Smart Libraries Newsletter

News and Analysis in Library Technology Developments

ALA TechSource
alatechsource.org

50 East Huron Street, Chicago, Illinois 60611-2795, USA

ISSN 1541-8820 February 2020 Volume XL Number 2

Smarter Libraries through Technology

High Stakes for Digital Lending in Public Libraries

By Marshall Breeding

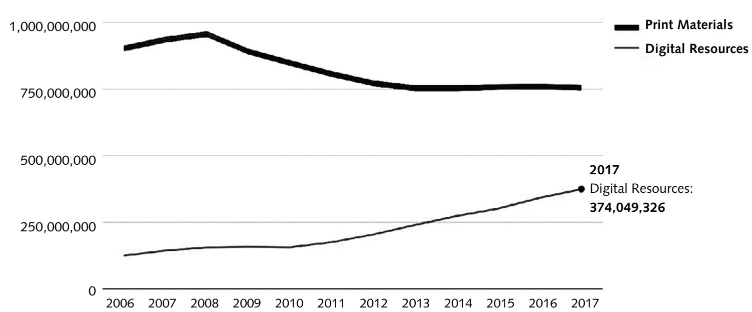
It's hard to imagine a topic of greater impact to public libraries than digital lending. Public libraries continue to invest higher proportions of their collection budgets to digital content. As illustrated in Figure 1, public libraries in the United States have steadily increased their investments in digital content. In 2017, the last year for which statistics are publicly available from IMLS, digital resources exceeded over $374 million. Most of this spending goes to subscriptions to digital lending platforms and licensing of e-book and audiobook titles. While aggregate spending on print materials by US public libraries has diminished since 2008, it has held steady in the last few years. If these trend lines continue their current course, access to digital materials may surpass acquisitions of print materials within a few years.

Patrons love library e-book lending services. In a recent press release, OverDrive reported a 20 percent increase in public library e-book and audiobook lending in the last year, with 326 million checkouts. Seventy-two libraries exceeded over one million digital loans. These figures include only the transactions carried out via OverDrive's own platform. Adding in those done via competing platforms, the volume of transactions is considerably higher.

Today, digital lending by public libraries faces enormous challenges. The pricing and lending terms offered by the publishers are not especially favorable to libraries. In recent months, the limitation set by Macmillan to offer only a single copy with no simultaneous use for an initial embargo period for new titles has sparked outrage by libraries, leading to some boycotts of digital content from this publisher. In previous rounds, the requirement for libraries to repurchase titles after a set number of lending transactions sparked concerns. The broader dynamics of library lending in relation to digital sales to consumers by the publishers and distributers remains an unresolved conversation. In a recent call, Steve Potash, CEO of OverDrive, reflects a view that most publishers see positive benefits in digital library lending, with those imposing restrictive terms not necessarily representative of the publishing industry.

In recent days a major industry event has taken place that has the potential to make a major impact on the public library digital lending ecosystem. The transfer of ownership of OverDrive from Rakuten to KKR, which also owns RBmedia, sets the stage

Figure 1: Material Expenditures for All Public Libraries in the United States



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for a possible consolidation of immense scale. Although the sale of OverDrive has not yet finalized and any consolidation is speculative, this event warrants close consideration by the library community. Such a consolidation into digital lending superpower raises concerns as it narrows options and choice. But it also may represent a beneficial advantage in the balance of power in the dynamics between those representing library interests for favorable terms in digital lending versus the pressures exerted by the publishers. It is possible that an organization with more clout could help libraries win more favorable pricing and terms.

This issue of *Smart Libraries Newsletter* features the proposed acquisition of OverDrive by KKR. It includes the details of the transaction currently available and context related to the business environment and the background of the companies involved. Readers can expect ongoing coverage of any additional events that might unfold, including any partnerships or consolidation among OverDrive and RBmedia or other related organizations.

OverDrive to Change Ownership

OverDrive, the largest commercial provider of e-books and other digital content to libraries, issued a Christmas Eve announcement of its pending change in ownership. The company's current owner Rakuten has entered into a definitive agreement to sell OverDrive to KKR, a major US-based investment firm. As digital lending continues its steady rise, this news sparks interest and raises questions for the library community.

OverDrive Position with Libraries

OverDrive holds the dominant market share as the leading provider of digital content to libraries for lending, with more than 43,000 libraries subscribing to its content lending platform. OverDrive's catalog currently offers 4.5 million books and audiobooks from over 25,000 publishers. Over 95 percent of public libraries in the United States and Canada rely on OverDrive for digital lending, often supplemented by other services. Though public libraries represent the largest portion of OverDrive's customers, it also works with schools and corporate libraries. Libby, introduced in 2017, enables library patrons to search, checkout, and read e-books and audiobooks that their library has acquired through OverDrive.

Rakuten: A Short-lived Relationship

Rakuten, a large multinational conglomerate based in Tokyo, acquired OverDrive in March 2015 via its subsidiary Rakuten USA in a transaction valued at $410 million. OverDrive resides within its digital content portfolio, which also included Rakuten TV, Viki, and the Kobo platform for e-books and audiobooks. OverDrive's position in library lending complemented Toronto-based Kobo's focus on e-readers and content for the consumer market.

Founded in 1997, Rakuten employs over 17,000 personnel spanning 30 countries and has an annual revenue exceeding $10 billion. The company's 2018 annual report emphasized the company's expansion as a telecommunications provider in Japan, working toward a fully cloud-based 5G mobile network. Within a company mostly focused on consumer-facing technologies and services, OverDrive was the company's only library-oriented business.

The acquisition of OverDrive by Rakuten would be described as a *strategic investment*, where a company is acquired by a larger entity with related business interests, usually with expectations enabling new synergies or efficiencies. Strategic investments usually endure for the long term, with the acquired company progressively integrated into the business and technical infrastructure of the acquiring organization. Within the library industry, companies like EBSCO Information Services and ProQuest periodically make strategic acquisitions and rarely sell off any of their portfolio companies.

The divestment of OverDrive after less than five years implies that Rakuten was not able to achieve the expected synergies within its digital content portfolio. In the context of the size of Rakuten and its broader business strategies primarily targeting consumers, OverDrive as a digital content provider to libraries may not have been a comfortable fit in the long term. Although no longer under common ownership status, the interoperability and partnerships between Kobo and OverDrive will likely persist.

Pending Sale to KKR

Upon close of the transaction, which is expected in the first quarter of 2020, KKR will assume ownership of OverDrive. Steve Potash will continue to lead the company as its Chief Executive Officer. Although the announcement did not disclose details of the transaction, a value of about $775 million can be inferred by combining the $410 million that Rakuten paid in 2015 with the 365.6 million profit Rakuten reported on this investment.[1]

The proposed acquisition of OverDrive by KKR is a *financial investment*, where the buyer, usually a private equity firm or other financial sponsor, expects to increase the value of the company over a finite term, typically five to seven years. Financial investments by private equity firms often take the form of leveraged buyouts, where the buyer contributes only a portion of the purchase price and secures loans from investment banks to meet the full purchase price negotiated with the seller. Financial buyers control the business strategies and operations of their portfolio companies via placement of representatives on their board of directors, usually in proportion to their ownership stake. The company itself is saddled with the responsibility to pay off the debts incurred. The debt and fees associated with a leveraged buyout are a component of the economic reality of companies following a leveraged buyout, but these transactions also provide the company with new capital to fund business expansion and product development.

With assets of $208.4 billion, KKR has a diverse portfolio of companies that span many industries. The acquisition of OverDrive was executed via its KKR Americas XII Fund. Both KKR and Rakuten have wide-ranging investments, including some in common. Rakuten is an investor in Lyft, holding an 11 percent stake in the company and reporting a $947 million loss on that investment in November 2019.[2] KKR made a substantial investment in Lyft in April 2017.

Potential for Consolidation

KKR also owns RBmedia, one of the major suppliers of audiobooks to libraries. In a transaction announced in July 2018, KKR acquired RBmedia from Shamrock Capital Advisors. This investment was also made through its KKR Americas XII Fund. KKR's investments in RBmedia and OverDrive were both shepherded by Richard Sarnoff, a veteran of the publishing industry and Chairman of Media, Entertainment, and Education for KKR. Sarnoff also holds a seat on the board of Cengage, in which KKR is also an investor.

RBmedia offers a subscription service for consumers in addition to its library lending platform. RBmedia, then known as Recorded Books, was acquired by Shamrock in August 2015. The previous month Recorded Books acquired competing audiobook publisher Tantor Media and in May 2014, Recorded Books acquired HighBridge Audio.

The common ownership of OverDrive and RBmedia raises the question of whether there will be some type of merger between these two companies. If put together either organizationally or via partnerships, RBmedia as the leading competitors for audiobooks and OverDrive with its prowess in e-book lending for libraries would represent a major consolidation in the digital content industry for libraries and related organizations.

The digital lending arena will continue to see commercial and nonprofit competition. Other players in the digital lending arena, including bibliotheca's cloudLibrary, ODILO, Baker & Taylor's Axis 360, and Hoopla represent significant competition, though a possible merger would shift industry dynamics substantially. A nonprofit alternative for library e-book and audiobook lending is available based on the Library Simplified initiative (http://www.librarysimplified.org/), the open source SimplyE software developed by New York Public Library, and the DPLA Exchange e-book marketplace (https://pro.dp.la/ebooks).

This possibility of consolidation remains speculative, especially since the OverDrive deal has not yet closed. It should also be noted that within the library technology industry, Golden Gate Capitol owned both Ex Libris and Infor Library Systems and did not merge the two companies. In this case, the two companies have been acquired through the same investment fund, which at the very least would likely mean common strategic leadership at the board level.

Library Lending in a Field of Giants

E-book lending takes place in the context of a highly consolidated publishing industry dominated by the "Big Five" and Amazon exerting its powerful presence. These corporate forces perceive library lending as intrusive to their commercial interests and are not motivated to offer favorable license terms. Pricing models that place restrictions on the number of circulations allowed before the title must be relicensed and embargos on front-list titles present significant challenges for libraries. OverDrive, with its dominant market share in the library lending arena, could add substantial leverage to library interests in negotiating more favorable pricing and terms.

OverDrive has a strong record of advocating on digital content issues for library interests. The company often takes the brunt of negative perceptions for unfavorable licensing terms available from publishers. In October 2019, for example, OverDrive CEO Potash spoke in front of the UK House of

Lords and presented evidence on how libraries make a positive impact on their communities and require more sustainable funding. OverDrive provided funding for the Panorama Project to study "data-informed insights on public libraries and their impact on book discovery, author brand development, and sales."[3]

Impact on the Library Community

The holiday announcement of the sale of OverDrive sparked alarm in the library community. Concerns mentioned include the negative impact of private equity ownership and industry consolidation. KKR's involvement with Toys "R" Us and its ultimate demise has been mentioned as an example. While private equity ownership comes with substantial financial overhead, it can also offer important benefits. The failure of a bricks-and-mortar retail chain in the context of massive online competition does not compare to the library digital lending arena in a phase of sustained growth.

It should also be noted that that OverDrive was controlled by private equity prior to its tenure with Rakuten. Private equity firm Insight Venture Partners made a significant investment in Overdrive in October 2010. At that time, two representatives from the investment firm joined OverDrive's board of directors. This ownership arrangement continued through March 2015 when the company was sold to Rakuten.

The possibility of consolidation of the top e-book lending and the leading audiobook distributor seems a more valid concern. The narrowing of providers and the emergence of a new superpower in the industry sounds legitimate alarms. In sectors involving the sale of products and services, fewer competitors can lead to higher prices to consumers. But in a sector where the pricing is controlled more by the publishers than the distributors, a larger-scale player could increase the leverage of library interests in future rounds of negotiating pricing and lending terms with the highly consolidated publishing industry.

The consolidation of an industry can also create opportunities for development and innovation at a level not possible among smaller companies. Especially when matched with new infusions of capital, increased development capacity can produce new products or services beyond the reach of smaller organizations. For libraries, a lot is at stake on whether this new industry dynamic results in better technologies to help them better serve their communities in an era where consumer technologies set an incredibly high bar and strengthen their hand in achieving better pricing and business terms for access to content.

Continuity in leadership also represents an important factor as a company makes ownership and investment transitions. The ongoing involvement of Steve Potash should be seen as a positive note since it strengthens the possibility that the company will continue on a strategic course of growth and expansion rather than follow the often-derided private equity playbook of cutting costs and maximizing profits.

Libraries need to pay attention to how these events unfold. Will the deal close? It is rare for a business transaction to fall apart once it has been announced. This announcement comes after a definitive agreement has been signed, though it can be expected that some financing and other details remain to be completed. Will KKR merge OverDrive and RBmedia? While speculative, it cannot be taken as an accident that the same financial backing and strategic architect is involved in both companies. Synergies may be gained via partnerships or through consolidated corporate structures. Will platform consolidation emerge? Interest in audiobooks continues to rise, possibly faster than e-books. For libraries, the complexities of implementing separate integrations for e-books via OverDrive and audiobooks via RBmedia could be simplified through a single platform or even through a set of common APIs. A single marketplace for e-books and audiobooks would offer some advantages, offset by concerns with narrowed competition. An interesting future for public library digital lending remains in flux among these multiple possibilities.

OverDrive Business History

- 1986: OverDrive is founded by Steve Potash.
- 2000: OverDrive enhances its platforms with digital rights management.
- July 2001: OverDrive licenses Adobe Content Server DRM.
- March 2001: OverDrive launches Content Reserve digital marketplace.
- November 2003: Mobipocket e-book format becomes available.
- May 2003: OverDrive launches its service for library e-book lending. Cleveland Public Library and King County Library System are early implementors.
- October 2004: OverDrive launches digital audio book service.
- December 2006: OverDrive announces support for EPUB e-book standard.
- October 2010: Insight Venture Partners acquires majority ownership of OverDrive.
- 2011: OverDrive introduces Media Console for Android and iPhone.
- September 2011: OverDrive announces compatibility with Amazon Kindle.

- March 2012: OverDrive acquires Booki.sh, an e-book provider based in Australia.
- May 2012: OverDrive enables APIs on its platform for integration with library catalogs and discovery services. OverDrive API supports catalog search, title availability, and checkout. By February 2018, its service has enabled one billion checkouts by library patrons via external apps and systems.
- April 2013: OverDrive moves into its new Blue Sky Campus as its world headquarters.
- March 2015: OverDrive is acquired by Rakuten.
- November 2015: Overdrive revamps its technology platform.
- September 2017: OverDrive introduces Libby as a patron-facing app for borrowing and reading.
- July 2019: Apple CarPlay is introduced.

Ex Libris Completes Sweep of Higher Education in California

Ex Libris has now sold its Alma library services platform to all three of the public higher educational systems in California. A recent announcement from the Systemwide Integrated Library System taskforce of the University of California libraries announced the final selection of Alma and Primo from Ex Libris, now part of ProQuest. The University of California system joins the California State University System and the Consortium of Community Colleges in the selection of Alma to provide shared infrastructure for the management of their collections and Primo for discovery and access. Each of these projects on its own would be considered massive; together these three systems represent an unprecedented level of involvement by the libraries in a single governmental jurisdiction with a single vendor.

This forthcoming implementation of Alma and Primo will provide a shared system for the ten campuses of the University of California, which includes 100 individual libraries. These libraries together hold over 50 million volumes.

The selection of Alma for the University of California campuses fits within a broad trend of consolidated automated systems among institutions within common governance or funding. Ahead of the selection and implementation of Alma, each of the ten campuses operated their own integrated library system or library services platform. Five of the campuses had previously selected Alma, including UC Davis, UC Irvine, UC Riverside, UC Santa Barbara, and UC Santa Cruz. UC

Table 1: University of California Campuses

Campus	Incumbent ILS	Number of Volumes (2018-19)	Enrollment (FTE)
UC Berkeley	Millennium	12,984,693	39,946
UC Davis	Alma	5,715,576	35,202
UC Irvine	Alma	4,079,195	35,267
UC Los Angeles	Voyager	10,911,750	39,649
UC Merced	WMS	2,103,239	8,570
UC Riverside	Alma	4,365,790	23,038
UC San Diego	Millennium	5,288,731	36,296
UC San Francisco	Millennium	1,202,970	
UC Santa Barbara	Alma	3,019,866	26,019
UC Santa Cruz	Alma	2,513,432	19,837
Totals		52,185,242	263,824

Source: Volume statistics have been gathered from "University of California Library Statistics July 2019," revised November 8 2019, https://libraries.universityofcalifornia.edu/groups/files/Library_Statistics_18-19.pdf.

Berkeley, UC San Diego, and UC San Francisco will be moving from Innovative's Millennium ILS; Riverside will migrate from OCLC's WorldShare Management Services; and UCLA will migrate from Voyager.

The University of California has a long history of shared discovery, though with separate automation systems for each campus. The Melvyl catalog, representing the combined collections of the ten campus library systems currently is based on OCLC WorldCat Local.

The system will also be used to manage the operations of the systems' two large-scale storage facilities, Northern Regional Facility in Richmond and the Southern Regional Facility in Los Angeles

The three selections of Alma represent a significant loss of business for Innovative Interfaces, which in previous times had been the favored system. With the pending acquisition of Innovative by ProQuest, this shift becomes less consequential.

The movement toward technical infrastructure shared by large numbers of libraries is driven by many of the same factors that have led to vendor consolidation. A tight economic environment demands organizational efficiency. Mergers and acquisitions result in less organizational overhead for development, support, and sales, even when the number of products remains constant. Likewise, the deployment of one or more ILS products for each academic campus requires more effort and resources than a single shared system serving the broader organization. The entities funding libraries increasingly favor a single shared system than individual deployments. Shared systems also provide increased opportunities for deeper collaboration in collection development, technical processing, and resource sharing.

The transition from separate campus ILS deployments to shared systems can be unsettling for the libraries involved. Such a strategy requires difficult compromises related to local campus practices as well as a shift of control toward the central organization. While shared systems offer strategic advantages in the long term, they are inevitably disruptive for operations in the short term.

Smart Libraries Q&A

Each issue Marshall Breeding responds to questions submitted by readers. Email questions to Samantha Imburgia, Managing Editor for ALA TechSource, at simburgia@ala.org.

Are there advantages to having a mobile library app when you have a responsive library website? If so, what are the advantages?

As suggested, it is paramount for libraries to ensure that their websites are responsive. Given that more than half of website traffic globally takes place through mobile devices, libraries must deploy their websites using designs and technologies that work well on smart phones and tablets in addition to desktop and laptop computers.[4] Responsive websites adjust their layout automatically to accommodate the size of screen and other characteristics of the device accessing each page.

A responsive site works well via a web browser on any type of device. There is no need to download an app or install software. Access to the site and all its featured are gained via its URL, which most users will find via a search engine. If the website has been well designed and follows the basic methods of responsive design, there will be very few limitations experiences by those accessing it on a smartphone. Content and images will flow according to the real estate available on the screen and users will navigate using the usual swipes and gestures.

Sites not deployed with a responsive design, in contrast, can be very frustrating to use on a small device. Users may have to pinch the screen to view content or to be able to click on links or buttons. While libraries have made great progress in shifting to responsive sites, I still come across many which don't work well on small devices.

For libraries that have not already made their sites responsive, any resources available should be channeled into making those improvements. It may be tempting for libraries with non-responsive sites to invest in native apps to deliver a better experience to mobile users. It is highly unlikely that users frustrated with accessing a non-responsive site on their phone would take the time to find and install a library app. Rather, they will probably move on to another site that may be easier to use, even if it does not offer the quality resources available through their library.

So, if your library has a nicely designed, fully responsive website, should you also invest in creating mobile apps? There may be some scenarios where apps may be needed. A responsive website, for example, cannot access the device's camera or built-in notifications. Libraries interested in enabling mobile self-service will need to develop or acquire a mobile app programmed to use the camera to scan barcodes or QR codes. Library mobile apps can also integrate capabilities for downloading and reading e-books that wouldn't be as effective as on a responsive website.

A mobile app might be appreciated by a library's most dedicated users. Only a small minority of the library's users are likely to find it worthwhile to install an app. But for these frequent users, there can be some nice benefits. Once the app has been installed, it provides easy access to the library's resources. Otherwise, the user would need to perform a search on their browser or search app. A library mobile app can also be designed for a persistent login so that users can easily check their account, place requests, or download e-books without having to sign-on each time.

Libraries considering the deployment of apps will need to consider a variety of factors. Will the benefits to the small number of patrons that install and use the app be a good investment for the library? Would it be better to channel these resources into improvements in the library's website and other services, especially in the area of better user experience for mobile users? Does the library have operational needs that depend on apps, such as increased emphasis on self-service on user-provided devices? What is the demand from library users for a mobile app? If many patrons are requesting an app, is it because they really prefer to use a dedicated app, or is it because they are frustrated with the library's website?

While some libraries may wisely proceed with developing or acquiring native apps for smartphones and tablets, I generally anticipate that most will focus their energies on delivering the best possible user experience for mobile users via responsive websites.

Notes

1. Jeremy C. Owens, "KKR to Buy Digital-Library Platform Overdrive from Rakuten," *MarketWatch*, December 24, 2019, https://www.marketwatch.com/story/kkr-to-buy-digital-library-platform-overdrive-from-rakuten-2019-12-24.
2. See "Rakuten Sees $947 Million Loss from Lyft Investment in Latest Quarter," Reuters, November 5, 2019, https://www.reuters.com/article/us-rakuten-lyft/rakuten-sees-947-million-loss-from-lyft-investment-in-latest-quarter-idUSKBN1XF0S2.
3. Panorama Project, https://www.panoramaproject.org/.
4. "Percentage of Mobile Device Website Traffic Worldwide from 1st Quarter 2015 to 3rd Quarter 2019," Statista, accessed January 11, 2020, https://www.statista.com/statistics/277125/share-of-website-traffic-coming-from-mobile-devices/.

Questions or suggestions for topics in future issues?

Contact Samantha Imburgia at **simburgia@ala.org**

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American Library Association
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February 2020
Smarter Libraries through Technology

Smart Libraries Newsletter

Marshall Breeding's expert coverage of the library automation industry.

Editor
Marshall Breeding
marshall.breeding@librarytechnology.org
Twitter: @mbreeding

Managing Editor
Samantha Imburgia
312-280-3244
simburgia@ala.org

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Production and design by the American Library Association Production Services Unit.

Smart Libraries Newsletter is published monthly by ALA TechSource, a publishing imprint of the American Library Association.

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