

9 15, 2008- Conference Call  
Executive Minutes  
CONFIDENTIAL

1. Review June Minutes

2. Financial Recap

- Month/YTD-- Janet
  - Month of August- \$20 million down. Sales way down from budget and prior year. We did have the pull forward, but we're still lower. In terms of expenses over budget and prior year. Everyone came through
  - August YTD- Down \$28 million and \$16 in expenses. Some conversion of expenses vs. YTD profits are below in excess of sales. Main driver is lower sales coupled with higher expenses. Some budgeted but taking toll because sales not there.
  - FX going to start playing in. We're going to start talking about true increases. Last year UK we were at 2 now it's lower. Expenses look better but with exchange they're not.
  - Cash Flow- Down \$21 million. We also have a hit coming into the year. You're seeing the impact of profit. But going forward we won't have anything to collect so it will deteriorate going forward.
  - September- Is down even with Oprah. \$24 million down.
    - Question will be is it structural, timing issue.

2. Quarter- Down \$54 million. Let's look at it versus last year

• \$54 million. Let's look at it versus last year. From prior year down \$21 million in revenue \$42 million in profit, we're really down in \$10 million in actual revenue with FX. Within quarter marketing M&P are 20% more than last year. It's mostly in UK and General Books. Direct expenses are up 9%, in excess of merit increases. Overhead G&A areas we're up 20% (severences, overhead, Borders reserve). That's explainable. Wipes our Profit

- YTD- We're down \$67 million in profit. M&P up 12% all the other are up close to 7
- N/A O5ther- Up \$16 million negative. It's where we have our BGI Reserve, severance, savings. Costs us \$5 million this year. Compared to last year, we did not run a business that ran \$165 million in profit last year. Within \$165 we had 15-20 million that got us there. Stock came in, insurance payment, etc. That brings us to \$150 and sales push cost us \$15 million in profit.
- Brian- We're pulling out the stops to get to the number for News and they won't be happy. Also, it seems to be continuing. We don't have anything to put to. What number should we pick as FY Forecast, how low? But, what changes do we need to make to get it to X number.
- Vicky- We have three extremes 1) we've given you 2) \$2 million off 3) \$3 more. We have normal forecast but it's not cautious.

• General Books:

(severences, overhead, Borders reserve). That's explainable. Wipes our Profit

- Sales are down. Big hits from last year that we can't replicate. We're not getting the billing from what we pulled but we're getting returns.
- Top 20 gross sales we're not having hits from last year. Edgar Sawtell has higher royalties.
- Higher Royalty provisions. and prior year.
- Top 20 Returns: \$6 million, in F08 was \$9. We're getting a lot of backlist returns. Overheads are up.
- Paper- We downgraded our paper for hard covers but it brings us back to budget. We're looking at jacket design. We're are managing T&E. I haven't pulled a lot on Marketing. We've raised some prices. Tasking sales to get backlist out there more. HarperStudio is costing us and not bringing anything in.
- Every year we've had a surprise hit, it's only 3 months in so I hope something will happen. I am meeting with publishers to see what books could break out.
- We can cut whatever we need to do.

• UK:

- We have a 4.6\$ million pension increase and investment changes. If you stip those out we have \$11 million positive.
- Q1 has been disappointing because costs have been hitting us. M&P is \$1.3 adverse, cost to get big books into stores.
- I would like to take \$2.1 million of profit. Revenue would be down to \$4. That's assuming a 50% mid-case scenario. Ed submitted a forecast that doesn't include any risks. Then you would be \$9 million pounds increase in revenue with flat in profit.
- List of risks: backlist run rates are down, it's a market situation. We're performing better than the market but still we're not having profit. It's mostly co-op. It's massive competition to get into Xmas promotions. We decided we have to pay this year.
- Margin on someone you have to pay all this co-op? ie Ramsey- 290 units we'd have a good margin. All the marketing costs go out in Q1 for holiday. In September they release, some of it will unwind.
- B- in shift from Q1 this year v. last year was there a lot? There was a little bit of damage by pulling books into last year.
- UK- Economy is doing terribly. That's why I think the number we put in is too high. UK could be in serious recession soon.
- Brian- Marketing one sticks up. Some of it unwinds. Vicky- We're looking at canceling some. If we shave too much marketing then we will lose revenue.

John Makinson, Markus Dohle, Carolyn Reidy, John Sargent- dinner. He's in publishing 101 mode. David Young organized dinner. Marcus- he's trying to understand how decisions get made. He was culturally and experience wise got a big learning curve. Everyone is worried about the economy. Hachette is doing well because of Stephanie Meyer. Marcus is looking at P&L and trying to understand valuations.

• Zondervan:

- Marketing Spend Analysis with help of Harper1 and two consultants. Spend 10% on marketing but don't sell a lot. H1 and Moltnoma sell a lot more books. The dollar amount is lower but percentage per book is high. H1 spends about .75/book but we sell so much less. We spend \$10 grand on a book and they spend \$25K.
- Marketing M&P has not gone up. Events business gets put in there and then it doesn't work.
- We had a 10\$ million beyond normal gap. We reduced it so now we have growth of \$6.4 revenue. Q1 yoy looks fine. Sarah Palin October 14 on sale. Revenue for forecast for year is up \$9 million .
- We have lost a lot of market share the last two years. Nelson did too. We have to turn that around.
- Q1 1.5 million help from Brian and came down another 1.1 million. EFR hit us by another million. Competitors are seeing returns like crazy that we're not seeing.

• Childrens:

- Narnia went from being a profit enhancer to depleter. This year we'll have -5 million returns. It's a huge disappointment. First movie had 20% return, this one we had 16 sales and 6 million back. We have a guarantee as a house to the CS Lewis estate, we have \$1 million a year on write offs. It was a staircase. We thought we'd do prequels but the estate is saying no to everything. If we can't do new books then it will be a profit depleter of over \$1 million/year. We never thought we'd have a write off in F09 because of the movie.
- Swing in Narnia is 22.8 million down. We have to reduce it as much as possible. We think we can reduce it to \$12.7. Projected to contribute 11 million negative swing.
- There are not usually things in news that will help us. LC is the closest. Marketing is title by title and nothing in here for books that we haven't signed. When you have P&L meeting they will say that we don't market aggressively enough (touring, advertising, creating materials, etc). 5.8 percent is what we spend.
- This is more optimistic than middle of the road. We usually have a shortfall of 18 we're saying we'll have a shortfall of 7. But I don't want to put it back.
- I took out investments. The only thing I put in was a business manager for new P&L structure. Digital person strategy is on to do strategy but no money there once it's done.
- I assume 5.5 million pull forward into F09 from F10. Janet- We don't want to do that.

We have to make a decision today/tomorrow. Budget is due Thursday. We have \$94 right now, it could be \$90. What's the responsible thing to do. How we position this is important for all of us. Janet- I would say \$86. Bring everyone to middle of the road. Last year we delivered \$165 do we want to go in at \$86?

Discussion of whether or not F10 will be better than F09 and we can say that to them. F09 is suffering from pulling into F08.

Let's say it's \$86 for now. Bonus would be lower (\$10 million benefit of budget \$17). We have to look at T&E and other costs, G&A positions. ERP project/infrastructure, should we look at consolidating warehouses, etc?

F10- \$160 is the number rolling up- General books would go up \$30, \$42 kids, \$24 Z, 2 million Canada, UK \$25. Other would come down. How comfortable is everyone with that? Is there a structural problem or is it a hangover from last year?

In a flat market should we be self funding are growth initiatives. If they give us some incremental money maybe we can make it work.

Zondervan- I have a structural problem. I can't cut costs. You did big layoffs. You're putting people back in the right places. Vicky- I think I've done that, I've cut people but we haven't put people back. If Z doesn't get revenue up there's not business.

Brian- Zondervan needs to figure out what the biz is without the CBA. Is there a time to look at one warehouse/1 system. Should we look at the footprints. Could that help

Vicky- UK and Australia getting out of distribution would be a good thing.

If we go with the lower number I would like to say next year will be good and these are the short term things we're doing to mitigate, and then also from long term perspective these are the changes.

UK Distribution- We looked at it. Lease goes to 2025. We have to try to get out of it. You don't want a distribution center there. We'd like to get out of it. I did speak to James Murdoch about looking at it as they look at property leases. Keith is also looking at getting rid of the pension fund. Brian- I would like to see fixed costs if you outsourced. Outsourcing could help UK and Australia. Maybe look at Arbaya (Fox DVD biz).

Zondervan- We look at it but we own the space. The customer service is good. Labor is low. I don't know if we can find something new between now and ERP.

Larry- HC configuration of 3 locations could be looked at.

Is there anything that can come out of fixed costs. They don't want to own warehouses.

Janet- 94 going down to \$86. What if for Q we put in \$2UK and \$2Kids and that gets us to \$100, \$10 for bonus. We go with that number for John. We take bonus out of corporate for now and then move it into divisions for next quarter. We'll be \$35 under budget.

## 2. Digital Structure- Carolyn/Charlie

- Book Army- Charlie
  - Launches in 9/22 beta. 200 people in UK using and testing it. Adding 200 more. Then adding US. Launches to public at Frankfurt
  - Book resource, Social Networking, referral engine. We've bought Neilson data base of 6million books. Anyone who googles will be sent into Book Army search, then they can access social network, etc.
- Projects Road Map
  - Authonmy, Naturalist web site, Tolkien ecommerce site, October- B2B.

- Authonomy- Digital slush pile website. Community of aspiring authors, best come to top. We will read top 5 titles every month. Going to offer POD service. Within a week there are 700 manuscripts, 3599 registered users. 10% visitors are returning 200x/month.
- Digital Structure
  - Harpercollins.co.uk- faces the wrong way. If people come to that site, then they want to find something about HC as a business. If you want to talk to consumers then it has to be about books.
  - Business 2 Business site- October 30 launch. Who we are, corp comm., author care, etc. Book
  - Book Army will be consumer proposition- 10/15 launch.
  - Revenue Generating business- ecommerce, ad funded business, etc. (lola love, Tolkien, Voyager).
  - Under it all is e-crm business. People are pushed around to the appropriate site.
  - We use data to drive the revenue business and marketing in general, and that pushes into database who we can market/sell to.
  - We will take all our different online assets and come up with a migration plan. Let's adopt this as a structure and for HC overall if it works. Can we focus our energy around this.
- HarperCollins U.S.
  - Basic book/author content also sits underneath. Content helps us drive traffic.
  - Sneak peak/full access is making a big difference. Pass along is 30%.
  - Author Assistant- 200 authors- how/where do we want it to scale?
  - Authors on Air- online radio channels.

Questions to examine—Brian:

- Symptio, book army, etc. at what point do we pick the areas of focus?
- Web hosting, IT support, etc. are there opportunities for better service, lower cost, etc. When do we get smart about it?
- Are we fully taking advantage of News Corp? FIM has 3 groups: publishers, audience network/montization, tech people (i.e. browse inside) build tools that are available to all News Corp and 3<sup>rd</sup> parties.
- At what level do we look at this from the big picture with all these great things. We could be tripling down.
- Do we have a vision for where we want to be in 2 years with content?

Janet- Please send me F10 number and 2) we have 10 million of investment spending in numbers in this year. How much have you not committed of that 10? Cash Flow we didn't talk about, \$11 million for company. We haven't been under 100 for the last 7 years.

4. Comp Strategy- Jim

- Proposed F09 Incentive Plan
  - Currently everyone is at the same rate. We evaluated consultants ideas made changes. We need to look at P&L managers we need to empower them to lead. I

want to meet with them globally twice a year. The second level was editors. We fine tuned something for editorial staff. Tailored opportunity to allow them to make more than they do today. Will help keep fixed costs down.

- Publisher Incentive Plan: Base 300K, could be up to 25% bonus. We want to change it so that if they blow away the cap would go to 50% bonus, not 25. Also, there is a long term incentive program (paid out over several years) tied global operating. Based on growth. Paid 50% in first year and the rest is rolled out over 4 years. People responsible for P&L and creative team.
- Editor Incentive Plan: We want to give them the opportunity to double their salary. Senior editor \$250, capped bonus at %15. Now we want to say 15% incentive bonus, and 85% “top hat” bonus, i.e.- Oprah pick. Still participate in annual bonus but could double salary.
  - Top Hat Metrics: Your project will deliver \$1 million contribution and 25% profit. Also, look at editors overall portfolio, if they have one great hit but the rest are bad, they won’t get full 85% (discretionary). Retention element as well- payout has 3 year payout.
  - Over time there have been realitively large bumps to keep people but now we don’t have to increase base. We’ll pay for performace, but through bonuses.
- Executive Teams: Will have a long term incentive plan.
  - Can earn 50% of salary on a long term basis.
- Long Term Incentive Plan Example:
- We’re trying to pay for creativity and changing the culture.
- Brian presenting to Peter on 9/24. We’ll roll out after approval.

#### 4. Zondervan

- Christian content distination with Fox Media
  - Audio, Video, bibles, manages content and lets consumers create their own content
  - Aggregation of authors.
  - Purposign a number of acquisitions
    - #1 bible sites, 8.5 million uniques/month \$6 million. Biblegateway.com
    - TheCity- Christian church community network. Lets churches manage community online. Owned by a church (in 2 months 5,000 people).
    - Church Communications Network- event market is a huge market and it’s growing. \$12 million. Allows us to broaden revenue streams.

#### 4. Larry- Update

- Paper market-
  - Continues to be bad. It’s going to get worse. There’s a lack of competition on big player. Working with News Corp to try to help. Europe is consolidating as well
  - Besides going down in grade, we can raise a little
  - Cost Savings Initiative
    - Teams created with focus areas. We expect huge submission of ideas.

Digital Print Program-

Can't keep up with demand. We shut it down Nov 1. Farmed it out and will save money on galley, ares etc, 735 K savings, hopefully 500K in this fiscal.

POD- Is exploding so we're trying to coordinate everything on a global basis.

Sony Waterstons, DPS group and ebook UK group- Team put out 2000 ebook titles in 3 months, \$20/title we made. It's been total chaos,

Amazon- Pushing/ Random UK- has gone to 50% discount with co-op everything. They want us to meet random with co-op in current year so we're going to say no. Not inclined to give more. UK/Zondervan- there's no more money to give. Paper prices are up 30%. I did say we will be raising prices. I don't think we can afford to give anything. Zondervan wants to move to our terms.

Borders- kicking off plan to get balance down with borders. Letter to g. jones saying all we're doing to cut costs and boost sales, and with borders we want a 12 person team that reviews EDI orders that come to us. Josh is following up with BGI team. Every EDI order will be reviewed over 24 hours and we won't ship what doesn't need to be. In borders we can look at slow/fast movers, etc. Since George is supporting, we're trying to reduce balance by half. Industry view is that no ones if they can survive.