

Profitable Books: How to Choose Winners

Panelist: Marion Gropen

Introduction

What can a number-cruncher contribute to picking the best books? The profit part! That is, after you have the market and the editorial work nailed down, you need to do a financial model. It comes last, because you use it to re-visit and sharpen the other two. A financial analysis is, in the end, a tool for providing feedback.

The important points here are

- that you and your colleagues must work as a team,
- that you must know your readers and your company's areas of expertise,
- that you must focus on how your cost structure and your distribution channels affect your projects, and
- that you must use the information from your financial model to re-work your projects until the bottom line projections meet your goals.

Teamwork is Critical

I cannot emphasize strongly enough that a successful publishing program must be a co-operative effort from all 4 parts of the company: editorial, marketing, production and financial. Leaving out any one of them substantially reduces your chances of success with any given book, but this kind of co-operation isn't common. It's certainly tempting to cut the corners, and save the time that co-operation requires. The solution is not to work in isolation, but to keep your meetings focused and find ways to keep communication flowing efficiently. (Using technology is a good start - shared documents or workspaces can help with this.)

Build your book from the beginning with the input of all four elements. Editors must talk with marketing people about the reader for the book and about which elements will make publicity easier. Some of the smallest changes, editorially, can have a huge impact on marketing.

Production must be consulted from the beginning as well, if the book is anything other than straight text. Again, small changes early on can have huge impacts how much it costs and how long it takes to bring a book to market, as well as on how the reader views the end result.

Your financial models of the book can also help to improve your performance. Each change to adapt to the market or to production

constraints should be judged based upon whether or not the results will justify the effort. And a spreadsheet is a very good way to summarize all the elements and their interactions, as well as giving some sort of overall total effect.

Serve Your Readers

While your team is working to improve your books, it is important that you focus **not** on making some sort of platonic ideal of the "best book," but on your readers and how your book can best give them what they want.

Start your financial analysis by turning your knowledge of the market and the topic into numbers.

- Who is interested in this type of book?
- How many readers are interested in which elements?
 - What else do they do?
 - Use census data, club memberships, magazine subscription bases, etc.
- What techniques will reach them?
 - How many will see it? Each place you can find readers will have a different population. Know how many are in each place. This makes estimating how many will buy from that group much easier.
 - How much will reaching them cost?
 - Materials
 - Time
 - Buying lists, ads, etc.
 - Comp copies and postage
- What response rates are you likely to get? (Start with 1% of those who see each of your marketing campaigns, until you have a better data from your own experience.)

Costs and Distribution Shape Your Profits

Know your cost structure and distribution channels, as these will have an enormous impact on what you can and cannot do profitably. "Profit" is a word that makes many publishers uncomfortable. But remind yourselves that publishing is still a business, even if we're in it for love. Profit is one very good measure of how good a job we're doing, and of how much we can do in the future.

In order to evaluate cost and distribution, and many other variables, you should have a title analysis P&L spreadsheet. This is a little different from the P&L your accountants prepare for your company. For example, it should not include overhead. Instead, the bottom line will be your contribution margin, that is, the amount your project contributes to supporting the company as a whole, and to your overall profit.

Let's look at your handout pages for a moment. The first page shows some of the guesses you make about most projects before you acquire them. It includes price, and the number of copies you think you might sell, the royalty terms you think you need to offer, the cost to edit and design a similar book, and the cost to print similar books. Last, it includes the costs of marketing and selling books, and the ever-popular miscellaneous items that don't quite fit anywhere else.

You'll look at your best guesses about the future three ways. First is what you think really will happen (also known as the most likely case). The second is what you dream might happen if everything goes right (call it the best case). And the last is your nightmare version, which we call the worst case.

The second page of your handouts shows how these numbers come together. Let's start with the bottom line. Your best case has a lovely \$28,000 contribution margin, but the worst means that you'll lose almost \$11,000 more than your overhead. And you think you are most likely to make less than \$5,000.

If you find that the most likely case is good enough to warrant undergoing the risk of the worst case, and that the worst case is one that you could survive, you're in good shape. In this case, you might want to try to improve the project before going forward.

When your analysis shows that the project isn't quite good enough yet, you can try to test possible improvements with "what-if scenarios." That is, you can look at one or more improvements, and adjust your spreadsheets to account for all of the consequences of those changes. Some things you might attempt include

- improving your design,
- bringing in another writer to fix the manuscript,
- doing less to improve the book,
- trying different types of marketing, and
- trying different sales channels.

Improve the design, to make the book more attractive to your target group or to improve costs. When you do this, you will need to adjust your plant costs, which are fairly low in the example, and may need to adjust your PPB. You will need to adjust your sales (up or down),

and that will shift your distribution costs, and your marketing budget. It may also shift your subsidiary rights expectation.

Bring in a book doctor. This will add to your plant costs, as editorial expenses, and should also increase your expected sales. If the manuscript is a good idea badly executed by an author with a solid platform, this might work.

Reduce the use of your in-house editorial time. This means not working as hard to improve the book, and it reduces the sales potential of the book, but also cuts the costs associated with the book, and makes it possible to acquire more projects. This is another way of saying cut your losses and move on.

Try different marketing approaches. Estimate the costs and results for each of them, and look to see if the overall contribution margin improves with each change.

Consider different distribution channels. Not all books do best through bookstores.

- Can this book do better in a special interest, non-book channel?
- Can you find other ways to reach the audience?
- Can you deliver the book electronically?
- Can you deliver the book as a non-book product, too, spreading fixed costs over more revenue streams?

Run the Numbers Over and Over

In each of these cases, you need to use your financial model to see if you have improved things or made them worse. In some cases, you will find that canceling a project is your best option. In others, you may have no projects that meet your requirements, but you may be able to combine 2 or 3 books that are easier to publish and manage to cover your overhead that way.

No matter what happens, it is important that you re-do the numbers until you understand the best way to do the project. Once you know the best way that this book can be published, you need to compare the contribution from your final version to what we call your "hurdle rate."

A **hurdle rate** is finance-speak for the minimum contribution margin that each project is required to make. Each project is required to clear that hurdle before getting approval.

How can you decide what your company's hurdle should be? You start with the overhead in your budget. Then decide what revenue you can expect to produce with that staff and those resources. Divide the

overhead by the revenue, and add the interest you may have to pay to get your working capital. That should be the rate. Multiply each title's expected sales by that rate, and you have the contribution margin that the title must exceed. Of course you also have to think about other considerations, but if the acquisition isn't going to clear this hurdle, you probably shouldn't do the book.

Some companies have difficulty finding enough new manuscripts that can be shaped into books that clear their hurdles. Those companies are usually tempted to pick the best manuscripts in front of them, and hope that something works out right. That may be their best option, but there are usually others.

- Consider changing your operation to reduce your overhead.
- Consider looking for books in other niches, niches that are related to the ones you already serve.
- Consider generating new projects to meet needs you see in the market, and then finding people to write those books.

Sometimes you are just facing a dry spell, and you know that you have other good manuscripts coming in that will support the company. You may, under these circumstances, have to accept a year with a significant loss in order to bring your company through the crisis. Even if this happens, continue searching for other brand extensions or manuscripts that can fill the hole. In the meantime, try to preserve as many options as you can, and pick the best of the manuscripts available. And, who knows, your acquiring editors may be able to make silk purses out of the current sows' ears.

Conclusion

Picking the best projects for your company is much easier if your team works together in evaluating every significant investment, and in every strategically important decision. Knowing and serving your readers' needs makes success much more likely. Failure to understand your market makes losses almost inevitable. Finding the best combination of ways to bring your books to their readers is critical to your success. Understanding how your costs constrain your options keeps you from blundering down dangerous paths. And last, finance and accounting are supposed to tell you useful things. If you aren't getting useful help from your numbers, you need better tools. Persist until you get them, and can use them easily.

Knowing how to tell which projects can be made into profitable additions to your list doesn't guarantee success, but it reduces the amount of luck you need significantly. And what more can we ask?

About Marion and Gropen Associates

Marion has been in publishing for the last 16 years, including 8 as an executive in charge of finance and operations for a modest-sized company (\$5 to 10 million/year in sales). For the last 3 years, she has helped very small publishers rise above many different types of challenges. You can find out more about her at www.GropenAssoc.com.

The texts and handouts from many of the other courses she has given are freely available from that site. While you are there, you may also want to explore the other resources (also offered without charge) in the Reference Desk section.

The handouts for this course use part of one of the downloadable tools available on that site for a nominal fee.