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***FASTEN YOUR SEATBELTS: THERE IS TURBULENCE AHEAD.
FUNDAMENTAL CHANGES AFFECTING THE BOOK INDUSTRY.***

Ladies, Gentlemen, dear friends and colleagues all,

We open today the 2009 edition of a very successful Frankfurt Book Fair, with a heavyweight as a Guest of Honour: China, whose influence, both in ancient and modern times, is undeniable today.

Ages of turbulence

As a tribute to China, I want to start with a quote from Lao Tse, “the Old Master” that gave birth to the Tao Te Ching (“way of virtue”) more than 2500 years ago, fundamental for understanding Chinese history and philosophy (Taoism, Confucianism), which arrived to the Western World in the XIX century. As you can appreciate, most of its lessons are applicable today, and allow summarizing what happens today in the book industry:

“Life is a series of natural and spontaneous changes. Don't resist them - that only creates sorrow. Let reality be reality. Let things flow naturally forward in whatever way they like.”

Still in the domain of quotes, I like to remember you the most famous opening sentence in modern literature, that comes from Anna Karenina, from Lev Tolstoy, and helps understand quite well what happens today in the publishing world:

“All happy families are alike, but each unhappy family is unhappy in its own way.”

I do not want to explore right now my personal interpretation of this very powerful sentence; instead, I will leave up to you to decide the happiness level that applies to the publishing industry, today, or, better said, to where is migrating this happiness that characterized the publishing industry a few decades ago.

Last year, a good friend of mine and very recognized author - also one of our most important authors in Planeta's catalogue - Paulo Coelho, shared with us his views concerning the importance of sharing ideas, and the enormous leverage that Internet provided to achieve this goal.

We all share Paulo's views, in the sense that, as publishers, we would not accomplish our goals if we would not leverage, as a means of creating readers, on Internet and all diffusion technologies at our reach.

The role of the publisher - a job description

But we have to keep in mind that the publisher's role relies on two well-defined axes:

- 1.- Contents creation.
- 2.- Contents distribution/diffusion.

Let's have a brief view of the publisher's role.

As in financial markets, the publisher's role involves a pretty strong market-making component. Indeed, we, as publishers, advance payments in terms of allowing novelists time to write; in some other publishing lines, we have in our own companies very professional colleagues creating contents. In addition to that, we finance the physical book production process, and we also design and execute marketing campaigns. Of course, we do the book logistics - also the reverse logistics - out of some book warehouses that we have built and manage, we send our commercial people to fight for space in the bookstores, and we keep good financial and administrative tracking of all this process, communicating authors and agents the results of our common effort, and sharing with them the financial results, complementing our advance payments with royalties.

As you can see, there are several roles embedded in the definition of publisher. And, in the same way it would be ridiculously simplifying to reduce Internet to down to diffusion, because, in fact, it is much more than that, since it allows new marketing perspectives, simplifies enormously content preparation and distribution - making it much more economical - , and opens new venues in terms of new publishing lines, it would be a great mistake to deny the value - added capacity of today's publisher, which entails all endeavours just mentioned, of which, I would like to stress:

- Market-making commitment, risking money to allow contents to be created.

- Selection criteria, which is a reference for readers, and allows them to navigate in a very dense ocean of contents.
- Own interdependence with the contents-creator, the author, very distinct of the new ways of distributing contents that we can anticipate.
- And, very importantly, the existence of real competition among publishers, a fact that allows authors to choose, and to get an adequate remuneration from them (as opposed to what you can anticipate in a near future).
- Lastly, it would only be fair to mention that today's publishing industry is not financed by advertising revenues, which allows a greater degree of freedom, in terms of contents creation and diffusion, compared with some other content-driven industries, such as radio, television, cinema, magazines or newspapers.

The idea of Europe

In an enjoyable, fascinating lecture delivered at the Tenth Nexus Lecture 2004, titled as "The idea of Europe", the well known scholar and humanist George Steiner asked a fundamental question, prior to give his own definition of what Europe is.

The question he posed was: "Why would we need an idea of Europe in order to conduct the day to day business? I would like to draw a somewhat unfair parallel, and to apply Steiner's question to today's situation of our publishing industry.

And Steiner's definition of Europe, probably one of the deepest we can come across, involves five axioms/concepts:

- 1.- The *coffee houses*, which pave European cities, and which have produced a profound mark in European culture, specially in the XVIII and XIX century. Opposed to British pubs or to American bars, "*European cafés*" have witnessed crucial episodes in European culture and literature.
- 2.- The *landscape*, on a traversable and *human scale*. In an American age, dominated by technology, it's difficult to imagine intellectual and poetic travelling as Sterne, Hölderlin or Wordsworth. In America, but also in Asia, Africa and Australia, large and empty spaces occupy the territory and travelling is dominated by technology, more than by patience and human contact.
- 3.- These *streets and squares named after statesmen, scientists, artists, writers*, as opposed to other more rational ways of dividing cities: streets and avenues, combined with numbers, and geographic references.

4.- *Europe's twofold descent from Athens and Jerusalem.* Europe can be defined as an intellectual invention combining - not always easily - philosophical and scientific elements from Athens together with Jerusalem's Christian morale.

5.- *The apprehension of a closing chapter.* European history is dominated by the idea of *fatalism*, probably due to the recurrence of Wars. Fatalism leads to introspection, and introspection produces literature in a different way to the one so called "the American dream".

To me, Europe can also be defined by its cultural effect. Coupled with economic progress, Europe has produced, in a relatively short period of time, an enormous abundance of great music, painting and literature. All of this enormous cultural creation has been possible because it has taken place in a legal context that has succeeded in giving incentives to contents creation. And Europe has managed to couple it with new industrial inventions that have made it accessible to the world's citizens.

Internet, a Trojan horse?

Why do American companies dominate almost all fields of content-driven industries, with the unique exception of publishing? Why do European companies today dominate the publishing industry? In fact, out of the 10 top publishers for 2008, we find:

- 7 European companies: Pearson (UK), Reed Elsevier (UK/NL), Wolters Kluwer (NL), Bertelsmann (Germany), Hachette (France), Planeta (Spain), and De Agostini (Italy).
- 3 American: Thomson Reuters (Canada), McGraw-Hill (US) and Scholastic (US).

In terms of publishing lines, and also in terms of accessing readers, we can appreciate a lot of differences between both areas. Generally speaking, European houses are more "art-driven" (or contents focused) and American companies are more "science-driven" (or diffusion/distribution focused). Probably the most significant of them is the vulnerability regarding the e-book phenomenon, which appears to be greater for European companies, which are also present in American markets, and worldwide.

This is the reason why some people, alluding to this fact, characterize the e-book as a "Trojan horse", to sweep out of the market European traditional leadership.

While it is true that the Google digitisation initially was a “broad piracy raid” (some colleagues of mine call it a “napalm-like approach”), today things are regarded with a higher degree of common sense and are conducted with somewhat higher respect to existing laws. Legal actions are taken to protect intellectual property rights, and Google, a true global company by birth - only eleven years ago - must develop its “local sensitivity”, to play a more even game, respecting existing laws, to leverage content diffusion capacity of today’s publishing industry. And, as publishers, this is the game we need, like and have to play.

In Search of a future for publishers, real teamwork is needed

But, today, what is at stake is this very difficult to achieve equilibrium between creation and diffusion/distribution. New technologies arrive, very powerful technologies that allow contents to be disseminated, in real time, throughout the world. And this imbalance puts in danger the delicate ecosystem in which we live and work.

If we take a second to compare the economic power of contents creation and distribution technologies, we will realize, for example, that Google or Amazon are much stronger than all American Publishing houses combined (by direct comparison of turnover, or, better still, earnings). This fact puts any negotiation in very difficult terms, and shows quite well the very different competitive intensity in both worlds. Publishing houses are atomized, and distribution companies - being physical or electronic - are, in practice, oligopolistic and even monopolistic. In Spain, no publishing house has more than 15 per cent market share, while, for example, Google, has a market share - in the searchers business - close to 97 per cent.

Although I come from Spain, unlike Don Quixote, I do not have any interest in fighting windmills that I know to be giants. On the contrary, I am closer to Sun Tzu, who established that “in the practical art of war, the best thing of all is to take the enemy's without fight”, or “to start fighting only if it is sure to result in victory”. Since you all know that this is not the case, therefore the best course of action is to prepare yourself, adapt to the new circumstances, and negotiate.

Moreover, the new technology giants manage to combine this extraordinary strength with a very populist approach, using arguments such as “fair use” that, behind two nice words, hide a profound disrespect to the existing property rights laws, which play the role of allowing quality contents to be created.

Some people might compare this “fair use” approach to the advent of communism, and some people even can anticipate, in a mirror approach, its effects. Initially, concentrating all wealth - or contents - on centralized hands

and giving it away sounds fine. Some years later, the lack of incentives to create quality contents sounds unavoidable, and the system becomes poorer than it was before.

In terms of avoiding an imbalanced polio-like growth, its crucial to respect existing legal environment, unless in what refers to incentives to content creation. To this goal, and seeing the magnificent power of today's technology tycoons, publishers should practice a game in which they have almost never succeeded: teamwork. And public authorities should also think deeply long-term, and act consistently.

Lessons learned from real life experience

Taking advantage, once again, of meetings like the ones made possible by the Frankfurt Book Fair, which, in its 61st edition, looks extremely strong and adaptative, we, people devoted to books, should responsibly analyze behaviours and effects that have already taken place in other markets. And today, the richest experience comes from the USA market. What has happened, then, in the USA publishing industry? Let's go for some facts:

- Market stagnation over the last few years (lack of growth in real terms).
- Profound changes in retail, with Amazon strongly leading e-sales of physical books, which account for more than 20 per cent of the market.
- Negligible growth of audio books.
- Recent high percentage growth figures concerning e-books, which still account for 0,6 per cent of the total book market (data referred to 2008), with some prospects for 2009 situating it above 1 per cent of book industry revenues.

So, it seems that we are attending to the birth of a new incarnation of book, which concerns very much US publishers:

- John Sargent, McMillan's CEO for US operations, stunned to discover that 90 per cent of its front-list titles were available on pirate sites, said, last September, referring to the book industry: "We are at the stage of the music industry just before file-sharing".

While today nobody discusses the real economy advantages that the web offers, and that fuels the book industry redesign process, I strongly believe that property incentives allowing today's contents creation can't be swept out without enormous risk.

In this same panel discussion organized by New York University's Center for Publishing, Gary Hoenig, general manager and editorial director of ESPN Publishing, said:

"I don't understand why our industry thinks it should be exempt from what G.M. and Chrysler are going through," noting that such pressures should encourage publishers to pursue better manufacturing processes, and make better products".

And, in fact, Mr. Hoenig's claim seems right to me, as nobody thinks that our industry is not affected by changes. The book industry, once again, will prevail, but some fundamental principles can not be removed. It would be very much like not recognizing R&D and industrial property rights for new inventions and processes governing the automobile industry. And for both the automobile industry and the book industry, we believe in property rights.

Still, by analyzing some facts regarding the US market:

- Development of e-readers, one of them, Kindle, in semi-monopolistic conditions (closed format).
- Around 1 million e-readers sold up to today, of which Amazon has a market share exceeding 50 per cent, with sales expectations for 2010 around 1 million readers.
- Discount policy between publishers and e-retailers not based on economic reasons. The same efficiency on e-book development applies both, to publishers and distributors. E-distribution should be much cheaper than physical distribution.
- Initial prices for e-books way too high.

In light of this all, it is safe to conclude that there is some room for improvement and, better still, that keeping an eye on publishing changes in the more advanced world market, is worth the effort.

A Spanish recipe, not cooked by Ferran Adrià

Last year, during the Frankfurt Book Fair, at a Breakfast at Villa Kennedy, I met a good friend, Brian Murray, who is one of the most skilled people I know concerning e-publishing and who, together with Jane Friedman, shared his views with Spanish Publishers at our annual conference in beautiful Santander two years ago. We also have had several productive talks with Ruediger Salat - Holtzbrinck and Richard Charkin - today in Bloomsbury. Probably, at the same time, Riccardo Cavallero was learning facts from e-publishing development at Random House.

Back in Spain, with Paco Cuadrado, Santillana General Manager, we concluded that it was not worth reinventing the wheel separately. Therefore, we decided to join forces, and to do so in a cooperative way, opening our platform, which is

under way, and which will allow 6000 titles to be accessible to Spanish readers by mid next year, giving access to the e-market to all Spanish publishers, regardless of their ability to committing resources to the project.

Our lessons learned apply also to efficiency associated to a single platform, to the need of embarking booksellers in this adventure (because physical books and e-books will coexist for a long time, since they still appeal to different targets, and there is an enormous variety of publishing lines with different characteristics). We are open to share our thoughts with anybody concerned.

Book industry: quo vadis?

In this same opening speech, last year, Paulo Coelho finished his bright intervention by saying: "In a way, there is an irony behind all this: Giordano Bruno was punished for voicing his ideas. In today's world: you will be punished if you don't."

Publishers have the task of voicing the ideas embedded in the books they publish. But publishers have also the commitment to reward authors in terms of providing them with incentives to write. And authors have to decide if they want to give their contents for free - which is a legitimate option for them - or get paid with a percentage of the advertising revenues that their contents generate.

But, in any case, should some authors and publishers decide in one way or another, it should be a free choice, not a compulsory one. In the same way it happens in all other fields of economic activity. And recently, with the "napalm-like" approach that has been followed by Google regarding digitisation, we are far away from the domains in which publishers and authors can make a free choice. And it is a responsibility of public institutions, commanded by Governments, to level again the field. Because if they don't, then the priority no longer would remain creating good contents, but having monopolistic control of e-searchers, or having a very high market share of Kindles, or speeding up the capacity of wifi lines to increase the bill of the telecom company providing service, favouring piracy as a tool to increase usage and profits. And we have to remind that ideas - which are the basic material of what books are made of - are not exactly the same than other goods and services. And that, in fact, piracy of existing contents is good for all, except for publishers, authors, and readers.

And levelling the field refers to property rights. And, as Adam Smith put it in "The Wealth of Nations", "it is not from the benevolence of the butcher, the brewer or the baker, that we expect our dinner, but from their regard to their own interest". And, as a society, we have to decide if we want to maintain existing mechanisms for value creation.

As a final thought, some wise words, from Chinese culture, to face the relationship between publishers and new technology tycoons:

“The best soldier does not attack. The superior fighter succeeds without violence. The greatest conqueror wins without struggle. The most successful manager leads without dictating. This is intelligent nonaggressiveness. This is called the mastery of men.” (Lao Tse)

We can find the same learning in “The Art of War”, by Sun Tzu:

“He who knows when he can fight and when he cannot, will be victorious.”
(Sun Tzu)

The second thought, coming from the Tao Te Ching, is my favourite:

“Respond intelligently even to unintelligent treatment.” (Lao Tse)

And lastly, a word of precaution:

“By three methods we may learn wisdom: First, by reflection, which is noblest; Second, by imitation, which is easiest; and third by experience, which is the bitterest.” (Confucius)

As Saint Augustine of Hippo established more than 1500 years ago, “in periods of turbulence, do not execute too many changes.”

In this sense, my recipe would be to adapt actively to the market changes, most of them technological, but that have enormous conceptual implications. In the same exact way that the advent of the movable printing machine invented, a few miles from here, by Johannes Gutenberg more than 500 years ago produced critical changes in the book industry, Internet, even in a more profound way, will do exactly so. And publishers will have to adapt to them. And to perform this course of action teaming up with competitors (publishers), noticing that is the only way of playing an otherwise very unlevelled game.

Thank you.