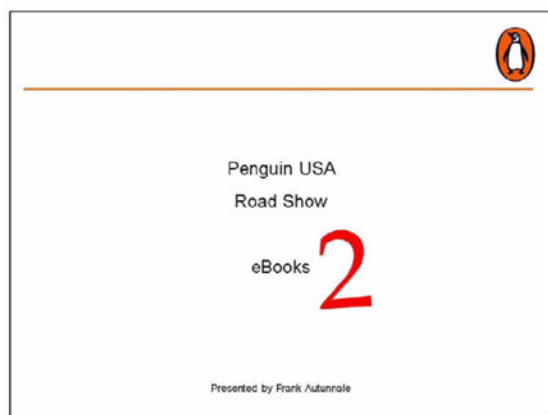


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Good Afternoon.


My name is Frank and I am the VP of Finance for Penguin Group (USA).

As some of you who were here last time Penguin hosted a road show, you may recall we presented an eBooks story. So, here we are again, two years later and thus eBooks 2.

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eBooks – Where are we today?

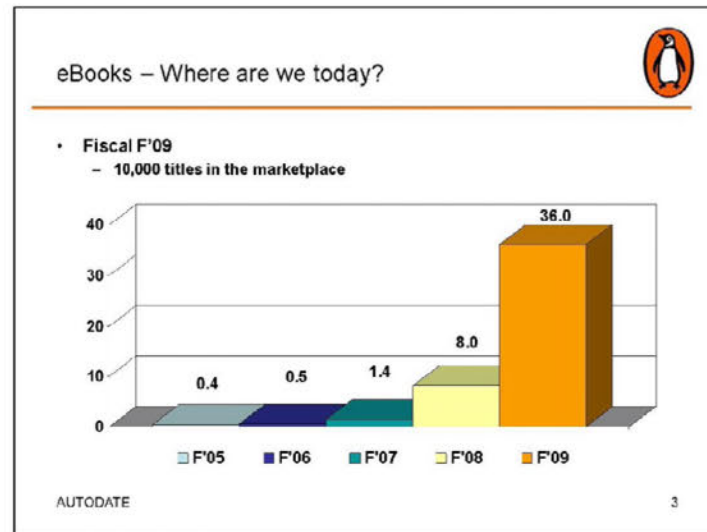
- **Penguin Road Show – Fiscal 2008**
 - Rumors continue to circulate that Apple will release an "iBook" or "iTablet" shortly.



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While preparing for this presentation and reviewing the last one we did, this slide jumped out and I thought this would be a great slide to start with. At that time, there was much speculation about the impact Apple would or would not have on eBooks. Two years later, the Apple iPad is here and has changed our business in more than one way, which will be addressed later on during this presentation.

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Where are we today, the theme of this presentation...

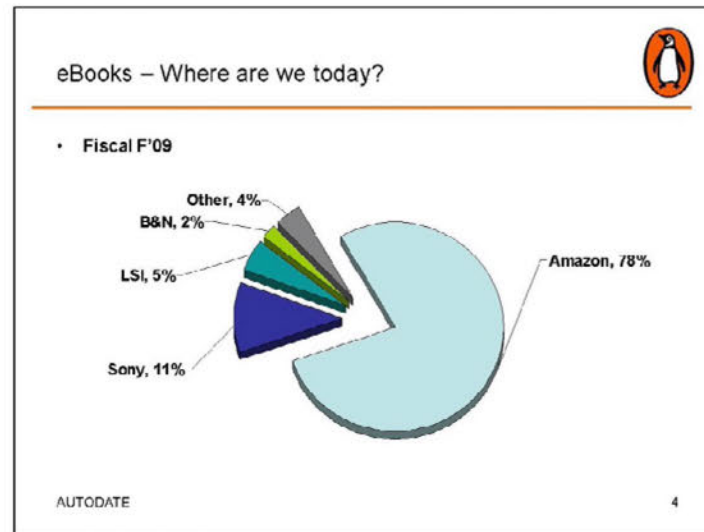
The best place to start would be to bring everyone up to speed since the last time we spoke.

We have invested to convert 10,000 titles to be available in the ebook format.

As you can see, eBooks is growing quickly or exponentially.

F'08 grew over 500% to approximately \$8m and F'09 grew by over 400% to about \$36m.

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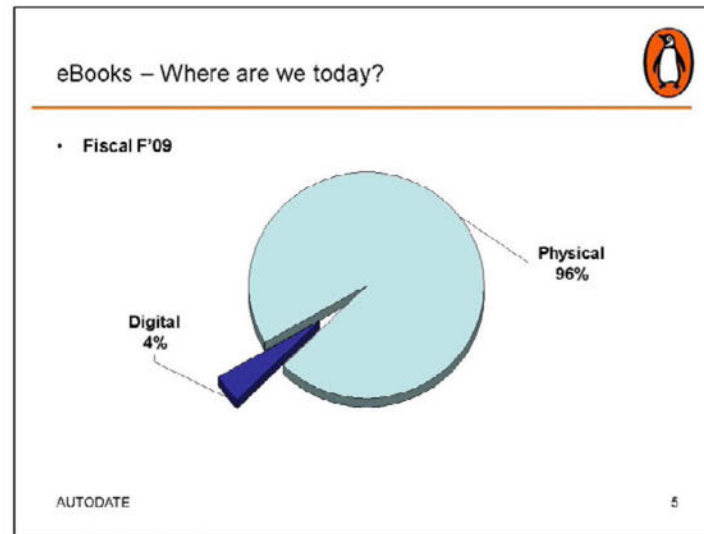


The customer profile shows a large concentration with Amazon, more or less controlling about 80% of the market share.

Sony has slightly decreased but is maintaining its share with loyal customers who enjoy the experience of the device and the interface.

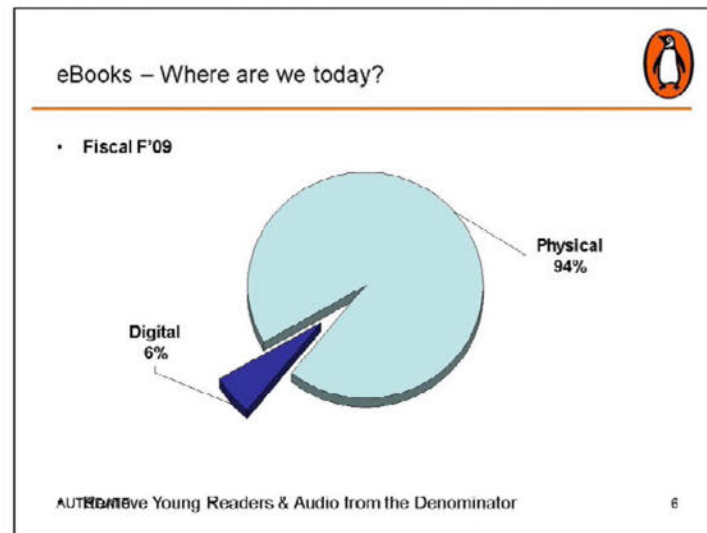
B&N at 2% was a late entrant into the market, sometime around Nov, and was growing quickly by the end of F'09.

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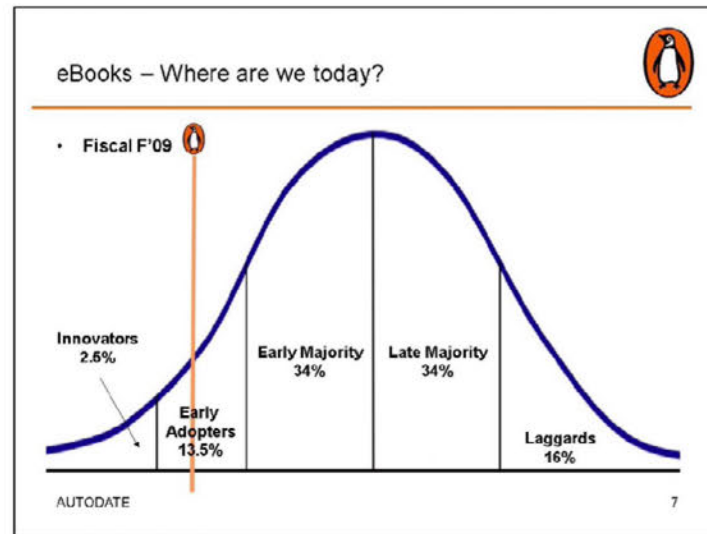
Although eBooks are fun and exciting, and some such as Tina may call them slick and sexy, this graph is very important as it reminds us that eBooks remains a small part of our business at 4% overall by the end of Fiscal '09.

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Perhaps a better metric would be 6% if we eliminated from this calculation businesses that don't really apply at the moment such as the Young Readers division and our Audio group.

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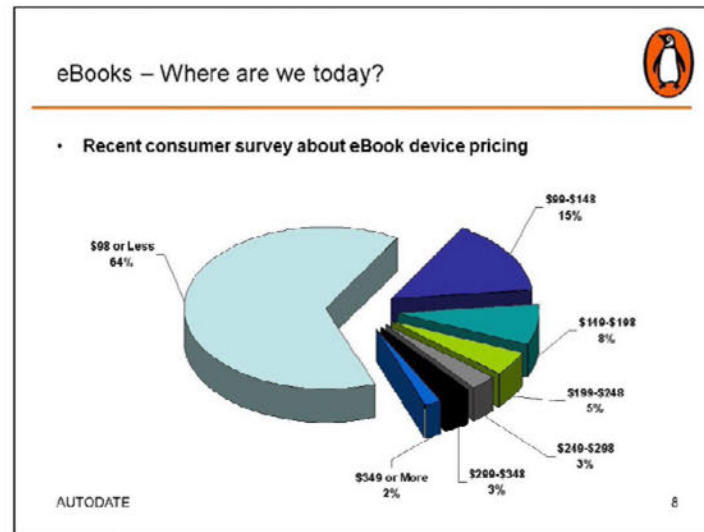
Assuming the 6% is somewhat accurate, what does this tell us about the future when compared to a standard lifecycle bell curve.

We can clearly see that by the end of F'09, we have moved into the early adopters stage.

Now, as Finance individuals, you may be wondering when we enter the next stage?

And that is a great question... so perhaps the next few slides will help us gain some clarity.

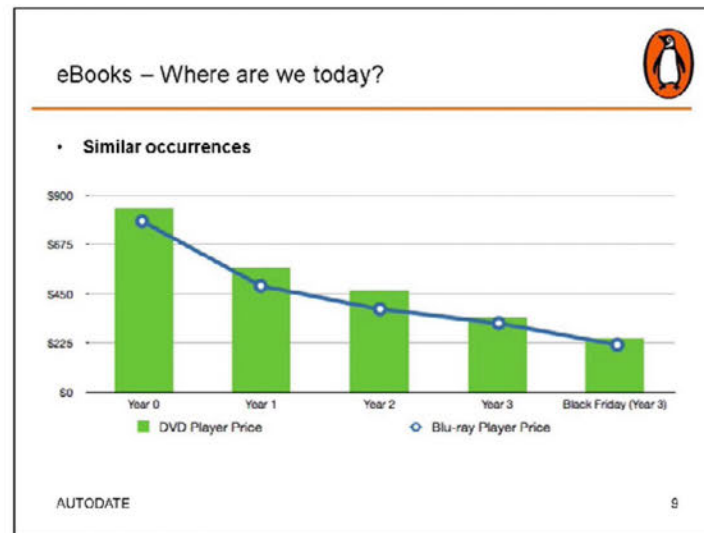
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A recent consumer survey completed by the Gartner Research firm found more than 60% of those surveyed would buy an ebook device if the price was about \$100.

Despite all the hype around the pricing of eBooks, the real discussion should be focused on the price decrease of the actual devices.

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Since eBooks and the devices are still in virgin territory, we have to rely on other similar occurrences to help us predict the future.


Looking at this chart, the DVD player and a Blue Ray player took a number of years for the price to decrease enough to be adopted by the mass market.

Flashing back to the chart, the catalyst which forced lower prices were cheaper devices coming from countries located in the pacific rim.

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eBooks – Where are we today?

- eBook device pricing
 - Apple iPad \$499 - \$899
 - Sony Reader \$299
 - Amazon Kindle \$259
 - B&N Nook \$259
 - Borders Kobo \$149



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Recall just a few slides ago, where more than 60% of the consumers surveyed would buy an ebooks device if the price was right.

So, here comes the Borders Kobo, about to be released very shortly. Will it be the device of choice? Unsure...

Will it put pricing pressures on the rest of the industry... maybe.

However, Apple as we all know doesn't bow to pricing pressures as demonstrated by the expensive Macintosh computer line.

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eBooks – Where are we today?

- **Windowing – November / December '09**
- Publishers have come to fear that the bargain prices will lead consumers to conclude that books are worth only \$10 or less.
 - HarperCollins Publishers, Simon & Schuster and Hachette
 - Delay publishing the eBook publication
 - Four weeks to six months
 - 5 to 10 titles each month
- **Defensive strategy:**
 - Dramatic stance against the cut-rate \$9.99 pricing
 - Protect the price of new hardcovers
 - Devaluation of books
 - Protect the brick and mortar stores

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Instead of driving the market with low cost devices, Amazon began to deep discount the pricing of eBooks. With approximately an 80% marketshare, this caused a lot of problems for publishers. Not so much because of the financial impact of the deep discount as Amazon was bearing that subsidy, but because of the perception of what an eBook should cost to the consumer. Publishers were concerned this price point would become the norm with consumer expectations.

Several publishers began to experiment with a concept called windowing whereby the ebook would be delayed anywhere from 4 weeks to as many as six months. This was really a defensive strategy designed to combat the low pricing by Amazon. Also, the brick and mortar stores, who have been our lifeline for years and cultivate grass roots sales campaigns were being negatively impacted by this pricing strategy employed by Amazon.


Penguin finance spent several weeks reviewing what if scenarios about what impact windowing would have on our business since any delay in the ebook would be severely impacted by missing the corresponding ad campaigns with the new release.

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eBooks – Where are we today?



- **Agency Model – (Jan - April 2010)**
 - Pricing control
 - Some discounting benefits
 - Eliminates the need for windowing
 - Apple & the iPad (2m units in 2 months)
- Who is in?
 - Penguin
 - HarperCollins
 - Simon & Schuster
 - Hachette
 - Macmillan
 - and a few others



Who isn't?

- Random House

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Before Penguin could make an executive decision on Windowing, the pending release of the iPad mad that concept irrelevant. As a way to enter the market place, Apple proposed moving the entire industry to an agency model.

Tim will explain the monumental effort this exercise took, but briefly...

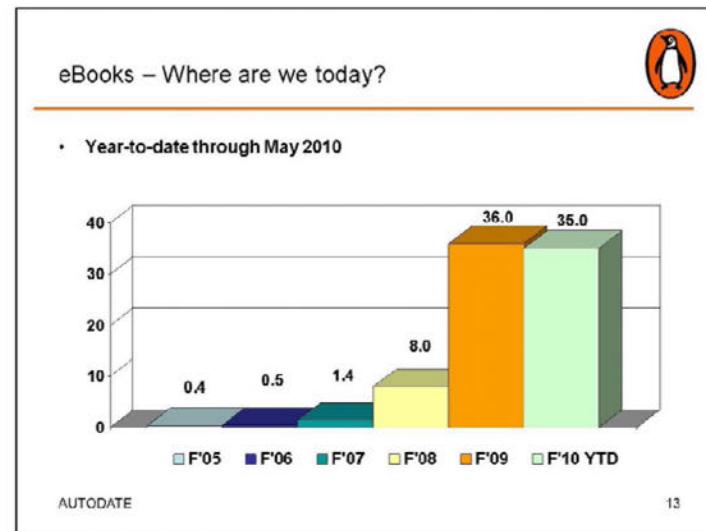
The “agency” model is based on the idea that the *publisher* is selling to the consumer and, therefore, setting the price, and any “agent”, which would usually be a retailer but wouldn’t have to be, that creates that sale would get a “commission” from the publisher for doing so. Since Apple’s normal “take” at the App Store is 30% and discounts from publishers have normally been 50% off the established retail price, publishers can claw back margin.

Walk through a simple model of

HC \$26 list, \$13 wholesale, agency about \$9

MM \$7.99 list, \$3.99 wholesale, agency about \$6.99

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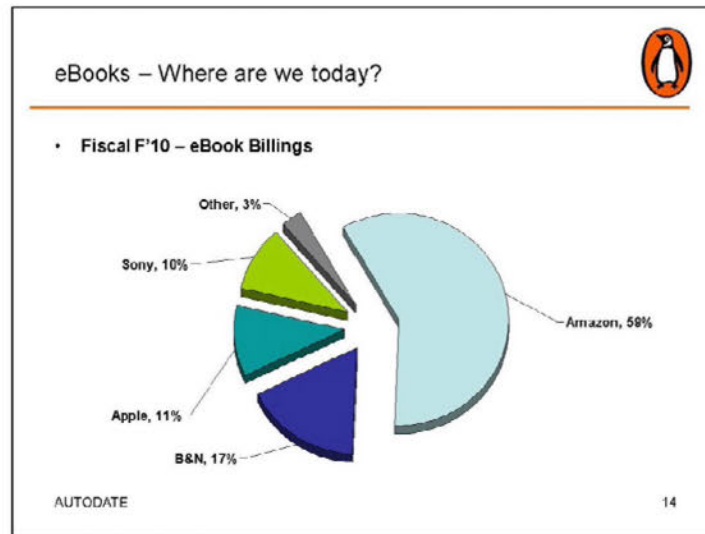


Where are we today?

Here we are in an exponential growth curve. We have been through a lot in the last six months and I will avoid discussing Cannibalism, proposed new royalty rates and piracy as we will save that for the next show in a few years. As finance individuals, I will assume more data is best...and with that said, as you can see, we are still experiencing strong growth in this channel. With 5 months behind us, F'10 is almost equal to the full year of F'09.

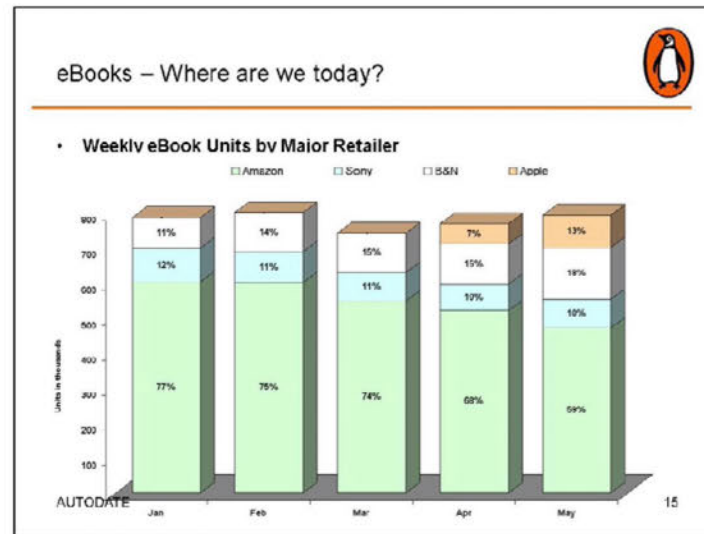
The change to the agency model hasn't really slowed this growth curve...

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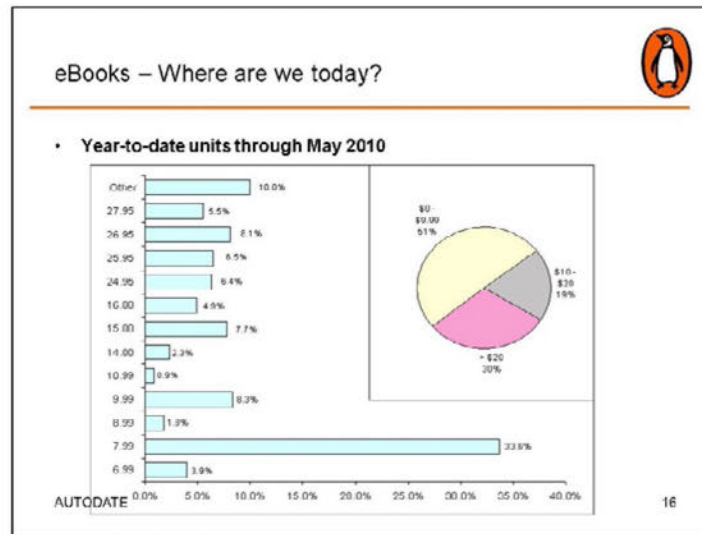
However, the Agency model has allowed Apple to gain a foothold in the marketplace, along with the organic growth from B&N and has decreased the market share for Amazon to approximately 60%

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This chart shows a trend analysis which will illustrate the decline in the Amazon stranglehold it once had on the marketplace.

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In response to some questions regarding price sensitivity, this profile of our business is very interesting showing more than 50% of ebooks sold were lower than \$10. Just to be clear, this price point is the physical price point, not the ebook price which fluctuates according to certain business rules.

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In Summary, where are we today – well... its been very busy time for us.

But...

The question is where are we going...

On the horizon is Google Books

iPad apps specifically designed for a book.

Imagine an animated Winnie the Pooh app... or A Very Hungry Caterpillar app.

More new devices...

And even some newer versions of existing devices – Kindle 3 due out in the 3rd quarter.

Simply, its not going to stop...

At this point I would ask if we could hold our questions til the end of the session, and I would like to welcome Tina McCormick up to speak next