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The future of the book industry

Digital or physical?

Case study: Amazon

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<p>Gutenberg's letterpress was once a revolutionary tool for the book industry. Mankind could now produce books in bigger scales and distribute in a greater amount than before. However, since then there has been little development inside of the book industry, until recently. The digital revolution of the internet changed big parts of the entertainment industry. The music and film industry first fell to their knees because of the downloading piracy and later on the online streaming services such as Spotify and Netflix. The book industries stakeholders held their breaths. New digital gadgets emerged and suddenly the E-Reader had found its way into the global market. Along with the internet came new ways of distributing books, both physical and EBooks. New actors such as Amazon that had also emerged from the early internet years era saw their big opportunity for an increasing online demand for digital and physical commodities. As the price for an EBook was set quite high in the beginning several stakeholders inside of the business had big problems with investing in the new digital format. However, Amazon changed all that by implementing a loss leader model where prices were heavily reduced to attract customers to their webstore. With the increasing sales of EBooks for Amazon, the six biggest publishers around the world signed an exclusive deal with Apple to increase the competition. The publishers tried to extort Amazon by saying that if they did not accept the same agreement as Apple they would not be allowed to sell their books anymore. Amazon backed off and agreed with some of the publishers. The American Department of Justice decided to charge Apple and the publishers and one by one they backed off the agreement with Apple. Apple lost their appeal and had to reimburse their customers for too high retailing prices. However, around 2012 the sales of E-readers peaked and since has declined as the EBooks. There has been a revival for the physical copy of the book and therefore retailers such as Amazon has decided invest also in physical stores across Northern America.</p>	
Keywords	Book industry, Digitalization, E-readers, eBooks

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1 Introduction

“This is the point. One technology doesn’t replace another, it complements. Books are no more threatened by Kindle than stairs by elevators” (Fry, 2009).

The book industry is going through a major change of distribution. From being a traditionally publisher-to-retailer-to-customer chain, new platforms of distribution have appeared on the market. The internet has been a revolution for digitalizing the entertainment industry such as music, film and, this reports subject, the book industry. However, while the other two industries have made a total transformation of business where the physical commodity has been replaced by digital copies, the book industry remain as a strong supplier of physical commodities.

This is quite remarkable as customers of the other two industries are using online distribution to make their purchases and therefore the traditionally brick-and-mortar music and film stores have almost disappeared. Meanwhile, the traditionally book store is still a significant retail outlet with loyal customers who like to browse the selection of the book store, despite the fact that strong online competitors have slashed their prices to gain shares of this desirable market. Some have even created huge loss leaders to attract their customers to webstores instead of brick-and-mortar stores. Nevertheless, the competition has become tougher and some traditionally strong book chains have been forced to close down as price and selling strategy appear to be more aggressive as it has been before.

This study will investigate IF the current trend inside of the book industry points to the same fate for retailers as in the other entertainment industries. There is a strong fear amongst publishers and retailers that they will be of no use in the future. Furthermore, it will also investigate how readers embrace this new format. This is a much-debated question as where the future for books lie, which is the main research question of this report. In the hand of the reader, yes. But in which format?

2 Literature Review

This thesis has been based on secondary sources, mainly researched from articles and online databases. There are vast number of articles about this subject as it debated often and well by different stakeholders within the business.

Contemporary articles about this matter reveal different attitudes towards the E-book versus the real book. So far, most of the relevant literature has given evidence of how the European and North American markets have coped with ongoing digitalization. Based on these articles, the North American market has embraced the E-book in a stronger way and has adapted more quickly to the new digital format. According to Inouye (2016), the American market experienced a rapid growth of the E-book market because of Amazon's introduction of Kindle in 2007. However, in 2014 the market plateaued and the market share for traditional books has since increased.

The European market has shown slow signs of embracing the digital format with open arms, as shown in Figure 1. People hold on to their physical format to read and are unwilling to invest in modern technologies, such as Kindle. Katsarova (2016, p.1) describes how the E-book has only recently taken off in Europe and "it still represents only 1.6% of the total book market in the leading EU markets". Furthermore, Katsarova (2016, p.4) describes how digitalisation has changed the supply chain of the market. From having an old linear supply chain, it has become a more global network with new emerging channels to distribute the product. This is similar to what occurred in the music business, however at a much slower pace as the new global channels in the music business erased all old structures within it.

	2008	2009	2010	2011	2012	2013	2014
Print	17.6	17.5	17.2	16.9	16.5	16.2	16
E-book	0.1	0.2	0.4	0.6	1	1.3	1.6

Figure 1 E-book market in the EU-5¹, 2008-2014 (billion euros), Katsarova, 2016, p.4

¹ EU5 stand for France, Germany, Italy, Spain and United Kingdom

The publishers and book stores around the world are watching this process in fear of being left behind. A new emerging platform such as Scribd² and Amazon have created anxiety amongst book retailers. There is a concern that there will be a “Netflix of books” in which for a small sum you will get unlimited access to millions of books online. This could be compared with the home video industry as Netflix was a direct result of people giving up on the physical format such as DVD and Blu-ray. Therefore, people outside the industry has voiced their opinion that the industry should be more courageous and adapt to new distribution channels (Publishing trends, 2016) even if they might fail. However, other sources claim that the publishers and retailers are scared of changes and the new platforms such as self-publishing web-pages (Anderson, 2013).

Furthermore, research published by Federation of European Publishing (FEP, 2015) that shows the statistics of employees and revenue between 2010 and 2014 has decreased in the publishing sector. However, the publishers around Europe have approximately 16.9 million of different titles in stock of printed books while they only have 3 million of titles in digital format. This amount is increasing every year because of the digitisation of the back catalogue. Furthermore, the article claims that there is a surge of self-published titles in the UK and this could be another small threat for the retailers in the country just as Scribd is in the US.

² Scribd is a subscription based online service where you can also publish your own book.

3 The book's impact on society

3.1 History of the book

The book industry has a long and important history in business and dates back to 300 B.C., when the Alexandrian library was founded in Egypt. The role of the library was to procure books to stimulate the people's knowledge, and it is believed that this influenced the first Athenian booksellers (Encyclopedia Britannica, 1911). However, books were still available in limited amounts because of the complicated process to manufacture a book and it was not until 16th century, 100 years after Johannes Gutenberg's Letterpress printing was introduced in Europe 1436, that books could be produced on large scale (Whipps, 2008). From here on the book became a business on its own and stores specialized in books opened up around Europe, especially in the lowlands. Moreover, a further important impact that cannot be underestimated on the book industry at this time is Martin Luther's translation of the bible in 1534. The bible had been translated to different languages before, but none that was intelligible to normal Germans at the time. As Gutenberg's letterpress printing, had helped scholars and theologians around Europe to print some books and pamphlets, it was time for Luther to print his version of most important book for the people at the time. The translation had a massive impact on the German society and the forthcoming Reformation. The first ever best-seller had been created (Krämer, 2016).

The book industry has since grown to become a big part of people's everyday life as more and more people were able to learn how to read and educate themselves. Today the book industry in Europe employs around half a million people which includes printers, designers and booksellers and in 2014 the market value in Europe was estimated to 38 billion euros (Federation of European Publishers, 2015). To see it from an even more holistic view the global book industry was estimated to a value of 151 billion dollars in 2012, which makes it the biggest share of the entertainment industry around the world (The International Publishers Association, 2014, p.20).

4 The Library

Mankind's striving for education started as early as the first letters were invented in Babylonia. Since then mankind have carved or written on many different materials to spread knowledge and information for generations to come. However, with the development of education the need for a place where to gather information became important. The first trace of archives can be found from temples in Sumer (Casson, 2001) where archaeologists have found tablets of clay with one of the earliest known systems of writing. Since then the library have become a cornerstone for education and information gathering all around the world for scholars and students. However, as the education were restricted to the upper classes of these societies and the prints of book were limited, not of a lot of people would have access to these resources. Nevertheless, as described in the previous chapter, Gutenbergs revolutionary printing technique increased the number of books around libraries around in Europe. But it was not until mid 19th century that the first public library opened up the door for the lower classes to come and read books without any special grant or scholarship from universities (BBC, 2002).

With time and the innovative development of the book printing there were other issues for the libraries, even though maybe less negative. With a larger number of books being acquired the space needed to expand and maybe the most important issue of all, the categorizing of books. Since the first libraries have been founded there has been some type of categorizing. However, not very effective as most of them were sorted after popularity and acquisition. With time this kind of simple categorisation was not feasible and new invention was needed. The first real classification had been done by Jacques Charles Brunet, but it was in year 1876 that Melvil Dewey published his first article about his "Dewey Decimal Classification" method which is still being used today all around the world. Dewey's based his classification after the scale 000 to 999 which simplified and made the categorisation much more efficient for libraries who practice this method. This method has been revised 23 times since the first article (OCLC, n.d., p.4) and has since revolutionized libraries around the world.

As education has increased amongst the lower classes around the world the urge for information has grown at an increasingly rate. The library has developed into a central place where people can execute several different services that relates to culture. Before the digitalization boom there was no other place than the library where you could gather

information for studies or private curiosity. A student, for instance, was restricted to books and the pad where he or she could write down comments for later using. However, this has all changed since introduction of digital tools that facilitates the process of researching and leisure time spending. Instead of using the library's physical resources people have started to use digital resources. Books of all kinds get digitalized and online databases are more efficient to use than searching in a library. From figure 2 we can see that the amount of people who frequents libraries in the UK have decreased steadily from 2005 to 2014 (Public Libraries News, 2017). We can also see that there is a correlation between amounts of visits and book loans, which is also decreasing. Meanwhile on the other side of the Atlantic sea, USA have the same trend as in the UK. The Atlantic (Meyer, 2016) reported that in an article produced by PEW (PEW Research Centre) in 2015 there were 44 percent of the Americans who had visited their local library or bookmobile. Three years earlier the amount was 53 percent (PEW, 2016).

Decline in use of English public libraries				
Year	DCMS: "Taking part" - % population who have visited a library in the past 12 months	CIPFA : "Active membership" - % population who have borrowed a book in the past 12 months	CIPFA: - Number of annual library visits per member of the population	CIPFA - Number of annual book loans from libraries per member of the population
2005/6	48.2	22.2	5.8	5.5
2006/7	46.1	21.4	5.7	5.3
2007/8	45.0	20.8	5.5	5.1
2008/9	41.1	20.1	5.4	5.1
2009/10	39.4	19.4	5.2	5.1
2010/11	39.7	18.8	5.1	4.9
2011/12	38.8	17.7	4.8	4.6
2012/13	37.0	15.9	4.5	4.2
2013/14	35.4	not yet available	not yet available	not yet available
Fall from 2005-2013	-23.2%	-28.4%	-22.6%	-23.8%

Figure 2 Decline in use of English public libraries, Public Libraries news, 2017

4.1 Digitisation of libraries

While the market for digital books have increased and more people are interested in the digital format, the library has yet not been able to embrace the concept totally and there are several reasons for this:

1. Financing of libraries
2. E-book licensing problems
3. Publisher vs Library

4.1.1 Financing of libraries

Unfortunately for public libraries they have a restricted budget as they are owned by the government in the land they are located in. As several austerities of budgets have been executed in countries since the financial crisis the culture section have experienced grim times. For instance, in the UK, BBC reported that “almost 8000 jobs have disappeared from libraries in six years” and “more than hundred libraries have closed” (BBC, 2016). As a result of this, the opening times of libraries have been reduced and the public have less access to resources that should be available to the public in the UK.

This is not only a concern for the UK, same problems are visible in the rest of the countries in the European Union (EBLID, 2013). Instead of increasing the budget for the culture section most countries have decided to make cuts to save. This has been a concern for the European Commission as they are proposing an increased EU budget for culture. However, EU themselves have admitted that libraries may face a tough future as the digital format is increasing and “it is difficult to build a sustainable business model” for the digitalisation (European Union, 2014, p.3).

On the other side of the Atlantic Ocean there are similar problems on the horizon. The current president has released a budget blueprint for 2018 in which he proposes tough cuts in support for the public libraries around the US. The blueprint report proposes that all funding’s to the Institute of Museum and Library Services (amongst others) should be eliminated (Office of Management and Budget, 2017, p.5). There was an immediate press release from the Institute of Museum and Library services in which they state that they support 123,000 libraries around in the US with a \$155 million population-based formula grant program (IMLS, 2017). This would mean a great loss of funding for a segment of culture that is already showing signs of decline.

4.1.2 E-book licensing problems

For a library who wants to acquire, a new novel for instance, to its E-book selection will have a few obstacles to go through. There are several different methods of licensing books to libraries around the world. For some contracts, the library can actually own the digital version of the book they have acquired and in some other cases they have bought licenses which they have to renew after some time.

Boston Globe (Vaccaro, 2014) reports about a publisher who only allows the library to buy one license per book with the limitation of 26 loans from the library. If the book reaches this amount of loans the library has to buy a new license.

Another library in America decided to acquire 300 E-books of E.L James bestseller *Fifty Shades of grey* for \$23,400 (approximately \$78 per book). In this case they will own the E-book so they will be able to loan it to the public as much as they want to (Greenfield, 2013). That could be considered as a quite large investment for a library in a book that will lose interest over time. The price for a sole book might seem very high but there is an explanation for this. In America, there is a big difference what the publisher has to pay to author if they license the book to libraries or sell the book in a normal way. Accordingly, to Paul Aiken, who is executive director of the Authors Guild in USA, the publisher has to pay the authors fifty percent for a license and twenty-five percent for a normal sale (Schwartz, 2013).

For an example in Europe, more precisely in Sweden, it is reported that the then newly released book "The girl in the Spider´s Web" from the popular Millennium series would cost approximately 200 SEK³ to buy as a physical copy for the libraries. After that the library will pay a few cents per loan to the publisher. Unfortunately, there is no mention about the licensing cost for the E-book but it will cost the library 80 SEK for every loan E-book loan (Samuelsson, 2015). This cost can become an enormous problem for a library if the book becomes popular and the library have a limited budget. Therefore, several libraries have implemented a limit in how many copies of the book can be loaned.

4.1.3 Publisher vs Library

As described in the previous chapter there are several different issues with contracts and licenses which publishers propose for libraries. With that information, it could easily be believed that this is all a question about money and who can pay for it. That is partly true. However, there are many publishers in Europe and USA that does not want the libraries to have access to the new bestsellers in their selections. Publishers have been reluctant with cooperation with libraries as they believe that the libraries will take a big

³ SEK = Swedish krona

part of their market. If they get access to one E-book they can spread it for free to consumers, hence the high costing prices of E-books for libraries.

A survey has shown that "more than fifty per cent of the latest E-book titles are not available to public libraries in Europe" (DBW, 2014). This was stated by the ALA⁴ president as they have a similar problem in North America and thus wants show solidarity to their colleagues in the European equivalent called EBLIDA⁵.

EBLIDA launched the "Right to E-Read" campaign in 2014 (EBLIDA, 2014). The aim of this campaign is to make the general public and policy makers in the EU aware of the difficulties for libraries around Europe to provide access to eBooks and other digital contents. EBLIDA has been an intermediary between the stakeholders from the book industry and the libraries in Europe. They have tried to convey the obstacles that the libraries are facing when acquiring books to publisher but with little results so far. Libraries main problems regarding publishers have been:

- Refusing to include certain e-book titles of packages;
- Subsequently removing certain e-book titles from subscription packages in order to sell the books exclusively to individual private customers; and
- Prescribing the terms for access (EBLIDA, 2014)

So mainly, ABLIDA is promoting a financial fair play inside of the book industry so libraries can acquire books at a decent price and provide e-books to an increasing number of e-users.

⁴ ALA = American Library Association

⁵ EBLIDA = The European Bureau of Library, Information and Documentation Associations

5 The Physical Book vs E-book

The idea of a mechanical gadget to facilitate reading is not new and was first introduced in 1949 (History Cooperative, 2016). Back then the computers were still in an early phase and it would take until the internet was fully developed before the E-readers could enter the market in full force.

The first successful attempt to digitalise books came before the E-readers were developed. Instead of portable gadgets, which was unthinkable of at this time, the developers of digital media set their eyes on the PC, aka Personal Computer. During the 1980s, the gaming industry developed at fast pace alongside early PC innovators. However, disk space was very limited and large and clumsy floppy disks were being used to store data. Therefore, games and educational information could only be stored and spread in small files. Move forward to the nearly 1990s and with the introduction of the CD-ROM⁶ there was finally a disc that could fill a large amount of memory.

Now it was time for the big players, such as Microsoft, to enter the market with their hyped software Windows 95, offering a totally digital encyclopaedia on CD-ROM. Instead of filling half of your bookshelf with heavy and tedious books you could now fit everything on CD-ROM. Microsoft presented their encyclopaedia which was called "Microsoft Encarta" in 1993. Microsoft had first approached Encyclopaedia Britannica⁷, but they however declined the proposal because they could not see a future for the computer market and the sales of printed media were still very strong in the late eighties (Ivović, 2007). This would be an unfortunate decision by the owners of the Encyclopaedia as they had to close down in 2012 because they could not compete with the online encyclopaedias. Instead Microsoft bought *Collier's* and *New Merit Scholars Encyclopaedia* and incorporated them into what would become Microsoft Encarta. The original price for the CD-ROM was \$395 but however it sold poorly because of their main competitors, Compton's

⁶ A single CD-ROM can hold as much information as 1,500 floppy disks (Miglore, 1986).

⁷ Encyclopaedia Britannica is one of the oldest and most acknowledged encyclopedias for the English-speaking world. The first edition was published in 1768 which contained three volumes while the last edition from 2012 contained 32 volumes (Flood, 2012). The owners of the encyclopedia decided to halt the prints of the volumes in 2012 because of the increasing competition from digital copies of encyclopedias (McCarthy, 2012).

Interactive Encyclopedia, was being sold for just \$129. Microsoft decided, reluctantly, to drop the price to \$99 for the holiday season in 1993 and it became a massive sales success. By the end of the year Microsoft Encarta was one of the best-selling CD-ROMs and in 1994 the sales passed a million copies (Stross, 2009).

The CD-ROM has nowadays become an obsolete tool for spreading information as the internet has taken almost all its share of the market. Software, Encyclopaedias and other things can be purchased and downloaded or used directly from the Net. The physical copies have almost totally disappeared.

The first modern E-readers were introduced to the market in 1998, namely the "Rocket eBook" and the "SoftBook Reader" (CNN Money, 2010). Both E-readers could almost do everything a modern E-reader can do today except some new features such as Wi-Fi downloads which is an essential feature for the modern E-reader.

Today there is vast amount of different E-readers that are available for customers and the most popular one is Amazon's Kindle. In 2016, Amazon reported that the sales of Kindle (and Amazon's Prime TV) soared so high that the profit was astonishingly 351 million pounds (Daily Mail, 2016). Unfortunately, Amazon does not report on individual items so it impossible to get an accurate number for just Kindle. However, from the same article the founder of Amazon reveals that they sold "twice as many tablets compared with the same period last year". This is interesting information as the sales of E-books have plateaued over the last years in US and the market in Europe has only grown slowly (Katsarova, 2016, p.4). Will this this give us a hint that the E-book sales will increase in the near future?

However, the traditional book store has not totally disappeared on the radar from an online store such as Amazon. Amazon managed to increase their market shares in the US so the former biggest bookstore chain, Borders Group, had to close down all their stores because they could not adapt to the digital changes (Katsarova, 2016, p.4-5). This has also affected the current biggest bookstore chain called Barnes & Noble, who had to close down around 150 stores across US because of Amazon's online market (Wahba, 2016). Barnes & Noble have since the tough competition opened up their own webstore to compete where Borders group failed. Even though Amazon is increasing its the market share annually because of its big online success, it has recently decided to open up

several bookstores across the US (Gibbs, 2015). This strategy is quite a U-turn by the company that for most of its existence have been selling its commodities online. The reason behind this could very well be that the "e-commerce still would represent only 10% of the global retail market" (Forbes, 2016) and to reduce prices even more. By having physical stores, they can add the "pick up in store" feature if you order online which will reduce the shipping costs with joint shipment with other commodities to the store. Furthermore, Amazon is also looking to gain shopping experience which it lacks by only having online shops. Customers around the world still enjoy the social factor of shopping, how they get served and what kind of experience they will have by entering a real shop.

One advantage for the traditional book is the non-existent competition between smaller languages on the global market. For instance, if you would like to purchase a book in Finnish you have to buy it from Finland as companies who work globally have no interest in that small market. If the Finnish publisher decides that they won't publish a digital version of the book the consumer is restricted to the physical format. This is one of the reasons why books still sell quite well in Europe as there are so many different languages and the competition is simply restricted to their own home markets.

Williams (2010) argues that this basically comes down to the language barrier and cultural differences to make it in America for instance. The market is quite brutal and favours the established authors as they are already signed up to big publishers with great connections. Subsequently, as Penn (2014) describes, as a new or relative unknown author the foreign markets is a steep hill to climb with lots of different pitfalls. Authors does not own the foreign publishing rights to their books, it's up to the publisher what they want to do outside the home market.

For a self-published author, it could be easier to get access to the English-speaking world as nowadays big distributors such as Amazon sign deals with authors who have translated their books themselves. However, if they are not able to translate the book themselves it could be a costly project.

6 Customer experience

6.1 Book store

Selling books from an online shop can be considered as a safe way of conducting business in today's fast developing environment. The core of the business could focus on the online improvements and promotions meanwhile warehouse work and customer service can be outsourced to other companies. Retailers however, have a physical product to offer their customers when they enter a shop. Here is the main difference between an online store and a retailer which could offer more than just a book. There are several elements that a retailer can take advantage of that a webstore cannot do. As Baker, et al. (1992, p.2) described "retailers do not generally engage in systematic research that enables them to examine the environmental factors that may influence the patronage decision". Baker and his fellow professors conducted an in-depth analysis of the Stimulus Organism Response⁸ (SOR) model, which affect a customer's decision and experience if stimulated with different colours, lightning and different floor planning for instance. The model was divided into three factors: Ambient, social and design.

Ambient factors included a store's music, lighting and smell which are a mix of visual and non-visual background conditions. Visible factors were included in the design part where aesthetics and interior planning of stores were amongst the important things. Finally, the social factor compromises the interaction between a customer and employee of the company. All these factors can have a direct impact on sales for a retailer and this concept is a good way for how companies can promote their in-store experience today.

Here is a clear advantage for retailers all over the world the digital market cannot really compete with so far. To be able to browse and look in books in different sections with different lightning and music is a way of increasing the customer experience which will encourage people to make purchases and come back. Here we must also take the 4Ps⁹

⁸ This model was created by Albert Mehrabian and James A. Russel in their publication called "An Approach to Environmental Psychology" (Gatautis, et al., 2017).

⁹ 4Ps stand for Price, Product, Promotion and Place. The marketing model was developed by E. Jerome MacCarthy and P Kotler in the 60's from an economic theory which also embedded some of its key assumptions into the marketing analysis tool (Håkansson and Waluszewski, 2005, p.111).

marketing model into consideration. To combine these two models which have similar goals to enhance the customers experience and increase the want to purchase a good should be a retailer's ultimate strategy.

6.2 Online webstore

Since the first empirical tests in the eighties of the effects of retail atmosphere and consumer decisions by Donovan and Rossiter (1982), things have changed dramatically. As described earlier in this report a large part of the business has moved over to online stores where the customer can choose between a greater amount of goods compared to the physical store. Supposedly they can even find cheaper goods and with delivery straight to the home door.

Hence, the SOR model has now been used on online stores to find out how they attract and retain their customer (Yoon, 2012). However, there are some factors that are not valid to webstores as it is for physical retailing stores such as the environmental and social factor. Here the olfactory notion and sensing books cannot be achieved as the customer never enters a real shop. Furthermore, the social factor is by all means missing as the customer cannot get personal assistance and recommendations. However, as Wu, et al. (2014) discusses there are several other ways for a webstore to attract customers by using the SOR model. The essential factors for webstores are the layout and atmosphere of the webstores. These two factors will have great impact on the visitor's emotions to make a purchase and revisit the store again.

Furthermore, the social factor might be less to a physical store but it is existing for a customer in a webstore also. Instead of getting a personal opinion from a seller the customer can instead read and give reviews of the product they have purchased.

Additionally, webstores nowadays also have an online chat which pop-up and ask the visitor if they can help. So, direct customer service is still available even though it has moved online

7 Stakeholders stance in the book industry

Previously in this thesis there has been discussion about how certain stakeholders affect other stakeholders within the book industry. We found out that libraries around the world have a hard time coping with the increasing demands of E-books and subsequently soaring prices. However, in this chapter I will discuss more in detail how the publishers, retailers and finally the readers, are influenced by the digitalization of the book industry.

7.1 Publisher

There are normally two ways of publishing a book. Either you sign a contract with a publisher or you self-publish. There are pros and cons with both ways of publishing but we will concentrate on the actual publisher in this chapter.

The publisher's role has always been to connect the authors and the readers with each other. It doesn't matter if it is a by a physical format or a digital edition. However, the market has changed with the digital revolution. More people are attracted by the digital version of books and therefore new platforms are needed for the distribution of this good.

It might sound counterintuitive that some publishers claim that the process of completing a digital version of a book is much more complicated than a normal physical version of the same book. The traditional book has been a simple commodity to sell. It is one package that suits all readers over the world. Nevertheless, with the increasing amount of different E-readers there is another problem to solve. Most of them have different file formats which requires the publisher to create different versions for all readers. It might sound easy in today's world but there is a challenge and it requires time and resources from publishers as they have to proofread and examine page flow for every format (Sourcebooks, 2010).

There is a file standard inside the industry called ePub which has been developed by publishing and technology companies. Apple's iBook store is using this format but in a slightly modified version which makes it hard to transfer to other platforms. For instance, you cannot transfer this file to a PC or a Kindle. Therefore, Apple has restricted its books

to Apple products only. The files in the iBook store are protected by Apples DRM¹⁰ called "Fair Play".

On the other hand, if you buy a book from Kobo and transfer it to a Nook (Barnes & Noble's E-reader) or the other way around the DRM is accepted on both readers, which does not limit the consumer.

So being able to have a release date at the same time for the physical book and the digital formats can be quite a task which requires publishers to undertake long-term planning and use more resources than before.

7.2 Retailers

7.2.1 Wholesale Model

The most traditional way for publishers to sell books to retailers has been by using the wholesale model. This means that the retailers will buy the book for a reduced or fixed price and actually own the book on the shelf in their store. Thereafter the retailer can set the price as they want with different discounts or offers. The wholesale model has been used for a long time in the book industry and it was not until the big E-book boom that the Agency Model was used by certain actors on the market (see below).

From Figure 3 we can see how the Wholesale Model works in practice. This model gives a lot of freedom for retailers to create their own business plan and strategies. Moreover, this model has been developed by some actors to create a more aggressive and competitive market.

For instance, Amazon has taken advantage of this model and created several "loss leaders"¹¹ to attract customers to their webstore. Instead of putting a reasonable sales price on a book they have reduced it so customers buy more goods as they are browsing the

¹⁰ DRO = Digital Rights Management, which is a copyright protection for digital media.

¹¹ Loss Leader is described as a commodity which is not profitable but will attract customers to the store and purchase something more. (Kotler, et al., 1999, p.729-730)

rest of Amazon's collection. This way of selling books has caused some upsets inside the industry and Rupert Murdoch, the Australian media mogul, stated that "We don't like the Amazon model of \$9.99...We think it really devalues books and hurts all the retailers of hardcover books" (Ionescu, 2010). However, the model is currently doing well for Amazon as there are reports that members of British Amazon who pay £79 to join Prime Service spend on average double the purchases of non-members, as they get better access to a greater amount of offers (Nair, 2017).

Some statistics have shown that Amazon was able to take 90 per cent of the E-book market with the help of the loss leader strategy (Streitfeld, 2012). Publishers around the globe became increasingly worried with Amazon's way of conducting its sales as there was no-one who could really compete with them. Subsequently the 6 biggest publishers signed a deal with a growing rival to Amazon to try and break its near-monopoly on the market.

Wholesale Model



Figure 3: Source: Spencer (2012)

7.2.2 Agency Model

Amazon has created tough online competition for other retailers that sell goods online as it is pursuing a loss leading wholesale model, as we discussed in the previous chapter. However, there are other big players on the E-market and Apple is one of those. In 2010 when Apple launched its online store for E-books, iBooks, it also introduced a new business model with five different publishers. This model is called the Agency Model. The

purpose of this model is that the retailer lets the publisher set the price of the book, which the retailer will sell it for, as we can see from Figure 4. In this model, the publisher will get approximately 70 per cent of the price its being sold for while the retailer will keep approximately 30 per cent of the sales (Filloux, 2012). The publisher is the only one who can decide if there should be a discount or sale campaign on the commodity. Subsequently all retailers that have the same agreement with that specific publisher will have the same prices on the discounts or sales offers. No exceptions are allowed, which means that the publisher will have 100 per cent control over the price.

This model generates more cash for publishers than the Wholesale Model as the price of an E-book is higher when the consumer purchases the commodity. It also means that the publisher will have stronger control of the value chain, from the creation of the commodity till the end purchase of the customer.

Apple's Agency Model

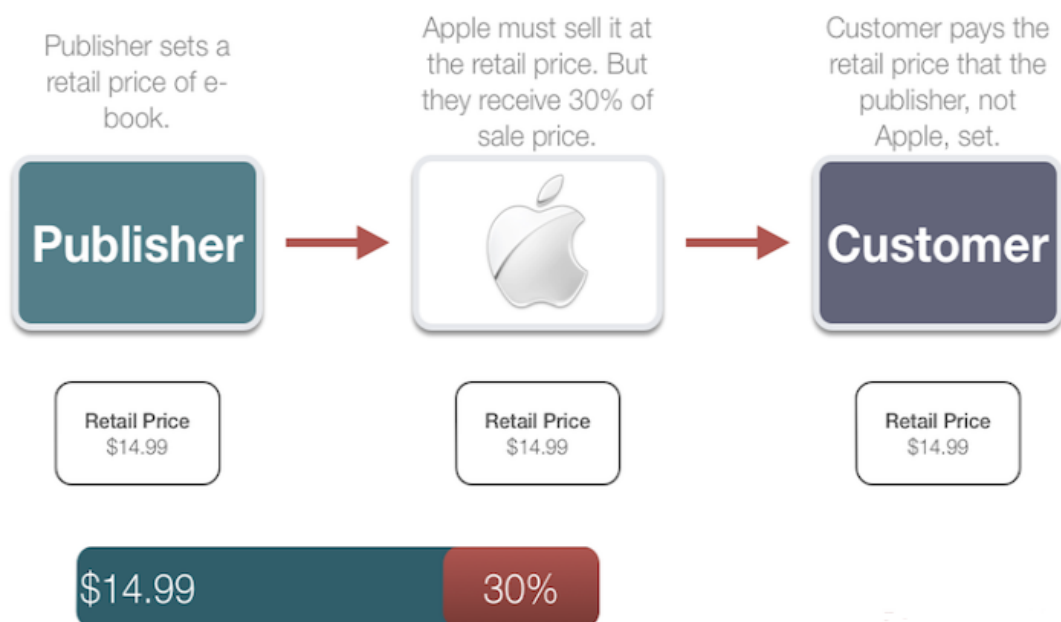


Figure 4: Source: Spencer (2012)

This model has solely been created for increasing the competition inside the book industry. As described in the previous chapter there were many publishers who felt a great worry about Amazon's strategy. Therefore, when the opportunity to create some countermeasures with a businesswise attractive partner such as Apple emerged, there was

no hesitation. However, things did not go as smoothly as the publishers thought at the start.

7.2.3 The Long Tail theory

Chris Anderson coined the expression "The Long Tail" in the magazine *Wired* in which he was the chief editor in 2004 (Anderson, 2004). Anderson argued that in this modern era where commodities and services become digitalized, there is a bigger demand for niched and lesser known products. With the digital age, we can find more and different type of products than ever on the internet. As we can see from figure 5 there are approximately 20 per cent of a store's products which is classified as big seller. The rest of the 80 per cent are less popular and therefore sells less in the store. This correlates to Vilfredo Pareto's 80-20 rule, also known as Pareto's principle, argues Anderson.

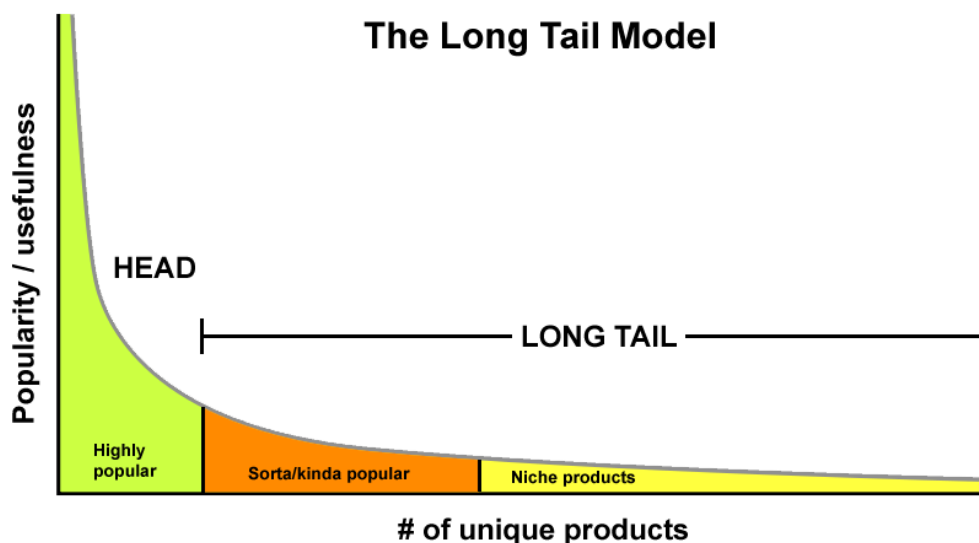


Figure 5: The Long Tail Model. Source: Childress (2015)

However, the Long Tail model is more prevailing today than in 2004 as the velocity of digitalisation has increased even more since then. For this model to actually be of use, a store needs to have a vast selection of goods. Furthermore, the speed to actually deliver the commodity to the customer is also a variable that is of utmost importance to this model. As the normal physical store might have very little of those lesser popular products the webstore has an enormous advantage to serve the customer's demand. In the physical store, we cannot get the same visible recommendations of products that are related or of similar style to the same extent as in a webstore. Therefore, the 80

percent of the products will sell less in a physical shop than in a webstore. The “Tail” will be longer in a webstore because the customer will be able to choose from a much larger selection of goods. Subsequently, Anderson argues, the 80 per cent of commodities that are low sellers sell as much as the 20 per cent that are big sellers because of the unlimited shelf space and storage that a web shop has. There are no real limits for today’s web stores.

7.2.4 The Long Tail criticism

The Long Tail theory was published more than ten years ago and is more relevant today than ever. However, with success comes also criticism. The Long Tail theory had been in practice before Chris Anderson coined the expression in 2004 but not in the same scope as it is today. The biggest difference is that today’s virtual web shops offers an almost unlimited storage for customers and they cost little to produce. For a physical store, it’s harder to compete as they have to reserve shelf place and cost for the inventory in the store.

Vena (2015) argues that when something costs nothing to produce, such as an E-book after being published, will the supply exceed demand? Well, most certainly not as Vena describes in his report but there is a risk of oversupplying the market with creative goods. This has in fact already happened inside of the music industry. Instead of 80-20 rule as predicted by the Long Tail theory, the top sellers are increasing their sales, instead of there being more balanced revenue streams (see Figure 6). The top 1 per cent accounts for 77 per cent of all recorded music income (Mulligan, 2014). Therefore, Vena’s criticism is very much legitimate in this case, as the music industry is more advanced than the book industry with respect to digitalisation. However, do the publishers/distributors care? As long as they are selling their commodity at a sufficiently profitable level they don’t care what is the big seller as long as it sells. This will be a much tougher business for the small creators of creative goods.

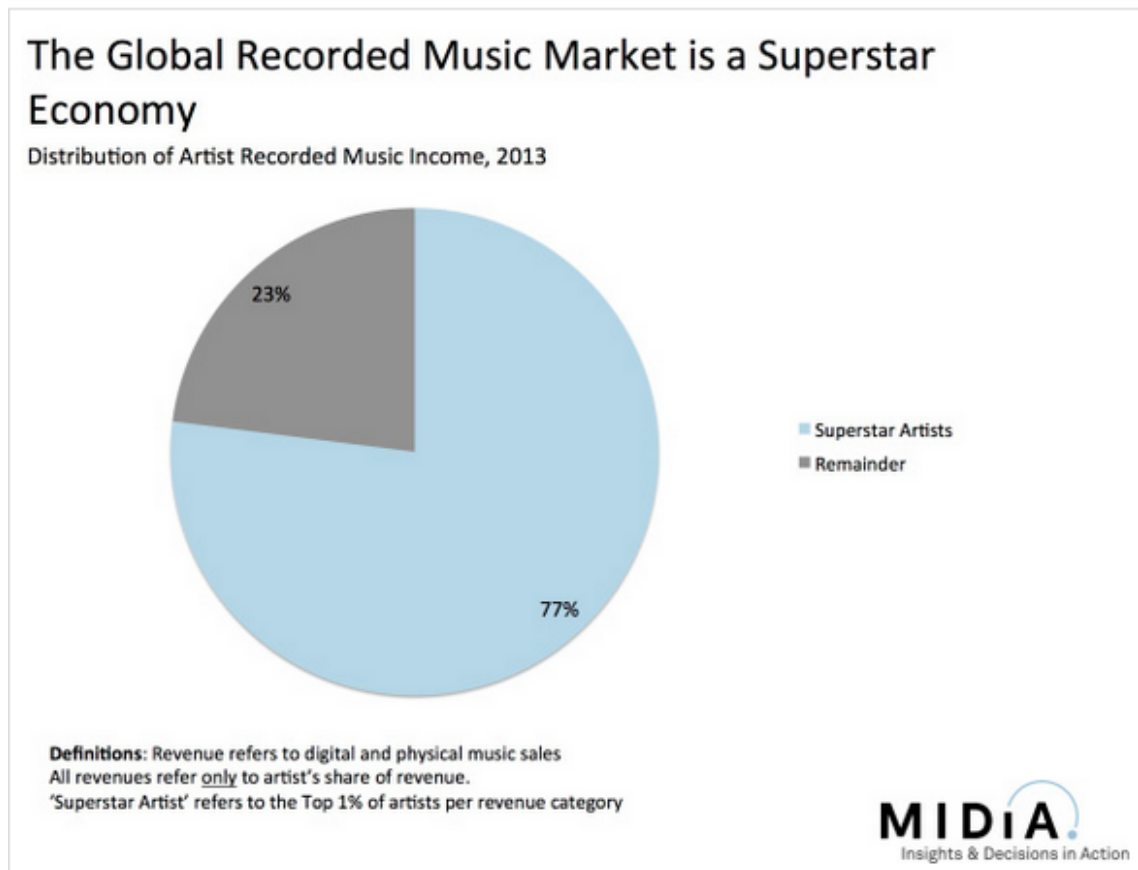


Figure 6: Sales figures in the music industry in 2013. Source: Mulligan (2014)

Vena describes in his article that it is too early to say anything about the book industry as the digitalisation is so recent and the effects of it has not been researched that well yet. However, the once world leading publisher Pearson have encountered enormous problems by selling off parts of their business that they do not consider as the essence of their business.

In 2015 Pearson sold their stakes in Financial Times and The Economist. The reason for this was that they wanted to focus on the core of the business, educational products for students all over the world (Barnato, 2015). Pearson's plan was to go from an analogue business to a more digital company. With hindsight, this was a catastrophic decision. Pearson's loss in 2016 was their biggest ever in history as they reported a £2.6 billion pre-tax loss (Sweney, 2017).

As it seems the students and teachers around the world switch from new and expensive books to cheap and rental copies (Bond, 2017). This could mean a great opportunity for big retailers such as Amazon that have a large selection of books. Expensive and cheap. They can take advantage of the Long Tail and attract customers to buy the less selling books but also get them to browse the rest of the selection which might result in other

purchases. This gives a hint that the Long Tail theory could be applicable on the book industry.

7.3 Readers

We have found out earlier in this chapter that the book industry has been going through challenges. Publishers have shown their strengths by creating new business models to stand up against big retailers such as Amazon who utilize older models to their advantages. So where does this leave the end consumer, the reader?

With the digital boom, many publishers around the world declared that this is the end of the printed book, while the digital format will take over the market. They stood and watched with anxiety as both music and film industries were transformed, first by piracy and then by streaming services. The old way of distributing commodities had been replaced by newer and faster platforms. And the consumers embraced it relatively fast. Purchases of physical copies in both film and music industries have declined ever since. Several streaming services have taken over as the preferred platform for listeners and viewers. Netflix, a subscription based film streaming service, has announced that it has 110 million subscribers. Between June and September, it added 5.3 million new customers (Richter, 2017). Furthermore, Spotify, which is a free and subscription based music platform for streaming, has announced that it has 60 million paying subscribers around the world (Statista, 2017). These two companies are the biggest market leaders of their own section of entertainment industry and there is tough competition with other fast-growing companies.

However, the book industry has been on its toes and has tried to cope with digitalisation. Readers around the world have been introduced to new digital gadgets to facilitate their leisure reading. From figure 5 we can see the sales of E-readers worldwide and how they peaked at 40 million in 2012.

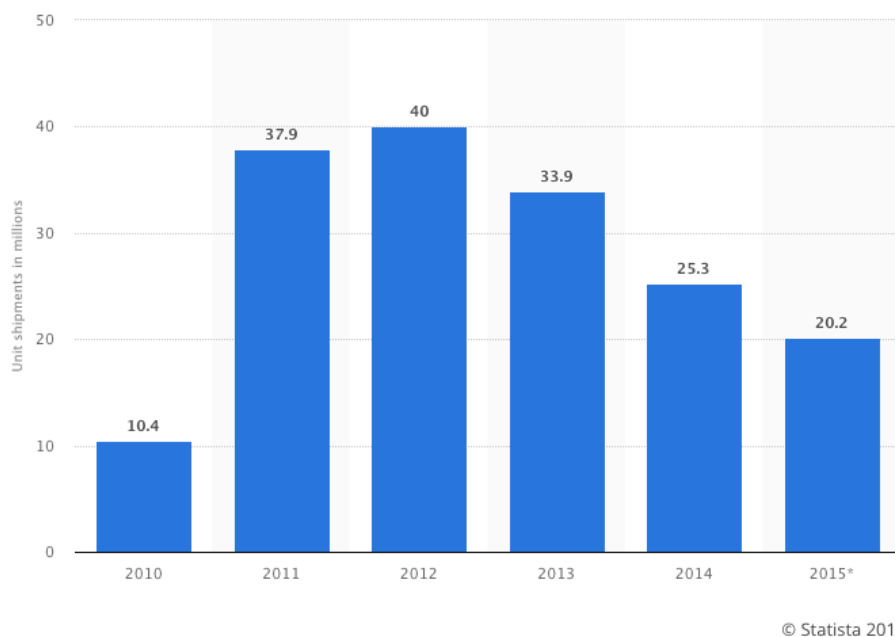


Figure 7 Unit sales of E-Readers worldwide from 2010 to 2015 (in millions), Statista, 2017

Nevertheless, the most interesting aspect of recently mentioned statistics is the big increase of sales from 2010 to 2011. IDG (2011) reports that the reason for this was an increasing interest from the public in E-readers and the low pricing of the product. From the same press release, there is mentioned that the shipment of E-readers went up 325 per cent from 2009 to 2010. The future must have been looking undoubtedly bright for sellers of E-readers and eBooks as it seems like the public is at last embracing the new technology.

This correlates with the statistics of Netflix and Spotify, until 2013 when suddenly the amount of E-Reader purchases starts to decline. Whereas both the music and television industry increase their amounts of customers, the book industry shows declining sales of E-readers. Subsequently, sales of the physical copy start to grow again for retailers around the world.

Sales of eBooks in the UK dropped 17 per cent in 2016 and the same trend could be seen in the US where it plunged by 18 per cent. At the same time the physical book sales went up by 7 per cent in both countries (Kottasová, 2017).

This is quite remarkable, and a big setback for manufacturers of E-readers and the producers of eBooks. Reasons for this according to Kottasová (2017) is that "Adults try to limit their screen time" and "One third of the adults in UK had attempted a digital detox

in 2016 by reducing the use of smartphones and other digital devices". Furthermore, it states that the sales of E-readers dropped by 40 per cent between 2001 and 2016.

There have been some attempts to create a "Netflix for books" by the earlier mentioned Scribd and another company called Oyster. Oyster for instance signed a deal with five big publishers and offered its readers a selection of one hundred thousand books for \$9.95 a month in 2012 (Fiegerman, 2013). Scribd on the other hand started its subscription based service in 2013 and signed up a deal with the same publishers as Oyster did. It only took three years until Oyster was closed down and bought by Google (Alba, 2015). Scribd had its own issues and in 2016 it scrapped the business model, which Netflix and Spotify use, the all-you-can-read model (Albanese, 2016).

These two major setbacks for the biggest players on the market show that readers are not up for the popular business model which Netflix and Spotify use. There is a big difference in the usage of the different commodities. Books might not work so well with this business model as they require more concentration and attention than music and film. And the most important variable, time. It takes much longer to complete a book than it does to watch a film or listen to an album of music.

8 Amazon Study Case

Amazon was founded in 1995 by Jeff Bezos, originally selling books only online. In fact, the first office was in Bezos' garage where he had his servers. However, Bezos had the vision that in the future it should be "an everything store" (Hartmans, 2017). It did not take long until there were more diversified items than simply books in the Amazon web-store and in 1999 Jeff Bezos was named Time magazine's "Person of the Year", which he received mainly because he managed to commercialise online shopping (Schneider, 2017). From Figure 8 we can see the dramatic increase of worldwide active Amazon accounts between 2007 and 2015.

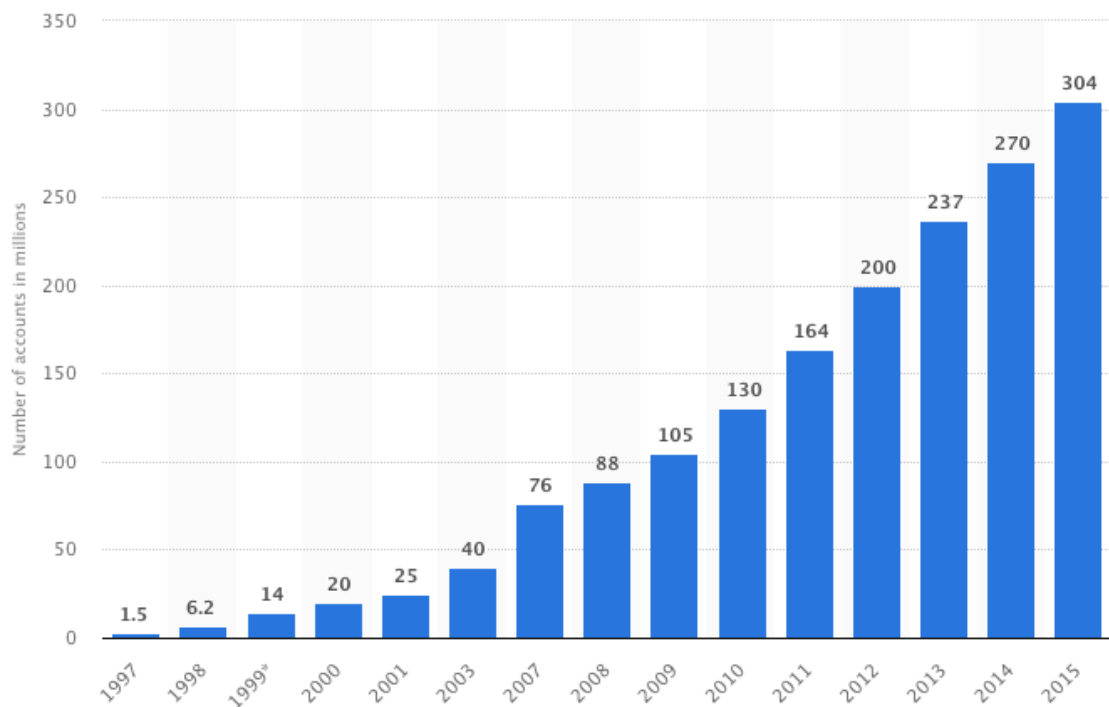


Figure 8 Annual number of worldwide active Amazon customer accounts from 1997 to 2015. Source: Statista (2017)

By the end of 2016 Amazon showed that its sales/revenue was 135.99 billion US Dollars which is an increase of approximately 27 per cent since 2015 (Marketwatch, 2017). At the time of writing, you can practically buy anything through Amazon if there are no regional restrictions and therefore Amazon has grown to become the biggest online retailer in the world.

8.1 Why Amazon?

In the early 1990s when the first online entrepreneurs started their web shops there was little knowledge about the market as it was in its cradle. However, the timing could not be underestimated for Amazon as they were a part of the online revolution and could therefore afford small steps at the time. Compared for a company starting up today it is a different landscape as the online competition today is so much stronger.

Amazon has never been afraid of new additions to its selection and this has attracted a lot of customers who now do not have to restrict their search values to another webstore. Furthermore, Amazon has been able to acquire other online companies, which it has been able to use as marketing for their own products. The best example of this is IMDb

(Internet Movie Database, see Figure 9). While browsing this popular website, film enthusiasts can also search Amazon in one click and then be able to buy the film online. There is also the possibility to stream the film if you are a member of Amazon Prime.

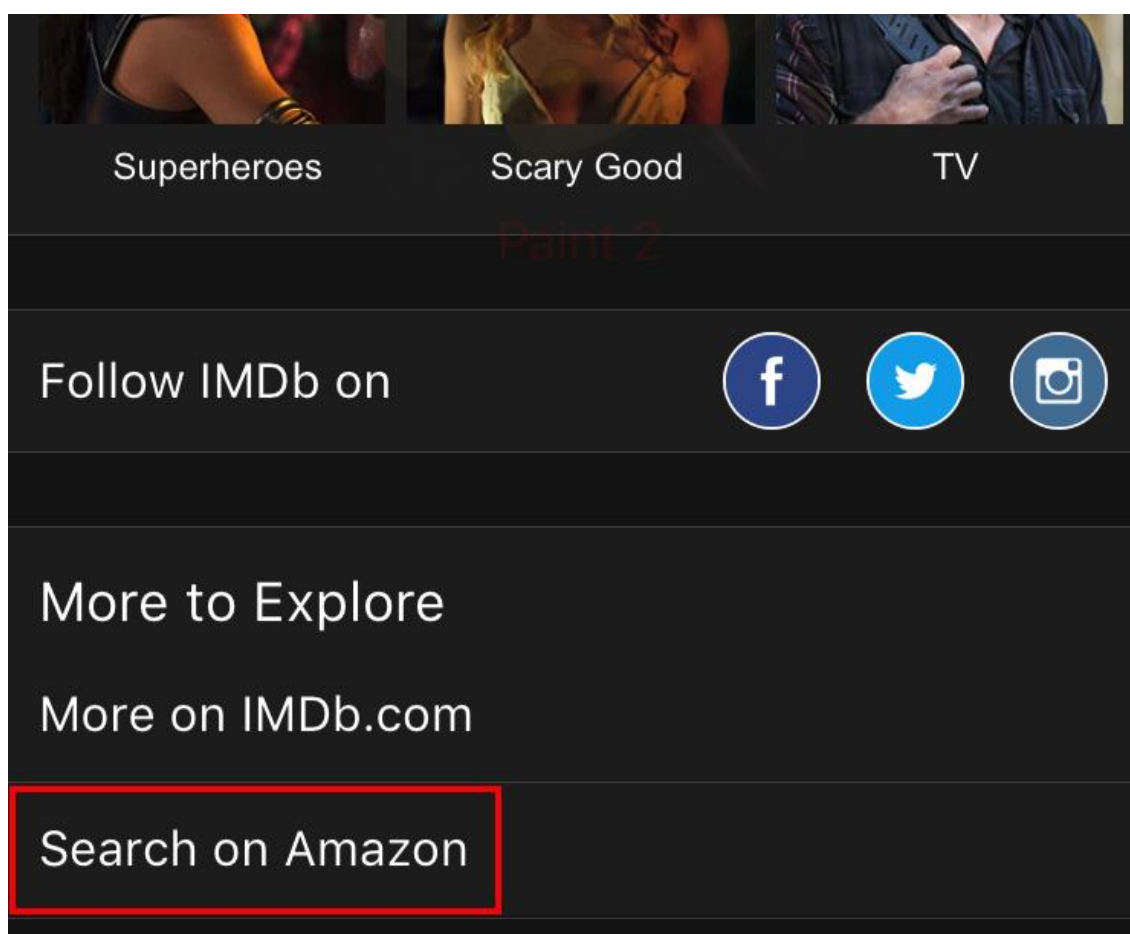


Figure 9 Source: IMDb.com, 2017

8.2 Amazons selling strategy

In previous chapters, it has been described how Amazon has taken advantage of the wholesale model and created loss leaders to attract customers to its website. This has been a major success factor for the company but has not been received so favourably by other actors inside the industry. However, Amazon is making very small profits in its business. Rosoff (2016) reports that the net income for Amazon is stable but very low (almost zero), while the revenue has increased to from zero to 100 billion dollars in less than ten years. All profit that Amazon makes it puts back into the company, following a long-term plan made by Bezos. Instead of feeling satisfied with his business he always looks ahead and invests for future prospects. This might be one reason why Amazon has decided to open up book stores in North America. As described above readers around

the world have started to buy more books and therefore the sales of E-readers plus EBooks have declined. As Gapper (2017) describes in his article: "We are in other words, witnessing not a bibliophile revolution against Amazon's digital hegemony but Mr Bezos changing his tactics".

This can seem rather confusing because Amazon has fought against the physical copies for a long time and promoted low prices for E-books but customers have returned to the physical copy in recent years.

8.3 Publishers vs Amazon

Amazon has fought a relentless battle with several publishers earlier this decade, including Simon & Schuster, Penguin, Hachette, HarperCollins and Macmillan, as well as with Apple. All these publishers were not satisfied with Amazon's way of setting prices for the growing EBook market and therefore decided to do something against it. Before Apple entered the picture the publishers were thinking of creating their own platform, but this did not come to fruition (Spencer, 2012). Instead the publishers agreed to negotiate with Apple who will help them distribute their books with the agency model. On 24 January 2010, all publishers signed the agreement, which came into effect on 3 April 2010. This was the same day as the release of the first iPad, which included the new iBooks app (Apple, 2010).

With more self-confidence, they gave the option to Amazon in the following months that either they adopt the agency model or lose their rights to sell EBook versions of the newly released books by the publishers. Amazon declined the offer at first and stopped selling some of the publisher's books. However, after some time reflecting on the offer it decided to agree with some of the publishers as it did not want to lose new attractive book releases (Patel, 2010).

It was at this time that the American government stepped in and declared that the publishers and Apple plotted against Amazon (Bosman, 2013). Shortly after that the US Department of Justice (DOJ) decided to charge Apple and all the publishers with collusion. In 2012, three of the publishers agreed to settle rather than facing a doubtful trial. Furthermore, they were forced to cancel the contact with Apple and other retailers that had clauses with the agency model in use (Lutz, 2012.) In 2013 the last publishers

offered their settlement with the American government and also with the European Commission, which meant that the retailers could set their own prices on the books (Sande, 2013).

After the lawsuit Amazon backed off and in 2015 it signed new deals with some of the publishers involved in this legal battle (Gapper, 2017). However, this came with fewer discounts on eBooks and later on also a higher retail selling price. Gapper argues that the business had reached to a "competitive equilibrium" and in which both parts could not really agree. Subsequently, the agreement could be seen as a mutual decision even though the parts are far from each other.

So where does this leave Apple? Three years after the lawsuit was finished, customers started to get money back for the overpriced books after Apple lost an appeal in 2016. Apple now has to follow the terms of the settlement that was made back in 2012 and therefore it has to pay out \$400 million to customers and \$50 million for litigation fees (Kastrenakes, 2016).

Apple has not just tried the book market, it has also launched a platform for streaming music, Apple Music, in 2015 (Apple, 2015). As described earlier the entertainment industry has evolved rapidly with digital formats and Apple has been part of the film industry with its Apple TV device. However, it was lacking a streaming music platform with which to compete against Spotify for instance.

With a bright start and lots of promise for customers, the reaction from artists and consumers was mostly negative (Tynan, 2016). Technical issues were part of this but the biggest critique came from artists and music labels. Universal Music Group reportedly banned artists signing exclusive deals with Apple Music and others as it was trying to lure customers with "exclusives" to get subscribers (Hein, 2016). Furthermore, a new customer would have a trial period of three months to decide if he or she would like to continue use the service. For some reason Apple decided that there should be no royalties paid out to artists during this period even if the customer would listen to their song. This created a big uproar from artists and independent labels who demanded payment for their products. Apple decided after some pressure from labels and artists to pay out royalties during the customers' trial period (Dredge and Ellis-Petersen, 2015). Universal

Music Group has since signed an agreement with Apple Music so its artists are promoted on the platform.

In 2017 Music Business Worldwide reported that Apple Music has 27 million subscribers on its platform. Spotify on the other hand has 53 million subscribers but attracts more than 140 million active users because of its free listens that include commercials (Ingham, 2017). Amazon Prime has 63 million subscribers, however with less range of music than Spotify and Apple Music (Shi, 2016).

8.4 Amazon Prime

Amazon has its own streaming service of music, eBooks and films. Also included in this is faster shipping, exclusive early offers of products and free game contents (Amazon, 2017), all for the prize of \$10.99/month (£7.99 in the UK). At the moment, there are few competitors that have the same wide selection as Amazon has online. You can of course pinpoint companies that have a more specified direction of business such as music and film and then giants like Netflix and Spotify could be mentioned. However, the existing competition comes from Ebay and Walmart, which has started to offer the same kind of exclusive offers for a pay up front membership in 2015 (Smith, 2015).

Lately the competition has also increased in both bricks-and-mortar and online stores as Amazon bought the Whole Foods chain, which has more than 400 grocery stores around North America (Lutz, 2017). This is a clear attempt to challenge Walmart's grocery dominance in the USA. However, Walmart is also trying to challenge Amazon's supremacy online. In 2016, it acquisitioned Jet.com (the American e-commerce company) and in 2017 they bought Bonobos (another American e-commerce company) to strengthen its online presence (Nicolaou, 2017). This is quite a U-turn made by Amazon as before it has concentrated on its core business, online retailing. However, now the retailing competition gets even tougher, both online and in physical stores.

9 Conclusion

The digitalization of the book industry is advancing rather slowly, in contrast to the rest of the entertainment industry, where it has been the complete opposite situation. New platforms have emerged from digital sources so the need for physical products in music and home video industry has changed the market. However, in the book industry the customers cling on to their traditionally made book, which retailers over the world gladly appreciate, but not without a concern for the fast-developing future.

So, what is the difference between these products, physical and digital?

Firstly, the music business could not stop the development of downloading and later on the streaming services with which they now try to co-operate. Gone is the need for a physical format and instead customers have a subscription of Spotify or Apple Music. Customers have adapted to the digitalization of the music business very well because the end product comes out of the same source as it has always done, the speakers. However, this is often in less good sound quality (MP3 format) but the common person cannot really hear this if he really does not try to compare with other formats such as CD or vinyl.

Secondly, the home video industry has had the same type of evolution. From the old VHS cassette to the Blu-Ray and finally to the subscription based streaming services such as Netflix, customers have now largely given up on the physical formats. The end product comes from the same source as it has always done, the television, in addition to computers and personal communication devices.

That leaves us with the final format, the book. Even though there has been a growing digitalization customers still value the traditional book over the E-readers, especially in Europe.

So, what differentiates this digitalization from the other two formats?

The end product does not come from the same source as it always has. Customers have to use a new digital source to be able to read the end product and this is where I think the main issue is for the digital format suppliers such as Amazon. People nowadays use

computers in almost all their work but they are not used to reading their books from E-readers in their leisure time. They are used to turning pages and smelling the book the first time they get it home. As stated in a previous chapter there is a trend among adults in Britain where they try to cut screen time at home. This is a perfect example where people return to the physical copy to get away from the everyday computer usage.

Before I completed this thesis, I was convinced that the digital revolution of the book industry would share the same fate as music and film. However, I am not so sure about this anymore.

The usage of the different products in the entertainment industry affects the business model. To read a book demands much more effort from the reader than listening to a music album or watching a film. No disrespect to these art forms but it takes more concentration and time to read a book. And time is a limited resource. You choose to invest in your time by reading than by doing other things. With music, you are not restricted to only listen to music. You can do so much more at the same time and therefore people have more time for music and thus invest in it.

It's for this reason I believe that the "Netflix of books" never really took off. People rather invest in music or film platforms as you don't have to spend a very long time in front of a screen, which you might already do at work or in school.

For the book to take off for real in digital format it has to offer the reader something new and innovative. At the moment, there is nothing like that, whereas the normal physical book remains convenient and rewarding for the reader.

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