping Norton agreeing how wonderful life was in the independent sector.

Six months later, the question of 'where is it all going' began to arise, as, with little money for stock, all the profits were being ploughed into developing the range (translated – paying suppliers).

Only then did a great truism suddenly come back to haunt me. On my first day working in the book trade, in January 1985, John Davey, the esteemed owner of the first independent I worked in, solemnly said to me 'Bookselling is incredibly capital intensive, you know.' Writing the cheques out brings home the reality of this great truth.

Managed well, stock is the one thing which can transform a book shop more than anything else. Well chosen stock, displayed attractively, can turn failing businesses around. Badly managed stock can kill bookshops, if dead stock goes out of control.

Customers are very intuitive. They can see that a bookshop is greater than the sum of the individual books, and that this holds true to each section. Stock gives sections and the shop their identity, and this gives customers confidence that you know what you are doing. Confidence leads to loyalty, and suddenly you have a business.

These notes are a distillation of what I have picked up about stock over the years. I have structured it accordingly…

(1) Stock Levels, and how to manage these effectively

(2) Buying

(3) Dead Stock and what to do about it

(4) Margin management

You may agree or disagree with some or all of these ideas, but hopefully it will get you thinking and set a few lightbulbs off.

Stock Levels

There is no perfect formula for arriving at a simple rule of thumb stock figure. Shopping centres are seasonal. Holiday resorts have different seasonal patterns, and stock for individual sections can fluctuate on a month by month basis.

As a rule, most shops aim to turn their stock over between 2.5 and 5 times a year, depending on rent and location. Anything less than 2.5, and there may be an argument for reducing space or diversifying, whereas anything over 5 may suggest that the business is underspaced.

There are two useful rules to bear in mind:

'It's not the size of the shop, it's the size of the market that counts'

You can use additional space in your shop to grow your market, but space on its own will not generate sales. The slower your stock turns over, the more likely your stock will become obsolete. This rule needs to be applied to sections as well as to the shop overall.

Apart from the risk of having to write off stock, there are considerable working capital implications to having too much stock in your business. I have provided a simple model below which illustrates this point.

'Stock expands to fill the space given to it'

A corollary of Parkinson's Law, and a great truth of bookselling. It is too easy to leave parts of the shop to linger because there is no pressure to do otherwise.

Every book in your shop must be:

- Waiting to be sold.

- Waiting to replace a book which has been sold.
- Waiting to be returned.

You have to ask yourself about every book in your shop, and *honestly* decide what is happening with it.

Stock & Working Capital

There is almost a mathematical link between stockholding, sales and working capital. At times, after a quiet month's trading, it can feel almost twice as hard to pay suppliers.

Most bookshops in the independent sector work with margins of 35% from suppliers overall, plus 30 days credit from the end of the month in which the books were purchased. If a shop's turnover is more buoyant – say £5,000 greater in a given month, the bookseller has the advantage of the use of this money. If turnover is conversely £5,000 below budget, one has the additional hit of having to fund £5,000 of stock, as well as not having taken the money in the first place.

I have an illustrated example below, which demonstrates the link between turnover and working capital. In our shop, we have stock of £80,000 at retail, obtaining a margin of c35%. The money required to fund this stock is £52,000, or 65% of £80,000.

If we turnover £10,000 in a given month, we can offset our capital by this amount reducing working capital to £42,000. In December, when we would hope to turnover £42,000, our working capital commitment drops to £10,000. The more you turnover, the less you need to fund your stock.

Stockholding at Retail	£80,000
Stockholding at Cost assuming 35% Discount and 30 days credit	£52,000

Turnover

Annual	Monthly	Working Capital for Stock
£120,000	**£10,000**	**£42,000**
£160,000	**£13,300**	**£38,700**
£200,000	**£16,700**	**£35,300**
£240,000	**£20,000**	**£32,000**
£280,000	**£23,300**	**£28,700**
£320,000	**£26,700**	**£25,300**
£360,000	**£30,000**	**£22,000**
£400,000	**£33,300**	**£18,700**

Seasonal Stock Management – Reducing Stock Levels at Quiet Times of the Year

We all continually reinvent our business, and you should use seasonal fluctuations in demand to do this. Introducing a controlled number face out and zig zag shelves for non fiction, education, atlases and children's books can be effective. The most effective thing you can do is to rip out fixtures and fittings – tables, spinners and dumpbins, reintroducing these at busier times of the year.

Stock Rooms

If you have a stock room, you should aim to empty it and put a chastity belt on the door. No customers ever visit a stock room, and bookshops can end up tying up fortunes in stock which will become obsolete if left unaddressed.

Buying

This is one of the most important activities in the business. The first thing to get right is to ensure that you are buying stock at a level appropriate to sales in the business.

The Open to Buy System

This is a simple system designed to help you manage your buying and stock levels. I have yet to come across a better system in 20 years of bookselling.

If you set yourself a target for your stock at the end of any given month, this system allows you to buy, and buy creatively, to ensure that your stock is within budget, and that you are moving the mix of stock in the right direction.

It follows the logic of this simple equation:

Amount to Spend (Open to Buy Figure) = Stock at Month End + Sales + Stock Returned – Current Stock Level – Money already Committed to New Titles

With this system, you set yourself a stock target at month end, and you derive yourself a purchase budget by taking account of sales, returns and your existing stock level.

You then monitor your purchases over the course of the month, ensuring that they get to an agreed figure.

You can ringfence funds for section development, so that long term priorities are taken care of. If you are running out of money, you can adjust your budgets, reduce orders or hold orders until the following month.

A worked example is included at the end of this section.

Understanding your Business and What is Selling

The component parts of your market are unique to your shop, and they fluctuate every month, sometimes not by much, and sometimes radically.

One important rule here to kick off with:

'90% of <u>all</u> useful information comes from your *customers*'

This is one of the most important competitive advantages which we have over chains, as we can calibrate our stock ten times more accurately than they can.
Head offices do not listen to customers – they listen more to publishers and the trade. Most chain front of stores are inconsistent at best.

It is good to take a thematic look at what is selling in your business – I have detailed a simplified version of this below. You could also go down to the next level of detail within the children's and non-fiction sections. This is your best source of information when reorganising sections, and you cannot afford to be sentimental here!.

You must look at bestsellers, reorder from sales reports and customer orders to see if there are any patterns you are not picking up on. Easy wins for us have included expanding Simpsons books, Diet books, Pink Fairy books and Australian Women's Weekly cookery books.

The sample week's analysis of our shop floor sales presented the following picture:

Sample Week's Sales

	Books	%	Cash	%
Children's	230	48	£1,428	33
Fiction	72	15	£707	16
Non-Fiction	81	17	£1,022	24
Bestseller Bay	38	8	£422	10
Customer Orders	57	12	£738	17
TOTAL	**478**	**100**	**£4,317**	**100**

When we expanded (+ 9 bays) last summer, I used similar information sampled over three weeks to identify what we needed to grow, and we have been 25% ahead of last year with our extra space.

Bestselling titles

Perversely, you can increase your sales and stockturn, and reduce your working capital by not underbuying bestselling titles. It is now time for another rule:

'Never assume that the market is exhausted for a bestselling title'

When I was in Milsom Street Waterstone's, we ordered 120 'Year in Provence' every week for six months. Keep going until they stop.

It is a brilliant idea to run a three months top 200 report. You will find at least 10 decent titles buried there. If they are selling in volume off the shelf, what will they do on a table or faced out?

To prove a point, it is confession time – we sold out of Paul McKenna's *I Can Make You Thin*, the new David Dimbleby book, and *A Short History of Nearly Everything* this weekend. These are not books to keep in sixes, but two of each would not have represented a major risk.

Everyone – even the best buyer – goes light. You should trust your instinct, but not purely based on reviews or what reps say. Keep your radar switched on behind the till!

Core Stock

Every shop has approximately 500 – 1,000 titles which they can never ever afford to be out of, as much for reputation as anything else. These can be identified as the good backlist titles from a top 1,000 on an annual bestseller list. Titles include Roald Dahl backlist, *The Highway Code*, *Stalingrad* and some Bill Bryson, to mention safe examples. A local history selection should be included as a matter of course. Identify and flag these on your system, and check availability monthly. Review the list twice a year and amend. By simply keeping these in stock, you could add £20 - £40 per day on average to your turnover.

Seeing Reps

We are just coming out of a phase of seeing reps, having made a polite and embarrassed retreat.

The following pros and cons are borne out from experience this year:

Pros

- Returns are wonderful, and some will even take back wholesaler stock.
- You do sell more and are better informed about their books.
- They are greatly beneficial in specialist booksellers, who will normally draw on customers from a wider catchment area.

Cons

- You need to budget £1,500 in additional stock for each rep, almost as a float.
- Their books prevent better selling stock from selling.
- Tighter budgets mean less stock for stock which you know you can sell.
- The centre of gravity of our new title buying was badly affected. Subscribing is reactive by nature.

Planning Christmas

We all know how critical to profit this is, given our fixed costs. Plan your November and December buying so that stock and demand dovetail properly.

You absolutely must run bestseller reports for the previous year to ensure that your quantities are appropriate to the current years demands. Experience has shown that this has had two specific benefits – we don't underbuy solid bestsellers such as *Now We Are Sixty*, and we don't miss out on local books which pop up once every December.

It is important not to get carried away with the trade press noise in August, September and October. Buy incrementally up to November, but strike, and strike hard, when titles like "Schotts Miscellany" and "Eats, Shoots and Leaves" materialise. Your customers will know what they are, and you will have them in stock 48 hours before the chains know what is happening!

The same sales applies, in diluted form, for the good bestselling titles. Speed, responsiveness and constant vigilance are the watchwords.

Open to Buy – Working Example

Month	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb
Target Stock At Month End	80	80	80	80	85	80	90	95	110	95	85	80
ADD *Budget/Forecast Shop Floor Sales*	25	19	18	24	19	17	25	20	24	44	17	17
ADD *Additional Sales (Schools/Harry Potter/Book Fairs etc)*	7	4	4	5	3(HP)	1	21	11	7	5	8	4
ADD *Forecast Returns*	2	2	2	2	2	2	2	2	1	0	6	4
MINUS *Actual Stock at Previous Month End*	80	77	72	77	80	86	80	90	95	110	95	110
EQUALS *Open to Buy Budget for Current Month*	***34***	***28***	***32***	***37***	***29***	***14***	***58***	***38***	***47***	***34***	***21***	***-5***

Notes:

(1) All Figures in £k.

(2) Five (March, June, September and December) and Four Week Months used.

(3) (HP) – Harry Potter 6, published in July 2005.

Comments:

- This example is based on my shop. Stock follows a constant level, building up in the Autumn to a peak at the end of November.
- Additional sales are virtually all school orders.

- In most months, stock is on budget, and the open to buy budget broadly equals the shop floor plus schools budget.
- The September buying figure is high due to the volume of school orders. I split the budget in two here.
- More is budgeted in November than in December. Last year in practice, we were understocked at the end of November, and spent more in December.
- At the end of January in this example, the stock figure is way over budget, due to hedonistic living. This leaves us with a negative open to buy figure, i.e. if we buy nothing, and sell and return everything expected, we will still be overstocked! When you get into this situation, you adjust subsequent end of month stock figures to glide you down to your original plan.

Dead Stock

The scourge of every bookshop. I saw a branch of Waterstone's close due to having 60% of stock not sold in a year. The shop looked beautiful and tidy, with everything well appointed but the stock was dire and the customers knew it.

There are a number of excellent rules to bear in mind here:

'Books which are not selling prevent books which are popular from selling'

This works from the point of view of shelf space as well as financial space.

The corollary to the above rule is:

'Don't compound a bad subscription / order by displaying it prominently'

If it is a turkey, it's a turkey. Stick it on the returns shelf!

When I was in Waterstone's, a brilliant piece of analysis highlighted the fact that stock productivity panned out as follows:

Most popular %	% of Sales
5%	*15%*
10%	*24%*
20%	*45%*
30%	*61%*
40%	*75%*
50%	*84%*
60%	*90%*
70%	*95%*

When the final 30% was analysed, it was found to be single copies of difficult to return single copies hiding on the shelves. You should quarterly go along your shelves and weed this stock out for return, using returns reports (on hand and not sold) to assist you.

We have 216 shelves in our shop with an average of 40 books per shelf. If three books per shelf are dead, then 16.2 shelves, or two bays are dead. We all have a project in our minds that needs those two bays!

When I analysed our returns last spring, the following pattern emerged:

Dead stock has accumulated over six months, in which our sales were £170,000.

	Books	Value
Uncollected customer orders	*72*	*£738*
Out of Date Travel Guides	*20*	*£316*
Out of Print Bertrams	*37*	*£352*
Out of Print Gardners	*46*	*£492*
Total Value		**£1,898**

This dead stock figure represented 1.16% of sales (about average for most bookshops). To prevent this happening, we could have taken more deposits, been quicker off the mark with travel returns, gone through our dues listings more carefully and not bought anything from Gardners.

One final tangential axiom, related to dead stock:

"You only see your failures, and never see your successes."
(Robert Topping)

A great danger when looking at dead stock is to take too defensive or cautious a view, which usually means ending up running out of bestsellers. If you have a dead stock problem, isolate the stock and sell it off.
If you invest the £500 you recover from a sale in bestsellers or developing new sections, you will quickly get more than your write-off back in extra sales.

Margin

From experience, this is more to do with tactical successes, rather than anything thematic. One major axiom has always influenced my thinking here:

'You end up compromising on margin to suppliers and customers when you are trading in weaker markets'

Giving discount…

We budget to give away 4% of turnover in discount. Whatever you do or don't do, you must budget for this.

We never discount children's books, and can usually stock order when wholesalers offer additional margin, confident that these will sell through.

We have ended up discounting mass market hardbacks by 20 – 25% to generate traffic at Christmas. We have less of a presence with the third of people who only ever visit a bookshop in December.

We knock 99p off reading group titles for bulk purchases, but this has massively raised our profile.

We aim to make 10% net profit from Schools, as long as they pay promptly. The cash flow benefit is useful to the business, and partly helped us stagger our capital expenses last year on our small extension.

Apart from this, we discount little. Our strength is our customer service, and loyal customers have sometimes been embarrassed when we have rounded things down, so we don't!

It can be wounding to hear people quote Sainsbury's / Waterstone's / Amazon prices, but I continue to believe in the silent majority. I monitor them, mind…

Getting discount…

We give everything to Bertrams, and get only 35% from Gardners as a consequence. Riding two horses doesn't work, in my view – on stock you are better going completely with one supplier. We record all reorders and normally stocked customer orders with Bertrams. We go to Gardners for their specific titles and little else.

We record all purchases at retail and cost, under four headings, and review this religiously every month.

A typical month looks as follows:

	Cost	Retail	% Discount
Bertrams	£9,784	£15,729	*37.7%*
Gardners	£1,320	£1,883	*29.8%*
Direct	£ 1,022	£1,715	*40.4%*
Small Parcels	£ 478	£ 524	*8.8%*
Total Purchases	**£12,604**	**£19,851**	**36.5%**

Sales for the month were £17,070 in the shop, plus £4,108 from schools, £21,178 in total.

We don't always order before 1 p.m. to get an EDI discount from Bertrams, but that is a confession. One really should, as customers do not notice the difference between one and two days for an order to arrive.

When we used reps, we upped the discount to 42% to 47%, but the £20k of extra stock needed to fund this more than outweighed the benefits.

We have direct supply accounts with the big suppliers, plus Heinemann for schools. We go direct for non basic items where possible. All special customer orders are phoned through direct where possible.

We are not too sympathetic with local publishers, as we are for once in a stronger position, so I usually ask for 40%. We promote them like mad, so they get the benefit.

I have not tried any less orthodox suppliers in the Christmas run in. I think that benefits are somewhat peripheral on a small number of titles, but may be wrong.

Non book products can increase your margin significantly. Very depressingly, I worked out that we made as much pure profit from our 4 card spinners than from our schools business. This really gave me cause to contemplate my mortality.

You should look at cards, bookmarks and stationery, as stable options but only on a sale or return basis, possibly only seasonally for some lines, and in such a way that the centre of gravity for your business is not significantly altered. If a relevant non book line delivers more than 55-60% gross profit, it is worth thinking about.

I stress the importance of not going mad on new title buying in September, October and even November! Hold your nerve, as you really will get great deals from wholesalers in late November. However, you have to be confident when spotting massive titles like *Schotts* or Lynne Truss. These usually break out in late November.

And keep the antennae switched on to beat reprints.

Conclusion

This really is a personal view from the front line, and obviously populated with information from my shop.

I hope you can extrapolate enough information for your own businesses and make a difference.

Good luck!