

# Finding the Right Equation



## The financial realities of operating a bookstore

By Joy Ferguson

Michael Neill, co-owner of Mosaic Books in Kelowna, BC and President of BookManager, shared his knowledge and experience with novice booksellers during CBA Super Saturday at BookExpo Canada.

The simplified version of Neill's advice is: Understand the budget equation for a bookstore,  $100\% \text{ sales} - 10\% \text{ rent} - 60\% \text{ cost of books} - 20\% \text{ for wages} - 10\% \text{ extras (supplies, credit card charges, etc.)} = \text{zero profit} \dots$  and then "tweak" it. Find ways to lower the cost percentages and raise sales. Bottom line, one per cent here or there can make a tremendous difference. A long list of factors influence bookselling success, and it is the sum of those that predict profits.

### Location! Location! Location!

In 1995, Neill and his wife, Michele, moved to Kelowna, BC and bought Mosaic Books. Mosaic Books was on a side street, not strategically placed, only 3300 sq.ft., but with a reputation (since 1968) as "The bookstore of the Okanagan." Neill became busy significantly growing sales until Chapters anchored in a mall near the edge of town. His sales dropped 30 per cent in one year. He knew that their side street location had become a liability, but he was not ready to give up. He moved to the most prominent downtown location and a bigger store (10,000 sq.ft.). Sales again climbed.

"Location of a bookstore is likely the biggest factor in determining the level of the store's success," says Neill. He cautions that towns "with a Chapters superstore within a one-hour drive generally have difficulty earning the owner a decent income." Other competition can be managed if the bookseller runs an efficient, well-stocked store, in a high traffic location. The high pedestrian traffic of busy downtowns and shopping malls with complementary retail stores is ideal. Choosing the right location is a combination of assessing the competition and finding a high traffic area with rent that fits into your business plan.

### Rent

As you would expect, high traffic locations demand higher rent. A bookseller must ensure that additional rent is in proportion to the potential for increased sales. At the same time,

## Ten Tips to Reduce Costs & Increase Sales

Neill warns, "Avoid the temptation of low rent." He gives the example, "A low rent store might bring in \$250,000 in sales after paying \$25,000 in rent (10 per cent of sales). Moving to a high traffic location might increase sales to \$600,000 but with rent of \$60,000 (10 per cent of sales)." Although \$60,000 in rent is a huge number, the high traffic area has allowed for an increase in sales from \$250,000 to \$600,000 (equals an additional \$350,000 in sales) while other operational costs (wages, phone, etc.) have remained the same. Neill's own experience has convinced him that bigger is often better—or at least more profitable: His rent went from \$3,000 to \$14,000 when he moved to a larger store and prime location, but his sales rose from \$700,000 to 1.5 million.

How can a bookseller know whether his market will allow for increased sales were he to move or expand? "Most booksellers average sales of around \$300 per square foot. If you are averaging higher, then you probably could do better in a larger store," suggests Neill. As an example, Calgary Alberta with a population of 1.2 million, has seven superstores. Neill explains, "If each store is 25,000 sq.ft. in size, the math tells us that it takes 6,800 people to support each 1,000 sq.ft. of bookstore space. If your town's population is 20,000, with no Chapters for at least an hour, your store should be able to support a bookstore with 2,900 sq.ft. of space. At a modest \$200 in sales per square foot, sales will be \$580,000. It stands to reason that many small communities in Canada have independent bookstores that are doing less than their potential."

So why don't all booksellers open in a high rent, high traffic location? Fear. "The fear of not meeting the sales projections needed to support the high-traffic-rent district location." "But," says Neill, "so long as you know how to stock a store properly, the increase in sales will be stunning."

### Inventory Turns

To determine how efficiently you are stocking your shelves, it is important to monitor inventory turns. "Inventory turns tell you how your investment in inventory is performing relative to your sales volume," explains Neill. All store space must be well stocked. Non-selling space (storage, receiving, etc.) should be minimized. And books that are not selling should be returned.

"Most profitable stores average three turns a year," explains Neill. For example, with \$100,000 retail inventory, expect yearly sales of \$300,000. Neill says, "If a store reaches about 3.6 turns, it will be difficult to increase sales further without carrying more stock. And to carry more stock, you may need more space." It is one of the reasons that Neill believes a bigger independent is a

1. Using two per cent of sales for advertising is a business rule of thumb, but bookstore ads are often ineffective. Consider reassigning this to rent in a higher visibility location.
2. Do not be tempted into a bad location just to get low rent. High pedestrian traffic equals high sales.
3. Create opportunities to partner with publishers and utilize co-op funds, rebates and shared markdowns.
4. Wage costs eat up profits. Keep them at 20 per cent of sales or less.
5. Insufficient cash to purchase inventory is a major problem for bookstore startups; budget carefully, and return unsold books before the 12-month publisher deadline.
6. Pay close attention to your store's gross margin and how it changes from year to year. Remember, discounts and freight will impact your bottom line.
7. Borrow from your suppliers first and credit cards last: Many suppliers offer early payment discounts, and, says Neill, "It is the cheapest money you'll ever get."
8. Be sure to use amortization depreciations. That is, you can depreciate one-time purchases—such as store fixtures—over time on your taxes.
9. Talk to other booksellers about their sources and buying patterns. These may present opportunities to increase your profit margin.
10. Recognize when change is needed. And, says Neill, "It is important to initiate change: If you try three new things and one of them works, that's progress."



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stronger independent.

If turns are low, it may be a sign that you are carrying dead inventory. This will limit your ability to buy new titles because your shelves are full—while your bank account is empty. If you persist in buying books at the same rate, the turns will continue to slide because you are buying books much faster than you are selling them. And, in a bookstore, selection is key to sales. Neill recommends keeping no book past one year—and most publishers allow only 12 months to return books. When books first arrive, Neill suggests including a date label—BookManager includes a coded date reference—to assist with tracking. Neill's research shows that old books sell at a rate so slow that those sales make up less than one per cent of overall sales, yet those books occupy up to 25 per cent of the shelf space—and cash outlay. Thorough thinning will allow you to see the holes in sections and fill them with a wide selection of new releases that keep existing customers content and entice newer clientele to keep coming back.

## Reducing Costs

When stocking shelves watch for opportunities to raise profits and increase traffic.

Magazines are traffic builders. Although margins on magazines are only 20 per cent, there is no risk since they are returnable. And the RDA (retail dealer allowance) is a quarterly rebate that Neill says increases his profit to about 24 per cent.

Neill sees remainders as a tremendous opportunity. He buys skids from publishers, such as Random House, that give him a 60 per cent profit margin. Two cautions from Neill: Avoid too many copies of the same title, and ensure you have storage space. Neill adds, "Remainders are key to letting my store show a 40.2 per cent gross profit, and interestingly, remainders do not seem to cannibalize the sales of new books."

Neill believes that if booksellers were more vocal, publishers would respond with more partnering opportunities. For example, Neill reasoned, if publishers pay Chapters for premium placement, then why not ask them to pay for his space? He offered them window and front table space for a monthly fee. The plan has suc-

ceeded, beginning with Raincoast's rental of a window for one month at \$250. Neill believes, "Booksellers have been too complacent. We need ideas that fit our model and then we must push publishers to be more supportive."

When Chapters opened in competition with Mosaic Books, Neill's sales dropped from \$1 million to \$700,000. At the same time, Coles—also doing \$1 million in sales—closed. Chapters' sales quickly rose to \$4 million. So, what had appeared—based on Mosaic and Coles' sales—to be a \$2 million dollar market, was actually a \$4.7 million dollar market. "So, where did the extra \$2.7 million come from?" asks Neill. His response: "I probably missed seeing the opportunity (untapped business) like so many other independents. Today, I do \$1.5 million (after expanding to a better location) and I know that my sales must dwarf theirs. And then there are the big box discounters who sell tons of books. Where is the ceiling in sales this time?" Neill will keep tweaking that equation until he bumps his head. CBA

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