

## **An Analysis of John Wiley & Sons, Inc.**

### **Versus**

## **McGraw-Hill Companies, Inc.**

### ➤ **INTRODUCTION**

For many business professionals, the publications of John Wiley & Sons are a common sight; countless accounting, business, and technology textbooks bear the Wiley logo. In addition, Wiley now publishes the “For Dummies” self-instruction books, which populate millions of bookcases all over America. Yet, despite all this exposure to Wiley products, how much is really known about the company? Is it a “here today, gone tomorrow” phenomenon, or a viable twenty-first century corporation? As a publicly-traded company, is it a sound investment?

The purpose of this report, an objective professional summary of John Wiley and Sons, is to provide a comprehensive analysis of the firm from a strategic management perspective. Ultimately, such an investigation must answer the questions: Does Wiley and Sons sustain competitive advantage so as to earn above-average returns? If so, how is this achieved? However, a thorough appraisal requires a more expansive inquiry. A general profile of the firm, selection of an industry benchmark, and a review of the publishing industry will provide context for interpreting the company’s performance data, revealing the conditions under which Wiley creates and implements strategies. The publishing industry’s nature, structure, market segmentation, and current issues are reviewed. The actual corporate analysis will focus on six “performance pressure points.”<sup>1</sup> They include Organizational Citizenship, Strategic Positioning, Profit, Equity,

and Share Value management, Debt, Cash, and Asset management. Finally, the results are summarized and conclusions are drawn regarding management's overall performance and the firm's future potential.

### Data Mining Process

The methodology for this assessment is suggested in *The Performance Scorecard*, by Raymond K. Van Ness, Ph.D.<sup>2</sup> The data-mining process included both qualitative and financial information, yielding a well-rounded assessment. Financial data has been culled from the Annual Reports of Wiley & Sons, McGraw-Hill, as the benchmark, and other firms in the publishing industry. The Financial and General Analysis (FGA) software included with *The Performance Scorecard*, was used to analyze this information; it outputs performance ratios, graphs, comparisons, and other analytical statistics.<sup>3</sup> Dozens of other sources, referenced in the Works Cited section, were consulted for additional input regarding Wiley & Sons and the environments in which it functions.

### Profile - John Wiley & Sons, Inc.

Before evaluating its current performance, consider the history of John Wiley & Sons and the company it has become. In 1807, during the presidency of Thomas Jefferson, Charles Wiley started a small publishing company.<sup>4</sup> It published authors like Herman Melville, Edgar Allan Poe, Nathaniel Hawthorne, Hans Christian Anderson, Victor Hugo, Charles Dickens, and Elizabeth Barrett Browning.<sup>5</sup> Over the years, various family members ran the firm (see [Exhibit 1](#)). In 1904 the company incorporated in New York and expanded into Canada, Europe, Shanghai, and Manila, which paid off after World War II, when the soaring demand for textbooks caused dramatic growth.<sup>6</sup> Wiley

went public in 1962, after 155 years of private ownership, and the first non-family CEO took the helm in 1979.<sup>7</sup> The 1980's brought expansion through growth and acquisitions; however, in 1990 a new CEO, Charles Ellis, took steps to strengthen the core businesses, eliminating weaker segments.<sup>8</sup> The company's website was established in 1995, William Pesce became CEO in 1998, Wiley's InterScience.com launched in 1999, and major acquisitions fueled continued growth.<sup>9</sup> In 2002 the company outgrew its headquarters in New York City and moved to a waterfront property in Hoboken, New Jersey.<sup>10</sup>

Today, Wiley's global operations include approximately 3,400 full-time employees, occupying sites in New Jersey, New York City, Ohio, San Francisco, Indiana, Australia, Canada, Germany, England, Singapore, Hong Kong, India, and Japan.<sup>11</sup> Wiley's fiscal year ends April 30th,<sup>12</sup> and KPMG provides the firm with accounting and auditing services.<sup>13</sup>

A review of Wiley's history underscores the family's continuing involvement in the management of the firm. (See Appendix [Exhibit 1](#)) Although actual ownership is more diversified, analysis verifies the family's ongoing interest in the business. As [Exhibit 2](#) reveals, non-family shareholders own 84% of total stock outstanding, 23.7% of which is held by institutional investors. The family holds only 14.8% of outstanding stock, and management holds the remaining 1.2%. However, decision-making power is concentrated in Wiley's Class B stock. Class B stockholders elect 70% of the Board of Directors, and in general voting situations, Class B stockholders get one vote per share; Class A stockholders get only one-tenth of a vote per share.<sup>14</sup> Members of the Wiley family control 76.4% of outstanding Class B stock. Wiley & Sons is led by a Board of

Directors, consisting of eight members; eleven corporate officers manage day-to-day operations. The composition of the Board of Directors is detailed in [Exhibit 3](#). [Exhibit 4](#) lists the corporate officers and their duties.

#### Selection of Target

Why was John Wiley & Sons selected for this assessment? The increasing visibility of Wiley's publications in business and academic environments, the firm's long history, accessibility to its financial documentation, and its uniqueness as a family-dominated, publicly-traded corporation combine to make this firm an attractive target for study.

#### Selection of Benchmark

McGraw-Hill is an excellent benchmark for use in analyzing Wiley & Sons for several reasons:

1. Wiley and McGraw-Hill are direct competitors in the publishing industry. The U.S. Securities and Exchange Commission categorizes both companies under Standard Industrial Classification (SIC) Code 2731- Books: Publishing or Publishing & Printing.<sup>15</sup>
2. On many levels, McGraw-Hill is one of the best performing companies in the book publishing industry, with extensive global markets and excellent brand recognition.

#### Wiley-McGraw Contrasts

A number of contrasts between Wiley and McGraw-Hill should be noted, since their impacts will be addressed in later sections. Like the Wiley family, the McGraw family has maintained close ties to the business (see [Exhibit 5](#)), but they hold less ownership and voting power. The family holds only 3.51% of voting stock; one institutional investor, Goldman Sachs, owns more than that, with 6.49% (See [Exhibit 6](#)).

Wiley and McGraw-Hill have developed differently. With regard to legal structure, McGraw was founded in 1909, one-hundred and two years after Wiley, and incorporated in 1925, twenty-one years after Wiley; however, McGraw went public thirty-three years before Wiley (See [Exhibit 7](#)).<sup>16</sup> Both companies have hastened their growth through acquisitions, but McGraw-Hill started making larger, more costly acquisitions earlier in its development, and at a faster pace. Although both use a business-level, focused-differentiation strategy supported by a functional structure, McGraw-Hill is further along in the strategy-structure evolution described by Chandler.<sup>17</sup> McGraw has outflanked Wiley in the first three progressive growth areas, including sales volume, geographic expansion, and integration.

It is important to recognize that the firms have adopted very different product and marketing approaches. While Wiley continues to emphasize traditional content, McGraw-Hill has expanded its definition of content, given the digital revolution, to include “more proprietary, higher value-added enabling information, analytics, and tools.”<sup>18</sup> For this reason, McGraw now describes itself as a “leading global information provider serving the financial services, education, and business information markets with information products and services.”<sup>19</sup> With this new view of “content,” the firm has broadened its product lines to insulate itself from publishing-industry fluctuations and declines. Most noticeable has been McGraw’s addition of financial and business-analysis content, developed by its *Standard and Poor’s* and *Business Week* operations.

The differences cited above have caused McGraw-Hill to become a larger company than Wiley & Sons. McGraw is now one of the world’s largest educational publishers, encompassing educational, financial, business, governmental, and

professional publishing and information services.”<sup>20</sup> The firm is included in the S&P 500, a listing reserved for the most highly valued firms, and it employs 19,600 full-time employees; that is 5.8 times as many as Wiley’s 3,400.<sup>21</sup> McGraw’s size allows it to leverage its economies of scale to improve its cost structure, increasing its profitability. In terms of capital structure, McGraw’s superiority over Wiley is obvious. As [Exhibit 8](#) shows, in 2005 McGraw had 365% more outstanding stock, a 43% higher share price, and 607% higher market capitalization. Due to its consistent stock value, the firm has a long history of stock splits. (See [Exhibit 9](#))

## **Publishing Industry Overview**

With Wiley for a target, and McGraw-Hill as a benchmark, it’s important to provide a context for interpreting their performance. For this reason, consideration is given to the industry in which they function. Particular attention is paid to the conditions affecting the development and implementation of company strategies. After examining the nature and structure of the publishing industry, a number of key issues will be considered. This assessment concentrates on domestic factors, since U.S. book publishing dominates the industry, but international perspectives are included when relevant.

### Nature & Structure

North American Industry Classification System (NAICS) code 511130 and Standard Industrial Classification (SIC) code 2731 refer to book publishing and printing.<sup>22</sup> However, this industry has evolved so much over time that this simple description now seems inadequate. In actuality, publishing firms focus more on the design, editing, and marketing activities than on the actual printing. Rarely, if ever, is

any printing done on site, and “books” can found in “print, electronic, or audio form.”<sup>23</sup>

Publishing industry structure is defined by distinguishing elements such as concentration, consolidation, economies of scale, and segmentation.

### Concentration & Consolidation

Because few entry barriers limit new start-ups and many small, niche-market publishers exist, some sources report the publishing industry to be less concentrated than other industries.<sup>24</sup> However, acquisitions and consolidations within the field have resulted in ownership concentration. The review of historical highlights provided in [Exhibit 10](#) notes the industry’s increasing consolidation through the 1990’s, with only seven firms left in control of most U.S. publishing. These were “multi-billion dollar publishers” who consolidated many smaller firms to “cut costs and reposition themselves for the onset of electronic publishing.”<sup>25</sup> International acquisitions also increased ownership concentration, typified by the 1998 takeover of Random House, one of the largest U.S. publishers, and Bantam Doubleday Dell, by German conglomerate Bertelsmann AG.<sup>26</sup> It’s important to note that the increasingly aggressive nature of recent acquisitions has impacted the strategic decision-making of the remaining stand-alone firms.

### Market Segmentation

Traditional publishing has evolved into defined product markets, or segments. Each segment is linked with a particular distribution channel or end-user market. The eight major segments, presented in current revenue-producing order (see [Exhibit 11](#)), are labeled: Trade (General consumer books), EI-Hi (Elementary and High School texts), Professional (STMB: Scientific, Technical, Medical, and Business), Higher Ed

(College texts), University Press, Religious, Mass Market Paperbacks, and Reference. The Standardized Tests segment is associated with EI-Hi and Higher Ed, and the Adult and Juvenile segments are subdivisions of the Trade and Mass Market Paperback segments; Professional STMB includes scholarly publications and specialty journals. Sizeable publishers participate in several, if not all, segments, but most specialize in, or become associated with, a limited number of segments and/or distribution channels, selected on the basis of sales potential.

### Migration to Digital Media

While digital content-development is practically industry standard, as late as 2005 most “sustainable and established” book publishers were still “based on paper output.”<sup>27</sup> A growing number of publishers have added online and other digital distribution services to their existing repertoire, and a smaller group has totally abandoned traditional output in favor of online and other digital media. This illustrates that the primary question in digital media adoption is how quickly to proceed? Industry experts predict “the market will develop in a hybrid fashion,”<sup>28</sup> and this poses additional challenges, including “management of the dual costs of online and offline content, cannibalism of offline markets, and cross-media competition.”<sup>29</sup>

### Copyright Management & Protection

Content, protected by copyright, is the “bread and butter” of the publishing business, and as such, it must be managed and protected as intently as any of the company’s tangible assets. Copyrights are under attack from several quarters, requiring constant vigilance on the part of publishers. Industry observers believe a “clash” over digital copyrights is “unavoidable,” but creative management strategies may prove them

wrong.<sup>30</sup> Others assert that “skillful management” of digital content, combined with publisher-client “development and funding” partnerships, may create new opportunities for publishers.<sup>31</sup>

### Used Books

The market effects of used book sales, affecting mostly the Higher Ed segment, include price pressures, generated by alternative options, and threats to brand value, resulting from debates over actual textbook values. The challenges facing publishers involve management of these two market effects. With regard to pricing, industry experts indicate that management may have to realign prices, accepting “the realities of a price-sensitive reading public,” because “aggressive price hikes have only added fuel to the used book fire,” whereas a new approach may “cool the debate” over textbook values.<sup>32</sup> The challenge may also be to develop innovative means to achieve growth in spite of Higher Ed price constraints. Innovation may also assist in preserving and enhancing brand value.

### ➤ **PERFORMANCE ANALYSIS**

After completing a general profile of the firm, the industry benchmark, and a review of the publishing industry, a comprehensive analysis of John Wiley & Sons, from a strategic management perspective, can be undertaken. As prescribed in *The Performance Scorecard*, the analysis will focus on the six “performance pressure points,” including Organizational Citizenship, Strategic Positioning, Profit, Equity, and Share Value management, Debt, Cash, and Asset management.<sup>33</sup> This approach is an effective way to evaluate the sources of Wiley’s competitive advantage, the “unique resources and capabilities” that contribute to its “core competencies.”<sup>34</sup>

## Organizational Citizenship

The first qualitative analysis focuses on organizational citizenship, “corporate social behavior,” or relationship management.<sup>35</sup> Since a review of all the firm’s interactions is impossible, eleven key factors are assessed.

### Employee Relations

*Fortune* magazine named Wiley & Sons, the only publishing company on the list, one of the “100 Best Companies to Work For” in 2004 and 2005, based on its policies, culture, and the opinions of the company’s employees.<sup>36</sup> Wiley has made the Human Resources department “part of the top management team,” and its head, William J. Arlington (see [Exhibit 12](#)), is a senior vice president,<sup>37</sup> a corporate officer who can help the firm become an “employer of choice for talented individuals.”<sup>38</sup> In 2003, *Working Mother* magazine called Wiley one of the “100 Best Companies for Working Mothers.”<sup>39</sup> Wiley’s Australia branch was awarded the *Employer of Choice* citation from the government’s Equal Opportunity in the Workplace Agency,<sup>40</sup> and employee testimonials praise Wiley’s casual dress code, friendly atmosphere, and small, but regular pay hikes.<sup>41</sup> An employee who “came to Wiley through the Hungry Minds acquisition in 2001,” reports, “Wiley is one of the very best companies I’ve worked for in my career.”<sup>42</sup>

### Customer Relations

In a global society, customer relations become more and more challenging, but successful firms work hard at it, knowing “returns earned from relationships with customers are the lifeblood of all organizations.”<sup>43</sup> Wiley & Sons employs varied resources to reach customers all over the world. Since 1999, the company has participated in PubEasy.com, an e-commerce inquiry and tracking service that allows

customers to shop for publications anytime, anywhere.<sup>44</sup> The richness of Wiley's customer relations is enhanced by the company's customer-centric policies. Displaying its active pursuit of affiliation with customers, Wiley places a strong emphasis on customer service and support, saying, "we try to accommodate them—they are our customers, after all."<sup>45</sup>

### Competitor Relations

In describing its policy regarding competitors, Wiley reveals its desire to encourage mutual respect, stating that information must not be "obtained through theft, illegal entry, blackmail, or through employees misrepresenting their affiliation with the Company or their identity."<sup>46</sup> Wiley's strategic partnerships with competitors both contribute to, and are the result of, good relations. In the ongoing battle against copyright violators, Wiley has teamed up with competitors such as Pearson,<sup>47</sup> Elsevier and MIT Press,<sup>48</sup> Houghton Mifflin and Oxford University Press,<sup>49</sup> and Thomson.<sup>50</sup> In competitive situations, Wiley demonstrates restraint, avoiding negative, bitter rivalries. According to an industry reporter, Wiley remains "exceedingly diplomatic."<sup>51</sup>

### Relationship with Directors

Since good corporate governance creates competitive advantage, Boards have become an important strategic force within firms. Optimally, a majority of board members, 67%, or even 75%, must be independent, either outsiders or related outsiders. Wiley seemingly agrees, asserting that it "is in the best interests of the Company."<sup>52</sup> However, as [Exhibit 3](#) demonstrates, only 62.5%, five out of eight, Wiley

directors are independent, which is a technical majority, but not optimal. In contrast, ten of McGraw-Hill's directors, or 83%, are independent.<sup>53</sup>

With regard to director salaries, healthy independence of directors increases when salaries are modest, perks are limited, and stock options are not awarded. Average annual board salaries in 2003 were \$152,000,<sup>54</sup> but Wiley directors currently receive only \$44,000 per year, but they all receive "individual stock awards" equal to 50% of their cash compensation.<sup>55</sup> McGraw-Hill's directors receive \$50,500 per year, \$1500 per meeting, and \$1500/committee meeting, and stock options.<sup>56</sup>

#### Government Relations

During World War II, when government secrets were closely guarded, Wiley was awarded a contract to produce instructional manuals for the military.<sup>57</sup> Wiley & Sons has maintained this good rapport down to the present. Compliance with laws and regulations, including anti-trust and price-fixing prohibitions, is seen as maintaining its reputation, and "employees, officers and directors" are expected to "comply with all applicable laws and regulations in countries where the Company does business."<sup>58</sup>

#### Environmental Record

Wiley's environmental record has been excellent. In 2004, the U.S. Environmental Protection Agency placed Wiley on its list of "Best Workplaces for Commuters" for offering outstanding commuter benefits; the New Jersey Department of Transportation added Wiley to New Jersey's Best Workplaces for Commuters SM List in 2005.<sup>59</sup> Although its operations are generally not affected by environmental legislation, the company remains alert to potential concerns. A search of the Environmental

Protection Agency website indicates that Wiley has never been named in any enforcement actions.<sup>60</sup>

### Community/Cultural Sensitivity

A firm's reputation for being community minded is a valuable resource in the quest for competitive advantage. As it conducts business, Wiley is responsive to local concerns. In 2003, Wiley received the Enterprise Award from the New Jersey Business & Industry Association for its contribution to New Jersey's economic growth.<sup>61</sup> In 2002, a Wiley supervisor spearheaded a campaign, called Books for Freedom, to restock the National Library in Afghanistan, devastated by years of civil war, and received the 2002 Shelley A. Marshall Award for The Enrichment of The Human Spirit.<sup>62</sup> Wiley & Sons consistently demonstrates sensitivity to local cultures. In China, the Chinese language *For Dummies* titles are produced locally in partnership with China Machine Press, in deference to local business customs.<sup>63</sup>

### Stockholder Satisfaction

One investment director recently commented that "excessive CEO pay is a symptom of a board that lacks accountability to shareholders."<sup>64</sup> So, how does Wiley shape up? Although CEO base salaries don't include sizeable perks, such as stock options, [Exhibit 13](#) reveals that, from 2001-2004 Wiley's CEO was paid more than any other publishing CEO, except McGraw-Hill's. In 2004, Wiley increased the CEO salary more than any other firm, except Houghton Mifflin. More telling is the relationship between CEO salaries, revenues, and net incomes. In 2004, Wiley's CEO salary increased 13% more than revenue, second highest to Houghton Mifflin, and it consumed 2.2% of net income, second highest to Thomas Nelson. In spite of its CEO's

hefty compensation, Wiley & Sons' statements reveal a sense of responsibility to stockholders, particularly with regard to "a fair return on their investments."<sup>65</sup> However, non-family stockholder rights are limited (see Wiley-McGraw Contrasts).

Do investors express confidence in Wiley? In a recent article in *Barron's* magazine, one investor described Wiley as "a stock for all seasons, a Company that delivers whether the economy is headed up or down."<sup>66</sup>

#### Communication & Public Persona

Wiley's encourages open communication with the public. The CEO is counseled to "establish and maintain effective communications with the Company's stakeholder groups."<sup>67</sup> The firm's public persona has been enhanced by numerous awards. In 1998, a poll of CEOs by the Financial Times named Wiley one of the "World's Most Respected Companies."<sup>68</sup>

#### Vendor Relations

Wiley's relationships with vendors are very positive. Company policy requires that "Each employee, officer and director should endeavor to deal fairly with the Company's suppliers."<sup>69</sup> IBM,<sup>70</sup> production-systems supplier, BEA Systems,<sup>71</sup> and Wordco Indexing Service,<sup>72</sup> all use Wiley as a reference on their websites. Even in stressful situations, Wiley exercises good relationship management, stating, "we want to maintain a good relationship."<sup>73</sup>

## Strategic Positioning

The second qualitative analysis focuses on strategic positioning. This analysis of Wiley & Sons considers five key factors including vision and mission, competitive advantage, responsiveness to the general environment, innovation, and expansion plans and progress.

### VISION & MISSION

Wiley's vision and mission statements are not only readily available, they are virtually unavoidable. They are prominently displayed on all company literature, and on the back cover of most Wiley publications.<sup>74</sup>

The company's vision statement reads: "Wiley is committed to providing more access to more content to more customers around the world than it ever has in its nearly 200-year history . . . in collaboration with partners who respect the intellectual property of our authors and our Company."<sup>75</sup> The statement demonstrates the firm's connection to reality by including a reference to the daunting problem of intellectual property rights.

The firm's mission statement reads: "Wiley provides must-have content and services to professionals, scientists, educators, students, lifelong learners, and consumers worldwide. Wiley is dedicated to serving our customers' needs, while generating attractive intellectual and financial rewards for all of our stakeholders — authors, colleagues, partners, and stockholders."<sup>76</sup>

Following through on its vision, mission, and strategy statements, Wiley & Sons pursues a differentiated business-level strategy, supported by a functional structure. This is a good strategy-structure match. Wiley's narrowly focused, differentiation

strategy centers on expanding definitions of content, seeking to develop more unique, digitally-oriented content, and aggressive copyright management and protection. Its marketing and distribution approach seeks to deepen and expand distribution channels, adding innovative distribution methods. Wiley selects segments on the basis of sales potential.

### COMPETITIVE ADVANTAGE

In assessing Wiley's strategic positioning, the next factor evaluated is competitive advantage. A number of resources and capabilities that contribute to Wiley's core competencies will be reviewed.

#### Brand Recognition & Content Quality

Wiley's brand recognition is extremely strong, with "industry-leading brands" like Frommer's, Dummies, CliffsNotes, Pillsbury, and Betty Crocker.<sup>77</sup> The Dummies series has been called "one of the great brands in the history of publishing."<sup>78</sup>

Content quality is a resource that Wiley leverages effectively for competitive advantage. The high quality of Wiley's Professional STM content has garnered worldwide attention. The *Chemical Abstracts Service*® cited an article from one of Wiley's journals as "the most requested article in 2004 from all of their products and services."<sup>79</sup>

#### Customer Service

Customer service is a capability that Wiley has turned into a core competency. Wiley credits its staff, who are "highly trained and thoroughly familiar with their territories," and its "global information network," for the company's status "among the

best worldwide in order processing and fulfillment.”<sup>80</sup> Wiley realizes it needs to “stay sharp” by having “enough flexibility in [its] business model . . . to meet the different needs of [its] customers,” because it “competes in different markets with a lot of rivals, many of which are larger than itself.”<sup>81</sup>

### Segment Selection

Selecting the most productive segments is another capability that Wiley has elevated to a core competency. Of the eight major industry segments, Wiley has chosen to focus on three of the four most profitable (see [Exhibit 11](#)), namely Professional (in its STM division), Trade (in its PT division), and Higher Ed (in its Higher Ed division). As [Exhibit 14](#) shows, Wiley’s Professional STM division leads. The firm wisely avoids the consumer trade segment, focusing only on professional trade.

### Synergies

Leveraging organizational resources to create synergies is also a unique capability that has become a core competency for Wiley. Wiley notes that it is “exploiting the connections among . . . businesses to drive growth and gain market share.”<sup>82</sup> All over the world, departments work together to capitalize on marketing opportunities, creating competitive advantage. By delivering appropriate content through its “formidable collection of highly regarded brands,” the firm exploits the natural synergies that exist between its content-development and marketing competencies.

### Growth Strategies

By understanding and capitalizing on its core competencies, Wiley selects growth strategies that complement its organizational strengths. Over the last forty years, acquisitions have been at the core of Wiley’s growth. One Wiley official summed up the

firm's acquisition policy, stating that "paying the right price, getting a good strategic fit, making the right decisions, and integrating well is a core competency of the company."<sup>83</sup>

Wiley has also become quite adept at growth through partnerships and alliances, both vertical and horizontal. The company says that it "drives growth through alliances with a broad range of corporations and organizations."<sup>84</sup>

### RESPONSIVENESS TO GENERAL ENVIRONMENT

Responsiveness to the general environment is a critical factor in a firm's strategic positioning. John Wiley & Sons asserts is that it has the "ability to adapt to the changing environment."<sup>85</sup> To assess its actual performance on this factor, Wiley's responses to educational trends, globalization, and copyright infringement will be reviewed.

A number of educational trends are having a profound effect on the publishing industry. How has Wiley & Sons dealt with the rise of for-profit universities and concerns about textbook price and value? Although "for-profit universities are the fastest growing segment of higher education" today, in 2006, Wiley anticipated this change and began preparing to take advantage of it.<sup>86</sup> Displaying adaptability and creative thinking, the firm created its "Business Solutions Group (BSG) to address the needs of this sector," in 2003.<sup>87</sup> Since the for-profits depended heavily on web-based courses, Wiley developed enhanced digital texts and support materials, including "a suite of new products for distance learning."<sup>88</sup> This proactive approach has paid off, since it accelerated Wiley's content-digitization. Concerns about textbook prices and value are being aggravated by the availability of used books. In response, Wiley created "innovative new products and services," including a new series of texts, which are "pared-down, economical paperback books designed to be used in combination with online and customized

components.”<sup>89</sup> This approach, according to Wiley, “offers opportunities for more customization and new pricing and business models.”<sup>90</sup>

Wiley saw globalization coming and acted to maximize its opportunities. Wiley anticipated India’s potential and established “a presence” there in 1965.<sup>91</sup> Wiley’s CEO states, “We’ve been in the country a long time, and we have built significant relationships there. We showed a real interest in the culture from the start, and we gained respect when we were small and struggling. In the long run, it has really paid off.”<sup>92</sup> “Wiley has been active in China since 1979, establishing a sales office in Beijing in 2000, and a sales presence in Shanghai in 2003.”<sup>93</sup> Now, China is “the largest Asian market for Wiley STM journals and is emerging as a vital source of STM content for a global audience.”<sup>94</sup>

Copyright have become an increasing problem for publishers, but Wiley was quick to recognize and respond to the threat, as [Exhibit 120](#) illustrates. Although some downplayed the threat, Wiley realized, early on, that the publicized infractions were “representative of a much larger pattern of abuse.”<sup>95</sup>

## INNOVATION

In the publishing industry, innovation is essential to strategic positioning. Wiley asserts that it is “leveraging [its] investments in technology to create value.”<sup>96</sup> Wiley’s investments in R&D have been substantial. Wiley’s “computer equipment and capitalized software” costs, representative of R&D investment bear this out.<sup>97</sup> As [Exhibit 16](#) shows, the firm invested increasing amounts over time. R&D investments, relative to Net Income, have always been sizeable, increasing by 74%, from a low of 99% (in

2000) to a high of 173% (in 2005). Compare that to “the top ten biggest U.S corporations,” whose R&D spending increased by only 42% since 2000.<sup>98</sup>

Due to innovation, Wiley says, “Over the past five years [2000-2005], we have introduced more new business models than we had in the previous 193 years.”<sup>99</sup> Many market-enhancing innovations have grown out of Wiley’s technological expertise. Wiley has pioneered cutting-edge content digitization, which enables online journals, online databases, like *InterScience*, Higher Ed’s *eGradePlus*, customized publishing, print-on-demand products (since 2003),<sup>100</sup> online distance-learning content, e-books (since 2001),<sup>101</sup> and “Amazon.com’s search-inside-the-book marketing.”<sup>102</sup> Wiley develops all content in digital format; it says that “digitization is a way of extending the life of . . . content,” and it intends “to embark on even more digitization,” envisioning “a future where no content need ever go out of print.”<sup>103</sup>

Organizationally, Wiley’s innovative systems “increase productivity throughout the Company.”<sup>104</sup> “People collaborate better, are better equipped to meet deadlines and make faster decisions,” so, in the end, the system is “greatly reducing administrative burden and costs.”<sup>105</sup> Now “the company is better positioned to handle future growth.”<sup>106</sup>

### EXPANSION PLANS AND PROGRESS

The final assessment, with regard to strategic positioning, evaluates Wiley’s ability to formulate plans and accomplish them through realistic strategies. Wiley & Sons is enthusiastic and confident about its future. Expressing that enthusiasm, the firm proclaims, “We are building a future that is not bound by organizational and geographic boundaries or print on paper. We are in the process of providing even more access to more content by more people than ever before.”<sup>107</sup>

Wiley conveys its interest in expansion, and its global mentality, saying, “our goal is to continue to increase [our] worldwide market penetration.”<sup>108</sup> More specifically, it explains, “In recent years, the company has focused its efforts on delivering Wiley's deep reservoir of "must-have" content to global communities of interest.”<sup>109</sup>

Wiley's expansion plans are well thought out and specific. Wiley's successful selection and integration of acquisitions is evidence that the company doesn't suffer from myopic planning. Demonstrating the firm's good judgment and flexibility, Wiley's CEO explained, “Next year's strategy will be, in some ways, dependent on opportunities. If I say let's consolidate this year, you can bet a long-term target will become available - that's just how it is. We certainly have plenty of new business to consolidate, so we'll keep busy, even if the big one doesn't come along.”<sup>110</sup>

Strategic, rather than tactical, approaches are emphasized when Wiley tells stockholders, “During the next year [2005], we will continue to focus on three strategic goals: building long-term customer relationships; increasing profitability, cash flow, and return on investment; and enhancing Wiley's position as *the place to be* for our authors, colleagues, partners, and stockholders.”<sup>111</sup> Wiley's credibility is unquestioned.

## **QUANTITATIVE ANALYSIS**

The Performance Analysis continues with a quantitative analysis of the company's financial management. Wiley & Sons' management of profit, equity, and share value, debt, cash, and assets will be evaluated using trend analysis, benchmark comparisons, and industry comparisons.

Trend analyses were developed by extracting eight years of financial data from Wiley & Sons financial statements, covering 1998-2005 (see Exhibits 17 & 18), then the firm's information was entered into the FGA software (see Exhibits 19 & 20). Benchmark comparisons were developed by extracting McGraw-Hill's 2004 and 2005 financial data from its financial statements (see Exhibits 21-23), and entering it into the FGA software (see Exhibits 24 & 25). Thereafter, FGA printouts (see Exhibits 26 & 27) were compared in each category. Comparisons to industry averages, although not comprehensive, were developed by extracting financial data from the 2005 financial statements of three additional publishing firms, including Pearson, Scholastic, and Thomas Nelson (see Exhibits 28-36). Industry averages in each category were analyzed (see Exhibits 37). Industry averages as well as individual firm statistics were arranged in graphs for each category (see Exhibit 38).

Trend analysis, benchmark analysis, and comparisons to industry averages will be considered for all factors cited. For ease of reference, each standard FGA factor is assigned a three-digit number, the first digit of which relates it to one of the four pressure points; supplementary factors are assigned similarly related numbers, followed by a letter.

## **1. Profit, Equity, and Share Value Management**

### PROFIT MANAGEMENT

The first focus of this "performance pressure point" is profit management.<sup>112</sup> Wiley did turn a profit, with \$83.8 million in Net Income for 2005, but were they profitable enough, given the level of revenue earned? To analyze the firm's earnings productivity, factors indicative of Wiley's profit management will be considered at three levels, after

Cost of Goods Sold is deducted (Gross Profit level), after expenses, but before taxes are deducted (Operating Profit level), and after taxes are deducted (Net Profit level). Gross Profit to Revenue (1.02), Operating Profit to Revenue (1a), and Net Income to Revenue (1.01), are the indicative factors.

Gross Profit to Revenue shows actual profit produced, before expenses and taxes, for each dollar of revenue. It shows if the company is controlling Cost of Goods Sold. Since 2003, Wiley's upward trend has been very good. In 2005, \$.66 of every dollar was retained as profit (see [Exhibit 38](#)), which is more than McGraw's \$.61, and more than the industry average of \$.461. Operating Profit to Revenue shows actual profit produced after expenses, but before taxes, for each dollar of revenue. In 2005, \$.145 of every dollar was retained as profit (see [Exhibit 39](#)), which is \$.132 less than McGraw's \$.277, but greater than the industry average of \$.114.

Net Income to Revenue (see [Exhibits 40 & 41](#)) shows actual profit produced, after taxes, for each dollar of revenue. It shows if the company is controlling taxes. Wiley's downward trend since 2003 has been poor. In 2005, only \$.086 of every dollar was retained as profit, which is a 10.4% decrease from 2004, \$.055 below McGraw's, and 14.6% over the industry average. Wiley explains that 2005's tax increase is the result of a "repatriation of approximately \$94 million of dividends from European subsidiaries" in order to take advantage of a "favorable one-time tax rate on dividends from foreign subsidiaries."<sup>113</sup> They add that this unusual tax hit will "be fully offset by a tax benefit that will be recognized in fiscal year 2006."<sup>114</sup>

In summary, Wiley did very well at controlling its Cost of Goods Sold and operating expenses, but less so with regard to taxes, for the reason stated. Wiley has

been pretty consistent in maintaining its margins, as [Exhibit 42](#) shows, despite 2005's slight decline in Net Profit Margin.

### EQUITY MANAGEMENT

The second focus of this section is equity management. This assessment evaluates Wiley's management of investor-entrusted capital. The factors relevant to this consideration include Return on Equity or Stockholder Investment (1.03), Paid-In-Capital to Total Capital (1.04), Earned Capital to Total Capital (1.05), and Percentage of Change in Total Equity (1.06).

Return on Equity, or ROI, is the "rate of earnings for each dollar of owner investment," Net Income to Total Equity.<sup>115</sup> ROI shows how well the stockholders' investment is performing, with "a measure other than market price."<sup>116</sup> Poor ROI may motivate investors take their money to a higher-performing firm. Although Wiley's 2005 ROI dipped by 1.4% (see [Exhibits 43 & 44](#)), it had been steadily increasing since 2002. Wiley's ROI was increasingly less than McGraw's, but Wiley's tax-related decrease in Net Income can't be ignored. Wiley's ROI was 80% above the industry average.

Paid-In-Capital to Total Capital explains the derivation of a firm's financial worth, the percentage of equity resulting from monetary investments, versus equity from earned profits.<sup>117</sup> Consistently low or downward trends are best.<sup>118</sup> Wiley's percentage of earned capital had been steadily declining since 1999 (see [Exhibits 45 & 46](#)), with a slight increase in 2005, indicating that, generally, an increasing percentage of capital was being earned, versus paid in. Wiley's ratio was 21.7% higher than McGraw's, indicating that Wiley had a higher percentage of Paid-In Capital than McGraw and the industry average.

Earned Capital to Total Capital also explains the derivation of a firm's financial worth, but it isolates the percentage of equity resulting from business profits, versus equity from monetary investments. It is the opposite of the previous ratio, so consistently high or upward trends are best, because a higher percentage of earned capital is preferred. Wiley's percentage of paid-in capital had been steadily increasing since 1999 (see Exhibits 46 & 47), with a slight decrease in 2005, indicating that, generally, an increasing percentage of capital was being earned, versus paid in. Wiley's ratio was 21.7% lower than McGraw's and than the industry average.

Percentage of Change in Total Equity indicates whether the firm's total pool of capital is growing or shrinking. Obviously, growth is desirable, since it comes from profit being earned or stock being issued; Total Equity decreases if the firm suffers losses, pays liquidating dividends, or purchases large amounts of treasury stock.<sup>119</sup> Wiley's Total Equity had been steadily increasing (see Exhibits 18 & 48), but since 2001, the percentages of change leveled off in the 20% range. However, in 2005 Wiley suddenly had a 4.5% decrease in Total Equity. McGraw, by comparison, had a 4.3% increase, and the industry had a 34.6% increase, making Wiley look even worse. No doubt, the combined effects of Wiley's 2005 tax hit (see Profit Management) and its stock repurchase plan were responsible for this anomaly.

### SHARE VALUE MANAGEMENT

The third focus of this section is Share Value Management. Share value is a reflection of market confidence, which must be earned through continued high performance. However, a firm must also take appropriate steps to guard and enhance its share value, so as to avoid a discrepancy between the firm's actual value and its share value. This is more than impression management, because a valuable firm with

undervalued stock would be a real bargain, and a tempting target for takeover bids. This evaluation includes a review of Wiley's stock repurchase plan, a discussion of their small market capitalization, and an analysis of share value indicators.

### Stock Repurchase Plan

Although Wiley is not actively selling stock, it has had an ongoing stock repurchase plan under way since 2002.<sup>120</sup> Such repurchase, or buyback, plans have become quite popular; McGraw-Hill also has one.<sup>121</sup> Wiley and other companies say they pursue buybacks to reduce the number of claims on the company, thereby increasing each remaining shareholder's stake. Some feel "the logic of buybacks is sound," however, many financial analysts think their real purpose is to offset the use of stock options in executive compensation packages.<sup>122</sup> It's interesting to note that Wiley's plan, detailed in [Exhibit 49](#), involves repurchasing roughly the same number of stock that would be required to cover its outstanding options, as shown in [Exhibit 50](#). Depending on an investor's perspective, this may increase or diminish share value.

### Small-Cap Status

With only \$1.82 billion in market capitalization, Wiley & Sons is considered a small-cap firm. Other major publishers, including McGraw-Hill, Pearson, and Thomson are much larger (see [Exhibit 51](#)). The question is, is this positive or negative for share values? Surprisingly, statistics tend to favor the small-caps. In a Morgan Stanley study that analyzed eighty years of data, "small caps outperformed by an average of 2.4 points annually over every 10-year period."<sup>123</sup> Analysts say that "growth seekers are choosing the smaller company."<sup>124</sup> However, some analysts assert that larger firms, with

more “cash to fuel acquisitions, capital spending, dividends, and share buybacks” could be in a better position to “protect their stocks.”<sup>125</sup>

### Share Value Indicators

Given the subjective nature of shareholder opinions the only reliable way to measure share value management is by analyzing factors that are traditional indicators of share value. Wiley’s Earnings per Share (1.07), Diluted EPS (1.08), Market Value of Stock (1.09), Price Earnings Ratio (1.10), and Book Value per Share (1b) will be considered.

Earnings per Share, or Basic EPS, measures the earnings per share of outstanding common stock, ignoring outstanding options.<sup>126</sup> Increasing trends and larger comparative values are preferred. Wiley’s EPS had shown steady upward trends (see [Exhibit 52 & 53](#)), until a 4% downturn in 2005. The tax factor considered in the Profit Management section was a factor here. McGraw’s Basic EPS, in contrast, increased by 13%. Wiley’s EPS was 20% lower than the industry average.

Diluted Earnings per Share, or Diluted EPS, measures the earnings per share of outstanding common stock, assuming the exercise of outstanding options.<sup>127</sup> In Wiley’s case, there was a 2.2% difference between the two, which is greater than McGraw’s 1.8% difference, but equal to the industry average. This is a positive indicator; a small span between Basic and Diluted EPS indicates that outstanding options pose little risk to future earnings. Comparisons to McGraw and the industry average remained about the same as Basic EPS (see [Exhibit 54](#)).

Market Value of Stock is “an indicator of “what value open market places on the company and its decisions.”<sup>128</sup> Wiley’s stock price has been on an upward trend since

2000, with a 2005 fiscal-year-end price of \$36.16 (see [Exhibits 55 & 56](#)). While Wiley's price was \$15.47 lower than McGraw's, Wiley increased by 18% as McGraw decreased by 44%. Wiley was 15.7% over the industry average.

The Price Earnings Ratio describes the market price of a stock as a multiple of the Basic EPS. It reveals how costly a stock is relative to its ability to produce earnings. The higher the number is, the more costly the stock is. If the PE Ratio increases over time the stock is getting more expensive. A negative number means "the company is losing money," but high positive numbers means the stock is considered to have a strong future; numbers over thirty "may be overpriced."<sup>129</sup> Wiley's PE Ratio had been fairly consistent since 2000 (see [Exhibits 57 & 58](#)); however, the multiple is getting larger so the stock is getting more expensive, but not extremely so. The high positive number means the stock is considered to have a strong future. The numbers have not been in excess of thirty since they leveled out in 2000, so it's not overpriced. Wiley's PE Ratio was 14% higher than McGraw's, and 44% higher than the industry average.

Book Value per Share "measures the amount that, in theory, would be paid for each share of CS if company were liquidated."<sup>130</sup> It shows how risky a stock is. Comparing Book Value/Share versus Market Value/Share reveals whether the stock is over or under-priced. If market value/share is greater than book value/share, the market has a positive outlook on the firm's long-term potential.<sup>131</sup> Wiley's Book Value per Share had been increasing steadily until a slight dip in 2005 (see [Exhibit 59](#)). Wiley's 2005 Book Value per Share was 40% lower than McGraw's, and 60% lower than the industry average. Wiley's Book Value per Share was 6.58% of its Market Value per Share, compared to McGraw's 14.6% and the industry average of 32.5%.

### Dividend Management

Dividend management is closely associated with share value management, since dividend payments attract investors, thereby boosting share value. Wiley's policy is to "steadily increase dividends."<sup>132</sup> McGraw has the same policy.<sup>133</sup> The important questions are: how high or low are Wiley's dividends, and how fast are they increasing? These can be answered by analyzing Wiley's dividend-management indicators, including Dividends per Common Share (1c), Dividend Payout Ratio (1.11), and Dividend Yield Ratio (1.12).

Wiley's Dividends per Common Share (see [Exhibit 60](#)) have been steadily increasing for the last eight years. While Wiley's dividends were lower than McGraw's, with \$.30 compared to \$.66, Wiley posted a 15% increase versus McGraw's 10%. Wiley's dividends were slightly under the industry average of \$.335. Dividend levels can be very subjective; Scholastic doesn't pay them at all. Overall, Wiley's dividends are good for a firm of its size, but not so extravagant as to generate concern.

The Dividend Payout Ratio measures the "percentage of current profits returned to stockholders in the form of dividends,"<sup>134</sup> the "amount paid to stockholders for each dollar of earnings."<sup>135</sup> It's the ratio of Cash Dividends to EPS. What percentage should Wiley pay out? The maximum is 60%, Fortune 500 companies pay out about 55% on average, but there are exceptions to every rule, and a firm should retain some portion of its earnings to fund future growth.<sup>136</sup> Wiley's Dividend Payout Ratio was 21.7%, a new high, breaking a consistent, but fairly conservative, trend hovering around 19% (see [Exhibits 61 & 62](#)). This was almost 8% below McGraw, although Wiley increased 20% over last year, versus McGraw's 3% increase. Wiley was 10% over the industry average.

The Dividend Yield Ratio relates Dividends per Share to Market Price per Share, revealing the rate of return, in cash dividends, earned by an investment in the firm's common stock, obtained at market price. Wiley's Dividend Yield Ratio had been on an upward trend, with slow, measured increases since 2003 (see [Exhibit 63 & 64](#)); however, it dipped in 2005. Wiley was 57% lower than McGraw, but Wiley decreased by 2% over last year, versus McGraw's 86% increase. In general McGraw's dividends were increasingly higher, relative to its market price/share. Wiley is below the industry average.

#### Financial Leverage Analysis

Financial leverage analysis provides a unique perspective on share value management, focusing on the profitability of shareholders' investment. Although not a required component of the FGA software, it is cited in the Performance Scorecard, and it provides valuable insight into the firm's performance.<sup>137</sup> The two factors considered are Rate of Return on Common Stockholder Equity (1d) and Financial Leverage Index (1e).

Rate of Return on Common Stockholder Equity measures the profitability of the shareholders' investments in the firm by relating Net Income to average Stockholders' Equity.<sup>138</sup> Wiley's Rate of Return, has been on a general downward trend, landing at 21.1% in 2005 (see [Exhibit 65](#)). That's below McGraw's 27.1%, but 5.8% higher than the industry average.

The Financial Leverage Index relates Return on Equity Investment (ROE) to Return on Invested Assets (ROI), defining whether the firm is more profitable with regard to invested equity or production assets.<sup>139</sup> If the ratio is greater than one,

financial leverage is being used successfully, equal to one is neutral, and less than one is unfavorable.<sup>140</sup> Wiley's Index, although well over one throughout, had been slowly declining since 2000, but 2005 brought a slight increase over 2004 (see [Exhibit 66](#)). Wiley's Index was higher than McGraw's, and 32% higher than the industry average.

## **2. Debt Management**

Debt management is the second "performance pressure point" assessed. The basic question is: Does Wiley & Sons manage its debt well by maximizing financial leverage? Leverage can boost returns when used properly.<sup>141</sup> Four aspects of debt management are considered, including Debt Strategy, Debt Coverage, Payment of Trade Debts, and Creditor Claims on Assets.

### Debt Strategy

Debt strategy is the first aspect of debt management considered because it reveals the overall approach being followed. To assess Wiley's debt strategy, its debt structure and asset distribution will be considered. To evaluate Wiley's debt structure Current Debt to Total Debt (2.13) and Non-Current Debt to Total Debt (2.14) will be analyzed. Wiley's asset distribution will be analyzed using Current Assets to Total Assets (2.15) and Non-Current Assets to Total Assets (2.16).

### Debt Structure

Healthy debt structure usually requires that increases in debt be non-current rather than current. While there can be exceptions, it is "not considered financially healthy" to increase current debt while decreasing non-current; this is called the "credit card approach," and it "can lead to insolvency."<sup>142</sup> Wiley's Current Debt to Total Debt ratio has been fairly consistent since 2002, hovering around 52%, with a slight increase

to 53.7% in 2005 (see [Exhibit 67](#)). No doubt, the unusual increase in tax liabilities was a factor (see Profit Management). Wiley's ratio was 14.1% lower than McGraw's, but 1.4% above the industry average. Wiley's Non-Current Debt to Total Debt ratio has been fairly consistent since 2002, hovering around 48%, with a slight decrease to 46.3% in 2005 (see [Exhibit 68](#)). As with Current to Total Debt, the unusual increase in tax liabilities was a factor. Wiley's ratio was 14.1% higher than McGraw's, and 1.4% below the industry average. In summary, Wiley's current debt increased from 2004 as its non-current debt decreased (see [Exhibit 69](#)). Although Wiley's 2004-2005 debt structure is precarious, further information is required to make a thorough evaluation of its debt strategy.

#### Asset Distribution

Healthy asset distribution usually requires that increases in assets be non-current rather than current; current assets pay bills, but non-current assets produce revenue.<sup>143</sup> After a sharp decline in 2000, Wiley's Current Assets to Total Assets ratio had been fairly consistent, hovering around 31%; however, in 2005 it rose slightly to 32.8% (see [Exhibit 70](#)). Wiley's ratio was 7.7% lower than McGraw's and 16.5% below the industry average. Since 2000, Wiley's Non-Current Assets to Total Assets ratio had been fairly consistent, hovering around 69%; however in 2005 it fell slightly to 67.2% (see [Exhibits 71 & 72](#)). Wiley's ratio was 7.7% higher than McGraw's and 16.5% above the industry average. In summary, Wiley's current assets increased only slightly from 2004 as its non-current debt decreased slightly more. A thorough analysis of Wiley's debt strategy follows.

### Debt Strategy Analysis

The primary concern with debt strategy analysis is the relationship between a firm's debt structure and its asset distribution. Sound debt strategy reflects an appropriate balance between long-term production needs and long-term financial leverage. Although companies need to upgrade and/or expand their assets, short-term debt increases, to finance long-term asset increases, is short-sighted and can move a firm toward insolvency. [Exhibit 73](#) details sound debt strategy and "dubious financing strategy," in terms of the ratios just assessed.<sup>144</sup> Analysis of Wiley's debt strategy reveals that although its Current Debt to Total Debt ratio is precarious, due to a slight increase, its Non-Current Assets to Total Assets ratio isn't increasing as its Non-Current Debt to Total Debt ratio is decreasing (see [Exhibit 74](#)). While Wiley's debt strategy doesn't appear optimal, it doesn't pose a serious threat to the firm's future survival; a substantial percentage of the Current Debt is actually Deferred Subscription Revenue, a common publishing industry phenomenon (see [Exhibit 75](#)). By comparison, McGraw's debt strategy is optimal.

### Debt Coverage

This is an important aspect of debt management, because it is possible to be insolvent despite being profitable, if cash flow isn't good enough to pay bills. Wiley's debt coverage will be assessed by analyzing two factors, namely, Times Interest Earned (2.17) and Current Cash Debt-Coverage Ratio (2.18). The Times Interest Earned ratio evaluates a firm's coverage of its financing costs, its interest expense on borrowed capital.<sup>145</sup> If Times Interest Earned is increasing, that's good, because the larger the number, the more capable the firm is of paying its interest expenses on

time.<sup>146</sup> Since 2002, Wiley's Times Interest Earned had shown a consistent upward trend, peaking at 25.251 (see [Exhibit 76 & 77](#)), then it decreased to 19.782 in 2005. Wiley's ratio was less than one-tenth of McGraw's 262, and it fell well below the industry average of 79. The Current Cash Debt-Coverage Ratio analyzes a firm's ability to pay off its current debt from its operating-cash flows.<sup>147</sup> Here, bigger is better, and increasing trends imply an increased ability to pay current debt. Wiley's Current Cash Debt-Coverage Ratio has been increasing since 2002 (see [Exhibits 78 & 79](#)), topping off at 71.3% in 2005. Wiley's ratio was 1.2% higher than McGraw's and 25.5% over the industry average.

#### Trade Debt Management

Analysis of Wiley's debt management becomes more specific with a profile of Wiley's trade-debt payments. The concerns here are: How quickly is Wiley paying its current trade debts, its Accounts Payable? Has this changed? Cost-reducing trade discounts can be lost if Wiley takes too much time to pay.<sup>148</sup> The formula for Average Payment Period (2.19) is 365 divided by Accounts Payable Turnover, which is Purchases divided by average Accounts Payable.<sup>149</sup> Wiley's Average Payment Period has been decreasing since 2002; in 2005 it was 80 days (see [Exhibit 80](#)). Wiley's Average Payment Period was 27 days more than McGraw's and 4 days less than the industry average.

#### Creditor Claims on Assets

The final assessment of Wiley's debt management examines how well the firm protects its interests, as opposed to those of creditors, through its debt-management strategies. Although some debt creates financial leverage, too much is not good. Since

reliance on creditors for financing increases their influence, this evaluation focuses on indicators of credit dependence, including Creditor Leverage (2.20), Debt to Equity Ratio (2a), Long-Term Debt to Equity Capital (2b), and Debt Coverage Ratio (2c).

By comparing total debt to total assets, the Creditor Leverage ratio provides an overall view of creditor influence. It clarifies what portion of assets creditors can claim. The larger the percentage, the more creditor-dependent the firm is; if the ratio is increasing, the firm is losing ground, and may even be having profitability problems.<sup>150</sup> Since 2002, Wiley's Creditor Leverage ratio had been decreasing (see [Exhibits 81 & 82](#)), but in 2005 it increased to 61.6%. Wiley's ratio was 10.3% higher than McGraw's and 12.9% higher than the industry average.

The Debt to Equity Ratio is similar to Creditor Leverage, except creditor dependence is measured relative to stockholder ownership, comparing total debt to total stockholders' equity. Again, larger percentages and faster increase suggest more vulnerability to creditor control. Wiley's Debt to Equity ratio had been decreasing since 2002, but it increased to 1.604 in 2005 (see [Exhibit 83](#)) Wiley's ratio was 52% higher than McGraw's and 65% higher than the industry average.

Long-Term Debt to Equity Capital isolates long-term debt. It reveals the firm's specific dependence on long-term creditors. Wiley's Long-Term Debt to Equity Capital ratio had been decreasing since 2002, but it increased to 74.3% in 2005 (see [Exhibit 84](#)). Wiley's ratio was 40.3% higher than McGraw's and 25.7% higher than the industry average.

The Debt Coverage Ratio, or Cash Debt Coverage Ratio, measures the firm's independence from creditors, revealing its ability to repay total debt from net operating

cash.<sup>151</sup> Wiley's Debt Coverage Ratio has been increasing since 2002, topping off at 40% in 2005 (see [Exhibit 85](#)). Wiley's ratio was 11% below McGraw's, but 15% higher than the industry average.

### 3. Cash Management

Cash management is the third "performance pressure point" assessed. The basic question here: Is Wiley's cash flow satisfactory? With Wiley's active stock repurchase program being "paid for out of existing cash balances," this assessment becomes even more relevant.<sup>152</sup> Wiley's cash management will be evaluated from three perspectives, including Short-Term Debt Payment Capacity, Self-Liquidating Ability, and Asset Liquidity.

#### Short-Term Debt Payment Capacity

As assessment of short-term debt payment capacity shows whether Wiley's cash management creates sufficient cash flow to meet its short-term obligations. Short-term debt payment capacity is indicated by Short-Term Debt Service (3.21), Quick Ratio or Acid-Test Ratio (3.22), Working Capital (3a), and Working Capital to Total Debt (3b).

The Current Ratio measures a firm's ability to pay its bills on time. It relates current assets (cash & near cash items) to current debt, revealing short-term liquidity.<sup>153</sup> The Current Ratio must be one or greater to pay bills as they are falling due,<sup>154</sup> but two or higher is preferred.<sup>155</sup> Wiley's Current Ratio has been less than one since 2000, except for 2004 (see [Exhibits 86 & 87](#)), but in 2005 it fell back to .993. Wiley's ratio was 14.8% lower than McGraw's and 52% lower than the industry average.

The Quick Ratio provides a more exacting measure of short-term liquidity. Instead of relating all current assets to current debt, it only includes cash, marketable

securities, and accounts receivable;<sup>156</sup> these are more immediately liquidated. A value of one or more is considered sufficient, since each dollar of short-term debt would be matched by a dollar of immediately liquid assets.<sup>157</sup> Wiley's Quick Ratio, like its Current Ratio has been less than one since 2000 (see [Exhibit 88](#)), landing at .749 in 2005 . Wiley's ratio was 26% lower than McGraw's and 42% lower than the industry average.

Working Capital provides another measure of short-term debt payment capacity. It subtracts current debt from current assets, revealing the amount that would be left to run the business. Wiley's Working Capital had been negative since 2000, except for 2004, but it returned to the negative in 2005 (see [Exhibit 89](#)). Wiley's Working Capital was \$368 million below McGraw's and \$3 million below the positive industry average.

Working Capital To Total Debt is a double-check on the Current Ratio, since changes in its trend demonstrate if the Current Ratio has been artificially inflated, by expanding current assets financed by long-term debt. If no manipulation has occurred, the Working Capital and Working Capital to Total Debt trends should match. Wiley's Working Capital to Total Debt trend, shown in [Exhibit 90](#), follows the Working Capital trend illustrated in [Exhibit 89](#) precisely. This testifies to the accuracy of Wiley's Current Ratio profile.

#### Self-Liquidating Ability

Cash Flows from Operating to Revenue (3.23) measures self-liquidating ability, or how much cash flow the firm's cash management approach generates from normal business activities (operations) for each dollar of revenue.<sup>158</sup> The higher the ratio, the less likely a firm is "to make desperate decisions such as selling assets to fulfill its cash requirements."<sup>159</sup> Wiley's Cash Flows from Operating to Revenue has been increasing

since 2002 (see [Exhibits 91 & 92](#)), landing at \$.25 in 2005. Wiley's figure was \$.01 less than McGraw's, but \$.098 over the industry average.

### Asset Liquidity

The final perspective used to assess Wiley's cash management is asset liquidity. Asset liquidity allows the firm to maintain strategic flexibility, allowing it to respond to changing environmental factors and new opportunities. Asset liquidity can be measured using Financial Flexibility (3.24) and Free Cash Flow (3c).

The Financial Flexibility ratio, or Cash and Equivalents to Total Assets ratio, relates liquid-type assets to total assets, showing what percentage of the firm's assets are available in the most liquid form. Larger percentages mean greater flexibility, but balance is required. If the ratio is too high, the firm is overloaded with less-productive liquid assets, versus productive fixed assets, and the firm could become a target for hostile takeover.<sup>160</sup> Wiley's Cash and Equivalents to Total Assets ratio had been consistently low since 2000, fluctuating between 3.5% and 8% (see [Exhibits 93 & 94](#)). In 2005, it rose to 8.7%. Wiley's ratio was 3% less than McGraw's and .8% lower than the industry average.

Free Cash Flow is the measure of uncommitted, liquid cash flow available. It is cash flow from operating activities less capital expenditures and cash dividends. Wiley's Free Cash Flow has been increasing since 2004 (see [Exhibit 95](#)). Wiley's Free Cash Flow was 86% less than McGraw's, but above the industry average.

#### 4. Asset Management

The final financial “performance pressure point” assessed is asset management. The question is: Is Wiley utilizing its assets appropriately? To evaluate this, revenue-generating efficiency, profit-generating efficiency, receivable collection, inventory turnover, and employee profitability will be considered.

Revenue-generating efficiency can be assessed using Revenue to Total Assets (4.25). Revenue to Total Assets shows revenue earned for each dollar of assets.<sup>161</sup> A higher number means more efficient revenue generation. Wiley’s Revenue to Total Assets ratio has been increasing since 2002 (see [Exhibits 96 & 97](#)). Wiley’s ratio was .4% higher than McGraw’s, but .4% lower than the industry. Profit-generating efficiency can be assessed using Return on Assets, or Net Income to Total Assets ratio (4.26), which shows the amount of profit generated by each dollar of assets. It is more of a “bottom line” evaluation, since it uses after-tax income rather than revenue. Wiley’s Return on Assets ratio has been decreasing since 2003 (see [Exhibits 98 & 99](#)). Wiley’s ratio was 39% lower than McGraw’s, but higher than the industry average.

Management of receivable collection can be assessed by using the Average Collection Period (4.27). This shows how long it takes to receive money from customers. Wiley’s Average Collection Period has been increasing since 2002 (see [Exhibit 100](#)). In 2005 it was 51.6 days. This was 16 days less than McGraw and 29 days shorter than the industry average.

Inventory turnover can be assessed using the Average Age of Inventory (4.28), which shows how much time passes before inventory is sold. Too much means money is locked in inventory, unnecessary carrying costs accrue, and deep discounts might be

required to move it; too little means sales opportunities can be missed. Wiley's inventory has been decreasing since 2003 (see [Exhibit 101](#)), but it was 41 days more than McGraw's and 2 days more than the industry average.

Employee profitability is dependent on labor productivity. [Exhibit 102](#) demonstrates that publishing-industry labor productivity is lower than other industries. However, Wiley's Net Income per Employee of \$24, 659 is quite good compared to other publishers, as well as to major firms in other industries (see [Exhibits 103 & 104](#)).

## ➤ **SUMMARY**

### **Comprehensive Review**

Having completed a thorough analysis of John Wiley & Sons, it is helpful to review the evidence considered. A general profile of Wiley provided a brief history of the firm. After summarizing the reasons for selecting Wiley and McGraw-Hill as target and benchmark, contrasts between the two were noted. An industry overview provided a contextual backdrop. The Performance Analysis evaluated Wiley's organizational citizenship, strategic positioning, and financial management.

### **Conclusions on Performance Scorecard Categories**

As prescribed in *The Performance Scorecard*, Wiley & Sons' performance analysis hinges on the six "performance pressure points," including profit, equity, and share value management, debt, cash, and asset management, organizational citizenship, and strategic positioning. All factors that contribute to each "pressure point" are graded very poor (1), poor (2), average (3), good (4), or very good (5), and entered into the FGA software, which generates a cumulative grade for each.

## Financial Management Evaluation

The financial, or quantitative, evaluation of Wiley & Sons includes the profit, equity, and share value management, as well as debt, cash, and asset management “pressure points.”<sup>162</sup> Each factor is graded, based on Wiley’s performance.

### PROFIT MANAGEMENT EVALUATION

Wiley’s profit-management indicators, Net Income to Revenue (1.01) and Gross Profit to Revenue (1.02), receive grades of good (4) and very good (5), respectively. The firm’s earnings productivity analysis reveals that Wiley is controlling Cost of Goods Sold well, with \$.66 of every dollar being retained as profit (see [Exhibit 38](#)), but expenses before taxes are not as well controlled, since Wiley’s Operating Profit Margin fell to \$.145 (see [Exhibit 39](#)). Taxes reduced the Net Profit level by 10.4% from 2004. However, Wiley’s temporary tax increase was a strategic decision that will save a great deal in taxes down the line.

### EQUITY MANAGEMENT EVALUATION

Wiley’s equity-management indicators reveal the company’s tendency toward strategic, versus tactical approaches. The Return on Equity/ROI (1.03), graded very good (5), shows that Wiley is creating value for its shareholders (see [Exhibits 43 & 44](#)), coming in 80% above the industry average. This bodes well for Wiley’s place in the market. The company’s Paid-In-Capital to Total Capital (1.04) and Earned to Total Capital (1.05), graded good (4), indicate that an increasing percentage of capital is being earned, versus paid in (see [Exhibits 45 & 46](#)). This demonstrates Wiley’s tendency to increase equity through earnings, rather than issuing stock. However, the Percentage of Change in Total Equity (1.06) grade of poor (2), though likely an anomaly

(see Equity Management and [Exhibit 48](#)), confirms Wiley's preference for long-term approaches; the company was willing to sacrifice short-term equity gains in favor of long-term tax advantages and reductions in outstanding shares.

### SHARE VALUE MANAGEMENT EVALUATION

Wiley's share-value-management indicators all reflect positively on management's performance. The Earnings per Share (1.07) and Diluted EPS (1.08) grades of good (4) are the results of steady upward trends (see [Exhibit 52 - 55](#)). The 1.5% difference between Wiley's Basic and Diluted EPS indicates that the firm is not allowing outstanding options to diminish its earnings potential too severely.

The company's Market Value of Stock (1.09) and Price Earnings Ratio (1.10) grades of good (4) and very good (5), respectively, both speak well of management's performance, since they reflect the increasing value Wiley's stock holds in the market. Although the 2005 PE Ratio increase of 23% (see [Exhibits 57 & 58](#)) exceeded the 18% increase in market value of the stock (see [Exhibits 55 & 56](#)), indicating that the stock is getting more expensive (15.7% over the industry average), the high positive number means the stock is considered to have a strong future, and its not being in excess of thirty shows it's not overpriced.

Wiley's Dividend Payout Ratio (1.11) and Dividend Yield Ratio (1.12), graded good (4), illustrate how the firm pursues strategic goals without alienating stockholders. Although Wiley's Dividends per Common Share have been steadily increasing for the last eight years (see [Exhibit 60](#)), satisfying shareholders, they are lower than McGraw's and the industry average. This allows Wiley to retain a greater portion of its earnings to fund future growth.<sup>163</sup> Wiley's Dividend Payout Ratio shows that Wiley is only returning

21.7% of Net Income to stockholders (see [Exhibits 61 & 62](#)); Fortune 500 companies pay out about 55% on average.<sup>164</sup> Likewise, Wiley's Dividend Yield Ratio reveals that the firm returns only .8% of Market Price per Share to stockholders (see [Exhibits 63 & 64](#)), which is less than McGraw and industry average.

### DEBT MANAGEMENT EVALUATION

Wiley's debt-management indicators generate evidence of a consistent management strategy. Wiley's Current Debt to Total Debt (2.13) and Non-Current Debt to Total Debt (2.14), graded poor (2), reflect a precarious shift to a 54% : 46% Current to Non-Current debt structure in 2005 (see [Exhibits 67 - 69](#)). Wiley's Current Assets to Total Assets (2.15) and Non-Current Assets to Total Assets (2.16), graded very good (5), reflect a healthy Current to Non-Current balance of 33% : 67% (see [Exhibits 70 - 72](#)). In summary, Wiley's debt strategy, although not optimal, doesn't represent a tendency to finance long-term asset increases with short-term debt (see [Exhibit 74](#)); heavy Current Debt, in the form of Deferred Subscription Revenue, is a publishing industry phenomenon (see [Exhibit 75](#)), and poses no serious threat to the firm's future survival, as confirmed by the next set of debt-management indicators.

The company's Times Interest Earned (2.17), graded poor (2), indicates that Wiley leverages its debt quite intensely. Consistent with the previous set of debt-management findings, Wiley's Times Interest Earned ratio reveals that the company tends to improve its payment capability (see [Exhibits 76 & 77](#)), but not nearly as fast as McGraw, or the industry average. On the other hand, Wiley's Current Cash Debt-Coverage Ratio (2.18) and Average Payment Period (2.19), graded very good (5), and good (4), respectively, accentuate that the firm's management does not utilize such

extreme debt strategy as to compromise its level of solvency. The company's Current Cash Debt-Coverage Ratio (see [Exhibits 78 & 79](#)) shows that 2005 operating cash flows could cover 71.3% of current debt. Wiley's Average Payment Period was 80 days in 2005 (see [Exhibit 80](#)), yielding more leverage than McGraw's 53 days.

Wiley's Creditor Leverage (2.20), graded poor (2), testifies further to the company's purposeful debt-leveraging strategy, and its risk of increased creditor dependency. Wiley's Creditor Leverage ratio had been decreasing since 2002 (see [Exhibits 81 & 82](#)), but in 2005 it increased to 61.6%, higher than McGraw's or the industry average.

#### CASH MANAGEMENT EVALUATION

Wiley's cash-management indicators demonstrate that the strategies previously identified, also extend to the firm's cash management.

Wiley's Current Ratio (3.21) and Quick Ratio (3.22), graded poor (2), both tell the same story. The company's Current Ratio has been less than one since 2000 (see [Exhibits 86 & 87](#)), even though two or higher is preferred.<sup>165</sup> Wiley's Quick Ratio, where a value of one or more is considered sufficient, has been less than one since 2000 (see [Exhibit 88](#)).<sup>166</sup> Consistent with previous findings, Wiley's Cash Flows from Operating to Revenue (3.23) and Cash and Equivalents to Total Assets ratio (3.24), graded very good (5) and Poor (2), respectively, demonstrate the company's concerted effort to constrain liquidity. The firm's Cash Flows from Operating to Revenue shows that Wiley generated \$.25 of operating revenue for each dollar of revenue in 2005 (see [Exhibits 91 & 92](#)). Although Wiley's figure is \$.01 less than McGraw's, it was \$.098 over the industry average. So the firm's solvency isn't in danger. However, Wiley's Cash and Equivalents

to Total Assets ratio has been consistently low since 2000 (see [Exhibits 93 & 94](#)). Wiley's ratio is 3% less than McGraw's and .7% lower than the industry average. The discrepancy between these two indicators suggests that management is purposely constraining its liquidity, perhaps to avoid becoming a target for hostile takeover.<sup>167</sup>

### ASSET MANAGEMENT EVALUATION

Wiley's asset-management indicators reveal that the firm's debt and cash management strategies, designed to maximize leverage and constrain liquidity, have not hampered the company's productivity.

The firm's Revenue to Total Assets (4.25) graded good (4), illustrates Wiley's revenue-generating efficiency. Wiley's Revenue to Total Assets (see [Exhibits 96 & 97](#)) shows that \$.943 of revenue is earned for each dollar of assets, topping McGraw's by .4%. Wiley's Net Income to Total Assets (4.26) graded good (4), shows that the company earned \$.081 of profit for each dollar of assets in 2005 (see [Exhibits 98 & 99](#)). This level of profit-earning efficiency was \$.051 below McGraw's but \$.007 over the industry average.

The company's Average Collection Period (4.27) graded good (4), indicates Wiley's receivables collection time was 51.6 days in 2005 (see [Exhibit 100](#)). This was 16 days less than McGraw and 29 days shorter than the industry average. The firm's Average Age Of Inventory (4.28) graded good (4), shows that Wiley's inventory turnover was 93.6 days in 2005 (see [Exhibit 101](#)), which was 41 days more than McGraw's, but only 2 days more than the industry average.

### **Organizational Citizenship Evaluation**

A very good (5) in all categories except one reveals that many of the sources of Wiley's competitive advantage originate with its healthy productive corporate culture. The relations with directors grade of good (4) reflects the fact that Wiley's director independence is marginal. However, there are no signs of difficulties between board members and management.

### **Strategic Positioning Evaluation**

Wiley's vision and mission statements are not only readily available, they are virtually unavoidable. Vision, mission, and strategies are prominently displayed and clearly defined. Wiley's grade for this factor is very good (5).

Wiley achieves its competitive advantage through brand recognition, content quality, customer service, segment selection, marketing, distribution channels, synergies, and growth strategies. The firm's functional structure facilitates its differentiation strategy, providing the flexibility to develop new competitive advantages? Wiley has had a "proven track record with acquisitions," and unsuccessful Wiley acquisitions are rare.<sup>168</sup> Partnerships and alliances serve to "add content, services, and capabilities,"<sup>169</sup> and create "cooperative marketing initiatives."<sup>170</sup> Wiley's grade for this factor is very good (5).

Wiley has demonstrated excellent responsiveness to the general environment with regard to educational trends, globalization, and copyright infringement, as illustrated by the many examples cited. Proactive strategies allow the firm to maximize its opportunities, and it is quick to recognize and respond to potential threats. Wiley's grade for this factor is very good (5).

Wiley's investments in R&D have been substantial, ensuring "the company is at the forefront of publishing developments and innovations," as illustrated by the many examples cited. Wiley's grade for this factor is very good (5).<sup>171</sup>

Wiley & Sons is enthusiastic and confident about its future. Wiley's expansion plans are well thought out and specific, its perspective realistic, and the company doesn't suffer from myopic planning. Strategic, rather than tactical, approaches are emphasized by Wiley's management. Wiley's credibility is impeccable. Wiley's grade for this factor is very good (5).

### **Management's Performance**

The purpose of this report is to provide a comprehensive analysis of John Wiley & Sons from a strategic management perspective. So it must answer the questions: Does Wiley and Sons have sustainable competitive advantage so as to earn above-average returns? If so, how is this achieved? In Wiley's case, the unequivocal reply to the first question must be yes, the firm does have sustainable competitive advantage. The second requires more expansive clarification.

A clear vision and mission have motivated Wiley & Sons to utilize its many resources, capabilities, and core competencies, many of which are valuable, rare, costly to imitate, and non-substitutable, to create sustainable competitive advantage (see [Exhibit 105](#)). Then, Wiley's capable management develops and implements strategies that utilize company resources and capabilities very effectively (see [Exhibits 106 & 107](#)).

While that explanation provides an outline of the facts, the FGA software's Grade Graph of Factor by Category, provides a more detailed assessment of Wiley's

performance (see [Exhibit 108](#)). It shows that organizational citizenship and strategic positioning make solid contributions, at values of 4.91 and 5, respectively. Profit is also a key factor, with a grade of 4.08. This is substantiated by experts who note that “over the long haul, this company has posted [returns on assets] that are some of its industry’s best.”<sup>172</sup> Asset management adds to the mix, with a grade of 4, but debt and cash management attract attention, since they trail with 3.38 and 2.75, respectively.

### **Problems & Solutions**

As mentioned previously, Wiley’s strategic approach to debt is to create maximum leverage, and with cash, it constrains liquidity, but why? CFO Ellis Cousens denies twice, in a three-sentence quote, that Wiley might be “a takeover target.”<sup>173</sup> Quoting Shakespeare, perhaps he “doth protest too much.”<sup>174</sup> This analysis is not unfounded, given the consolidation frenzy that is rampant in publishing (see *Industry Concentration & Consolidation*). In fact, Random House, Bantam Doubleday, and Dell were taken over by German conglomerate Bertelsmann AG in 1998.<sup>175</sup> So Wiley’s desire to minimize liquid assets, especially cash, maximize current debt, which is can well afford to eliminate, and repurchase stock at a feverish pace, could well be aimed at maintaining its independence and diminishing its appeal as a takeover target.

However, a number of questions beg to be asked. How long can this financial protectionism be maintained, before it actually impedes the company’s growth potential? Would this be such a problem if the Wiley family were less entrenched in the business? Might Wiley & Sons be a bigger, stronger company if this strategic approach weren’t being followed?

It's possible, at some point, that Wiley's failure to democratize the company's ownership may inhibit future growth potential. This challenge is alluded to by an investment service, noting that Wiley's "sustainable growth rate is quite a bit less than the rate at which its earnings per share have grown. That means that the company will probably have to raise additional capital from outside sources at some point."<sup>176</sup> Will the family be prepared to relinquish its dominance to allow the company to continue growing and expanding? Does Wiley have core competencies that result in competitive advantage, or "core rigidities" that prevent it from developing new competitive advantages?<sup>177</sup>

The obvious comparison here is McGraw-Hill. Since family members relinquished control, the firm has catapulted into stardom, capitalizing on its size to fuel greater success. McGraw-Hill became a strong, powerful company that is known for "using scale to build [its] growing global organization with improved market penetration and operating impact."<sup>178</sup> McGraw asserts that "In a digital world, scale is crucial and provides new opportunities to generate value [by] improving cost structure, increasing leverage, and producing greater profitability."<sup>179</sup>

### **Future Potential**

Is John Wiley & Sons positioning itself for a bright future? Given its warm, altruistic culture, and its truly remarkable capabilities, one would hope so. Unfortunately, the world is changing, and all must adapt to thrive. Given Wiley's keen sense of innovation, and its history of adaptation, it seems likely that the firm will find its way through. Although diversifying its ownership seems the most reasonable choice, some

other strategy, as yet unknown, may be attempted. In either case, Shakespeare's words, uttered in *Julius Caesar*, seem quite apropos:

There is a tide in the affairs of men,  
Which, taken at the flood, leads on to fortune;  
Omitted, all the voyage of their life  
Is bound in shallows and in miseries.<sup>180</sup>

