TUCK SCHOOL OF BUSINESS AT DARTMOUTH
GLASSMEYER/MCNAMEE CENTER FOR DIGITAL STRATEGIES
Case #6-0004

Simon & Schuster

It was the spring of 2001 and the sun was setting. Jonathan Newcomb (D'68), Chairman and Chief Executive Officer of Simon & Schuster, turned in his chair and looked out his office window in Rockefeller Center in New York City. Darkness was enveloping the nearby buildings and Newcomb was in a pensive mood.

Newcomb realized that he would soon have to make major strategic decisions that would determine the future of Simon & Schuster. He thought about the company's gilded past, the state of the industry and the radical changes that had made the future so uncertain.

The Company

Simon & Schuster (S&S) was one of the world's preeminent publishers of consumer books in a wide variety of genres and formats. S&S was founded in 1924 by Richard Simon and Lincoln "Max" Schuster. They started the business with $5,000 (mostly borrowed) and their initial project was the first ever crossword puzzle book. The book became a runaway best seller and by the end of S&S's first year of operations, the company had sold nearly one million books and generated profits of $100,000.

From the 1930's to the 1970's, S&S grew to become one of the leading publishers in the US. It developed a reputation for innovation in the industry. In addition to the first crossword puzzle book, S&S was the first to apply mass market production and distribution techniques to books. It launched the US paperback revolution in 1939. S&S was also the first to offer retail booksellers the right to return unsold copies for credit.

In 1976, S&S was sold to Gulf + Western. The parent company, through a succession of mergers and name changes, eventually became Paramount Communications. In the meantime, during the 1980's and 90's, S&S expanded by adding significant educational, professional and reference imprints. It acquired top brands such as Prentice-Hall, with its

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large international operations, and Macmillan, with its strong juvenile and computer book businesses. In 1994, S&S's parent Paramount was acquired by Viacom, a diversified entertainment company.

In 1997, Viacom made a strategic decision to focus on consumer entertainment and at the same time pay down debt. In a highly publicized auction process, Viacom unwound the S&S acquisitions of the previous years, selling off the education, professional, reference and international operations to Pearson plc, a UK-based media conglomerate, for $4.6 billion. Although S&S remained a global publishing powerhouse valued at over $600 million, S&S had returned to its origins, focusing exclusively on consumer books.

Innovation remained a part of the S&S ethos. In March of 2000, S&S brought worldwide attention to the phenomenon of electronic publishing. Stephen King's 66-page novella, *Riding The Bullet*, an original and exclusively electronic publication, was downloaded over 400,000 times within 48 hours of its release.

In 2001, S&S was a multi-faceted, multi-format global publishing company that generated over 2,100 titles per year. Over time, some of the S&S best selling authors and titles were:

Stephen King – *Dreamcatcher, Bag of Bones*

Frank McCourt – *Angela's Ashes*, *'Tis*

Ernest Hemingway – *Snows of Kilimanjaro, A Farewell To Arms*

Mary Higgins Clark – *You Belong To Me*, *All Through The Night*

Jackie Collins – *Hollywood Wives*, *Dangerous Kiss*

Iyanla Vanzant – *Yesterday I Cried*, *One Day My Soul Just Opened Up*

Marion Rombauer Becker, Ethan Becker and Irma Rombauer – *Joy of Cooking*

Joseph Heller – *Catch-22, God Knows*

Clive Cussler – *Shockwave, Atlantis Found*

Michael Porter – *Competitive Strategy, Competitive Advantage of Nations*

Richard Marcinko – *Rogue Warrior, Leadership Secrets Of The Rogue Warrior*

David McCullough – *Truman, John Adams*

Bob Woodward – *All The President's Men* (with Carl Bernstein), *Shadow*

Stephen Covey – *Seven Habits of Highly Effective People, First Things First*

S&S was well known in the industry for the success of its fiction, historical non-fiction and political non-fiction authors. S&S also focused significant efforts in children's publishing, audiobooks and interactive media products.

S&S's parent, Viacom, owned cable network, television, motion pictures, video rental, radio, outdoor advertising, websites, and publishing companies. Some of Viacom's best-known brands were: CBS, MTV, Nickelodeon, Showtime, Blockbuster Video, Comedy Central, UPN, Black Entertainment Television, Paramount Pictures, Paramount Parks and Marketwatch.com. S&S had developed joint publishing projects with Viacom's Nick At Nite, Nickelodeon, MTV, Star Trek and other programs. Viacom revenues were $22.3 billion in 1999 and $24.0 billion in 2000.

An Industry of Multimedia Giants

The multimedia industry, which included segments such as television, film and publishing, had been the fastest growing sector of the US economy for several years. From 1995 to 1999, the industry grew at a 7.9% compounded rate, easily outpacing US GDP.[1] Factors that helped drive this growth included the development of the Internet medium, technology advancements, proactive government legislation, and increased media consumption. Exhibit 1 shows various multimedia industry segments ranked by operating income margins and return on assets. Exhibit 2 demonstrates the growth in historical and projected consumer spending on entertainment media.

Technological advances had helped companies offer customers more information and entertainment faster and cheaper. Broadcasting, cable and satellite, among others, were the beneficiaries of government legislation that encouraged consolidation. This led to better-managed and well-distributed products and services for consumers. US consumer e-commerce grew from $2 billion to $14 billion in 1999 and reached $45 billion in 2000.[2] Internet dot coms were major buyers of advertising in traditional media in the late 1990's.

The above average growth of the multimedia industry led to intense competition and significant merger and acquisition activity among growing media giants. The ten largest publicly reporting media companies in the world accounted for approximately 39% of multimedia industry revenues in 1999.[3] The media giants included AOL/Time Warner, Bertelsmann, Pearson, Walt Disney, Viacom, NewsCorp and Vivendi Universal.

Summarizing the media giants' main strategies, Viacom was the No. 1 platform in the world for advertisers, while AOL/Time Warner was the world's first Internet-powered media and communications conglomerate, and focused on building its already strong subscription-based revenues. NewsCorp was leveraging its technology (developing sophisticated delivery mechanisms such as satellite and digital) and Bertelsmann was vertically integrating its content (from printing operations to book clubs to Barnes&Noble.com). Pearson was growing fast and focusing on education and new media. Vivendi was transforming into a telecom and media colossus. Walt Disney was focusing on reviving its struggling film and entertainment divisions. Exhibit 3 shows detailed financial results for the largest media conglomerates. Appendix 1 describes the companies in further detail.

[1] Veronis Schuler Communications Industry Report, 2000.
[2] Veronis Suhler Communications Industry Report, 2000 and Jupiter Research.
[3] Veronis Suhler Communications Industry Report, 2000.

Legions of Publishing Competitors

In contrast to the multimedia industry, book publishing was a highly fragmented but nevertheless consolidating business. The book publishing industry generated $24 billion in net sales in 1999 and $25.3 billion in 2000.[4] The Association of American Publishers categorized the publishing industry into consumer, professional, K-12 textbooks, college textbooks, university presses, standardized tests and subscription reference. Exhibits 4 and 5 show the historical and projected growth of these book publishing sectors. In 1999, approximately 24% of consumer book sales were generated by the top 5 publishers.[5]

The consumer book publishing industry was sub-divided by the Association of American Publishers according to distribution methods. These categories were: trade books (sold via bookstores), religious books (sold through conferences and associations), mass market paperbacks (sold through discounters and grocery stores), book clubs (subscription-based), and mail order. Exhibit 6 demonstrates the segmentation of the industry by topics such as art, biography and science fiction. As a result of the sale of certain divisions to Pearson, Newcomb considered S&S to be among the purest of the trade publishers. Unlike its competitors, S&S did not publish reference, how-to or religious books, nor did it have book clubs. Instead it focused on producing high-quality fiction and non-fiction titles that were sold through retailers.

S&S's significant competition included Random House (Bertelsmann), Harper Collins (NewsCorp), Penguin Putnam (Pearson), Time Warner (AOL), Scholastic and Harlequin (Torstar). Appendix 2 lists several other publishers that Newcomb believed were not S&S's most direct or pressing competitors. Exhibits 7, 8 and 9 rank consumer book publishers by sales, segments and bestsellers.

Among the competitors, Random House was the largest and it was taking advantage of its size to derive economies of scale from its backoffice operations. Harper Collins was growing by acquisitions while reducing title output and headcount to increase its profitability. Penguin Putnam was also expanding through acquisitions. According to an industry executive, publishers were typically valued at a multiple of 1.0 to 1.2 times sales.

Random House

Random House was by far the largest consumer book publisher in the world and its books were sold in almost every country. Books published by Random House had won more major awards, including Nobel Prizes and Pulitzer Prizes, than those of any other publisher. Random House had more than double the number of bestsellers as its closest competitor. Its stable of superstar authors included John Grisham, Tom Brokaw, Frances Mayes and Jon Krakauer. Bertelsmann acquired Random House in 1998. Random House generated revenues of $1.7 billion in 1999, which represented approximately 13% of Bertelsmann's total revenues.

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[4] http://www.publishers.org/home/stats/index.htm
[5] Trade Book Publishing 2000, Simba Information, Inc.

Random House imprints included Bantam, Doubleday, Crown, Ballantine, Knopf, Fodor's and Princeton Review. Bantam was the largest publisher of mass market paperback books in the United States. Joint ventures with Disney and Children's Television Workshop had been structured to produce books based on Disney characters and movies made from successful Random House books.

Harper Collins

Harper Collins was owned by NewsCorp. Harper Collins was founded in 1817 by brothers James and John Harper. Harper Collins had significant interests in the US, Canada, UK and Australia. It published classic works by Mark Twain and Charles Dickens along with books written by modern authors such as Barbara Kingsolver, Isabel Allende and Sebastian Junger.

Harper Collins broke through the billion dollar mark in sales for the first time in its fiscal year ended June 30, 2000. Revenues were up 35% to $1.03 billion and profits were up 85% to $89 million. In 1999, Harper Collins' sales of $764 milllion were 6.6% of NewsCorp's $11.5 billion in revenues. The president of Harper, Jane Friedman, indicated to reporters that the results were primarily from successful hits (57 titles on the bestseller lists in one year) as well as from fiscal responsibility. In addition, Harper had acquired Hearst's book publishing group and several smaller publishers in 1998 and 1999. Friedman stated that Harper Collins would focus on publishing fewer titles more profitably.

Penguin Putnam

Penguin Putnam was owned by UK-based media giant Pearson, plc. The publishing giant was formed in 1997 when Pearson bought Putnam Berkley and merged it with its Penguin division. Penguin authors included Amy Tan, Tom Clancy, Dalai Lama, John Steinbeck, Patricia Cornwell and Nora Roberts. Book imprints included Viking, Dutton and Puffin. Penguin had 11 imprints dedicated to children. It had developed joint ventures with teen-oriented Web sites to better understand that demographic segment, which had plenty of disposable cash but also had notoriously fickle and enigmatic tastes. Pearson acquired the textbook and educational divisions of S&S in 1998 as part of its strategy for expanding into learning and new media. In 1999, Penguin's sales of $644 million represented 12.9% of Pearson's $4.9 billion in revenues.

Time Warner

Time Warner intended to leverage its products after the January 2001 merger with AOL. Synergies were already being developed across all in-house brands, including the book publishing division. Authors included James Patterson, David Baldacci, Peter Jennings, Bill Gates, Jane Goodall and George Stephanopolous. The Time-Life series of books was well-known by consumers. Time Warner had joint ventured with Bertelsmann to develop the largest book-of-the-month club in the industry. Time Warner generated consumer book revenues of $1.6 billion in 1999, however only a small portion was trade publishing, which competed directly with S&S through its Time Warner and Little Brown imprints. Consumer book revenues were 17.3% of the parent company's proforma revenues of $9.5 billion. In 1999, Time Warner had 36 books in the *New York Times* bestseller list.

Scholastic

Scholastic was a global children's publishing and media company. Scholastic created quality educational and entertainment products for use in schools and homes, including children's books, textbooks, magazines, technology-based products, teacher materials, television programming, videos and toys. In June 2000, Scholastic acquired Grolier Incorporated, a leading operator of direct-to-home book clubs for children, and was the leading print and on-line publisher of children's non-fiction and reference products sold primarily to school libraries. In 1999, Scholastic's consumer publishing revenues were $793 million, representing 68.7% of total company sales of $1.15 billion. For fiscal year 2000, Scholastic increased revenues to $1.4 billion.

Harlequin

Harlequin was owned by Canada-based Torstar. Torstar was a diversified media company with major holdings in newspapers, book publishing, continuing education, television and interactive media. Harlequin was founded in 1949 and sold mystery, Western and cookbook paperbacks. The company evolved and ultimately specialized exclusively in romance novels. Harlequin revenues in 1999 were $375 million, which were 36.6% of Torstar's total revenues of $1 billion. In 2000, Harlequin sold 160 million books in 23 languages and 100 countries.

Newcomb thought about his key competitors and looked at a recent issue of *Publishers Weekly* magazine on his desk that described yet another newly formed online publisher. Consolidation at the top of the industry was accelerating while technology was fostering new entrants and changing the rules of the game. Newcomb wondered how S&S could best position itself to protect its core business while taking advantage of the recent trends. Something was bound to go wrong for the new entrants, the industry leaders or perhaps everyone in the industry.

Product Mix

Frontlist vs. Backlist

Publishers spent significant time, labor and capital marketing new titles and authors. Those were known as "frontlist" issues. Some publishers were managing their portfolio of content in order to increase sales from "backlist" titles. Backlists were books that had been published in prior years and may have had multiple printings. Once publishers incurred the initial costs of editing, typesetting and marketing books, subsequent printings were highly profitable.

Traditionally, biography, children's, reference and a small number of top-selling fiction books from authors such as Stephen King and John Grisham were good candidates for backlisting. Art and gardening titles also had good backlist potential, while business, health, "how-to" and mystery were considered to have medium backlist potential. Sports and travel titles tended to be more frontlisted. Further descriptions of segments are detailed in the next section.

Publishers typically earned about 50% of revenues from backlists, but some publishers were slowly shifting their product mix to earn "annuity" type cash flows from backlisted, consistent winners. Publishers that focused primarily on children's books, for example, earned higher than average revenues from backlists. Backlist books also offered increased sales potential from international markets, where reputable authors had a better chance of selling books than unknown authors.

Avery, a publisher of health, nutrition and cooking paperbacks, structured its portfolio of authors and titles to generate 85% of its income from backlist. This accomplishment made a strong impression at Penguin Putnam, which acquired Avery in September of 2000.

The development of superstores and online stores was a boost for backlists, since more shelf space was available for displaying classic titles and powerful search engines allowed customers to research titles without being overly influenced by new book promotions.

S&S generated less than 50% of its revenues from backlists because of its traditional strength in launching new titles. This strength was demonstrated by the 8.1% increase in its revenues from 1998 to 1999, which was primarily due to eight newly published blockbusters written by Stephen King, Mary Higgins Clark and Frank McCourt. Three blockbusters per year were the norm for S&S.

Retail booksellers thrived on backlists but they used discounted frontlist books to drive traffic into stores. Once customers were in stores there was a higher likelihood that they would make impulse buys. Over 60% of bookstore earnings were from backlisted books.

Many Market Segments

According to a 1999 report by the Book Industry Study Group, popular fiction represented 53% of adult consumer book purchasing, followed by cooking/crafts (10%), religion (9%) and general non-fiction (8%). Simba Information, an industry data provider, estimated that popular fiction books represented 25% of the *New York Times* bestseller list and that S&S was ranked in the top 3 publishers of bestsellers. Newcomb knew that S&S had developed an enviable reputation in the industry for its fiction as well as its historical and political non-fiction titles.

According to Simba Information, among topic segments in 1999, S&S was strong relative to its competitors in biographies, self-help, science fiction, and cookbooks. S&S was the second largest publisher by sales in each of those segments. For 1999, S&S was also in the top 5 sales ranking in the children's, business, how-to, and mystery segments. Exhibit 10 shows S&S revenues by segment, according to Simba Information. The following segment descriptions are based on information in *Trade Book Publishing 2000* by Simba Information.

Biography. Publisher revenues from biographies grew modestly, rising about 8% for the period from 1995 to 1999. While fewer titles were released in 1999, 45 titles reached the *New York Times* bestseller list compared to 40 in 1997. Consumer-oriented biographies from personalities such as Nelson Mandela, George Bush, Princes Diana, and Michael Jordan became more popular. Random House was the leader in this segment in 1999, followed by S&S and Harper Collins.

Self-Help. The market for self-help books was strong in the early 1990's but soon suffered from a glut of titles. While the segment had growth of 27% from 1995 to 1999, it grew only 4% from 1998 to 1999. Of the 51 titles in the 1999 New York Times miscellaneous bestseller list, 11 were from the wildly popular "Chicken Soup For The Soul" series. More than 50 million copies had been sold and the series helped propel Health Communications to the top of the self-help publishers ranking. S&S and Random House were also leaders in this segment. Self-help titles were considered of medium potential for backlisting.

Science Fiction. Science fiction books had continuously lost market share for the previous five years. The segment had grown less than 1% from 1998 to 1999. S&S focused on the mass market format for sci-fi titles in 1999 and one of the cornerstones of its program was the *Star Trek* series. Sci-fi tended to have more frontlist titles. Random House and Torstar were other top publishers in the segment.

Cookbooks. Cookbooks benefited from the growth of beginner-level buyers and customers that considered cooking a hobby. The segment was composed primarily of backlist titles, although new ethnic and specialty titles were also successful. S&S benefited from continuing sales of classics like *Joy of Cooking*. Random House and Time Warner also led in this category in 1999.

Children's. The children's book segment had been the fastest growing in 1999 (15%) and was expected to continue to grow at above-industry rates. Random House, Penguin Putnam and S&S were the top publishers in the category. Scholastic had been the beneficiary of the Harry Potter craze, which not only generated millions in sales but also raised broad-based awareness of the entire children's book market.

Computer. Though computer books had been one of the fastest growing categories (60% from 1995 to 1999), no titles had appeared on the *New York Times* bestseller lists. The segment had low backlist potential compared to other segments. The top publisher in 1999 was Pearson PTG, a recently formed unit of the Pearson conglomerate. Pearson PTG united computer book publishing divisions of Macmillan and Prentice Hall (acquired from S&S), Addison Wesley and others. Hungry Minds/IDG was the second largest publisher with its "For Dummies" titles.

Romance. Since the mid-1990's, romance books had been generating over $1 billion a year in sales. Revenues grew at 23% from 1995 to 1999. The Romance Writers Association estimated that over 18% of the reading age population had read at least one romance novel a year. Publishers were expanding the market, with sub-themes such as Westerns and science fiction. Titles tended to have low potential for backlist compared to other segments. Harlequin, owned by Torstar, dominated the segment, followed by Random House and Penguin Putnam.

Religion. Increasingly, religious books were finding their way onto bestseller lists and into the hands of readers who previously would not have picked up a religious title. The segment grew 16% from 1995 to 1999. This segment had medium potential for backlisting. Publishers had been turning away from straight-forward religious non-fiction and toward inspirational topics. The top publishers were Thomas Nelson, Harper Collins and Tyndale.

Audiobooks. The audiobooks market had grown significantly during the previous five years. Sales had increased over 50% from 1996 to 1999. Top publishers, of which S&S was one, saw sales increase by an average of about 10% from 1998 to 1999. Exhibit 11 shows details of the audiobook segment.

Exports. International markets offered many opportunities. As English became the lingua franca of the world, demand for US, Canadian, UK and Australian titles increased. Also, as world literacy rose, sales of translations of works by English-speaking authors increased. Exhibit 12 shows the growth of book exports from 1998 to 1999. Canada, Australia, Japan, Mexico and the Netherlands seemed to offer large markets with the best growth opportunities.

Granular Business

As Newcomb liked to say, publishing was a “granular business” with thousands of individual products and transactions. Regardless of segment, topic, format or language, each book was a unique product. Each product required its own unique contractual arrangements, editing, production, marketing campaigns as well as tracking and accounting of royalties and other intellectual property such as subsidiary and foreign rights. Thousands of titles and millions of books had to be tracked from production, through multiple levels of distribution and at retailers warehouses and stores. S&S itself had over 1 million square feet of warehouse space. As Newcomb also liked to say, that was “enough room to fit a bunch of 747s.”

Like other major publishers, S&S understood how to negotiate the various rights associated with a single title, those for hardbacks, softcovers, mass market paperbacks, audiobooks, international rights and digital rights. Along with its competition, S&S had made significant investments in accounting systems that handled complex royalty payments from thousands of sales.

As S&S’s largest competitors continually leveraged the backoffice efficiencies and technological platforms of their corporate parents, they were able to generate greater margins and higher profitability. Publishers with many international offices could more easily build global demand for their products.

Publishers had mastered the management of hundreds of thousands of inventory units. They had spent substantial capital in infrastructure buildup. In effect, volume became a key driver to profitability because of high technology costs and other fixed overhead. Newcomb wondered if product mix and inventory management skills were enough for S&S to survive and thrive in the new millennium.

Margin Pressures

Revenue Decline

S&S's net sales in fiscal year 2000 were $596 million, a decrease of 2.3% from 1999. Earnings before interest, taxes, depreciation and amortization were $71.3 million, a decrease of 3.6% versus the previous year.[6] 2000 was the first down year for S&S since Newcomb had joined the company in the early 1990's and Newcomb was not pleased. At least S&S had outperformed the trade book industry, whose net sales had decreased 3.7% that year.

A Challenging Cost Structure

Exhibit 13 shows the typical P&L for the publishing industry and indicates the largest expenses. Exhibit 14 shows the profitability of several publishers in 1998 and 1999. The typical P&L shows net sales, thus it does not indicate the adjustment to gross sales: books returned by retailers. Books returned were the bane of the publishing industry. Ironically, as mentioned earlier, S&S was the first to offer this service to retailers as a way to generate more business. Over time, books returned became a stubborn and serious problem for the industry and, by 1999, represented 25% to 30% of gross sales in most categories of books. Due to complex agreements with retailers, publishers had to extend their accounts receivable, often for over 90 days.

Newcomb knew that new technologies, such as on-demand printing, would begin to have a positive impact on publishers margins in three to five years. Books returned would be reduced, customers would have access to books wherever digital printing presses and in-line binding machines were located. These presses and binding machines would be connected as a miniature manufacturing system to produce books in limited numbers, thus avoiding waste. Because of the current high expense of setting up short-run digital printing and binding machines, the Wal-Marts and Barnes & Nobles of the world would rely on their traditional warehousing and distribution systems for the time being. Newcomb was concerned about how and where to squeeze down costs in the interim.

The $4.6 billion price for which Viacom had sold the non-consumer operations of S&S to Pearson was a sum that many in the industry considered outstanding by any measure. As part of the sale agreement, S&S's accounting, order processing, royalty tracking, customer service, and inventory management systems were transferred to Pearson and supplied under contract back to S&S for a set fee. S&S retained ownership of its substantial warehouse

[6] Publishers Weekly, February 19, 2001, p. 14.

facilities. The contractual agreement limited S&S from taking advantage of economies of scale and technology developments to reduce costs.

Searching for Better Margins

Reference and professional books, where S&S was no longer strong, tended to have higher margins than consumer books. Reference and professional customers typically had a higher need for specific information and were therefore less price sensitive. In addition, publishers could easily reorganize chapters, concepts and data into multiple formats and publications in order to generate several revenue streams from the same information. These book categories were likely to be the initial beneficiaries of in-line printing and binding.

The sale of S&S's education and professional businesses to Pearson was clearly a financial triumph. Yet Newcomb wondered what would have been possible if S&S still had its backoffice systems and its variety of businesses, some of which were better positioned to take advantage of technological change.

Authors and Agents: The Rights Issues

Newcomb had often been quoted as saying "Publishers are the merchant bankers of the intellectual property market." S&S invested in numerous titles much as a venture capitalist would invest in many startups, hoping that one or two would be big hits.

S&S received thousands of unsolicited manuscripts per year but worked almost exclusively through agents, since agents served as an effective screening mechanism. Once a book was deemed worthy of publishing, the rights to the work were negotiated, usually through agents. New authors typically earned 5% to 15% royalties on book sales, and agents received their fees from the authors' royalties. Bestselling authors received significant advances, often in the millions of dollars, and negotiated higher royalty percentages. Authors were typically loyal to their agents and publishers, especially to editors, although occasionally authors would make changes. They also were sometimes able to keep the movie rights to a book and sell them to studios in a separate transaction from the book publishing rights. Publishers took significant risks by paying authors' advances and spending global production and marketing efforts on titles without being able to fully predict their relative success. Copyrights typically lasted for the authors' lifetime plus seventy years and thereafter works became public domain.

There were thousands of literary agents. Some of the best known included ICM, William Morris Agency and Wylie Agency. William Morris represented more than thirty *New York Times* bestselling authors as well as winners of the Pulitzer Prize, the National Book Award and the National Medal of Literature. In the past year, the agency had made more than sixty book-to-screen sales and numerous of its authors had seen their work translated into $100 million plus blockbuster movies. Multi-book deals for superstar authors were common, though authors rarely committed to exclusivity with one publisher.

Traditionally, rights were negotiated between agents and publishers in person or by phone. For example, publishers would be involved in telephone auctions whereby they would have to call in their bids every half hour until a winner was announced. Rightscenter.com had emerged as the leading worldwide online marketplace where agents, sub-agents, scouts, editors and publishers review and negotiate publications, film, software and multimedia works. For the publishing industry, users could securely read manuscripts and negotiate multiparty transactions online. The site eliminated the need to print and mail manuscripts and catalogs. Rightscenter had over 8,000 members and over 30,000 titles.

A literary agent from the LitWest Group in Palo Alto, California had recently closed a six-figure deal using the Rightscenter auction process. She auctioned the book rights for *Fast Alliances*, a groundbreaking book on Internet alliances by a relatively unknown author. Using the site, the agent made her submissions privately to eleven major book publishers nationwide, and within two weeks, reached an agreement with John Wiley & Sons. Using the traditional publishing route and mailing the proposals would have added at least two months to the process.

In January 2000, Harper Collins became the first major publisher to enter into a comprehensive global agreement with Rightscenter. Harper Collins agreed to list a minimum of 500 adult and children's frontlist and backlist titles on the Rightscenter system in 2001. Through Rightscenter, Harper Collins would be able to extend its reach into foreign markets, increase exposure to backlist titles and create new opportunities for authors while lowering its backoffice expenses.

Electronic rights became an important issue as new reports from research firms showed the potential impact of technology in the publishing industry. Forrester Research estimated that revenues from digitized book publishing would rise from an estimated $838 million in 2001 to $7.8 billion in 2005.[7]

Random House filed suit against Rosetta Books in March of 2001 for illegally selling electronic versions of books by Random House authors.[8] The suit was at the heart of a long-simmering battle between publishers and authors over the rights of publishers to issue electronic versions of already published titles. Authors argued that electronic rights have to be specified in contracts, much like foreign publishing rights. Many publishers had contracts with authors that dated back to the times when computers were barely invented, leaving contract wording such as "forms of books" and "style and manner" subject to interpretation. RosettaBooks had signed agreements with about 100 authors and offered about 40 titles.

Previously, in late 2000, Random House had raised its royalties to authors of e-books from 15% of retail price to approximately 25% in order to avoid losing authors to upstart Web publishers,.[9] The company had chosen to incur the expenses of digitizing its backlist of titles and making them available electronically.

[7] http://www.inside.com/jcs/Story?article_id=23078&pod_id=8
[8] The Wall Street Journal, February 28, 2001.
[9] The Wall Street Journal, November 8, 2000.

Newcomb knew that rights were increasingly being sliced into thinner and more discrete components, each of which would have to be negotiated carefully to avoid any disagreements.

Wholesalers and Retailers: Getting in the Game

Wholesalers Evolve with the Times

Ingram Book Company was the leading wholesaler of books, audiobooks and magazines, with over 50% of those markets in 1999. It had more than 32,000 retail accounts, carried over 15,000 publisher imprints, had an inventory of 500,000 titles and distributed over 175 million units per year. Ingram also offered a package of digital fulfillment services to the book industry, including print-on-demand and e-book distribution.

Baker & Taylor was a leading distributor of books, videos and music products to Internet and traditional retailers and to libraries in 2001. The company shipped over 1 million ISBNs (SKUs) per year. Baker & Taylor offered print-on-demand services via Replica Books. Replica Books worked directly with authors and publishers to keep their books in print. Each title was maintained in an electronic database, and the books were printed on a high-speed printer and individually bound in paperback or hardcover.

Publishers Group West was the largest wholesale distributor for independent publishers in North America in 2001. It distributed books in categories such as health, travel, business, children's, music, among others. Over 90% of Publishers Group West billings were generated from its top 50 clients. In 1999, PGW established e-book, CD-ROM and academic book distribution subsidiaries and in 2000 it began expanding into Europe. PGW had an in-house fund which invested in publishing companies and publisher's projects. Three recent investments of the fund were combined into Avalon Travel Publishing, which had become a subsidiary of PGW. Exhibit 15 shows unit sales and revenues in the wholesale book industry.

Superstores and Internet Retailers Take Charge

Amazon.com was the largest online bookseller in the world and was also the most recognized e-commerce brand. It was started in 1995 and by early 2001 had 29 million customers from 160 countries. In 1999, online sales of books accounted for only 4.4% of the market, while traditional large chain bookstores accounted for 24.6%. Although the combination of online prices and shipping costs resulted in no savings for buyers in comparison to bookstore prices, for the fiscal year ended in December of 2000, Amazon's revenues increased 68% to $2.76 billion. Net losses for the period increased 96% to $1.41 billion.

In 2000, Amazon opened its e-book store offering over 1,000 for-charge and free titles as well as downloadable audiobooks. Amazon also had expanded from books into music, video, software, electronics, toys, cars, auctions and other consumer products. The book division accounted for less than half of all sales, though it was still far larger than its closest online competitor Barnes&Noble.com. By February of 2001, Amazon had cut about 15% of its workforce in order to attempt to achieve profitability.[10]

Barnes & Noble had the largest chain of bookstores in the world and the second largest online bookselling operation. In 2000, over 85% of Barnes & Noble sales came from its superstores. Superstores had progressively accounted for a larger portion of the company's total sales. Barnes & Noble had 26% of sales in the bookstore market in 1999. For its fiscal year 2000, Barnes & Noble had $3.4 billion in sales and net income of $124.5 million.

Barnes & Noble spun off its Internet operation, Barnes&Noble.com in 1999, selling a 40% share to Bertelsmann and taking 20% public. In 2000, Barnes & Noble purchased Fatbrain.com, an online bookseller specializing in professional and technical titles for corporate users. Barnes&Noble.com expanded into textbooks, music, software, magazine subscriptions, online courses and several digital initiatives but continued to generate losses for its owners.

In 1998, Barnes & Noble's proposed acquisition of the nation's largest wholesaler distributor, Ingram Book Group, was blocked by the Federal Trade Commission. Independent booksellers were critical of the potentially unfair competitive advantage Barnes & Noble would have had after the purchase.

Barnes & Noble had purchased publishing and distribution rights to over 2,000 titles. It had been publishing public domain classics, whose copyrights had expired, under its own brand. To Newcomb, retailers and wholesalers that started their own publishing divisions were "nibbling around the edges." He did not consider them major threats.

Borders Group was the second-largest operator of book superstores and the largest operator of mall-based bookstores in the world based on both sales and number of stores. As of December 2000, the Company operated more than 335 superstores primarily under the Borders name and also under the Waldenbooks and Books, etc. names. For the fiscal year ended 2001, Borders had generated $3.2 billion in sales and net income of $43.6 million.

Books-A-Million was started by a 14-year old who opened a small newsstand in Alabama in 1917. In 2001, the company was the third largest book retailer in the US and owned 182 stores in 17 states, mostly in the Southeast. Of those stores, 135 were superstores that generated over 75% of revenues. Books-A-Million also had book wholesale and distribution subsidiaries, American Wholesale Book Company and Book$mart. Books-A-Million had an exclusive agreement to distribute books to Wal-Mart. BAM's subsidiaries were providing fulfillment services for various online retailers. BAM had recently agreed to acquire the assets of 19 of the bookstores of defunct Crown Books. Crown Books had declared bankruptcy twice in three years by 2001. Exhibit 16 has an analysis of the retail book industry.

[10] Publishers Weekly, February 5, 2001, p. 9.

Independent bookstores had a 33% share of the book market in 1991.[11] By 1999, their share had shrunk to 15% as they lost customers to malls, superstores and the Internet. However, their share held steady in 2000 due to BookSense, a coordinated marketing campaign of over 1,200 independent stores which developed a bimonthly list of 76 of the best books in numerous categories.

The Electronic Rollercoaster

Electronic Publishing – Operations and Distribution

Printing presses were invented over 500 years ago. The process of publishing books on paper remained essentially unchanged from that time until the late 1990's. By 2000, Xerox and 3M had already developed an experimental thin, flexible and reusable film that displayed electronic text. The physical and virtual worlds were melding and book publishers were being forced from snail's pace developments to riding high-speed technology rollercoasters in virtual darkness.

Two stories about S&S's high-profile, exclusively electronic publishing of Stephen King's *Riding the Bullet* said much about the industry. First, the entire process of editing, proofing, cover design and marketing took two weeks from the time Stephen King delivered the manuscript. This was a publishing miracle, considering that most books had a gestation cycle of 9 to 12 months. Second, according to industry publications, less than 20% of the 600,000 people that downloaded *Riding the Bullet* ever finished reading it.

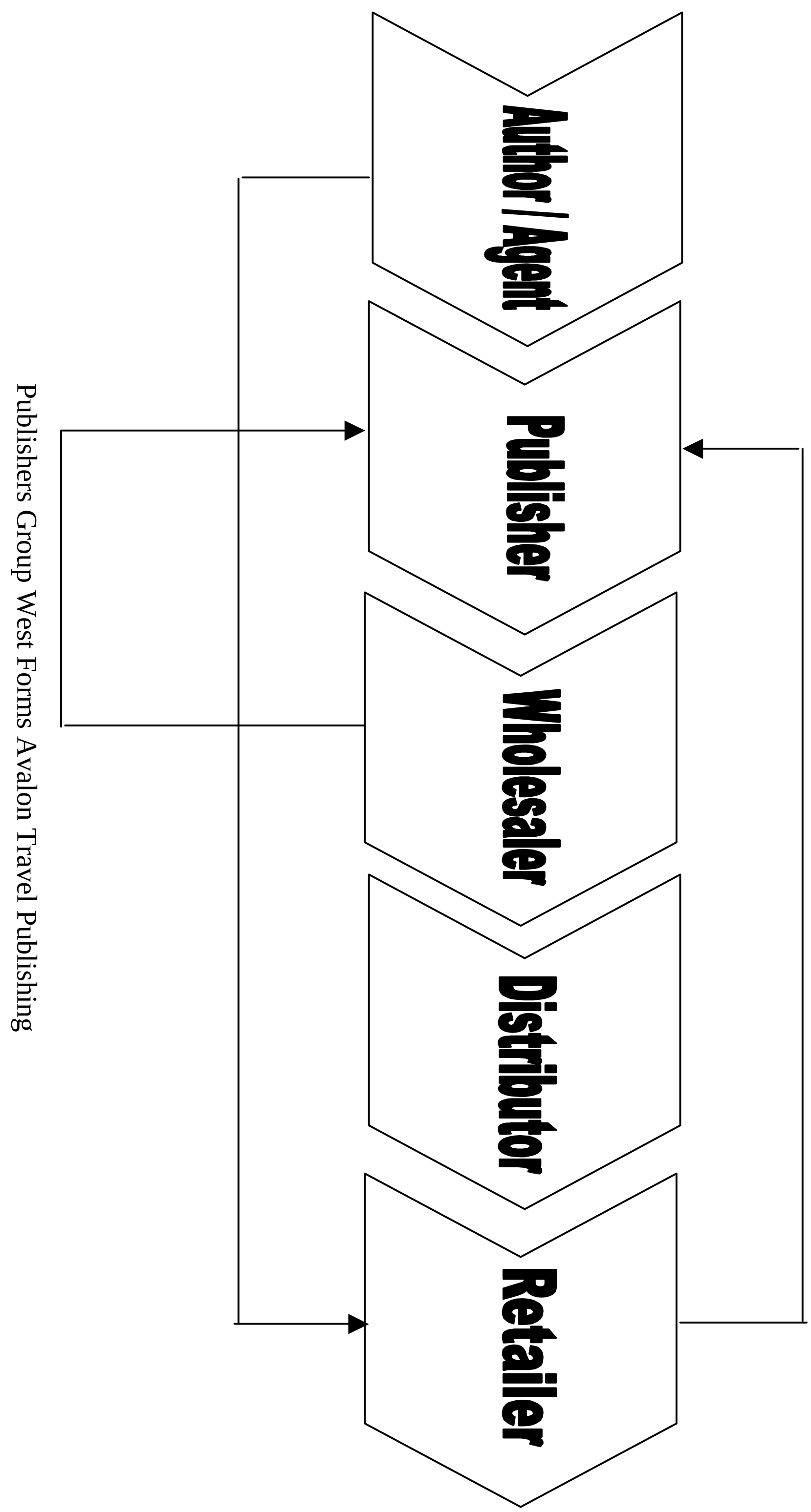
Companies such as Random House had been making substantial investments in enterprise resource planning (ERP) software during the late 1990's to globally integrate their backoffice systems. By 2001, most large publishers had ERP in place and practically every publisher had its own website.

S&S's site offered a number of features to attract readers, including excerpts of new releases, discussion boards, chat rooms, contests and unique information about bestselling authors. The site also served book retailers and wholesalers and S&S forwarded leads from interested book buyers to Amazon. Sites offered the potential for publishers to better understand the book-buying public. This was a marked improvement for publishers that traditionally did not know their customers at all because of retailers and wholesalers did not share data about sales patterns and customer behavior with publishers. Registrations and chat rooms offered significant information about demographics and preferences of book buyers.

Many startups were launched with the intent of revolutionizing one or more aspects of the publishing industry. For further details of the effects of technology on the industry, see Appendix 3. Figure 1 shows changes in the traditional book industry supply chain.

[11] http://www.nytimes.com/2001/03/19/business/19INDY.html

Figure 1: Examples of Changes in the Traditional Book Publishing Supply Chain



In July of 2000, S&S agreed to a long-term strategic alliance with Lightning Source, a digital fulfillment service owned by Ingram Book Company. At that time, S&S had the largest collection of e-book titles of any major trade publisher. Lightning Source's range of services to over 700 publishers around the world included digital file conversion, digital rights management, e-book delivery to various devices and on-demand printing.

The Unrealized Promise of E-Products

While technology offered the potential to radically change the experience of readers by adding multimedia capabilities, the promise of broad customer acceptance of e-products remained tantalizingly elusive. Estimates of e-book sales by reputable research firms varied widely, leading to a lack of certainty about the timeline and growth of the trend.

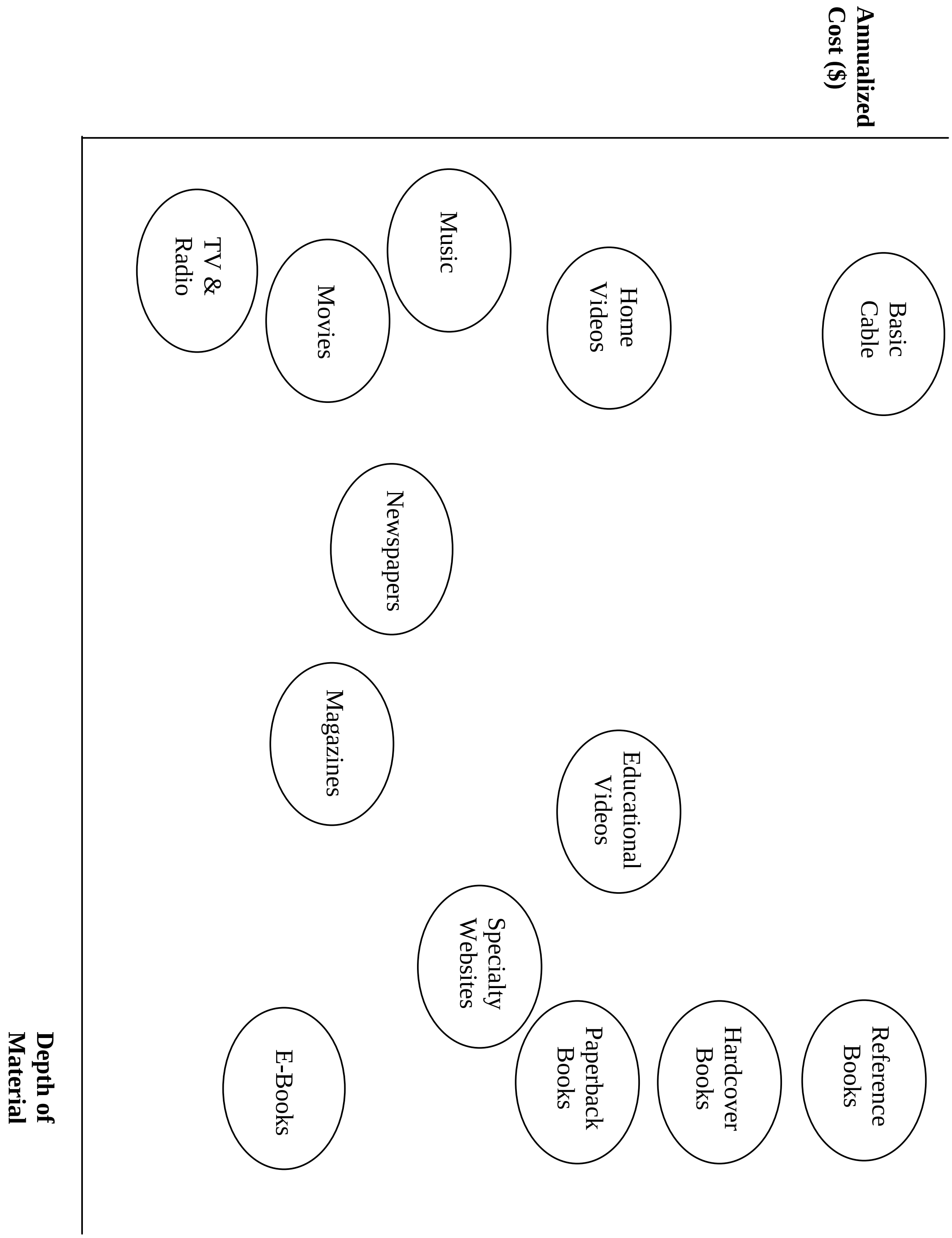
Arguably one of the top three literary agents in the world, Andrew Wylie was quoted in *Financial Times* as saying "You might as well forget about the trade publishing e-book market for the time being. It is not a strong business."[12] He based his statement on the sales results of a novella from one of his author-clients. The e-book rights sold for $80,000 and the publisher sold only sixteen copies.

John Feldcamp, the co-founder of online publisher Xlibris, saw only problems. "No one has figured out a good way to distribute e-books or even what to charge," he said. He added: "Do e-books ultimately win? Yes, absolutely. Do they win this year (2000) or next year? No. This isn't even slightly cooked yet."[13] Xlibris allowed authors to retain all publishing rights, paid 50% royalties, and had systems to convert manuscripts into hardback books, paperbacks and e-books within a few weeks. Random House Ventures, the investment subsidiary of Random House, made a significant minority investment in Xlibris. In essence, e-books eliminated printing costs and lowered retail prices, but the real battle was for consumer's time.

Websites and data management tools allowed publishers to better understand the characteristics and habits of book buyers. Figure 2 shows a stylized analysis of book substitutes. Note that compared to substitutes such as TV and newspapers, books had a distinct disadvantage as a medium for advertising.

[12] Financial Times, March 20, 2001.
[13] The Wall Street Journal, October 2, 2000.

Figure 2: Stylized Analysis of Book Substitutes, Price vs. Depth of Material



Random House chairman, Peter Olson, had stated that despite electronic publishing initiatives, traditional publishing would remain the foundation as well as the main engine for growth.[14] Newcomb had the same opinion, the Internet was a powerful ally and print-on-demand would eventually be impactful, but e-books were not the immediate future of S&S.

A Hard Look in the Mirror

Newcomb assessed the powerful forces affecting the publishing industry. He evaluated his alternatives and thought about the costs, benefits and ramifications of each choice. First, S&S could develop value-added products and services to its customers, diversifying from books into distribution services for retailers, data services or magazine publishing. Second, S&S could launch into the future by focusing all its efforts on accelerating the adoption of on-demand printing and in-line binding while developing more robust revenue models for e-commerce and e-books. Third, S&S could stay the course, grow organically and become more customer-centric, providing more books on subjects selected through reader surveys and market research. Fourth, S&S could even choose to eliminate certain imprints and narrow the scope of its publications to higher growth and higher margin segments. Lastly, there was the divestiture option. S&S could become a part of another company with major strategic interests in consumer publishing, but this would require a strategy to maximize the valuation of S&S.

Newcomb took a deep breath. He knew that Viacom would not give him the funds to do all he wanted, so he would have to prioritize his projects. The Viacom management, the shareholders and the S&S employees were counting on him to use his best judgement. He felt the weight of his responsibility to make the right decision.

[14] Publishers Weekly, July 3, 2000, p. 10.

Case Questions

Use the extensive data provided in the exhibits as you evaluate your answers to the following questions:

1. Analyze the traditional paper-based book publishing industry using the Five Forces model. Based on your analysis, what should Jon Newcomb do?

2. How does your Five Forces analysis change if you include the effects of recent and upcoming technological changes in the industry? Is S&S destined to be disintermediated? What could Newcomb do to leverage these technological changes into greater profitability?

3. How do you view the five strategic alternatives that Newcomb is considering? How would you carry them out? What would you do?

Appendix 1: Multimedia Company Descriptions

AOL Time Warner was one of the largest content owners and distributors in the world. It operated in six businesses: interactive services (AOL), networks (Turner Broadcasting, HBO), publishing (Time, Inc., Time Warner Publishing), film (Warner Brothers, New Line Cinema), music (Warner Music Group) and cable (Time Warner Cable). AOL-Time Warner's core growth drivers were subscriptions, advertising and content. The integration of AOL and Time Warner was focusing on cross-selling opportunities and leveraging multiple brand synergies. Time Warner had already generated over 800,000 new subscriptions from AOL's 27 million subscribers. Conversely, promotions in Time Warner magazines had become one of AOL's top 10 sources of new members. On a pro forma basis, the combined AOL Time Warner companies generated $9.5 billion in revenues in 1999 and over $10 billion in 2000.

Bertelsmann was a privately held, Germany-based media conglomerate. Its publishing empire spanned the globe with book, book club, printing, magazine, television, film, radio, music, professional information and Internet subsidiaries. As of the end of Bertelsmann's fiscal year in June 30, 2000, sales were up 23% to $15.4 billion, due primarily to growth in book and music operations as well as consolidation of TV and film divisions. CEO Thomas Middelhoff's edict to his managers was to be number 1 or 2 in their markets.

Bertelsmann had $7 billion in cash after selling a stake in AOL and planned to continue a string of acquisitions of key media properties. Bertelsmann made a $60 million investment in Napster in 2000 to leverage the peer-to-peer site's more than 50 million users. It also owned part of Barnes&Noble.com. Over 25% of Bertelsmann's revenues were derived from book operations.

Pearson, plc was a global media company based in the UK with key operations in education, business information, consumer publishing and television markets. Pearson was the world's largest textbook publisher, with Prentice Hall, Addison Wesley and other first-class imprints. It also owned Penguin, Putnam and other consumer book imprints; the *Financial Times* international newspaper; and part of RTL European radio and television broadcasting. Pearson's sales were over $5.9 billion in 2000.

NewsCorp was an Australia-based international communications company. It produced and distributed movies and television programs; published newspapers, magazines and books; developed digital broadcasting; produced advertising services; developed subscriber management systems; and created and distributed online programming. NewsCorp owned the Fox network of film and television companies, Harper Collins book publishers, the Los Angeles Dodgers, the *New York Post*, BskyB broadcasting service, and STAR TV satellite service in Asia, among others. For the fiscal year 2000, NewsCorp generated over $11 billion in sales.

Vivendi Universal was for many years a slow-growth French utility and real estate company. Through acquisitions it evolved into the second largest media and entertainment company in the world. Vivendi's strategy was to become the world's preferred creator and provider of digital content, entertainment and services. Vivendi had recently merged with Seagram, which gave it ownership of Universal Studios' movies, TV shows, music labels and theme parks. Vivendi sold off the Seagram liquor operations.

Vivendi covered the entire value chain from content creation to aggregation to distribution. Its publishing division included literature, health, education, games and information delivered via books, websites, Wide Area Protocol (WAP), Personal Digital Assistants (PDAs), CDs and software. Vivendi also purchased Canal Plus, Europe's biggest pay-TV and digital TV operator with more than 14 million subscribers. Vivendi Telecom was Europe's leading private telecom operator and it was expanding further into Europe, the Mediterranean countries and Africa. Vivendi sales in 2000 were over $55 billion, of which 6.9% were from publishing. Havas publishing group focused on reference and education books sold primarily in France and non-U.S. markets. The company had no debt and annual cash flow of $3 billion.

The Walt Disney Company was a diversified worldwide entertainment company with operations in five business segments: Media Networks (ABC), Studio Entertainment (live-action and animated movies, television animation, music and theater), Parks and Resorts, Consumer Products (which licensed cartoon characters and other intellectual property for merchandise and published books and magazines), and the unprofitable Internet Group. Disney generated over $25 billion in revenues in fiscal year 2000, of which only $55 million derived from consumer publishing, mainly through its Buena Vista imprint.

Appendix 2: Additional Major Book Publishers

(Ranked By Revenues)

Reader's Digest was founded in 1922 as a magazine publisher. The book publishing division focused on how-to titles, children's, cooking, reference and abridged works of fiction. The abridged works were published in 16 languages and sold in 27 countries. Fifty five percent of the company's revenues of $937 million in 1999 came from outside the United States. Reader's Digest was expanding into multiple distribution channels including direct-response television, display marketing, catalogs, retail and the Internet. In 1999, Reader's Digest had one of the highest operating margins in the industry: 17.8%.

Holtzbrinck was founded in 1948 by Georg von Holtzbrinck and had become a global powerhouse with operations in all continents. It owned Henry Holt, St. Martin's Press and Farrar, Straus & Giroux in the US. It also owns Macmillan in the UK. Holtzbrinck's products included trade books, college books, book printing, reference materials, business information, German newspapers, and *Scientific American* magazine. Holtzbrinck increased its revenues by 25% to $346 million from 1998 to 1999.

Rodale Press was founded in 1930 by J.I. Rodale, a farmer who wanted to raise the quality of farming techniques and improve the public's nutritional habits. The business was still family-owned in 2001 and had a number of well-known magazines such as *Runner's World* and *Men's Health*. Rodale's books focused on health, fitness, gardening, crafts and inspiration. Rodale was the first company to institute a no-smoking policy and refused to accept advertising from liquor and tobacco companies. In 1999, Rodale generated $203 million in revenues.

Hungry Minds had a portfolio of technology, business, consumer and how-to brands in 2001. Its brands included "For Dummies", Cliffs Notes, Frommer's, "The Unofficial Guide", Weight Watchers, Webster's New World and Betty Crocker. Hungry Minds focused on helping people learn through a number of mediums such as books, audio tapes, newsletters, CDs, games, videos, Web sites. In February of 2001 it was forced to lay off about 20% of its staff due to declining advertising and licensing revenues from its sites. Hungry Minds' main education site offered 17,000 online courses through joint ventures with numerous institutions such as UC Berkeley, Michigan State University and New York University. Revenues in 1999 were $180 million.

McGraw Hill had a strong business and computer publishing program for consumer books. However, sales of $129 million from those segments represented only 3% of its $4 billion in combined revenues in 1999 from financial services, education and business information.

Appendix 3: Technology and Publishing

Production. A typical hard-cover bestseller was retail priced at about $25. Going completely digital would eliminate printing and binding costs of about $3 per book and warehousing expenses of about $2 per book. Including overhead and other cost reductions, savings would be as much as 40% of retail price. Even without going fully electronic, the turnaround time from manuscript to print plus the flexibility to make changes to content later in the production cycle would surely lead to expanded margins, especially for textbooks, academic journals and computer books.

Readers received timelier information so the perceived and actual value of the material increased. A major publisher reported that its computer book publishing division had cut in half the time it took to edit a book by working electronically. At the very least, online communication had resulted in a more collaborative working relationship among authors, editors and designers.

Authors and Disintermediation. Newly published authors stood to gain from online publishing because they could demand a higher percentage of royalties from publishers and distributors. Backlisted authors, however, could possibly lose because of insufficient detail in royalty agreements regarding rights to re-use the work after it went out of print. With electronic storage, a book would never go “out of print.”

In January of 2001, Barnes&Noble.com announced the creation of an electronic publishing imprint, Barnes & Noble Digital, which would create a direct link between authors and readers, giving authors a greater share of income from their works while lowering retail prices. It would provide authors with a one-stop, direct-to-market process, featuring editorial support and online sales monitoring. Barnes & Noble Digital would also make its works available for e-book retailers and would publish digital versions of Barnes & Noble titles in print at the time.

Print-On-Demand. Publishers such as S&S planned to use print-on demand technology to control inventory better and to offer works of lesser known authors and volumes that had been out of print. According to an industry publication, for every five books manufactured, S&S sold three or four, because of copies used for retail display or returned unsold. Print-on-demand created the possibility of significantly increased margins from inventory management.

Barnes & Noble purchased interests in print-on-demand and digital publishing companies. Barnes & Noble and IBM had teamed together to provide printed books on demand at retail stores and at Web sites. However, print-on-demand meant publishers and book sellers would have to invest in distribution centers and high-quality, high-speed printers in stores. A Barnes & Noble executive predicted that digital laser presses would be in bookstores within three years.

New Players

Mightywords.com specialized in producing and distributing original works such as essays, short stories, condensed books, serials, speeches and research reports. This type of content did not fit the typical profile for traditional publishers but filled a need in the marketplace. Well known authors such as Arthur C. Clarke, Toni Morrison, Newt Gingrich and Seth Godin had created original content exclusively for Mightywords.com. Mightywords was a launch pad for new authors and offered royalties of as much as 50%. The site included business, health, humor, literature, fiction, mystery and romance topics, among others. Mightywords received $20 million from Barnes and Noble in exchange for a 50% ownership. Time Warner and Random House were among several top level publishers that had agreed to make selected and excerpted material available at Mightywords.

Reciprocal was one of the leaders in digital rights management in 2001. It had developed secure methods of encryption, protection, billing and downloading of content, which included audio, text, graphics, software, and video. Reciprocal had joint ventures with numerous content and distribution companies such as AOL/Time Warner, Advanced Marketing Services, Sony, Harper Collins and Random House.

Books24x7 offered an innovative model in 2001. The venture-funded company was a Web-based aggregator of branded, high-value business-to-business content which was offered on a subscription basis to consumers. Since the site launched in September of 2000, over 10,000 subscribers, mostly corporate professionals, had agreed to pay fees of as much as $299 per person for unlimited access to over 1,000 technical reference books. The content access was by search engine and online viewing rather than by downloading. As an additional service, the site also offered hard-copy versions through an alliance with Barnes&Noble.com.

Books24x7 had partnerships with John Wiley & Sons, McGraw-Hill, Microsoft Press and MIT Press. Publishers liked the revenue-sharing model with Books24x7 because they generate fees every time a page of their content was accessed. Books24x7 was also outsourcing its core competency. It was licensing its patented search engine technology includes bookmarking and annotation capabilities to publishing, education and training sites.

Critics wondered about Books24x7's revenue model. One of the competitors of Books24x7, Ibooks.com began operations in 1999 as a retailer and aggregator of content, with many of the same publishing partners as Books24x7. By 2001, Ibooks had fired many of its staff and was refocusing on becoming an application service provider (ASP) offering content conversion, digital warehousing and distribution capabilities to book publishers, distributors and retailers. Creative destruction was alive and well in the publishing industry.

Netlibrary.com digitized books held by most major public libraries and institutions and made them available for downloading to student computers. Netlibrary had joint ventures with colleges and major publishers and was planning to make textbooks available in the Fall of 2001 using proprietary technology that allowed searching, browsing, highlighting and communication among professors and students. Over 3,500 traditional works of literature such as Hamlet, Canterbury Tales and Beowulf were also available in proprietary e-book version at Netlibrary.

Sample Competitor Moves. Random House executives had indicated that the company would invest aggressively in new technology, services and alliances. They intended to expand their digital archives of content in order to take full advantage of electronic publishing, short print runs, on-demand digital publishing and Web-based retailing and marketing. Harper Collins had recently launched HarperTools, a site for Web retailers which offered publicity plans, promotional material, jacket art, catalogues, ordering and tracking information. The goal, according to company president Jane Friedman, was to provide a higher level of service to retailers.

E-books. Online versions of books were generating losses, since installing new technologies and Web site backend operations were very expensive. Companies with deep pockets had the luxury and the staying power to experiment until profitable and scalable revenue models were fully developed. As many business-to-consumer sites had realized in previous years, online customers were loathe to pay money for original content. Many of the younger generations had been "Napsterized"; they had developed the attitude that all content had to be free. This notion was an imminent concern for many traditional book publishers.

E-book formats were numerous and were creating confusion for customers. Formats included Adobe PDF, Glassbook by Adobe, Peanut Press (for the Palm Pilot), e-Book-Gemstar and, more recently, Reciprocal (also for the Palm Pilot). While an Open eBook Format standard was used by publishers, not all devices could read every e-book format. The search functions of e-book devices made them especially useful for technical readers and mobile professionals that needed access to data.

The eBook by Gemstar was a dedicated electronic reading device holding from 6,000 to 130,000 pages of text. Models manufactured by RCA sold for $300 to $700 and weighed one to two pounds. Books could be downloaded via built-in modem or USB connections to computers. Copyright protection was accomplished primarily through encryption and the inability of the devices to store file-sharing software. Most major publishers had made at least some of their works available to Gemstar for the eBook, and some titles were initially made available only through the eBook in order to generate consumer interest.

Major technology firms were finding ways to leverage electronic publishing. In April 2000, Microsoft unveiled Pocket PC Windows, an operating system for palm-sized computing devices. Pocket PC supported e-books, digital music and Web surfing. It included MS Reader which recreated the sharply focused typeface that readers were accustomed to seeing on paper. Additional functions included bookmarks, highlighting, annotations and built-in dictionary access. MS Reader also worked in laptops. Many online book retailers offered e-books at prices 50% to 90% cheaper than traditional books.

Exhibit 1: Communication Industry Segment Rankings, Operating Income Margins and ROA°, 1995-1999*

Rank	Segment or Subsegment	1999 Margin	Rank	Segment or Subsegment	1999 ROA
1	Television Station Broadcasters	21.3%	1	Telephone Directory Publishing	26.5%
2	Newspaper Publishing	21.1%	2	Newspaper Publishing	20.0%
3	Radio Network Companies	19.6%	3	Consumer Magazine Publishing	19.8%
4	Business Information Services - Financial	19.0%	4	Business Information Services - Financial	15.9%
5	Out-of-Home Media	18.7%	5	Interactive Entertainment and Information	12.3%
6	Television Network Companies	17.6%	**6**	**Consumer Book Publishing**	**12.1%**
7	Radio Station Broadcasters	17.3%	7	Other Business Information Services	11.3%
8	Business-to-Business Communications	14.1%	8	Business-to-Business Communications	10.4%
9	Other Business Information Services	13.9%	9	Television Network Companies	8.8%
10	Interactive Entertainment and Information	13.9%	10	Traditional Advertising Agencies	8.6%
11	Consumer Magazine Publishing	13.1%	11	Business Information Services - Marketing	8.5%
12	Traditional Advertising Agencies	12.4%	12	Radio Network Companies	8.5%
13	Telephone Directory Publishing	12.3%	13	Business Information Services - Healthcare	8.4%
14	Specialty Publishing	10.8%	14	Specialty Publishing	8.2%
15	Business Information Services - Marketing	10.3%	15	Television Station Broadcasters	7.5%
:					
19	**Consumer Book Publishing**	**7.7%**			

°Combined results of 560 publicly traded companies representing 52% of total communications industry.

* Source: Veronis Suhler Communications Industry Report

Exhibit 2: Consumer Spending on Entertainment, 1995-2004*

1) Consumer Spending Per Person Per Year, 1995-1999

$ Year	Broadcast Television	Cable & Satellite	Radio	Recorded Music	Newspapers	Consumer Books	Consumer Magazines	Home Video	Box Office	Video Games	Internet	Total
1995	0	125	0	57	52	79	42	80	25	11	8	479
1996	0	139	0	57	53	81	43	86	27	11	13	510
1997	0	154	0	56	53	81	45	86	29	16	21	541
1998	0	166	0	62	53	84	44	92	31	18	28	578
1999	0	181	0	65	54	86	45	95	33	23	42	624
2000E	0	194	0	71	54	89	46	106	35	28	46	669
2001E	0	207	0	73	55	92	47	113	37	35	50	709
2002E	0	219	0	75	55	95	49	116	39	42	54	744
2003E	0	232	0	71	56	98	50	120	41	50	58	776
2004E	0	244	0	68	57	101	51	123	43	58	61	806

* Source: Veronis Suhler Communications Industry Report

Exhibit 2: Consumer Spending on Entertainment, 1995-2004 (continued)*

2) Growth in Consumer Spending Per Person Per Year, 1996-2004

% Year	Broadcast Television	Cable & Satellite	Radio	Recorded Music	Newspapers	Consumer Books	Consumer Magazines	Home Video	Box Office	Video Games	Internet	Total
1996	0	11.1%	0	1.0%	1.6%	2.2%	3.0%	7.6%	6.9%	8.9%	56.5%	6.7%
1997	0	10.6%	0	-3.4%	-3.4%	-0.5%	4.2%	-0.4%	6.5%	43.4%	57.6%	5.6%
1998	0	8.1%	0	11.1%	11.1%	4.5%	-0.5%	7.9%	8.1%	12.4%	32.4%	7.7%
1999	0	8.8%	0	5.6%	5.6%	2.1%	1.2%	3.3%	6.0%	24.3%	51.2%	7.9%
2000E	0	7.2%	0	9.4%	9.4%	3.5%	2.1%	10.8%	5.3%	22.9%	10.8%	7.4%
2001E	0	6.8%	0	1.8%	1.8%	3.2%	2.6%	7.0%	5.6%	22.4%	8.7%	5.9%
2002E	0	6.1%	0	2.9%	2.9%	3.2%	3.0%	2.6%	5.6%	21.5%	7.2%	5.2%
2003E	0	5.6%	0	-5.4%	-5.4%	3.1%	2.5%	3.3%	5.8%	18.0%	6.8%	4.1%
2004E	0	5.4%	0	-3.2%	-3.2%	3.1%	2.4%	2.3%	5.7%	17.1%	6.4%	4.2%
95-99 CAGR	0.0%	9.6%	0.0%	3.4%	3.4%	2.1%	2.0%	4.5%	6.9%	21.5%	49.1%	7.0%
99-04 CAGR	0.0%	6.2%	0.0%	1.1%	1.1%	2.5%	2.5%	5.2%	5.6%	20.4%	8.0%	5.3%

* Source: Veronis Suhler Communications Industry Report

Exhibit 3: Media Conglomerates by Income and EBITA, 1999-2000*

($ millions)

Viacom	1999	2000	99-00 Change	% 2000 Revenue
Revenues				
Cable networks	3,610	4,082	13.1%	17.0%
Entertainment	2,668	2,785	4.4%	11.6%
Video	4,464	4,960	11.1%	20.7%
Broadcasting	7,678	7,900	2.9%	32.9%
Infinity (radio& advertising)	3,540	4,013	13.4%	16.7%
Publishing	611	596	-2.5%	2.5%
Online	43	113	162.8%	0.5%
Other/intercompany	(276)	(471)	70.7%	-2.0%
Total Revenues	22,338	23,978	7.3%	100.0%
				% 2000 EBITDA
EBITDA				
Cable networks	1,296	1,566	20.8%	29.8%
Entertainment	321	369	15.0%	7.0%
Video	520	535	2.9%	10.2%
Broadcasting	1,050	1,459	39.0%	27.7%
Infinity (radio& advertising)	1,507	1,788	18.6%	34.0%
Publishing	74	71	-4.1%	1.3%
Online	(82)	(231)	181.7%	-4.4%
Other/intercompany	(228)	(297)	30.3%	-5.6%
Total EBITDA	4,458	5,260	18.0%	100.0%

Vivendi Universal	ProForma 1999	ProForma 2000	99-00 Change	% 2000 Revenue
Revenues *				
Music	6,005	6,959	15.9%	12.6%
Publishing	3,528	3,789	7.4%	6.9%
Film and TV	7,732	9,258	19.7%	16.7%
Telecom	4,119	5,547	34.7%	10.0%
Internet	2	51	2300.0%	0.1%
Utilities	22,062	27,907	26.5%	50.5%
Other/intercompany	2,866	1,774	-38.1%	3.2%
Total Revenues	46,315	55,285	19.4%	100.0%
				% 2000 EBITDA
EBITDA				
Music	884	1,218	37.7%	16.0%
Publishing	466	559	19.9%	7.4%
Film and TV	342	812	137.2%	10.7%
Telecom	520	1,372	163.8%	18.1%
Internet	(36)	(194)	441.2%	-2.6%
Utilities	2,867	3,731	30.1%	49.1%
Other/intercompany	76	95	25.0%	1.2%
Total EBITDA	5,120	7,592	48.3%	100.0%

* All figures derived from reports in Euros at exchange rate of 0.95 E/$.

* Source: Thomas Weisel Partners

Source: Vivendi.com

Exhibit 3: Media Conglomerates by Income and EBITDA, 1999-2000 (continued)*

Walt Disney	1999	2000	99-00 Change	% 2000 Revenue
Revenues				
Media networks	7,970	9,615	20.6%	37.9%
Studio entertainment	6,166	5,994	-2.8%	23.6%
Parks and resorts	6,139	6,803	10.8%	26.8%
Consumer (incl. publishing)	2,954	2,622	-11.2%	10.3%
Internet and direct mktg.	206	368	78.6%	1.4%
Total Revenues	23,435	25,402	8.4%	100.0%
				% 2000
EBITDA				EBITDA
Media networks	1,711	2,438	42.5%	48.7%
Studio entertainment	218	164	-24.8%	3.3%
Parks and resorts	1,977	2,201	11.3%	44.0%
Consumer (incl. publishing)	690	558	-19.1%	11.2%
Internet and direct mktg.	(184)	(359)	95.1%	-7.2%
Total EBITDA	4,412	5,002	13.4%	100.0%

Bertelsmann	1999	2000	99-00 Change	% 2000 Revenue
Revenues				
BMG Entertainment	4,166	4,778	15%	28.9%
Book publishing	4,253	4,332	2%	26.2%
Magazines	2,755	2,931	6%	17.7%
Printing	1,940	2,239	15%	13.5%
Television and Radio	N/A	1,665	N/A	10.1%
Multimedia	250	477	91%	2.9%
Scientific literature	462	684	48%	4.1%
Other/intercompany	(537)	(582)	8%	-3.5%
Total Revenues	13,289	16,524	24%	100.0%
				% 2000
EBITDA				EBITDA
BMG Entertainment	175	223	27%	12.6%
Book publishing	131	29	-78%	1.6%
Magazines	349	384	10%	21.7%
Printing	156	188	21%	10.6%
Television and Radio	90	357	297%	20.2%
Multimedia	(125)	(261)	109%	-14.7%
Scientific literature	25	64	156%	3.6%
Other/intercompany	451	786	74%	44.4%
Total EBITDA	1,252	1,770	41%	100.0%

Note: Some figures may not match exactly with those given in other exhibits due to variations in sources, classifications, fiscal year versus calendar year reporting, choices of exchange rates and effects of mergers.

* Source: Walt Disney 10-K Report

Source: Bertelsmann Annual Report

Exhibit 3: Media Conglomerates by Income and EBITDA, 1999-2000 (continued)*

($ millions)

NewsCorp	1999	2000	99-00 Change	% 2000 Revenue
Revenues				
Filmed entertainment	3,753	3,242	-13.6%	27.2%
Television	2,962	3,098	4.6%	26.0%
Cable programming	305	1,063	248.5%	8.9%
Magazines	1,181	840	-28.9%	7.1%
Newspapers	2,192	2,358	7.6%	19.8%
Book publishing	649	866	33.4%	7.3%
Other/intercompany	503	431	-14.3%	3.6%
Total Revenues	11,545	11,898	3.1%	100.0%
				% 2000 EBITDA
EBITDA				
Filmed entertainment	337	151	-55.2%	8.6%
Television	595	668	12.3%	38.1%
Cable programming	(44)	94	N/A	5.4%
Magazines	298	224	-24.8%	12.8%
Newspapers	465	566	21.7%	32.3%
Book publishing	45	79	75.6%	4.5%
Other/intercompany	34	(30)	N/A	-1.7%
Total	1,730	1,752	1.3%	100.0%

AOL/Time Warner	ProForma 1999	ProForma 2000	99-00 Change	% 2000 Revenue
Revenues				
AOL	1,618	2,059	27.3%	20.1%
Cable	1,406	1,594	13.4%	15.6%
Filmed Entertainment	2,387	2,411	1.0%	23.6%
Networks	1,732	1,793	3.5%	17.5%
Music	1,258	1,264	0.5%	12.4%
Publishing	1,333	1,429	7.2%	14.0%
Other/intercompany	(274)	(319)	16.4%	-3.1%
Total Revenues	9,460	10,231	8.2%	100.0%
				% 2000 EBITDA
EBITDA				
AOL	412	652	58.3%	26.9%
Cable	660	767	16.2%	31.7%
Filmed Entertainment	218	183	-16.1%	7.6%
Networks	447	443	-0.9%	18.3%
Music	198	178	-10.1%	7.4%
Publishing	267	290	8.6%	12.0%
Other/intercompany	(83)	(92)	10.8%	-3.8%
Total EBITDA	2,119	2,421	14.3%	100.0%

* Source: Multex.com

Source: Raymond James & Associates

Exhibit 3: Media Conglomerates by Income and EBITA, 1999-2000 (continued)*

Pearson, plc	**1999**	**2000**	**99-00 Change**	**% 2000 Revenue**
Revenues				
Educational publishing	2,619	3,300	26.0%	55.6%
Consumer publishing	815	1,100	35.0%	18.5%
Newspapers	1,074	1,300	21.0%	21.9%
Other/intercompany	475	230	-51.6%	3.9%
Total Revenues	4,983	5,930	19.0%	100.0%
				% 2000
EBITDA				**EBITDA**
Educational publishing	385	504	30.9%	50.4%
Consumer publishing	97	112	15.5%	11.2%
Newspapers	228	285	25.0%	28.5%
Other/intercompany	152	99	-34.9%	5.7%
Total	862	1,000	16.0%	100.0%

Note: Some figures may not match exactly with those given in other exhibits due to variations in sources, classifications, fiscal year versus calendar year reporting, choices of exchange rates and effects of mergers.

* Source: SEC filings and Business Week

Exhibit 4: Book Publishing Industry Net Sales, 1996-2000*

$ millions	1996	1997	1998	1999	2000	Change 99-00	CAGR 96-00
Consumer	9,962	10,005	10,521	11,246	11,071	-1.6%	2.1%
Professional	3,985	4,156	4,419	4,720	5,129	8.7%	5.2%
K-12 Texts	2,619	3,005	3,315	3,425	3,881	13.3%	8.2%
College Texts	2,486	2,670	2,889	3,129	3,237	3.5%	5.4%
University Presses	349	367	392	412	402	-2.4%	2.9%
Standardized Tests	179	191	205	219	234	6.8%	5.5%
Subscription reference	706	737	767	789	809	2.5%	2.8%
Other	493	510	526	542	559	3.1%	2.5%
Total	20,779	21,641	23,034	24,482	25,322	3.4%	4.0%
Consumer sub-categories:							
Trade	5,643	5,774	6,149	6,792	6,541	-3.7%	3.0%
Mass market paperbacks	1,554	1,434	1,514	1,552	1,559	0.5%	0.1%
Religious	1,093	1,133	1,178	1,217	1,247	2.5%	2.7%
Book clubs	1,092	1,143	1,209	1,272	1,292	1.6%	3.4%
Mail order	580	521	471	413	432	4.6%	-5.7%
Total consumer books	9,962	10,005	10,521	11,246	11,071	-1.6%	2.1%
Consumer books as % total	47.9%	46.2%	45.7%	45.9%	43.7%		

* Source: Association of American Publishers

Exhibit 5: Book Publishing Industry Net Sales Projections, 2001-2004*

	Actual	Projected				CAGR
$ millions	2000	2001	2002	2003	2004	01-04
Consumer	11,071	11,684	12,168	12,672	13,193	3.1%
Professional	5,129	5,243	5,522	5,815	6,121	3.9%
K-12 Texts	3,881	3,795	4,014	4,232	4,469	4.2%
College Texts	3,237	3,649	3,930	4,226	4,539	5.6%
University Presses	402	452	474	496	519	3.5%
Standardized Tests	234	249	265	283	302	4.9%
Subscription reference	809	849	882	916	949	2.8%
Other	559	559	559	559	559	0.0%
Total	25,322	26,480	27,814	29,199	30,651	3.7%
Consumer sub-categories:						
Trade	6,541	7,146	7,477	7,819	8,174	3.4%
Mass market paperbacks	1,559	1,546	1,616	1,685	1,754	3.2%
Religious	1,247	1,306	1,353	1,401	1,450	2.6%
Book clubs	1,292	1,338	1,380	1,424	1,468	2.3%
Mail order	432	348	342	343	347	-0.1%
Total consumer books	11,071	11,684	12,168	12,672	13,193	3.1%
Consumer books as % total	43.7%	44.1%	43.7%	43.4%	43.0%	

* Source: Association of American Publishers, Book Industry Study Group, Inc.

Exhibit 6: Major Consumer Book Categories, by Revenues, 1995-1999*

($ millions)

Category	1995	1996	1997	1998	1999	98-99 Change	95-99 Change	1999 Concentration Ratio*	
Art	140	141	141	143	144	0.7%	2.9%	67%	Top 3
Biography	375	381	400	400	405	1.3%	8.0%	40%	Top 4
Business	617	679	726	791	862	9.0%	39.7%	21%	Top 5
Children's	1,327	1,448	1,379	1,489	1,721	15.6%	29.7%	45%	Top 5
Computer	500	586	638	722	798	10.5%	59.6%	73%	Top 5
Cookbook	400	395	402	404	404	0.0%	1.0%	47%	Top 4
Gardening	175	192	190	195	197	1.0%	12.3%	51%	Top 5
Health	375	400	432	450	481	6.9%	28.3%	28%	Top 5
How-To	125	126	125	128	129	0.8%	2.8%	66%	Top 5
Mystery	350	350	345	350	356	1.7%	1.7%	67%	Top 5
Reference	535	510	500	498	501	0.6%	-6.4%	30%	Top 5
Religion	1,036	1,093	1,132	1,178	1,210	2.7%	16.7%	39%	Top 5
Romance	971	1,000	1,010	1,170	1,195	2.1%	23.1%	36%	Top 5
Science Fiction	500	487	475	480	482	0.4%	3.6%	44%	Top 4
Self-Help	462	500	538	563		4.4%	27.3%	65%	Top 5
Sports	100	105	110	115	117	1.7%	16.5%	50%	Top 4
Travel	142	143	156	160	168	5.0%	18.3%	66%	Top 5

* Sources: Simba Information, Association of American Publishers, Book Industry Study Group

Exhibit 7: 20 Largest US Consumer Book Publishers by Revenue 1999 vs. 1998*

($ millions except Revenues Per Title)

Publisher	1998	1999	98-99 Change	# Consumer Titles in 1999	Revenues Per Title ($) in 1999
Random House	1,610	1,691	5.0%	3,000	564
Time Warner	1,574	1,637	4.0%	805	2,034
Readers Digest	1,033	937	-9.3%	90	10,411
Scholastic	698	793	13.6%	591	1,342
Harper Collins	737	764	3.7%	1,700	449
Penguin Putnam	613	644	5.1%	2,451	263
Simon & Schuster*	565	611	8.1%	2,100	291
Encyclopedia Britannica	465	465	0.0%	N/A	N/A
Grolier	450	450	0.0%	N/A	N/A
Harlequin	355	375	5.6%	936	401
Holtzbrinck	275	346	25.8%	1,985	174
Hearst	210	214	1.9%	N/A	N/A
Rodale	225	203	-9.8%	120	1,692
Hungry Minds (IDG)	142	180	26.8%	700	257
Thomas Nelson	164	170	3.7%	200	850
Barnes & Noble	160	164	2.5%	N/A	N/A
Golden Books	150	136	-9.3%	350	389
DK Publishing	103	130	26.2%	550	236
McGraw Hill	124	129	4.0%	N/A	N/A
Andrews McMeel	115	121	5.2%	437	277
Total Top 20	9,768	10,160	4.0%		
Total Industry	23,034	24,482	6.3%		
Top 20 as % Total Industry	42.4%	41.5%			
Top 5 as % Total Industry	24.5%	23.8%			

1998 results are pro forma due to divestitures.

* Source: Simba Information

Exhibit 8: Ranking of Publishers by Sales in Categories, 1999*

(1 = top rank)	Random House	Simon & Schuster	Harper Collins	Penguin Putnam	Time Warner	Meredith	Rodale	Readers Digest	Hungry Minds/IDG	Harlequin	Harry Abrams	Abbeville	John Wiley
Art					2						1	3	
Biography	1	2	3	4									
Business	3	4	1										5
Children's	1	3	5	2									
Computer									2				
Cookbook	1	2			3	4							
Gardening	4				1	3	5	2					
Health	2	4	5	1			3						
How-To	2	3				4	5	1					
Mystery	2	3		1	4								
Reference			4										3
Religion	5		2	4									
Romance	2		4	3						1			
Science Fiction	1	2		4									
Self-Help	3	2	4	5									
Sports	1	2	3										
Travel	2								1				

* *Source: Simba Information*

Exhibit 8: Ranking of Publishers by Sales in Categories, 1999 (continued)*

(1 = top rank)	McGraw Hill	Pearson	Health Comm.	Microsoft	St. Martin	DK	Houghton Mifflin	Merriam Webster	Thomas Nelson	Tyndale	Kensington	Torstar	Golden
Art													
Biography													
Business	2												
Children's													4
Computer	4	1		3									
Cookbook													
Gardening													
Health													
How-To													
Mystery					5								
Reference						1	2	5					
Religion									1	3			
Romance											5		
Science Fiction												3	
Self-Help			1										
Sports													
Travel													

* Source: Simba Information

Exhibit 9: *New York Times* and *Publishers Weekly* Bestsellers, 1999-2000

1) *New York Times* Bestselling Consumer Book Publishers, 1999[*]

	Hardcover		Paperback		Total		% Share
Publisher	**Titles**	**Weeks***	**Titles**	**Weeks***	**Titles**	**Weeks***	**Titles**
Random House	79	675	73	556	152	1,231	33.6%
Penguin Putnam	34	262	33	178	67	440	14.8%
Simon & Schuster	30	236	30	258	60	494	13.3%
Harper Collins	27	148	23	231	50	379	11.1%
Time Warner	17	131	18	127	35	258	7.7%
Other	46	344	42	336	88	680	19.5%
Total	233	1,796	219	1,686	452	3,482	100.0%

2) *Publishers Weekly* Bestselling Consumer Book Publishers, 2000*

	Hardcover		Paperback		Total		% Share
Publisher	**Titles**	**Weeks***	**Titles**	**Weeks***	**Titles**	**Weeks***	**Titles**
Random House	69	505	55	377	124	882	29.2%
Penguin Putnam	39	269	49	266	88	535	20.7%
Simon & Schuster	29	166	31	196	60	362	14.1%
Harper Collins	29	196	29	216	58	412	13.6%
Time Warner	19	143	15	153	34	296	8.0%
Other	23	129	38	251	61	380	14.4%
Total	208	1,408	217	1,459	425	2,867	100.0%

* Combined weeks for titles.

[*] Source: #1 = New York Times bestsellers lists and #2 = Publishers Weekly

Exhibit 10: S&S Revenues in Categories in which it Ranked Top 5, 1998-1999*

($ millions)

Category	1998	1999	% 1999 Revenue
Biography	33	35	5.7%
Business	89	31	5.1%
Children's	114	130	21.3%
Cookbook	43	43	7.0%
Health	16	16	2.6%
How-To	10	10	1.6%
Mystery	31	32	5.2%
Science Fiction	43	50	8.2%
Self-Help	85	86	14.1%
Sports	14	15	2.5%
Other	105	163	26.7%
Total	583	611	100.0%

* Source: Simba Information

Exhibit 11: Audiobook Market Analysis, 1995-1999*

($ millions)

1) Audiobook Revenues, 1995-1999

	1995	1996	1997	1998	1999	95-99 Change
Audiobooks	347	387	428	479	527	52.1%

2) Leading Audiobook Publisher Revenues, 1999 vs. 1998

Publisher	1998	1999	98-99 Change	% of Total Revenues in 1999
Random House	73.5	77.2	5.0%	4.6%
Harper Collins	29.5	32.5	10.2%	4.3%
Simon & Schuster	27.5	29.7	8.0%	4.9%
Timer Warner	18.9	21.2	12.2%	1.3%
Others	330.0	366.7	-25.4%	N/A
Total	479.4	527.3	10.0%	2.2%

* Source: Simba Information, Association of American Publishers

Exhibit 12: Foreign Markets for US Books, 1999 vs. 1998*

($ millions) Country	1999 US Exports	98-99 Change	1999 Imports Into US	98-99 Change
Canada	831	2.9%	215	-4.2%
UK	261	10.0%	276	-12.2%
Australia	140	-11.4%	10	29.1%
Japan	84	-36.9%	54	-8.6%
Mexico	69	17.2%	23	32.9%
Netherlands	69	51.0%	20	12.1%
Germany	44	51.0%	51	-19.5%
Singapore	42	56.7%	89	-6.5%
Taiwan	26	7.9%	9	-0.7%
Belgium	25	N/A	20	0.7%
Korea	23	42.6%	29	11.1%
New Zealand	23	6.0%	3	140.4%
Hong Kong	21	0.1%	226	12.9%
South Africa	18	18.2%	N/A	N/A
France	15	31.2%	22	-7.8%
Brazil	15	-20.6%	N/A	N/A
Phillipines	14	36.9%	N/A	N/A
China	13	N/A	142	41.4%
Italy	10	10.1%	95	-7.5%
Argentina	8	-12.7%	N/A	N/A
Other	163	N/A	128	N/A
Total	1,914	3.9%	1,412	2.6%

* Source: 2000 Bowker Annual: Library and Book Trade Almanac

Exhibit 13: Sample Publishing Income Statement*

		% Sales
Total net sales		100.0%
Edition cost (paper/print/bind)	23.0%	
Plant costs	4.0%	
Inventory write-down	2.0%	
Royalty expense / write-off	28.0%	
Total cost of goods sold		57.0%
Gross profit on net sales		43.0%
Distribution fee / subrights	7.0%	
Total gross profit		50.0%
Operating Expenses		
Freight / warehousing	8.0%	
Editorial	4.0%	
Production	2.0%	
Advertising / selling	14.0%	
General & administrative	12.0%	
Total operating expenses		40.0%
Contribution income		10.0%
Other income	1.0%	
Operating income		11.0%
Plus: depreciation	2.0%	
Plus: amortization	0.0%	
EBITDA		13.0%

Note: Goodwill amortization excluded

* Source: Industry sources

Exhibit 14: Publishers' Profitability, 1999 vs. 1998*

$ millions	1998			1999			98-99
Publisher	**Revenue**	**Op. Income**	**Margin**	**Revenue**	**Op. Income**	**Margin**	**Margin Change**
Golden Books	194	(102)	-	166	(17)	-	-
Harcourt	1,445	199	13.8%	1,654	246	14.9%	8.0%
Harlequin	346	64	18.5%	375	61	16.3%	-12.1%
Harper Collins	737	37	5.0%	764	48	6.3%	25.1%
Houghton Mifflin	862	102	11.8%	920	112	12.2%	2.9%
Hungry Minds (IDG)	142	17	12.0%	180	23	12.8%	6.7%
John Wiley	467	62	13.3%	508	63	12.4%	-6.6%
McGraw Hill*	1,620	202	12.5%	1,735	274	15.8%	26.7%
Meredith	769	101	13.1%	774	120	15.5%	18.0%
Penguin Putnam	869	80	9.2%	909	105	11.6%	25.5%
Readers Digest	1,033	100	9.7%	937	167	17.8%	84.1%
Scholastic	1,058	48	4.5%	1,155	78	6.8%	48.9%
Simon & Schuster**	565	53	9.4%	611	54	8.8%	-5.8%
Thomas Nelson	253	25	9.9%	261	21	8.0%	-18.6%
Time Warner***	4,496	607	13.5%	4,663	679	14.6%	7.9%

* Educational and Professional Division.
** 1998 results are pro forma due to divestitures.
*** Includes magazine division.

* Source: Simba Information

Exhibit 15: Wholesaler Analysis, 1995-1999

1) Total Unit Sales By Wholesalers, 1995-1999

	1995	1996	1997	1998	1999	95-99 Change
Units	156	159	146	156	166	6.0%

2) Leading Wholesalers By Revenues, 1999 vs. 1998

($ millions)

Wholesaler	1998	1999	98-99 Change
Ingram	1,350	1,400	3.7%
Baker & Taylor	883	1,021	15.6%
Publishers Group West	100	120	20.0%
National Book Network	33	44	33.3%
Total	2,333	2,541	

Exhibit 16: Retail Outlet Analysis, 1996-1999[*]

1) Book Purchasing By Outlet, 1996-1999

Outlet	1996	1997	1998	1999
Large chain bookstores	24.8%	25.1%	25.3%	24.6%
Book clubs	18.4%	20.3%	18.0%	17.7%
Independent/small bookstores	18.6%	17.2%	16.6%	15.2%
Discount stores	9.1%	8.7%	9.2%	9.2%
Warehouse clubs	6.2%	6.0%	6.5%	6.5%
Internet	0.0%	0.4%	1.9%	4.4%
Mail order	4.7%	5.3%	4.9%	4.4%
Food/drug stores	4.8%	4.3%	3.6%	3.5%
Used bookstores	3.7%	3.4%	3.0%	3.0%
Multi-media stores	1.3%	1.0%	1.0%	0.9%
Other	8.5%	8.4%	10.0%	9.6%

2) Revenues of Largest Bookstore Chains, 1996-1999

($ millions)

Chain	1996	1997	1998	1999	1996-1999 Change
Barnes and Noble	2,448	2,796	3,006	3,486	42.4%
Borders	1,959	2,266	2,590	2,981	52.2%
Books-A-Million	279	325	348	404	44.8%
Total of Largest Chains	4,686	5,387	5,944	6,871	46.6%
All Bookstore Sales	11,547	11,824	13,179	13,662	18.3%
Largest Chains as % of All Sales	40.6%	45.6%	45.1%	50.3%	

[*] Source: Simba Information, Multex.com

Exhibit 16: Retail Outlet Analysis, 1996-1999 (continued)*

3) Revenues of Leading Web-based Booksellers, 1998-2000

($ millions)

Web Site	1998	1999	2000	1998-2000 Change
Amazon.com	610	1,640	2,762	353%
Barnesandnoble.com	62	202	320	416%
Fatbrain.com	11	29	N/A*	N/A
Borders.com	-	5	18	260%
Total	683	1,876	3,100	175%

*Fatbrain.com was acquired by Barnes&Noble.com in 2000.

* Source: Simba Information, Multex.com