Copyright Clearance Center
Beyond the Book
A podcast series on the business of writing and publishing

SPECIAL EDITION

Recorded live at the 20011 BookExpo America in New York City,
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The Arc of Publishing

KLEBE: Good afternoon, everybody… The Arc of Publishing, that's my topic today. I'm going to be talking about where publishing is going, what works, and how it's getting – and how we're going to move there. I work for Copyright Clearance Center. I've been there for 15 years. As a technologist, I've designed databases that hold tens of millions of rights for mass clearance of works across the publishing spectrum. I've designed DRM applications. And I've also written a couple novels. So I do a lot of things involved in publishing. I've been involved in the industry for a long time.

So I want to talk about the Arc of Publishing. What I'm talking about is predicting the future. And that's really hard, right? People get the future wrong all the time. In fact, I bet that soon people won't even try to predict the future anymore. Thank about it. But some futures are very predictable. An advanced readers copy, one kind of arc, is a prediction of the future of extremely good foreknowledge. It's what the real book is going to look like. It's easy to predict the future when you know what's coming.

It's like I'm throwing a ball to myself. If I throw the ball and it curves through the air, I know how to catch it. But that's not something I always knew. Right? That's something we have to learn. You throw a ball at a baby, and you're lucky if it even moves its head.

But when we learn the rule we can predict the future well enough to be able to catch the ball pretty easily. Most futures aren't that controlled, so the most we can hope for is that they're like a ball that someone else is throwing. If we see where it starts, if we can see it in flight, we've got an idea where it's going. With that in mind, let me ask, does the future of publishing have a predictable arc? Does this kind of curve look familiar to anyone out here? It's the S curve of growth over time as described by Clay Christensen in his book *The Innovator's Dilemma.*

We see over there at the left an early period of slow growth before a new model takes hold. Then a new model takes over and we have a period of extremely rapid growth, as a new entrant becomes a dominant player in a new market. Then as the

market matures, finally we see growth leveling off. This is a pattern typical of disruptive innovation, in which companies succeed by tearing apart the market as it existed before, and promoting a new one.

So where does the dilemma come in? Why does Clay Christensen call it a dilemma? And the problem is that when you're one of those companies up there on the far right, it's nearly impossible to recover the kind of earth shaking of innovation to kind of adopt the new models that are how you get to that period of rapid growth again.

Let me give you an example. Say you have a million dollars because you're a big mature organization, and you're trying to decide between starting an earth shattering new invention in which you might spent two years trying to find new customers, figure out whether it works. And at the end of that point in time, you might have zero return on that million dollars. Or you could spend that million dollars building a new sales office in the southeast region. It's obviously a better decision to go and build the sales office in the southeast region because you'll get a measurable predictable return from it, until the model changes entirely and you can't sell anything anymore.

The book *Innovator's Dilemma* shows dozens of examples of this behavior in wildly different industries, from steam shovels to disc drives. But here is a more recent example that hits a little closer to home. It is one of the big dotcom darlings, still a going concern with billions of revenue today. You see, just out of the book, an initial period of flat growth before the new model takes hold, then the stunning period in which revenue increases by four-fold over a mere three or four years. Then we have a peak around '07, and then a gradual tapering off. Any guesses? Well, it's Yahoo. And it must be said, I think Yahoo will be fortunate to get back to the revenue of 2007, let alone to surpass it.

So what happened? As it turned out, they got whacked by a disruptive innovator. And Yahoo's meteoric growth looks pretty flat compared to the ten-fold revenue growth of a player that entered just a little after they did. Never has a company's name seemed more ironic than at the bottom of this page.

So what is Yahoo's business? Yahoo has portals. Yahoo has – you know, they were one of the earliest Internet radio providers. And their business, from day one, has always been to get people to come to their site so they can show them ads that they had sold. Now Yahoo's ad model, although it was on the Internet, wasn't at all that dissimilar from ad models that prevailed for ages, and ages, and ages. Yahoo's ads were display ads, you know, which used to be little rectangles. Now they're the squares, and they have animation, or movies, or maybe even a game to show in them. And they were sold through a fairly high contact sales process to larger

corporations, with a higher price to get in, larger campaigns, and a longer commitment.

So who is the innovator that completely destroyed the advertising model on the Internet? And of course, we all know it's Google. Well what do they do? Google actually bought a company that had this fledgling, not too successful advertising model that they renamed AdWords. If you're a search engine this is a great model, because it's about placing ads against things that people search on.

Google didn't just take the technology though, they applied a new business model to it. These are not very impressive ads. They're just words on a page of the link. So they said we're not going to try to get thousands of dollars, or hundreds of dollars, or even tens of dollars per impression. They created a bidding model that allowed anybody to buy placements against their chosen terms. So you could get into advertising on Google with a budget of just a few dollars. Then they turned that around and allowed ads sold through this process to be hosted on any website through a modification called AdSense.

You can tell a lot of different stories about how Yahoo lost its way. But Google's disruption of the online ad market, which impacted Yahoo's revenue directly, has to be at the center. So this is also the story of the news business, by the way, despite the fact that Google publishes virtually no content of its own outside the company blogs. Because what business are newspapers in, after all? Advertising.

One way to look at it is that newspapers, if you are their customer, are selling you to the people who buy their ads. Advertisers historically value this access so highly they paid enough of it to support a fairly large amount of veritably altruistic journalism. Macy's never wanted to send war correspondents to Europe in World War II, or Vietnam in the '60s, or even Iraq in the '90s. But they were willing to pay enough historically that the *New York Times*, and every other newspaper, could afford to do so.

But what happened here is that the Web made it very easy and cheap to get new content out where anybody could look at it. And then Google and a few other companies learned how to turn all that new cheap content into ad inventory. Cheaper to get into, new people could buy ads, so that even though no new news mega giant has appeared to replace the ostensible function of news publishing, we can see the news business is again disrupted from below.

And the numbers back it up. These are all from the U.S. Census Department. They're self-reported numbers. We can see this huge tail-off in news revenue starting in about '05. And was this ad revenue? Well yes, it was ad revenue, because we can see that even through the end of 2009, newspaper subscription

revenue has been holding steady. And who'd have believed that? But, ad revenue has fallen off a cliff. And this also shows you that the newspaper business is all about ads. It's the same in mass market periodicals. We see that the revenue from subscriptions hasn't been tailing off nearly as fast as the revenue from ads.

If we add book publishing though we see a different story. Throughout the period of the news industry's decline, and indeed throughout the horrible economy in the last couple of years, the book publishing industry – and this is trade publishing, by and large – has remained remarkably, even eerily, steady.

It's nice not to have a dependency on the ad model when advertising is getting blown up all around you, isn't it? On the other hand though, here is another way to look at it. During that same period of time, the population of the United States has increased by 30 million people, or 10%, while book publishing has remained eerily steady, again. That's not the best trend.

So that's the Arc of the Innovator, and it repeats again and again. Yesterday's hot new innovator becomes today's industry leader, and eventually becomes next year's stumbling dinosaur. The real problem is what happens to you after your market is disrupted. It's not good.

The reason it's hard to see Yahoo growing its revenue beyond 2007's peak is that the whole game of online advertising, their business, has changed around them. The customers that they were good at selling at before have moved on, either to the new model and buying key words on Google, or they're buying display ads from Google too. Because Google used the enormous wads of cash that it was taking in from that low-margin business, to move up the value chain to capture those high-margin customers as well.

It's a lot easier to predict Yahoo entering a severe decline at this point, than it is to see them resuming their growth. The path that got them here won't work again. They need a lot more money than a lot of small customers flowing in to a tiny new business can make for them. The Internet property that they've given up on, search, is now owned by Google.

So who is Google worried about themselves? It's certainly not Bing. And it's certainly not, well, Yahoo, which is also Bing. It's Facebook. Because that has a – Facebook's business is, again, selling you to their advertisers. Same as Google. Same as newspapers before them. And Facebook can probably do that at a much lower cost per page than Google can.

So let's review the core characteristics of market disruption in slightly more detail. You start with a stable market. You have dominant players with well established

value chains. You have new technology entering that market that has the potential to deliver a similar service. And because it's different, one of the things you can do is it allows you to serve different customers who deliver lower margins than those bigger established companies can afford to sell to. In fact, they're taking up business that the dominant player doesn't even want, that they're walking away from, we can't worry about those guys. So then you mix the two together. We have new providers entering the market using new technology to serve new customers, and move up the value chain for higher margins. Hmm. Does that sound anything like the state of publishing today?

Well let's go point by point. We certainly have dominant players with the well established value chains. Some of these companies can write histories of themselves that stretch hundreds of years. But behind the big six you have literally tens of thousands of smaller independent publishers. And it's quite likely that every single one of them is trying to figure out how to win at ebooks, for instance, in one way or another. And the most obvious new technology that springs to mind is the ebook marketplace. So you've got new technology, similar service. Books, ebooks. Only one letter difference, right?

You certainly do have lower margins, right? Because ebook prices are way lower than the prices we're used to from print before. I saw a tweet from another conference earlier today where an analyst was saying that the average ebook sale prices was like $7 or so. And an average print book sale prices was over like $12. Is there a $5 difference in production cost per title to bring a book to the Kindle, or whatever, for a publisher than paper? Probably not. So that's where your lower margins come from. I think the margins look substantially lower.

So are the customers different though? Does anybody think that the people who are buying, these e-readers, to read books on them, are people who would not have read books before? So if I'm reading – if I'm a book-a-year guy, and there are a lot of book-a-year guys out there, am I buying a Kindle to make it easier for me to read my one book a year? Probably not. So let's hold on to that.

So that's disruptive change in a little nutshell. But it's not the only kind of change we see in the marketplace. There's change every day. Publishers start new imprints, shutter old ones. You know, up through a couple years ago Vampire books were totally hot, and now it's vampire movies instead. In the dawn of the ebook age, we have to wonder what kind of arc we're in. Is it an arc of disruption, or is it just one of the natural motions of a business adjusting to new entrants?

To figure that out, we first have to look backward a little way to see where the movement started. Everybody remember the ebook war? If you blinked you might have missed it. January 20, 2010, Amazon de-lists all Macmillan titles, ebooks and

print as part of a fairly hardball negotiating strategy trying to fight off a request by Macmillan. They were going to stand up there and hold solid for the benefit of their customers in the sacred $9.99 ebook price point, until January 31, a couple days later when they announced they were going to put Macmillan all back up.

It took them a little longer than that. If you remember, it might have taken more than a week, in some cases, to get all those buy buttons back up, to the extent that Amazon-Macmillan recently announced they were going to try to make their authors whole from the lost sales during that week. Because Amazon wound up – they were playing hardball with Macmillan. But the people they wound up really irritating were the authors and their readers. And authors were able to mobilize their readers to a degree that probably wasn't possible in the '60s or the '70s, or whatever.

So why am I pointing to this, where the movement started? It has to do with the changing sales model for ebooks. If we go all the way back to 2009, early days, ancient days, dinosaurs roaming the earth – I got these numbers from a *New York Times* article early in 2010. A $26 hard cover bestseller, half goes to the retailer, half goes back to the publisher. You've got some fixed costs over there to the left. Their numbers were maybe less than a buck for designing the book averaged out over a print run, maybe a dollar averaged out over the print run for marketing, any of the floating costs like printing, storing, shipping, returns. And then you have the author royalty and the publisher net very close to each other, very similar shares of the sale. And if you change the actual numbers around, this chart probably remains pretty ballpark accurate for decades.

Amazon, at that time, sold every Kindle book for $9.99, as strange as that may seem today. And it was on a 65/35 royalty share, where they kept the 65. So the economics of this are completely different. If the publisher is taking home $3.38 from a $9.99 sale and has those 80¢, or a dollar or so marketing costs, they have to pay the author, the publisher is not going to make any money on that. So they didn't do the design, they didn't do the marketing, so you had very poor looking ebook editions back then. And you had no marketing to speak of. It was piggy-backing on whatever they did for the paper. Obviously, this would seem like a strong motivation to delay the introduction of the digital edition to capture profits from those higher revenue formats first. More like a very unprofitable paperback.

So what happened right around the beginning of 2010? Apple. And not just Apple, but it's Apple's willingness to entertain the agency model, in which publishers were able to set prices. The seller acts as an agent for the sale, rather than as a retailer. And it's a 70/30 split, but this time the publishers keep the 70.

One of the earliest leaks of information about the iPad was one that says not only is there going to be an iPad, they're going to have a book store and do the agency model. And this was publishers working with Apple behind the scenes pre-launch. An agency sale looks completely different from that retail model ebook. Publisher net of a $12.99 ebook is almost $7. The retailer is still making money on that, and the author is getting $2.27 out that $12.99.

One of the signal differences here is that, although the shares are certainly better than they were in the $9.99 ebook, but the publisher share and the author share are no longer very similar. The publisher is able to keep a lot more of this, according to the prevailing royalty model. So it's no wonder that Amazon chose to push back on this model, since they were losing the benefit of that 65 share they were getting before. But they did give in. And by now, all of the big six now employ the agency model at least some of the time. And Random House was the last to join.

But there is a twist on how Amazon implemented it. Because they also opened – this market opened to everybody who wants to upload a book, pardon me. But if you're not one of the publishers they have a special agency deal with, to get that 70/30 share you have to price between $2.99 and $9.99. And the price has to be equal to the lowest available on any platform. And these are important provisions that continue Amazon's overall strategy of pushing book prices down to the lowest possible that their providers will tolerate.

Amazon's move here created a new value chain. It wasn't just like the publisher to the etailer to the reader anymore. So think about new providers using new technology to serve new customers. The new customer for Amazon and the other etailers isn't the reader, it's the author. They're offering a publishing service and access to a market to existing customers of the dominant players at a much better price. So this has given rise to a new phenomenon never seen before, I think, in the history of publishing. The successful self-published author.

So if we dig into this, we can call it The Author Scenario, the thrilling tale of the brave men and women who strike out for the great unknown turning their backs on the three-book deal and the end-cap at Barnes & Noble, for the uncertain promise of higher royalty rates from ebook retailers. So it's about cutting out the middle man with the publisher as the middle man. And I'm sure publishers, on the whole, over centuries, have not thought of themselves as being the middle man.

There is a very vocal proponent of this model, a successful thriller-suspense author, named Joe Konrath, who also writes as Jack Kilborn. Now, he wasn't always – he wasn't a Kindle native author. He didn't get his start there. He went the traditional route, had a standard actually pretty good mid-list deal, three books, six figure, and

he has blogged his progress for a year. And nobody has ever, as far as we know, worked harder at promoting his works through the standard channel.

Authors in the audience, think about making 500 bookstore visits in 55 days. He did that. I think he says he did over 1200 by the time he stopped doing that. But now he publishes his new work in his back list to the Kindle, and only on the Kindle and the other etailers.

In January, he says he made more in that one month than he made from his third novel, *Rusty Nail*, in five years from all channels – hard cover, paperback, foreign rights, translation, everything together. So that's a powerful story. As you can see, one of the things that works for him is a lower price and that 70% cut that he gets.

But he's not the only one doing this. And a number of authors, that you may or may not have heard of, have enjoyed success to a greater or lesser degree. Let's look at some of the common factors we see in these authors who have experienced this success.

First of all, they're pretty good authors. Their work is solid professional, for the most part. It's not like there is a – they're not the slush that you do see in that stock. They also, a lot of them, have literary agents. And that's sort of the matrix style, a literary agent I guess. What does an agent do? There are a lot of things an agent can still do. If you were here the last time, we had an agent from the Andrea Brown agency talk about how one of her authors wasn't getting a real book deal, so they helped launch that author as a Kindle author. And that's a very interesting approach.

There is also contracts. More complicated, more subtle differences from prior contracts. Authors aren't good at everything, especially contracts. So another thing that all of these authors have in common is that they're all genre fiction. They write thrillers. They write romance. They write science fiction, urban fantasy things like that. Of course, these are the most popular sections of fiction, particularly romance. And then you also have people who are readers who are more open to authors they've never heard of before. Because I know it's a romance, it's got the right cover. I know it's a thriller, it's got a gun on the front of it.

And finally, of course, there is price. I mentioned this a minute ago. All of these authors, without exception, publish their works well below the original $9.99 threshold, the top end of what Amazon will allow them to charge, and which is, of course, well below the $12.99, $14.99, $15.99 that publishers are releasing the major author titles at.

But what's interesting is that many of these authors who've been successful with these lower prices have found that there is movement in both directions. If you go down too low and keep it there, that's some kind of quality signal in which your work just looks like it's part of the masses. Whereas, at the $2.99, $3.99, and $4.99, you're in the middle of what most of the most popular authors are using.

Interesting though, how much of the success of these authors is just that they're cheaper than Lauren Hillenbrand, James Patterson, and so on? Does this hold up over time as this generation of author gets famous? Does it affect prices, as a whole, throughout the industry? And this is something we all have to be very concerned about.

One thing that's very interesting though, and I don't think many of the authors acknowledge this, is the first mover advantage that all of them are enjoying. By definition, they're all early starters. That's one way that price helps them, because you're more willing to go to someone you've never heard of if it's one-third the investment.

One of the authors that Joe Konrath talks about benefited from being the first urban fantasy author available on the Nook, which meant that she went right up to the top of the urban fantasy best seller list on The Nook. And that proved a huge promotional benefit for her. And because she was good at it, her books were good, she managed to hold on to high rankings and sells tens of thousands of units a month.

You can't discount this first mover advantage effect. It's exactly what Gladwell talks about in *Outliers*, where if you're good at what you do and you hit a new market at exactly the right time, you have a huge advantage over people who tried too early. And that advantage will evaporate. So the people who come after you may never be able to achieve the same kind of sudden success.

So where does all this go? Because I've read articles in *The Wall Street Journal*, *The New York Times*, all over the place, on this scenario, this author direct scenario. But most of the discussions I see treat this as an end state. So you have this centuries old multilevel market with sophisticated powerful players with tremendous revenue today transforming organically, over a couple of years, into a single-level market with a mass of essentially individual contractors, selling their wares to two, maybe three or four highly technical retailers. And then it stays that way. I find that inconceivable. There's another movement that's going to come into play that's going to shake that up as well.

So let's look at some of the pressures that would develop in this unstable market. Say you have a almost successful Kindle author doing almost OK, wishing she

could do better. Let's have a couple more, because there will sure be plenty of them. Individually, they're just scraping by. But if they join forces they might be able to hire someone to help them out, maybe a cover artist, one with experience for designing Amazon style thumbnails.

That's a big difference. Traditional books are designed to look great and stand out from across the room. And then when you shrink it down into an inch and a half by an inch, it looks like a muddy thing, maybe clashing fluorescent colors, and you can't read anything. So the cover artist is willing to work for the three of them maybe at a lower rate, because he's getting three jobs at once instead of one. Probably there's a freelance editor looking for work, because authors need editors, and signs up to work for with a couple of them for a fee or for some royalty points. So things start to pick up.

As a group they start to get occasional mentions in high traffic blogs, or whatever, that they talk about books a lot, like Whatever, or Boing Boing, or the The Awl. And sales really pick up after one of those. And they realize they could do even better if they had someone working on promotion more often. And all of a sudden you've got a publisher. Because every author, for that matter every person, isn't good at every task in any value chain, let alone publishing. There are structural advantages in collaboration. That's why corporations form in the first place. It's cheaper to hire an artist, or an editor, or promoter to do a bunch of jobs at the same time than to hire three artists to make one cover each. It's another natural arc of business, the arc of consolidation. It's a movement that's driven by transactional costs and relationships. And it's happened in every healthy marketplace since we started to be able to pay attention to such things.

That won't be the only one. Over time, more and more of those appear. And it doesn't have to be that sort of organic, like let's raise a barn together and hold a concert kind of consolidation I just talked to right there. You'll have venture funded start-ups trying to (inaudible). You've already got them. I mean, you've got Smashwords. You've got FastPencil. You've got some – Story Plan was a new kind of publisher that was just talked about at the last panel. They're stepping in to provide services from the publishing value chain. Maybe they're trying to do the whole value chain. Maybe they are just doing a piece of it. Who knows, maybe a really enterprising start-up with a financial bent might start to offer authors loans against future royalties, and then call them advances. Not quite the same thing. Maybe a few of these organizations consolidate as well, just so they can handle more authors or cut better deals with the retailers. Authors start wanting to belong to these organizations, so they're outside banging on the glass.

If you're the guy in the middle, guy or whatever in the middle, you have to be selective. You can't offer the full credit, the full brand, the full power of the

organization to every guy who writes a book about his goldfish. So what's the difference between this and a publisher? You've got gate keeping. You've got overhead. You've got relationship management.

But one thing to pay attention to is that I haven't mentioned anything so far that would cause this organization to purchase rights from the author, and hang on to them for awhile. But you could see that too. If you put the full force of your brand, your credibility, your relationships behind an author, you're going to want some kind of payback over time. And you can imagine, after awhile, it could get pretty hard for an author without the advantages of these kind of publishers. You could still list your works with Amazon, or whatever. But the kind of valuable promotional space that really drives sales is going to be harder to come by. Can you see the two indies here? It's pretty crowded.

Larger organizations naturally develop better relationships with the retailers. It's easier for the retailer to work with a huge group as a single unit, rather than as a bunch of individuals. The deal that Macmillan gets with Amazon is different from the deal that Joe Konrath does, although Joe Konrath is pretty special to Amazon right now. So some of these organizations could be very well these same organizations that we are familiar with today. An earlier panel I saw tweeted a lot, they were asked what percentage of the big six will be around in five years? Two of the three panelists guessed 50%. And the other one guessed 100%, but half of them will own the other half.

But there is another force that we haven't talked about yet, and that's competition. Let's focus on those little guys down along the bottom border of the slide, the etailers. These proportions are all wrong though. If you're looking at trade publishing as a whole, it's something like this. Amazon dotcom has 25%, somewhere between 22 and 28%. I've seen different numbers. Barnes & Noble slightly less than that today. And looking at trade publishing as a whole, Apple barely figures, Google barely figures.

Has anybody bought a book from the Google ebookstore yet? Data point.

(laughter)

If we look at ebook publishing only though, it's more like this. I've seen throughout this year numbers for Amazon at around 80%. Somebody was saying it was around 65% earlier. But I'd be a little surprised at that. Apple. The other guys are basically bit players at this point, despite the holiday success of The Nook, the launch of the iPad and it's apparent – they claim a million unit sales in their first year. And again, Google ebookstore.

If we add the publishers to this based on market cap, it's more like this, Amazon is a way, way, way bigger company than any major publisher. Sol (sp?) stated earlier today that the entire publishing industry was around $60 billion in revenue, which is on order of magnitude what Apple does. So these are very big companies that have a lot of power of their own.

Now in the specific domain of ebook publishing, publishers were able to win the ebook war against Amazon, because they had what Amazon needed, the titles that they needed to sell. Publishers are still strong. They swing a lot of weight in publishing. Well, hence the name, publishers. But if they were severely weakened, relative to Amazon, Amazon would have no reason to leave so much money on the table with its authors.

In a hypothetical world where most of Amazon's book sales came from independent authors, not through publishing deals, Amazon would have no reason at all to maintain the 70/30 royalty split. So that's one arc. And the consolidation competition affecting that arc of destructive innovation. But this is typical in these scenarios. It's not actually a really bad thing to be one of those wealthy high-revenue powerful companies at the far right-hand of the graph. It's what every company aspires to, to have revenue, power, relationships.

So although this period of disruption can be a tough scenario for publishers, I'm not at all convinced it's game over. You know, publishers can still compete with it. The canonical advantages of the mature company are revenue and other resources. So if there is a contest, if there is a battle that comes down to – that money and relationships can win for you, those little guys at the left-hand side are not going to win. The big companies win those every time.

So big publishers will use, and we'll see this continuing, their financial resources to win and retain their star authors. They might even have a chance at a best case – how many people talk about best cases for publishing these days – where the digital only market functions as a kind of minor league, where authors develop off-publisher payrolls and migrate to big publishers only as they become reliable sellers.

Here's another curve. It's author revenue against the number of authors. What does this mean? Well it means that at the left-hand side we have a very small number of very successful authors who deliver huge revenue to their publishers. You know their names – Stephenie Meyer, J.K. Rowling, James Patterson, all of those people. And in fact, those authors make so much money for their publishers that when Stephenie Meyer has trouble figuring out what the next vampire book is going to be, Hachette has to mention it on their financial filings. It's a material impact if there’s no new vampire book this year. Oh yeah, oh yeah.

So naturally there are a lot more authors with a very little revenue. And actually, this looks like it's the standard asymptotic curve, but if you add in traditional vanity publishing where the author is paying to be published, that line goes below the X axis. There are authors who function year after year at a net loss. So publishers have to spend money to bring books to market. And think about formatting, do I go ePub and key in my own meta data? Do I do paper? You know, all that stuff. And they also have to pay authors. So over at the right-hand side you have authors who don't earn back their advances, let alone the cost of bringing them to market. There's a loss.

Here's their revenue leftover. That's the green. And it's heavily weighted toward the left. So this means, as I was saying, that if you lost that right-hand side of the tail, it wouldn't be a bad thing. Your returns are better. You're making more money. You're more profitable. In fact, even if you lose a few of your solid mid-list entries, you could – it's not game over. It's a real challenge, but you can continue to work with that. It's when you lose the top end of the curve, the left-hand side of the graph. The big ticket authors, if they start to go over, that really leaves a mark. There's a real challenge there. So the next question, how is that looking so far?

Let's read that classic *A Tale of Two Authors*. The first author is Barry Eisler, award winning author of eight thriller novels since 2003, a solid mid-list author maybe on the upper end of the mid-list. Eight books in eight years, all of them good sellers. He's getting movie rights sales. This is a Japanese language movie, but Gary Oldman. And so he is doing well.

The second author is Amanda Hocking. I hear her name here a lot today. She has self published nine novels on the Kindle since January 2010. 2010, January. Estimated sales in January 2011 alone – remember, January 2009 she didn't have anything out yet –450,000 units, not dollars. Units. And she tried for years to find a publisher through the traditional route. And she apparently has another eight books in her desk.

So why do I care about – why am I comparing these two? Because within a couple of days of each other, in March of this year, they both made major announcements. Barry, on March 21st, turned down a half million dollar two-book deal from St. Martin's Press. Amanda, on March 24th, signed a $2 million four-book deal with St. Martin's Press. That must have been a hell of a week in those offices.

So Barry had a very nuts and bolts business oriented return on investment approach to the decision he made. He thinks he identified a break-even point around 2014-2015, where he would have made more money under the old deal. But by owning

his own rights, having a bigger return on just the digital stuff, he would have made it back. So solid savvy marketing based decision.

Amanda Hocking, on the other hand, has already made millions from her books. She is looking at people who couldn't get them. You can't find her books in a book store. You can get them in hard cover from POD. So she wants to reach new readers, and probably the remaining 65% of book sales that still come from the print.

Interesting, one of the bidders for her rights was a novel entrant, as it were, a partnership between Amazon and Harcourt, where Amazon would deliver to the digital end of the deal, and Harcourt the print. Went with St. Martin's anyway. But Amanda had a very thoughtful approach as well. And she has a great understanding of how she got where she is – the impact of luck, the impact of being good enough – that her story isn't going to work for everybody equally well. Every case is different. As she says, every author is different. That's true for all of us as well, because opportunities vary tremendously depending on who you are and what you want to do.

New value chains always open new opportunities for new players. All over the place you hear of new straight technology plays. There is a rich ebook vendor of the month, virtually, tool developers for people to produced enhanced ebooks as well, and new ways to deliver services to authors. I mentioned, you have Smashwords. You have the Story Plan. A guy here before is a new completely author-focused deal in which they're solely focusing on new authors. So some of the new technical plays are pretty interesting, and they have really different approaches.

The Elements was one of the first really big selling book apps for the iPad. It was created by a guy named Theo Gray. He wrote a very successful coffee table book about the collection of elements that he amassed with his *Mathematica* millions. So he wanted to use his technical abilities to deliver this content in a much richer more vital format. And he actually has 360 degree rotating videos of all of his pieces of metal, and so on. So he wrote software to create an active multi-media sort of database oriented application, like this, with 114 different elements, as it were. And he has now formed a publisher, and he has brought to market, since the success of his initial volume, two more from other authors, one on the solar system and one on gemstones.

Al Gore has a new book called *Our Choice.* And he brought it to the iPad app market, again with the help of a technology partner called Push Pop Press. And this is a very slick, very well produced offering. Everybody who looks at it says the scrolling is gorgeous, the video, the photograph integration is terrific. But this is

much more traditional content. This is page oriented content. You can see the print down at the bottom. You scroll through it and you go from chapter to chapter. So a completely different kind of work from *The Elements*.

And if we really bust out the creative stuff, we have *History of Jazz* by a firm called 955 Dreams, which is video, it's music, it's graphical elements, animation, and text about the history of jazz. So you can read about Miles Davis, and you can see video and hear recordings from him at the same time. There is no way that you could deliver this rich an experience through a traditional paper formatted book.

And finally, I want to talk about *Alice for the iPad*, another very early successful book delivered as an app, in which the combination of classic Tenniel illustrations and some new illustrations were given life with the introduction of a physics engine. So you see that watch that dangles realistically back and forth. There are pages where there is so much animation it's almost like a game on those pages.

Now this was written by essentially a – I think it was one man, or a very small shop, that then went into the business of producing these books. And now they have a – the original company is Atomic Antelope, which became part of Smashing Ideas. You may have heard Smashing Ideas mentioned a couple of weeks ago when Random House bought them – excuse me, Bertelsmann, AG bought them, the parent company of Random House. So that's the power of a mature organization, by the way. They have the money to drop tens or hundreds of millions of dollars on new providers that they can see leveraging to get into a market. And that's also consolidation in action.

Let's look at a completely different way for new providers to add value. This right here, I'm sorry if you can't see the text. It's a page from a highly customized ebook collection of the poems of Yahuda Halevi, which was produced for Nextbook by a company named Philidor, a small press that specializes in Judaica. Every page is different. Every page is sized to fit the size of the poem that it offers. The text is arranged carefully for balance and aesthetics. Philidor even designed a brand new Hebrew type face just for this edition based on the work of Yom Nivea and the *Polyglot Bible*, which is held to be a landmark of the art of Hebrew type design.

I love this example, because Philidor isn't a high-tech company. It's a small press. It's got a lot of small press skills. Their type face design work is one of the most unusual things they do. But it shows that in the turn to digital, you don't need to be a software developer. It doesn't need to drive out the turn to beauty.

And how does digital help this? Well how could you deliver a book where every page is a different size in paper? It wouldn't sit right on the shelf. And how could afford to design a new type face unless you could put it on really nice paper so you

could tell the difference. And then you'd have a really expensive book for a really small audience.

Digital distribution makes this kind of innovation economical. So they're not a tech company even though they're providing a technical service. This is key, because the opportunities that you want to pay attention to are the ones where you can make a difference. So authors, I know you're in here, of course you have to know your rights. Where is your back list? When do you rights revert? There is a very interesting question I'll mention. Let me put on my I am not a lawyer hat. It has a long plume coming out of it.

For older works, published before the dawn of the ebook age, there is a case. There was a case that never quite went to trial to determine whether publishers owned ebook rights for things that were published before there were ebooks. It's called Rosetta v. Random House. Rosetta was a very early ebook producer. And they said, well, it doesn't say ebooks in the – these authors came to us. We looked at these authors. They don't have ebook in their contracts, so how could you have the rights? And Random House says when we publish something in book form, well that meant ebook. And unfortunately, this was never settled.

So this case, the two parties, came to a settlement that did not resolve the legal question of whether Random House was right or Rosetta was right. So this is something that authors need to pay attention to, particularly if you've been in the market. Who owns your rights? How do you get your rights to revert? Are you getting the best return on your material? And if you're a new author, what's most valuable to you? Because if you want the end cap at Barnes & Noble, well Amazon is not going to get that for you with the Kindle.

Agents, step back out of the matrix, come back into the publishing world. So take care with contracts, because very subtle differences have started cropping up in new author agreements that affect who owns the rights and what rights are conveyed. If you're an agent, you're helping the author find the best return, that's what your existing business model helps you do, find the best return for the author however the work gets published.

Very interestingly though, as recently as like two weeks ago, *Publisher's Weekly* reported the U.K.-based agency Ed Victor had launched its own ebook and POD parent and publishing arm called Bedford Square Books. And they were launching with half a dozen other clients' back-list books. Andrew Wylie tried a similar move last year. Other agencies appear to be considering similar moves.

So that's agent as publisher, a completely different model, possibly fraught with conflict, possibly the way that agents have to act in order to do the best for their

clients. So one of the things that makes this happen, of course, is how slight the hard technical barriers are, how low the barriers are to entry to become a publisher. You can deliver print. You can deliver digital without owning any presses or big type setting shops. Things always go both ways though.

I read in Futurebook, which is a European book publishing blog, Random House had negotiated directly with Tom Sharpe, who is a hysterical English humor writer, for his back-list digital rights bypassing his agent. So that's how everyone is trying to figure out which way things are going.

Technologists, I mean, you know there is a new ebook of the month – rich ebook vendor of the month publications, those are currently produced and sold on almost a consulting model, where Al Gore hires Push Pop Press. Other players do one off, or two off, or three off. There is no real common technology basis to deliver really the ebook application, which goes into the app store, as opposed to the enhanced ebook. Tools aren't great for enhanced ebooks either, with EPUB 3 just coming out now.

I think there is a big discoverability problem with the app store today with regard to books. If you love a rich ebook by your favorite author, how do you find the other one? It's not easy. Apple's apps were not designed for books. So if there is a discoverability problem, there's got to be a discoverability opportunity as well.

Publishers, you have to know your rights. I'm sure you're already on that, but the very interesting point is how do you manage the P&Ls for ebooks versus the print books by the same author? Are ebooks a different division? Do you have a digital division that's competing with the print division for sales? Maybe the best return on a title on the rights for that title might be to consolidate those P&Ls. I've been hearing today that that's just something that's under consideration, but isn't there yet.

The price competitiveness issue is not going to go away. Would you make more money per title as opposed to per reader at a lower price entry point? Are those higher price points going to survive as more and more enters the market? And of course there is the specter of, since virtually of the ebooks published by publishers since the flexible pricing entered have the same price, there is an explicit competitiveness issue as well.

If you're building a digital vision do you build it, do you buy it, do you outsource? You probably just can't just buy a bunch of digital experience in one company and bring it in house, and talk to it through your traditional publishing agency. You're going to need people who are invested in your organization, or committed to you

organization who are familiar with the digital world, who can talk to and manage those people.

Overall, if your authors can sell their ebooks better than you can, you're missing an enormous opportunity to leverage the power and resources you have at your disposal as a mature organization. But no matter who you are, you are, and you and you alone, are responsible for predicting your own arc. Nobody is going to catch the ball for you. So where do you want to go, and how are you going to get there?

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