Against the Grain

Volume 28 | Issue 3 Article 35

2016

Straight Talk--Private Equity Firms and Their Influence in the Library Marketplace

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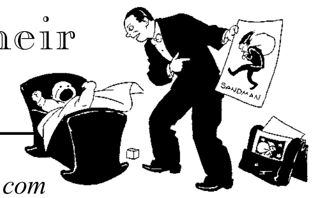
Recommended Citation
Tonkery, Dan (2018) "Straight Talk--Private Equity Firms and Their Influence in the Library Marketplace," *Against the Grain*: Vol. 28: Iss. 3, Article 35.
DOI: https://doi.org/10.7771/2380-176X.7381

Straight Talk — Private Equity Firms and their Influence in the Library Marketplace



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The recent announcement that **Follett Corporation** is buying long-time library supplier **Baker & Taylor** has been met with surprise and shock by many including comments about what is going to happen to the cats. I got calls and emails from many of my friends asking what is going on and what does it mean for the library community. What does this mean and why now? What is going on in our industry?

Well, for the most part nothing is going on! Yes nothing! There is no grand plan, no conspiracy, and no strategy. Yes, **Follett Corporation** is buying **B&T**. End of story. But why now? What is really going on? Is the library market in such disarray that all of our vendors are buying each other up?

The answer is fairly straight forward. The sale of **Baker &Taylor Books** is the final transaction, clean up and sale for **Castle Harlan Partners IV, LP**, a New York-based private equity fund managed by the **Castle Harlan, Inc.** firm that acquired **Baker & Taylor** for $455 million in July 2006. That's quite a jump in price as only three years earlier **Willis Stein & Partners, LP** paid only $255 million for the company. Someone told me that the high price paid was due to the expectation that **Baker & Taylor** would have a major role in **Amazon's** distribution network, but in the end **Amazon** built their own distribution centers and bypassed **B&T**.

The **Castle Harlan** private equity firm has owned **Baker & Taylor** for ten years and I have reason to believe that they originally overpaid and have been looking for a way to get out of this situation for several years. I happen to know that **Castle Harlan** tried to sell **YBP, a B&T** business unit for about 18 months before **EBSCO** bought them in 2015. About the same time that **YBP** was sold to **EBSCO**, **Baker & Taylor's Marketing Services** and **Baker & Taylor's Publishing Group** were acquired by **Readerlink Distribution Services LLC**. So now, with two units of the **Baker & Taylor** group sold off, **Castle Harlan** only had the largest unit to sell.

Finally, after flogging **Baker & Taylor** to a number of venture firms and other potential buyers on both coasts for months, **Castle Harlan** finds a willing buyer and hopes that they have the unit all wrapped up, spit shined and ready for a new home. So the answer to everyone's question: the sale of **Baker & Taylor** is a simple acquisition from a private equity owner that has been trying to sell this company for months. The timing is related to when they could find a buyer, plain and simple. I don't think that **Follett Corporation** was planning on buying or seeking out this acquisition. But when the **Castle Harlan** sales pitch came they made **Follett Corporation** an offer too good to ignore. However, this not the first time that the **Follett Corporation** tried to buy **Baker & Taylor**, in 1994 there was a serious effort by **Follett Corporation** to buy **Baker & Taylor** from another private equity group, **The Carlyle Group** and after months of negotiations that deal fell through.

Private equity firms are a good way for companies to raise capital, and **Baker & Taylor** have had a long history of private equity owners starting back with the **Carlyle Group** that acquired **Baker& Taylor** from **W.R. Grace** in 1970. Each private equity firm for the most part has made a better than average return without making any significant investment. The **Carlyle Group** lucked out and left **Baker & Taylor** alone but did pay attention to the deal that **B&T** did with a new start-up in Seattle. **Baker & Taylor** licensed their title database and publisher files to **Amazon** for a modest upfront fee and **B&T** took a stock position which **Carlyle** later cashed in and made more money from the **Amazon** stock sale than they might have received from the sale of **Baker & Taylor**.

Baker & Taylor is not the only library services company that has private equity ownership or involvement. I am not here to judge whether private equity ownership is necessarily good or bad for the library industry but one thing is clear: the financial returns of the private equity firm are always maximized for the shareholders and not for the library clients and customers. As usual, library customers carry most of the cost of these deals in terms of higher prices, delayed development and diminished customer service. Too often, the private equity firm has no idea what they are buying, what business they are in, nor do they care about the market.

Some recent examples of private equity plays in the library marketplace would be in the ILS marketplace. Nearly everyone is aware of **ProQuest's** acquisition of **Ex Libris** in 2015. I think many librarians are still shaking their heads at the whopping $500 million plus price that **ProQuest** paid a venture firm for **Ex Libris**. Yes, over $500 million, and most of that paid for by subordinated debt with a group of bond holders who are financing that debt. **Ex Libris** has had an interesting history with private equity ownership starting in the early days with **Hebrew University** and some other organizations that invested $4 million. From that small $4 million investment the growing company was able to find their next investor, **Francisco Partners**, who invested $62 million in June 2006. In August 2008, the next private equity firm, **Leeds Equity Partners** paid $150 million for **Ex Libris** which they sold to **Golden Gate Capital** for a little over $200 million. But wait there's more… at the end of 2012, less than two years later, **Golden Gate** was able to flip **Ex Libris** for over $500 million. Not a bad payday for their investors!

ProQuest must now meet certain performance goals in terms of sales, etc. in order to satisfy the bond holders. Any time your company takes on debt, that debt always comes with someone looking over your shoulder on a quarterly basis. If you are unable to meet the performance criteria then you possibly end up like **Cengage**. Again the library community may be indirectly involved in helping to manage that debt by paying rising database prices and/or higher maintenance prices.

Another example of a private equity acquisition is **Innovative Interfaces, Inc.** where **Huntsman Gay Global Capital** and **JMI Equity** made a strategic investment in **Innovative** in March 2012. **Innovative** was founded in 1978 and had long been one of the libraries' favorite companies with a broad base of support and a huge customer base. **Innovative** was in serious need of a technological engineering overhaul. They chose to raise capital from the private equity community. In the end, **Jerry Kline** decided to sell out to a venture group and let someone else deal with the task of reengineering the various systems and platforms into the next generation systems. As an outside observer, it was interesting to note that one of the first tasks that the private equity firm undertook was a reduction of a number of well-known and highly respected library veterans that had worked for years at Innovative who understood the unique aspects of the academic and research library marketplace. It will be interesting to follow the developments in Emeryville, CA.

While several of the ILS vendors are owned by private equity firms, there are other examples of venture ownership in our industry. **High Wire Press**, a hosting service founded by **Stanford University** as an auxiliary unit of **Stanford University Libraries** in May 2014, received a significant equity investment to support its strategic growth from **Accel-KKR**, another private equity firm. **High Wire Press** received a much needed investment that will enable **HWP** to develop the next generation hosting service. **High Wire Press** had been under pressure from a number of their publisher partners to reengineer their services. This investment will enable them to remain competitive in this niche market. Recently, **High Wire Press** announced the opening of a new European Office in Belfast, Northern Ireland and the addition of 74 new positions over the next three years. I cannot help but wonder if this is the first step to moving all the software development to a much lower cost area. Maintaining a software development team in

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Redwood City, one of the most competitive and high cost locations where software engineers are constantly looking for the next opportunity is a challenge.

My final example of a private equity play is **OverDrive**, the Cleveland based company supplying digital content to libraries, primarily schools, public libraries, and public library systems. **OverDrive** caught the wave of the shift from print to electronic formats and experienced a dramatic growth spirt. It needed a cash infusion to help pay for expansion and for a new headquarters. In 2010 **Insight Venture Partners**, a private equity firm provided the necessary cash investment and became the primary shareholder and majority owner. In five years with continued growth **OverDrive** became a hot target and in 2015 **Insight Venture Partners** sold **OverDrive** to Japan's **Rakuten, Inc.** for $410 million. The **OverDrive** example is another great payday for a venture firm. Anytime you can turn $30 million into $410 million is an impressive win.

Back to my original question: Are private equity firms in the library marketplace good or bad for our industry? One thing is certain, a number of private equity firms have made investments in ILS, Book supply, and e-books that have yielded impressive returns. We can expect that private equity firms will remain players in our marketplace. In addition, private equity firms allow library service companies to raise much needed capital for expansion or for buying other companies.

On the other hand, private equity firms are focused on maximizing their profit potential and have little to no interest in growing, developing or even understanding our market place. A private equity firm most likely will have ownership positions in ten or more companies often in a variety of businesses. The library company they invested in is just a balance sheet to watch over and make sure that the profits grow. In some cases, the venture firm makes a wrong investment and after attempting and failing to find an exit strategy is left with the option of stripping the company of all its cash and/or other assets and simply walking away and leaving the company to fail. Recent examples of this type of venture play include both **Swets** and **Faxon**.

My money is on vendors that are long term players in the marketplace, who are conservative and who have a deep understanding of the marketplace. Libraries should avoid companies that are saddled with huge debt and pay attention to what is going on in the marketplace. The **Swets** situation is a prime example of too many people ignoring the warning signs. Investment banks were having second thoughts about **Swets** and in the end they stripped out all the cash, protected their investment and pocketed many libraries' prepayment payments. Several major U.S. libraries each lost more than a million dollars.

My final thought… All of these private equity firms are investing enormous amounts of money chasing deals all over the world. When you stop and think about it, the money they are using is mostly from retirement funds. Your state, university, or other retirement program is supplying the cash for the various private equity funds. I guess we can all sleep well at night knowing that someone is using our money creatively… or not!

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Center for Research Libraries

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OFFICERS: Bernard F. Reilly (President). Board of Directors at: *www.crl.edu/node/177.*

ASSOCIATION MEMBERSHIPS: ARL, **IFLA**, and **ICOLC**.

KEY PRODUCTS AND SERVICES: Cooperative collection development; print and digital primary source collections; licensing of databases and related analytics.

CORE MARKETS/CLIENTELE: Independent and academic research libraries.

NUMBER OF EMPLOYEES: 80

HISTORY AND BRIEF DESCRIPTION OF YOUR COMPANY/PUBLISHING PROGRAM: In March 1949, ten major U.S. universities entered into a formal agreement establishing the **Midwest Inter-Library Corporation (MILC)**, the forerunner of today's **Center for Research Libraries**. The founding institutions were the **University of Chicago**, the **Illinois Institute of Technology**, the **University of Illinois**, the **State University of Iowa**, **Indiana University**, the **University of Kansas**, **Michigan State College**, the **University of Minnesota**, **Northwestern University**, and **Purdue University**.

Today the **Center for Research Libraries (CRL)** is an international consortium of over 200 university, college, and independent research libraries. Since its founding **CRL** has supported original research and teaching in the humanities, sciences, and social sciences by preserving and making available to scholars a wealth of rare and uncommon primary source materials from all world regions.

ADDITIONAL ITEMS OF INTEREST TO ATG READERS: CRL is an umbrella under which many communities of interest collaborate, to build and share resources that support original scholarly research on all world regions. **CRL's** deep and diverse collections are built by specialists and experts at the major U.S. and Canadian research universities, who work together to identify and preserve unique and uncommon documentation and evidence, and to ensure its long-term integrity and accessibility for researchers in the **CRL** community.

CRL also hosts and supports the *LIBLICENSE* model license initiative and its active discussion listserv.

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For 30 years, the **Software & Information Industry (SIIA)** has conducted the CODiE annual awards program and the CODiE program is the industry's only **peer-reviewed** awards platform. I understand that **ACI** beat out two strong finalists in this CODiE category: **Elsevier Reference Module in Biomedical Sciences** and **ProQuest Ebook Central**. **Pat Sabosik** the manager of the **ACI Scholarly Blog Index** has been in the industry for many years. I first met her when she was editor and publisher of ***Choice magazine***. On the personal side, **Pat** has a grandson in Greenville and she recently vacationed in Hilton Head! She is also planning a panel in Charleston during the **2016 Charleston Conference**!

http://aci.info/2016/05/18/aci-scholarly-blog-index-named-siia-2016-codie-award-winner-for-best-scholarly-research-information-solution/

On the Elsevier page — BA Insight and **LexisNexis Legal & Professional** have announced a strategic alliance that integrates **Lexis Search Advantage** natively into law firms' **Microsoft SharePoint** environments using the **BA Insight Software Portfolio** to

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