APPLE INC. AND THE EBOOK READER

TABLE OF CONTENTS

Introduction

Sitting comfortably in his Cupertino office, Apple's CEO Steve Jobs reviewed the media coverage of a new eBook Reader being developed. When asked about the unveiling of Amazon's Kindle in a 2009 interview with the New York Times, he had responded, "It doesn't matter how good or bad the product is, the fact is that people don't read anymore. Forty percent of the people in the U.S. read one book or less last year. The whole conception is flawed at the top because people don't read anymore." In fact, a recent polling done by the National Endowment for the Arts claimed that only 57% of Americans read a book in 2002, 4% less than the previous decade [1].

However, with the recent success of the Kindle, Jobs questioned whether this was a possible market for Apple to pursue. Amazon released the latest version Kindle DX one month earlier in April 2009. To compete with Amazon in the eBook business, Sony announced a content partnership with Google in March 2009.

Is it too late for Apple to enter the eBook Reader market? Apple has a history of famous breakthrough products, from the iMac in 1998, to the iPod in 2001, and most recently the iPhone in 2007. Do we expect to see an 'iReader' next?

Company Overview: Apple Inc.

Apple Inc. designs, manufactures, and markets consumer electronics products - personal computers, portable music players, cell phones - as well as related software, services, and peripherals. Apple sells its products worldwide and provides support through its website and at more than 250 retail stores around the world [1].

Additionally, Apple distributes digital entertainment content through its iTunes Store. While initially offering only music, the store has grown to include videos, television shows, films, and audio books. With the introduction of the latest iPod Touch and iPhone in 2008, users could also purchase applications and games, including eBooks, for these mobile devices from the App Store in iTunes.

Apple has established a coveted reputation in the consumer electronics market. According to surveys by J.D. Power, Apple enjoys the highest brand and repurchase loyalty of any computer manufacturer [2]. Additionally, in 2008, Fortune magazine named Apple "the most admired company" in the US [3].

HISTORY: BEGINNING

Steve Jobs and Steve Wozniak co-founded Apple on April 1, 1976. Initially, they planned to design a simple micro-computer board that could be sold to small businesses. However, the duo eventually went on to build a microcomputer kit called Apple I, the company's first product [1]. One year later, Apple was incorporated as "Apple Computer Inc". The Apple II, one of the first commercially successful personal computers, debuted that same year [2]. The Apple II distinguished itself from its major rivals by incorporating color graphics and an open architecture. Known for its ease of use, features, and expandability, the Apple II helped Apple grow into a profitable, well-regarded company. In 1984, Apple released the Macintosh, which provided advanced graphics capabilities and a revolutionary Graphical User Interface. Following the success of Apple II and the introduction of Macintosh, the company had its IPO on September 7, 1984.

DECLINE

Between 1984 and 1985, Apple's net income fell 17% due to poor follow-up sales of the Macintosh computer [3]. Jobs was forced out of the company, while CEO John Sculley, who was previously brought into the company by Jobs, assumed control. Later risky ventures such as the Newton PDA caused market share and stock price to drop at an alarming rate. Additionally, Apple was involved in a prolonged lawsuit against Microsoft for using proprietary elements of Apple's Lisa GUI. From 1994 to 1997, Apple experienced record-low stock prices and severe financial losses. After two changes in CEO between 1993 to 1996, the Apple Board of Directors brought Steve Jobs back as CEO in July 1997.

REVIVAL

Upon his return as CEO, Jobs immediately terminated the licensing agreement allowing licensed Macintosh replicas and focused the company on designing high-quality and easy-to-use products, cutting 15 of the company's 19 existing products. The new products struck a chord with the consumer market. In August 1998, Apple introduced an innovative all-in-one computer called the iMac. Nearly 800,000 units were sold in the first five months, returning Apple to profitability for the first time since 1993.

In May 2001, Apple opened the first official Apple retail stores. Later that year, the company introduced the iPod, a portable digital music player. The product was phenomenally successful. Over 100 million units were sold in six years, with Apple capturing over 70% of the market.

In January 2007, Apple dropped the word 'Computer' from its official name, reflecting the company's changing strategies with the ongoing expansion into consumer electronics market. The iPhone and Apple TV were introduced in the same year. As of September 2008, Apple had more than 35,000 employees worldwide and annual sales of $32.48 billion.

LEADERSHIP

The return of Steve Jobs as CEO in 1997 was widely credited for Apple's re-emergence as a market leader in both computers and consumer electronics. Jobs' emphasis on quality, aesthetics, and ease of use restored the Apple brand. Jobs is currently on leave due to health reasons. Because of Jobs' strong role in defining Apple's strategic vision, many investors are concerned about Jobs' health, and succession plans in the event of his eventual retirement. According to Fortune magazine, "there's the widespread opinion inside and out of Apple that the Magician of 1 Infinite Loop simply can't be replaced" [1]. Timothy Cook, Apple's Chief Operating Officer, is currently the acting CEO until Jobs' expected return in June 2009 (Exhibit 1).

CORPORATE STRATEGY

Apple designs its products to complement one another in order to create a complete solution [1]. For example, iTunes provides digital content that can be used with both the iPod and iPhone.

Apple's success has rarely come from a first-to-market advantage; instead, after studying the consumer response to a product, Apple targets consumers in ways different from predecessors [2]. Apple has differentiated itself through fashionable design, ease of use, clever marketing, and effective distribution. The introduction of new user interfaces, like the iPod click wheel and the iPhone touch screen, also distinguishes Apple's products from other hand-held electronics devices in the same category.

Apple is well-known for having a loyal customer base, as noted by Steve Jobs: "I get asked a lot why Apple's customers are so loyal. It's because when you buy our products, and three months later you get stuck on something, you quickly figure out how to get past it. And you think, 'Wow, someone over there at Apple actually thought of this!'" [3].

Apple has been known to arouse media interest through leaked rumors and mysterious shutdowns of its online store, which fuel speculation on imminent offerings. This expertise in creating media hype maintains excitement among technophiles who often line up to purchase new Apple products.

In addition, Apple is known for its innovative product design. For example, the MacBook model released in October 2008 featured an aluminum unibody enclosure made from a single piece of aluminum. This gave a unique feel of durability to the product while also acting as a heat-sink. As Steve Jobs once stated, "Design is not just what it looks like and feels like. Design is how it works" [4].

CORPORATE CULTURE

Apple's casual work environment and reputation for fostering individuality and excellence consistently attracts talented employees. As Steve Jobs explained, "Innovation has nothing to do with how many R&D dollars you have. When Apple came up with the Macintosh, IBM was spending at least 100 times more on R&D. It's not about money. It's about the people you have, how you're led, and how much you get it." [1]

EXISTING PRODUCTS

Macintosh: Introduced in January 1984, the Macintosh (Mac) is a platform of desktop computers targeting the home, educational, and professional markets. Included in this line are the iMac, which helped Apple recapture success in the personal computer market; the Mac mini, a tiny desktop computer targeting price-conscious consumers; and the Mac Pro, a series of high-performance machines. Over the past ten years, Apple has never claimed more than five percent of the desktop computer market, but has remained profitable by marketing to a high-margin niche segment rather than the mass market. [1] "Wintel" (Windows based PCs with Intel microprocessors) manufacturers provide strong competition to the Mac product line.

MacBook: In May 2006, the MacBook replaced the iBook and PowerBook series of personal notebooks as Apple transitioned from the use of IBM PowerPC microprocessors to the Intel chip line. Performance, power consumption and interoperability were key points in this decision. According to the sales-research organization NPD Group in October 2008, the low-end model of the MacBook has been the single best-selling laptop of any brand in US retail stores for the preceding five months. The MacBook line also includes high-end machines such as the performance-oriented MacBook Pro and the ultraportable MacBook Air. The success of the existing MacBook lines has allowed Apple to grow in the notebook market.

iPod: The iPod was launched as a line of portable digital music players in 2001 and has since evolved into a portable entertainment device capable of storing photos and playing

videos. The iPod Touch is also capable of running applications. All iPods work with the company's digital music management software, iTunes. The iPod product line includes: the iPod Classic, the Shuffle, the Nano, the Touch, and the iPhone.

In the years following iPod's initial release, Apple developed several models to blanket the portable media device space. As of September 2008, more than 173 million iPods had been sold worldwide, making it the best selling digital audio player series in history [2].

iPhone: Released in June 2007, the iPhone marked Apple's entry into the rapidly growing smartphone market. The original iPhone combined a 2.5G quad-band GSM and EDGE cellular phone with iPod-like MP3 Player functionality. It also featured a scaled-down version of Apple's Mac OS X Operating System, with a touch screen display. The iPhone is compatible with both Macs and Windows-based computers. GPS functionality and faster network connectivity were added to the iPhone 3G, the latest model in this series.

The iPhone faces competition from smartphones being developed by its competitors, including the Samsung Instinct, BlackBerry, and other smartphones based on the Windows Mobile or Google Android platforms.

iTunes Store: iTunes is a digital media player application used to manage audio and video files. It was introduced in early 2001 as a free download on various platforms, and supports a variety of multimedia formats.

With iTunes version 4.0, the iTunes Music Store was introduced. Later renamed the iTunes Store, it allows a user to download songs, audiobooks, movies, television shows and music videos each for a small fee. In July 2008, the company launched the iTunes App Store, which allows a user to browse and purchase third-party applications for the iPhone and iPod Touch products. Nine months after its launch, one billion applications had been downloaded from the App Store website [3].

On April 3 2008, the iTunes Store became the number one music seller in the US, and the service had over 6 billion songs downloaded as of January 2009 [4]. However, iTunes is unprofitable. In a reversal of the classic razor and blades business model, Apple uses the iTunes store to drive sales of the its more lucrative hardware products.

There is competition in this area from other online services based on pricing and less restricted licensing agreements.

Apple TV: Launched in 2007, the Apple TV is a digital media receiver designed to play content from an Internet media service or any computer running iTunes. It allows users to easily view photos, play music, and watch video from a high-definition television [5]. Due to the growth of digital TV and consumers turning to Internet media services, sales of 6.6 million Apple TVs are predicted by the end of 2009 [6].

Software: Apple uses its own UNIX-based operating system for its computers, the latest of which is called Mac OS X Leopard. Apple also develops its own software for all of its products, which is world-renowned for its high quality user interface and ease of use. In addition to their OS, Apple has developed a large suite of software for word processing, productivity management, picture categorization, web publishing, image editing, and music composition.

PROSPECTIVE PRODUCTS

"iReader": In a January 2008 interview with The New York Times, Jobs shared his thoughts on Amazon's Kindle eBook reader, saying the Kindle would fail because Americans have stopped reading [1]. Others disagree with Jobs. "Why don't we own this market?" one of the investors on The Mac Observer's Apple Finance Board asked. "Apple had all the elements here, the capacity to design, the money to market, and the distribution system already in place via the App Store and the iTunes Store" [2].

"iTablet": With iPhone and iPod Touch product lines, Apple has already developed the technology needed to develop a tablet computer. According to The Wall Street Journal, "people privy to the company's strategy say Apple is working on new iPhone models and a portable device that is smaller than its current laptop computers but bigger than the iPhone or iPod Touch" [3].

The iPhone and iPod touch seem like natural extensions to read electronic books. In fact the App Store already has at least two eBook and one Kindle application. However, in March 2009 a patent infringement case was brought against an unnamed eBook application. This has been an additional cost for Apple, even before it has entered the eBook market.

FINANCIALS

Apple's profits have grown steadily since Jobs' return in the late 90s. In the first quarter of 2000, the company posted a net profit of just $183 million. By comparison, Apple profited $1.21 billion during the same quarter of 2009 [1]. Remarkably, the company did not experi-

ence much slowdown during the market collapse beginning in 2007. Instead, Apple's first quarter 2009 profits increased 15% from the same quarter in 2008.

Currently, Apple has approximately $25 billion in cash and marketable securities (See Exhibit 4). Numerous rumors have surfaced regarding potential acquisitions. The San Jose Mercury news reported on May 6, 2009 that Apple was interested in purchasing the online social networking site Twitter. In April 2009, the Wall Street Journal reported that Apple is building a team to design its own processor chips, a break from the long-time trend among consumer electronic companies to outsource chip design [2].

The Evolution of the eBook Reader

The eBook reader is a piece of hardware specifically designed for reading electronic versions of traditional print media including books, journals and newspapers. The main advantages of these devices are portability and long battery life. Many eBook readers incorporate specialized "e-paper" screen technology to improve battery life. It should be noted that any Personal Data Assistant (PDA) capable of displaying text on a screen is capable of being an e-book reader.

eBook readers and similar devices have existed for more than a decade. In the early 90s, Sony launched its Electronic Book Player, an eBook reader which used CD-ROM technology to provide reading content. In response, Franklin developed its own product, The eBookMan. Both of these devices required consumers to purchase discs or cartridges in order to view books. One of the factors hindering the success of these early products was the limited range of titles available for purchase. Today, eBook content is more widely available, and can be purchased and downloaded online. File formats vary by device, and users can read eBooks either using their eBook reader or computer.

TECHNOLOGY AND INNOVATION

A dedicated eBook reader has many advantages over computers and PDAs. In addition to displays that reduce eye wear, eBook readers do not require fast processors or powerful operating systems, leading to lower power consumption, longer battery life, and ultimately lower cost. eBooks also hold many advantages over traditional paper books, most notably the ability to carry a large number of books in a small device and instantly purchase content. Many eBook readers provide features such as variable font size, cross-linking of text, search and bookmarks.

FILE FORMAT

eBooks are available in a wide variety of file formats, and copyright management is a major concern. The Amazon Kindle supports a variety of unprotected standard file formats such as Adobe's portable document format (PDF). However, eBooks sold through its Amazon store are protected by Digital Rights Management (DRM) technology, which impose limitations on the usage of digital content.

Groups such as the International Digital Publishing Forum (IDPF) are currently trying to create a universally-accepted eBook format which provides DRM protection for publishers. This initiative has resulted in the EPUB format, which is steadily gaining support in the publishing community (See Exhibit 5). The EPUB is an XML-based format, featuring dynamic text size [1].

Despite attempts to standardize on a universal eBook format, no single format has assumed dominance in the market. This is because publishers have no clear preferences. Adam Rothberg, vice president of Corporate Communications at Simon & Shuster said, "Ultimately, the consumer will decide what he likes."

ELECTRONIC PAPER

Central to the concept of the eBook Reader is the technology known as "electronic paper" (See Exhibit 6), a display technology designed to mimic the appearance of ordinary ink on paper. Unlike a conventional flat panel display, which uses a back-light to illuminate its pixels, electronic paper reflects light like ordinary paper and is capable of holding text and images indefinitely, without continued consumption of power. Due to the stable image, the wider viewing angle, and the fact that it reflects ambient light rather than emitting its own light, electronic paper is considered more comfortable to read when compared with conventional displays. However, the low refresh rate negatively impacts the interactivity of the reader and limits the ability to display zoomed in text and images.

To display content on the electronic paper, the E ink material is printed onto a sheet of plastic, which is laminated to a layer of circuitry. The circuitry forms a pattern of pixels that can then be controlled by a display driver. These micro-capsules are suspended in a liquid "carrier medium" allowing them to be printed, using existing screen printing processes, onto virtually any surface, including glass, plastic, fabric and even paper.

CONTENT PROVIDERS

Amazon.com: Amazon currently has 275,000 titles available in its eBook library. The company has also moved to make deals with 3 of the 4 major textbook publishers in the United States and subscription agreements with 37 newspapers. Kindle book sales currently

constitute approximately 35% of Amazon's print sales for titles available in both digital and hardcopy [1]. EBooks sold on Amazon use the proprietary Kindle format and therefore cannot be read on many other eBook Readers. Moreover, Kindle's Terms of Usage forbid transferring eBooks to another user or a different type of device.

Google: Google Book Search, one of Google's earliest efforts to "organize the world's knowledge", was launched in late 2004 as Google Print. Google has a collection of nearly 7 million scanned books with an average of 8.2 million users per month at Google Book Search. Most importantly, books that are in-copyright but out-of-print, which maybe difficult to find, will become available for preview and purchase with consent from the author. Google recently entered into a settlement agreement with the Authors Guild and the publishing industry, in which authors and rights holders of out-of-print books indexed on Google's site will receive 63% of all advertising and e-commerce revenues associated with their works.

Barnes&Noble: Barnes & Noble, the largest bookseller chain in the United States, is on the verge of re-entering the eBook distribution market. The company discontinued its previous eBook offerings in 2003 because of low demand. In March 2009, they acquired Fictionwise, the online electronic book retailer, for $15.7 million in cash. With an existing inventory of 1 million titles, the move positions Barnes & Noble to be a formidable competitor to Amazon as a distributor of digital content. Fictionwise currently stocks 59,791 titles and an average of 25,000 users visit the website every month. However, its prices are regularly more expensive than those from Amazon [3].

eBook Library (EBL): eBooks Corporation's online bookstore, eBooks.com, calls itself "the World's Leading Source of eBooks", offering 168,000 eBooks.

Project Gutenberg: Project Gutenberg is an open source volunteer effort to digitally archive cultural works, in order to "encourage the creation and distribution of eBooks." This is a nonprofit project, and in its collection are the full texts of most public domain books. As a result, the eBooks provided by Project Gutenberg are available for little or no cost [5].

TARGET MARKET

eBook Readers are still at an early growth stage (See Exhibit 7), and primarily appeals to consumers who demand the latest technology and are willing to pay a premium price for it. Potential eBook customers come from a variety of market segments, with each demographic having specific needs (See Exhibit 8). Although multiple potential customer groups exist, nearly 70% of eBooks have been sold to users over the age of 40 (See Exhibit 9).

The college textbook market, which totals $5.5 billion annually in the US alone, is an attractive market for eBook companies. Most publishers now offer electronic versions of their textbooks. For example, McGraw-Hill Education publishes 95% of their books electronically. Amazon has addressed the textbook and newspaper market by partnering with textbook publishers Cengage Learning, Pearson, and Wiley, and plan to sell electronic versions of their textbooks for the Kindle [1].

DISTRIBUTION AND SALES

eBooks are distributed mainly through the Internet using two methods:

• Download: An entire book is downloaded at once and stored locally.

• Streaming: Sections of the book are downloaded and stored, as they are needed.

eBooks can be downloaded directly onto an eBook Reader or onto a host computer, which then transfers the material to the eBook Reader. Direct download requires the eBook Reader to have a connection to the Internet, typically through wireless networks.

Over the past few years, eBook sales have climbed rapidly while print sales have remained flat (See Exhibit 10).

PIRACY ISSUES

Many publishers who are at risk for losing revenues from illegal sharing of eBooks, actively seek non-intrusive ways to protect their copyrights. Copyright protection in eBooks is most easily implemented through software modifications. Anti-circumvention laws are often invoked to restrict what the users can or cannot do with an eBook. For instance, transfer of ownership of an eBook to another person is often restricted, even though such a transaction is common with physical books.

eBooks read on electronic devices typically employ Digital Rights Management (DRM) techniques to limit copying, printing and sharing of eBooks. One of the significant drawbacks of DRM techniques is the potential loss of data in the event of a device crash, as the books are keyed to the serial number of the device they are downloaded onto [1].

The Business Ecosystem

The eBook market is still emerging, and the success of early eBook Readers hinges on the surrounding product ecosystem. eBook Reader manufacturers need to take into considera-

tion a wide range of hardware suppliers, content publishers, distribution channels and customers.

RISKS

Due to the early growth stage of eBook technology, the primary factors differentiating eBook readers are capabilities, not price. eBook readers must target frequent readers that are willing to pay a high price for the technology. eBook readers range in price from $300 to at least $600 at the high end. Further, the content is relatively expensive. Unlike songs, which retail for less than a dollar online, Amazon charges $9.99 for even the best-selling eBooks.

Maintenance concerns may also limit consumers' readiness to adopt eBooks. Since the market is still in an early growth state, eBook technology is certain to change with the addition of new features. Potential eBook customers may worry that their DRM protected content will not transfer to the next generation of eBooks and eBook Readers.

COMPETITION

As of 2009, the market leaders in the eBook reader space are Amazon and Sony. Other products exist but have not gained significant market share. A side-by-side comparison of the major eBook Readers is given in Exhibit 11.

INDUSTRY COMPETITORS

Kindle: Currently in its third generation, the Kindle is the market leader in the eBook reader space. The Kindle I was released in 2008 and had enough memory to store around 200 titles. With storage for around 1500 titles, the Kindle II was released in February 2009 with a significantly thinner profile and a text-to-speech feature. Amazon has also announced the Kindle DX, with a larger 9.7" screen, an accelerometer to allow for page orientation detection and the capability to display PDF files. The Kindle II retails at $359 and the Kindle DX will retail at $489.

According to Citigroup Investment Research, Amazon is projected to sell more than 1 million Kindle readers in 2009, doubling the 500,000 it sold in 2008. "Amazon sold more units of the Kindle than were sold by the iPod in its first year," said an Internet analyst at Citigroup [2]. Furthermore, Amazon's retail clout ensures a wide selection of books, blogs, and periodicals.

However, the Kindle is not without limitations. The book content is restricted by DRM, making it impossible to use the eBooks on any other devices without first installing Amazon's Kindle application. To view PDFs on the Kindle I and II, Amazon charges a conver-

sion fee of $0.10 per file. The Kindle DX natively supports PDF files. The Kindle also lacks a touchscreen display or a back-light.

Sony Reader: The Sony Reader was launched in the U.S. in 2006. Two years earlier, Sony had launched LIBrie in Japan and was the first of the second generation eBook readers to use the E-Ink technology. Sony sells the base model of its latest reader for $299. In December 2008, Sony disclosed that it sold 300,000 units of its Reader from when the device launched in October 2006 to December 2008, which was above Sony's expectations.

In March 2009, Sony announced a partnership with Google to battle Amazon in the growing eBook market. It will give the Sony Reader users access to more than half-a-million public domain books for free from Google's ambitious book digitization project [3].

Other eBook Readers: Various other eBook Readers have emerged in the last few years, but have gained little ground, including eBook Readers from iRex Technologies, the Hanlin eReader from Tianjin Jinke Electronics, Foxit's eSlick, and the Cybook by the French company Bookeen (See Exhibit 12).

N E W   E N T R A N T S

Plastic Logic: With the first model of Plastic Logic's Reader expected to be released in early 2010, the product is already considered a major potential threat to Amazon's Kindle. The eBook Reader will be equivalent in size to a pad of paper, weigh less than a magazine and launch with an electronic store that includes eBooks, newspapers, magazines, trade journals and blogs. Advanced features will include touchscreen capabilities, a simple design, and a larger size for ease in both holding and reading. It will use E Ink technology and support multiple file formats [4].

Papyrus: Samsung will release its eBook Reader, named Papyrus, in Summer 2009. Papyrus will have an A5 paper size screen and 512MB of memory, and will come in multiple colors. Papyrus will integrate PDA features such as a calculator, scheduler, calendar, clock, and contacts list. Papyrus will use an E Ink enabled touch screen display. However, the device will not support wireless connectivity [5].

FirstPaper: With major funding from Hearst Corporation, FirstPaper is developing an eBook Reader to be launched within the next two years. The Linux-based wireless reader will be the size of a tablet and will incorporate a flexible color version of the E-Ink technology. If brought to market at a price comparable to other competitors, FirstPaper could become a serious contender in the eBook Reader market [6].

S U B S T I T U T E P R O D U C T S

Notebooks/Laptops: Laptop and Notebook computers can display eBooks of different formats, these devices have often have a superior display and more functionality compared to an eBook reader device, many of new generation the ultra-portable laptops and tablet PCs are extremely compact and light making them a direct substitute for eBooks, however these devices are generally more expensive and have a shorter battery life due to their more extensive electronics.

SmartPhones: Existing smartphones such as Apple's own iPhone could potentially be a substitute for eBook readers. However, these phones are limited by their small screen size and typically lower battery life (compared to eBooks).

The Apple App Store currently lists nearly 4,300 applications under the 'Books' category. Included in this category are eBook reading applications, audiobooks, and self-contained eBooks. Amazon's new Kindle for iPhone application was released in March 2009. The application allows users to read Kindle-format eBooks on the iPhone.

Apple's own iPhone seems to suffer the least from small screen size and battery life because it was also designed to play video.

Books, Newspapers, and Other Print Media: Traditional hard copy forms of books, newspapers, and magazines are the primary forms of substitute products threatening the ebooks and online content markets. According to the the Association of American Publishers, book sales in 2007 were $25 billion and growing at a yearly rate of 2.5% [8]. These sales are concentrated on a relatively few blockbuster titles with about 2% of titles selling more than 5000 copies and 80% selling less than 100 copies [9].

Many people find it hard to read literature from screens due to eye strain. As a result, they prefer to print out their electronic documents and read the hard-copy versions. Furthermore, print media is battery-free and is easy to transfer without DRM restrictions.

Alternative Entertainment Sources: With the rapid growth and popularity of electronics, reading has taken a backseat to other forms of entertainment and information resources that are fostered by these products. Apple reported that a record of 22.7 million iPods were sold during the first quarter of 2009. This represented a 3% unit growth over the same quarter in 2008 [10]. In 2006, US handheld game software sales reached $1.7 billion, and game hardware (including console and handheld) reported revenues of $6.5 billion [11]. As a result, games, movies, TV, and music on portable electronics can now be considered major threats to the eBook.

Hardware suppliers

Electronic Paper

E Ink Corporation is a privately held manufacturer of E Ink® Imaging Film, a type of electronic paper. It has partnered with various companies, including Sony and Amazon, in the development of their eBook readers, which utilize the E Ink technology [1]. Recently, E Ink released a broadsheet prototype kit aimed at developers to experiment around its display and build their own prototype readers. Exhibit 13 lists current eBook Readers using E Ink technology.

Network Connectivity

eBook Readers usually obtain content through Internet, either directly through a wireless connection or through a computer connected to the Internet. The Kindle currently delivers eBooks through the Sprint 3G cellular network. Many ODMs produce cellular or wireless network chips at low costs. Similarly, off-the-shelf components for USB and Bluetooth connections are also available.

Value Network

A value network is a complex set of social and technical resources. The activities and interactions between the main players in the eBook value network, namely the publishers, authors, and advertisers, are illustrated in Exhibit 14.

Publishers

Jeff Abraham, executive director of Book Industry Study Group Inc., claims that the entire publishing industry generates revenues of around $25 billion per year [1]. However, book sales are often under reported, because smaller publishers are not required to report their sales.

eBook readers demand cheaper prices from publishers compared to conventional books because they believe that suppliers pay less for distribution and have more bargaining power to receive discounts. For Amazon's Kindle, however, publishers sell their eBooks at the same price as the hard-copy version while the best-selling eBooks can be purchased at prices up to $25.99. Paul Aiken, the executive director of the Authors Guild, an advocacy organization for published authors, said that at some point Amazon will likely put pressure on publishers and authors rather than raise consumer prices.

In a recent poll performed by global supply chain management giant IBS and the Bookseller and Book Industry Communication (BIC) of publishers at the London Book Fair, only 53% of booksellers had arrangements in place to sell their books in digital form. Of those who had the arrangements, 40% planned to sell books directly through their own website, 21% planned to sell through third party sources, and 33% were still unsure [2].

INTERNET-ONLY PUBLISHERS

Hard Shell Word Factory and Online Originals were among the first Internet-only publishers of eBooks established in the 1990s. Each pioneered different aspects of what has since become common practice amongst eBook publishers, such as the support of multiple formats such as PDF and the payment of much higher royalty rates than conventional publishers. Hard Shell Word Factory has set the first professional standards for commercial eBooks and pioneered author-friendly contracts. Online Originals was the first eBook publisher to win mainstream book reviews in The New York Times and a nomination for a major literary prize, the Booker Prize.

SELF PUBLISHING

Self-publishing is the publishing of books and other media by the authors themselves, rather than by established publishers. This method of publishing has become popular amongst individuals that are new to the industry and do not have the finances to utilize the services of conventional publishers. Though it represents a small percentage of publishing in sales terms, this practice has seen an increase in activity with the advancement of publishing technology, desktop publishing systems, print on demand, and the internet. The internet and other electronic means of distribution have especially made self-publishing feasible.

AUTHORS

Due to the low distribution cost, eBook publishing allows authors to retain more earnings from each sale. It provides an easy method of self-publishing, which is especially helpful for novice authors who may not have the finances to purchase the services of commercial publishers.

Unlike the traditional print books model, in which authors only earn a few dollars per book sold, authors normally receive 80% to 90% of the sales revenue from each purchase of an eBook. For example, Michael Webb, an author of multiple ebooks for sale at ClickBank, an online retail outlet for digital product vendors, explained, "I have very 'successfully' published my first book with a top NY publishing house. It has continued to sell quite well and is in its 8th printing. However, because I only make about $2 per title sold, the royalty

checks (every six months) don't get me all that excited. I make more with some of my ClickBank titles in one month than I make with this 'best seller' all year" [3].

ADVERTISERS

Publishers can leverage their existing magazine and newspaper advertisement models and use them in eBooks and electronic periodicals. They may also be ale to take advantage of the wireless technology in most eBook readers to stream embedded advertisements over the Internet. This could lead to the development of an alternative price model where advertisements make up for a reduced sale price.

REVENUE MODELS FOR EBOOK CONTENT

ONLINE NEWSPAPERS AND MAGAZINES

Traditionally, newspaper and magazine companies have three sources of revenue: news-stand sales, subscriptions, and finally advertisements. Newspapers have recently seen significant declines in subscriptions and paper prints. In 2008, more people in the US read their news online for free, rather than purchasing print newspapers and magazines [1]. Today, almost all newspaper agencies provide their articles online for no cost, although some, such as the Wall Street Journal, charge a subscription fee.

Magazines also follow a similar revenue model. As eBook reader prices go down, some publishers may even start to give away free devices to customers, moving towards a service model currently offered by some cell phone and wireless providers.

EBOOKS

In contrast to the traditional revenue model for books, the eBook model does not require retailers and wholesalers. As a result, more profits are shared by the authors and publishers.

In December 2008, Apple began selling eBooks, ranging in pricefrom $8.99 to $25.99, through its iTunes Store. As with songs and movie downloads from iTunes, Apple makes a small profit from each sale. A recent iPhone application allows customers to purchase and read eBooks directly from Amazon.

Strategic Options for Apple

Stay out of the eBook Reader market

Apple could decide that the eBook Reader market does not offer large enough growth prospects, given the dominance of Amazon and Sony, and instead focus on developing and sustaining its current product lines or developing new products in other markets.

Leverage iPhone and iPod as eBook Readers

At the same time, Apple could grow the eBook reading capacity for its mobile devices, such as iPhone and iPod Touch, by integrating a reader into the platform and introducing new applications to support eBooks from other sources with different file formats. It could potentially chose to leverage existing eBook content or expand iTunes to support digital book, newspaper, and magazine content. In March 2009, Amazon even released a free iPhone application for reading titles purchased at their Kindle store [1].

Design an innovative eBook Reader

Apple could decide that it is again time for product diversification, and develop its own eBook Reader, thus setting themselves apart from earlier technologies. They would have to decide how to handle content distribution and product details, how to align themselves with publishers, and how to compete with the market leader, Amazon. In addition, a sustainable business model and pricing strategy would have to be developed.

Together with the eBook Reader, Apple could provide an eBook library, competitive with other eBook providers in quality and quantity. Another option would be to only manufacture the eBook Readers and either partner with a content distributor or to wait for a universal eBook standard to be developed by IDPF and make their product standard compliant. If Apple chooses to enter the eBook market, it needs to decide how to integrate its eBook Reader into its existing product ecosystem.

Acquisition or Partnership

Given that there are many eBook Reader providers especially outside the US (See Exhibit 12), Apple could use its large resource of cash to acquire one of these manufacturers. This could help Apple save on R&D and shorten the overall release cycle. In addition, Apple could form a partnership with an eBook provider, resulting in a larger eBook repository.

E XHIBITS

Table of Exhibits

1. Apple Executive Team and Board of Directors

2. Current Apple Products

3. Timeline of Apple Products

4. Apple Balance Sheet

5. Supporters of the EPUB eBook File Format

6. Electronic Paper

7. eBook Sales by Quarter

8. eBook Market Segment Characteristics

9. Kindle User Age Demographics

10. eBook Sales Compared to Print Sales

11. Comparison of eBook Readers

12. Other Major eBook Readers

13. List of Devices that Use E Ink Technology

14. eBook Value Net

EXHIBIT 1: APPLE EXECUTIVE TEAM AND BOARD OF DIRECTORS

Executive Team
Under Steve Jobs, the Apple executive team, listed below, comprises of talented individuals that span across all areas of the business. Their dedication and teamwork has contributed to the success of the company [2].

  * Steve Jobs, Chief Executive Officer
  * Timothy D. Cook, Chief Operating Officer
  * Peter Oppenheimer, Senior Vice President and Chief Financial Officer
  * Philip W. Schiller, Senior Vice President of Worldwide Product Marketing
  * Mark Papermaster, Senior Vice President of Devices Hardware Engineering
  * Jonathan Ive, Senior Vice President of Industrial Design
  * Bertrand Serlet, Senior Vice President of Software Engineering
  * Ron Johnson, Senior Vice President of Retail
  * Sina Tamaddon, Senior Vice President of Applications
  * Scott Forstall, Senior Vice President of iPhone Software
  * Bob Mansfield, Senior Vice President Mac Hardware
  * Daniel Cooperman, Senior Vice President, General Counsel and Secretary

Board of Directors
In addition to the CEO, the board of directors jointly oversees the activities of Apple [3].

  * Bill Campbell - Chairman and former CEO, Intuit Corp
  * Millard Drexler - Chairman and CEO, J. Crew
  * Albert Gore Jr. - Former Vice President of the United States
  * Steve Jobs - CEO, Apple
  * Andrea Jung - Chairman and CEO, Avon Products
  * Arthur D. Levinson, Ph. D. - Chairman and CEO, Genentech
  * Dr. Eric Schmidt - CEO, Google
  * Jerry York - Chairman, President and CEO, Harwinton Capital

EXHIBIT 2: CURRENT APPLE PRODUCTS

	Products	Description	Lauched
Mac	iMac	Consumer all-in-one desktop computer, whose popularity helped revive the company's fortunes.	1998
	Mac mini	consumer sub-desktop computer	2005
	Mac Pro (PowerMac)	Workstation-class desktop computer	2006
	MacBook (iBook)	Consumer notebook	2006
	MacBook Pro (PowerBook)	Professional portable computer alternative to the MacBook	2006
	MacBook Air	Ultra-thin, ultra-portable notebook	2008
	Xserve	Rack mounted, dual core, dual processor 1U server	2002
iPod	iPod Classic	Portable media player, currently available in 120 GB	2001
	iPod Nano	Portable media player, currently available in 8 and 16 GB	2005
	iPod Shuffle	Digital audio player, currently available in 1 and 4 GB	2005
	iPod Touch	Portable media player, personal digital assistant, and Wi-Fi mobile platform, currently available in 8, 16 and 32 GB	2007
	iPhone	Internet-connected multimedia smartphone	2007
	Apple TV (iTV)	Digital media receiver device designed to play internet digital content onto an high-definition television	2007

EXHIBIT 3: TIMELINE OF APPLE PRODUCTS

EXHIBIT 4: APPLE BALANCE SHEET

	March 28, 2009	September 27, 2008
ASSETS:		
Current assets:		
Cash and cash equivalents	$ 4,466	$ 11,875
Short-term marketable securities	20,547	10,236
Accounts receivable, less allowances of $60 and $47, respectively	1,932	2,422
Inventories	312	509
Deferred tax assets	1,539	1,447
Other current assets	5,057	5,822
Total current assets	33,853	32,311
Long-term marketable securities	3,865	2,379
Property, plant and equipment, net	2,546	2,455
Goodwill	207	207
Acquired intangible assets, net	268	285
Other assets	2,498	1,935
Total assets	$ 43,237	$ 39,572
LIABILITIES AND SHAREHOLDERS' EQUITY:		
Current liabilities:		
Accounts payable	$ 3,976	$ 5,520
Accrued expenses	2,761	3,719
Deferred revenue	7,014	4,853
Total current liabilities	13,751	14,092
Deferred revenue – non-current	3,460	3,029
Other non-current liabilities	1,715	1,421
Total liabilities	18,926	18,542
Commitments and contingencies		
Shareholders' equity:		
Common stock, no par value; 1,800,000,000 shares authorized; 891,911,821 and 888,325,973 shares issued and outstanding, respectively	7,643	7,177
Retained earnings	16,653	13,845
Accumulated other comprehensive income	15	8
Total shareholders' equity	24,311	21,030
Total liabilities and shareholders' equity	$ 43,237	$ 39,572

E X H I B I T 5 : S U P P O R T E R S O F T H E EPUB eB O O K F I L E
F O R M A T

List of EPUB eBook Format Supporters

UK Publishers	US Publishers	Supply Chain
Random House	HarperCollins Publishers	Adobe
HarperCollins	Harlequin	LibreDigital
Penguin	Hachette Book Group	Ingram Digital
Simon & Schuster	John Wiley & Sons Inc.	OverDrive
Pan MacMillan	Penguin Group USA	eBook Technologies
Mills & Boon	Macmillan	Publishing Dimensions
Cambridge University Press	Pelican Publishing Company	VitalSource Technologies
Oxford University Press	Cengage Learning	Mobipocket
Gardners Books	Workman Publishing	Rosetta Solutions
Taylor & Francis	Seattle Book Company	Innodata Isogen
Value Chain International	National Science Teachers Assoc.	TexTech
	CQ Press	codeMantra
		DNAML

E XHIBIT 6: E LECTRONIC P APER

EXHIBIT 7: EBOOK SALES BY QUARTER

US Trade Wholesale Electronic Book Sales
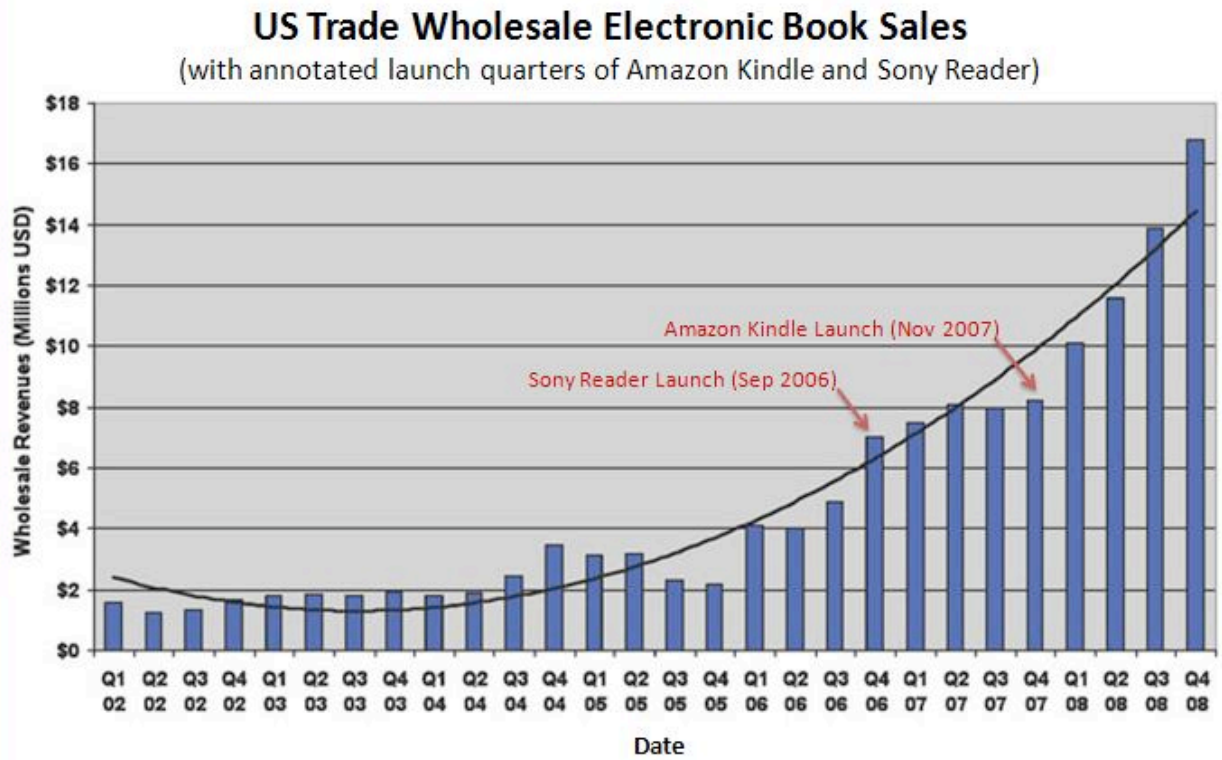### (with annotated launch quarters of Amazon Kindle and Sony Reader)

E XHIBIT 8: E B OOK M ARKET S EGMENT C HARACTER -
ISTICS

Category	Online Affinity of Audience	Importance of Fast Delivery	Key Word Value	Customizability of Content	Potential for Multimedia Enhancement	Scarcity
Textbooks	◐	◐	●	●	●	◐
Professional and Technical	●	○	●	●	◐	●
Business	●	◐	◐	●	○	◐
Fiction	◐	○	○	○	○	○
Non-Fiction	◐	○	◐	◐	◐	◐
Juvenile	○	○	○	○	◐	○
Reference	●	○	●	◐	◐	◐
Travel	●	●	●	●	●	◐

● High	◐ Medium	○ Low

Source: Jupiter Communications, " eBooks: An Emergent Opportunity, but Stephen King Is Not the Model," August 2000.

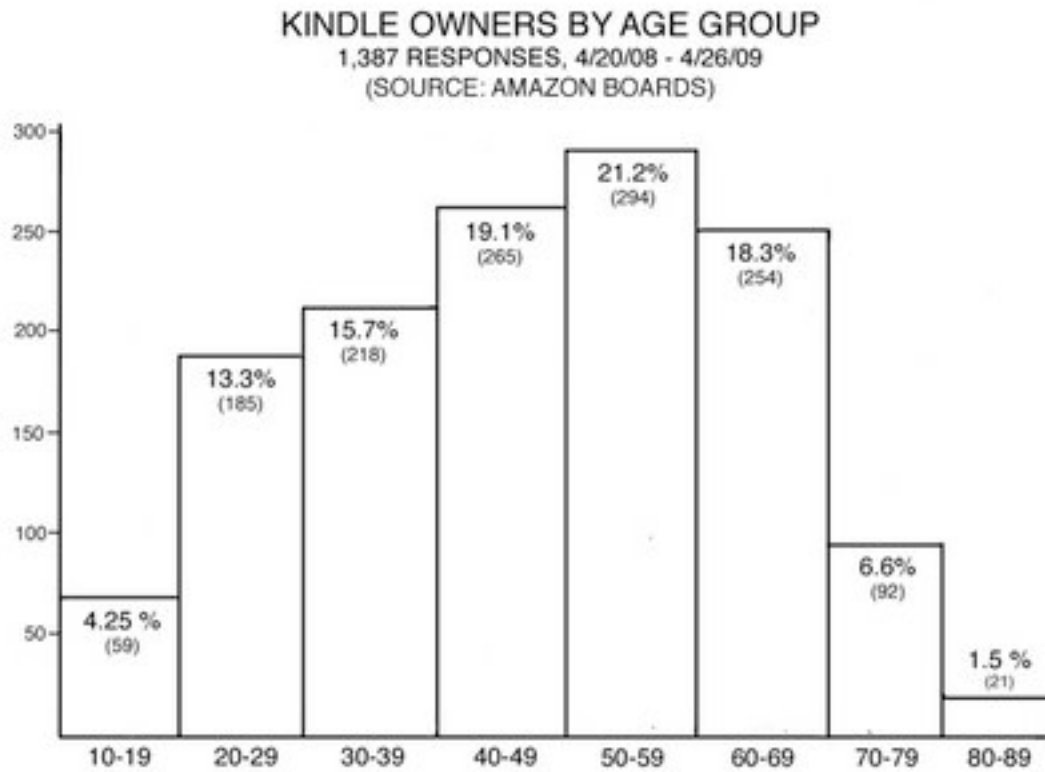E XHIBIT 9: K INDLE U SER A GE D EMOGRAPHICS

KINDLE OWNERS BY AGE GROUP
1,387 RESPONSES, 4/20/08 - 4/26/09
(SOURCE: AMAZON BOARDS)

E XHIBIT 10: E BOOK S ALES C OMPARED TO P RINT
S ALES
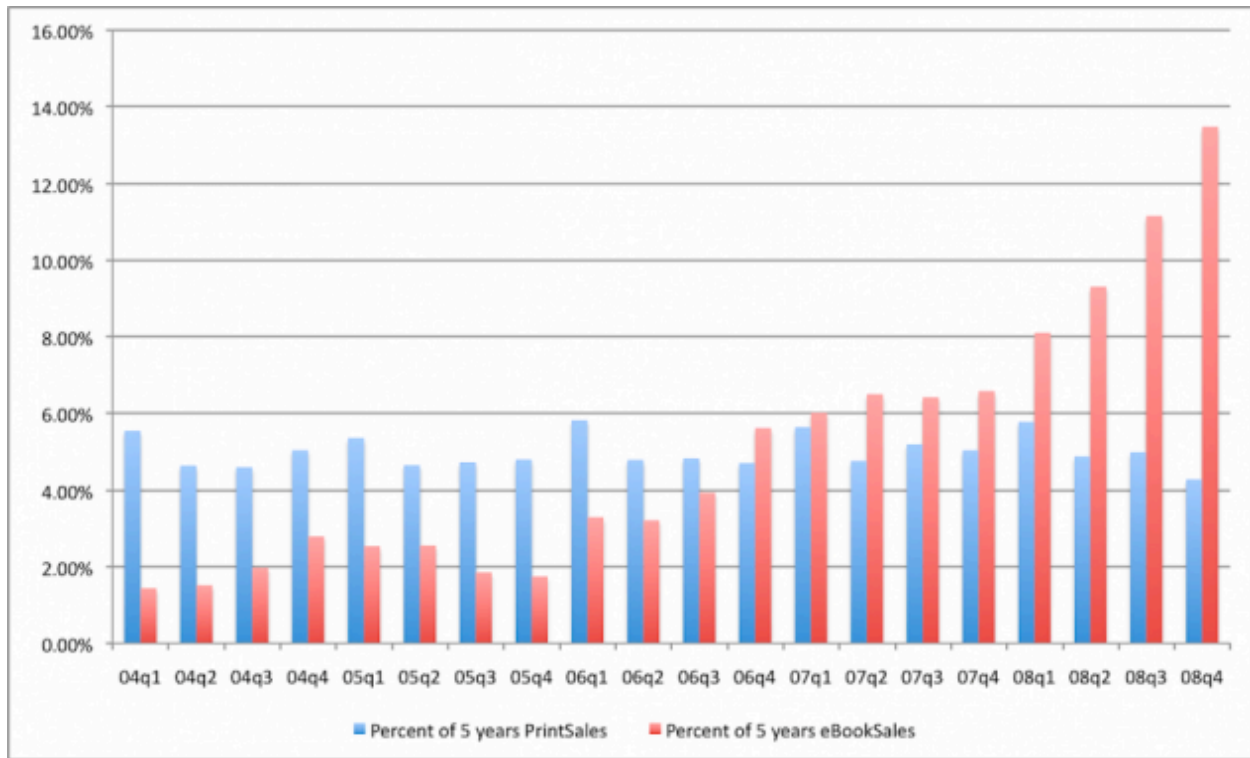
EXHIBIT 11: COMPARISON OF EBOOK READERS

eBook Reader Comparison

	Amazon Kindle	ECTACO JetBook	Sony Digital Reader
Format and Features			
eReader Size	7.5x5.3	6.9x4.2	6.9x4.8
Screen Size	6"	5"	6"
Electronic Paper Display Tech.	Yes	No	Yes
Resolution	600x800	600x800	600x800
Multiple Font Sizes	Yes	Yes	Yes
Internal Memory	256MB	128MB	192MB
SD Memory Cards Supported	4GB	2GB	2GB
Weight (Ounces)	10.3	9	9
Computer Connectivity	USB	USB	USB
Audio formats	MP3/AAC	MP3/AAC	MP3/AAC
Book Selection	120,000+	Unclear	40,000+
Features Unique to Kindle			
Wireless connectivity	Yes	No	No
Newspapers & Magazines	Yes	No	No
Price on Amazon.com	$399	$330	$270

Source: Company data; Citi Investment Research

E X H I B I T   12:   O T H E R   M A J O R   e B O O K   R E A D E R S

Major Competitive eBook Readers and Release Date

- Kindle DX by Amazon (May 2009)
- FLEPia by Fujitsu (April 2009)
- Kindle 2 by Amazon (February 2009)
- eSlick by Foxit Software (2009)
- PRS-700BC Reader Digital Book by Sony (October 2008)
- Digital Reader 1000 by iRex Technologies (2008)
- Kindle by Amazon (2007)
- Cybook Gen3 by Bookeen (2007)
- GeR2 by Ganaxa (2007)
- Star eBook STK-101 by Star eRead (2007)
- Hanlin eReader by Jinke (2007)
- Sony Reader by Sony (2006)
- iLiad by iRex Technologies (2006)
- Librié by Sony (2005)

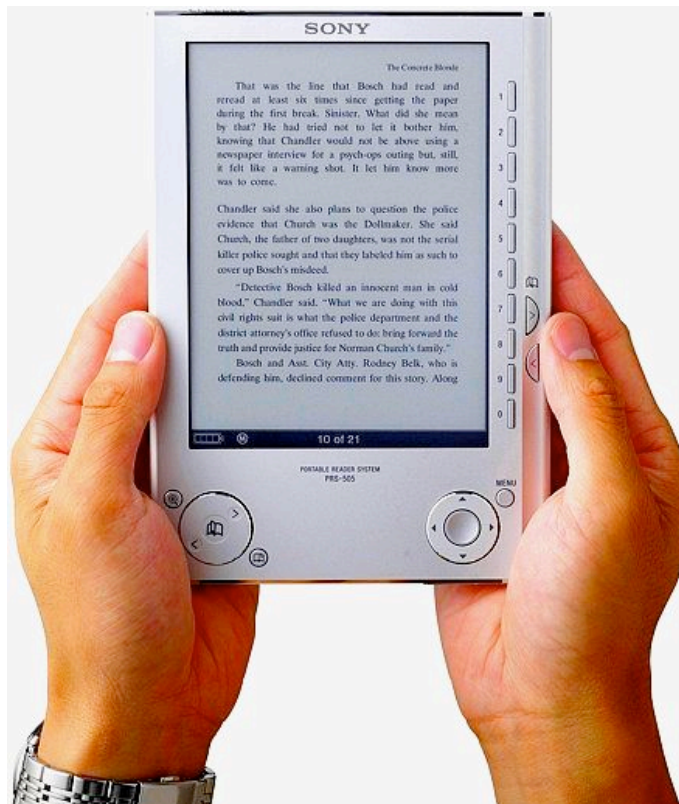iRexiLiad:
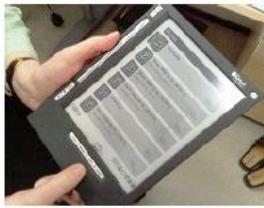
Foxit eSlick Reader:

Fujitsu FLEPia:

Cybook eReader:

Hanlin eReader:

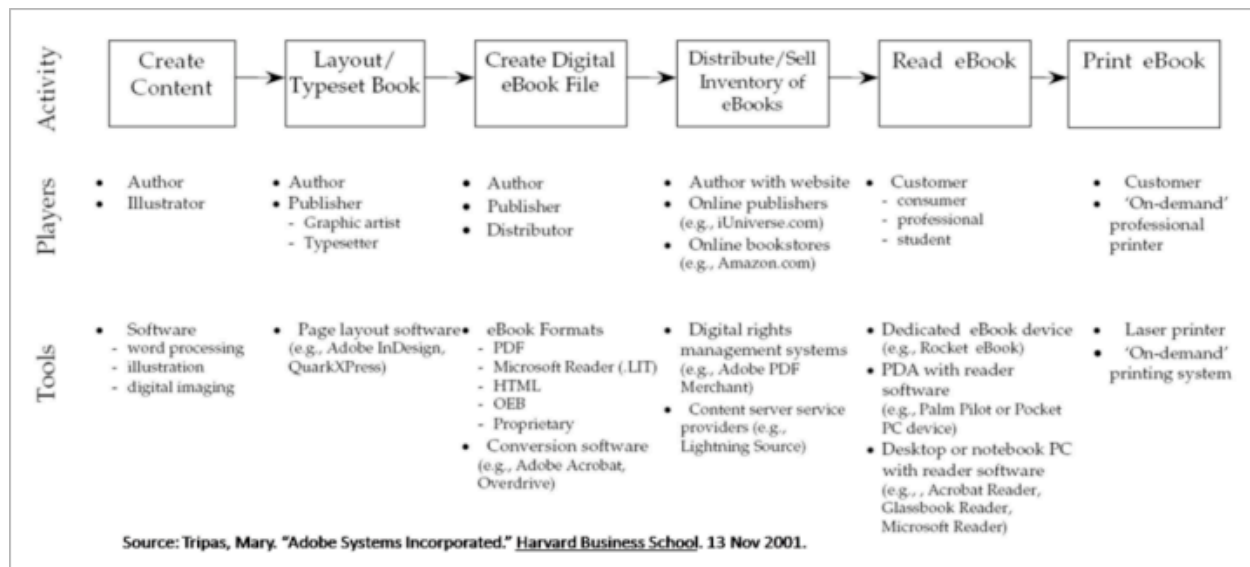

GeR2:

SONY EBOOK READER

iRex Technologies	iRex Technologies, a spin-off from Phillips, first launched its e-book reader in 2006. Larger than the Amazon Kindle or Sony Reader, the iLiad eBook Edition, the second generation of the reader, has an 8.1-inch screen and weighs 15.3 ounces. The iLiad also has built in Wi-Fi capability with an option for external Ethernet networking. It comes with 256MB internal flash memory, of which 128 MB is accessible to the user, and supports text, PDF, images and HTML format. With a market price of $600, not only is the iRex iLiad more expensive compared to its competitors, but it is also about 5 ounces heavier and only supports Mobipocket files.
Hanlin eReader	The Hanlin eReader from Tianjin Jinke Electronics was released in 2007. Feature-wise there may not be much to differentiate it from its competitors. It has all the basics: a 6-inch display, 32-MB SDRAM and support for the usual text, docs and images. It runs Linux OS but has no wireless capability. The Hanlin eReader is available under different brand names, such as BeBook in Netherlands.
Foxit eSlick	Foxit's eSlick's price tag is probably its main appeal. Emphasizing PDF performance as an advantage over other eBook readers as well as cost, Foxit's eSlick will be sold for $259, undercutting its competitors. The device offers features similar to the Kindle and the Sony Reader. However, at only 6.4 ounces, eSlick is among the lightest readers on the market and comes with internal memory of 128 MB and a 2-GB SD card, and the standard 6-inch screen. Features such as a built-in MP3 player makes the eSlick unique and attractive. At the same time this device doesn't support popular eBook formats and requires USB connection to a PC to download new titles since WiFi is not supported. [12] paidContent.org has noted that "The cheaper eSlick seems better poised to compete with Sony's device, as it doesn't have the WiFi/subscription content that has drawn Kindle buyers in droves."
Cybook	//Cybook//, produced by the French company Bookeen, is a 4.7" x 7.4" x 0.3" eBook Reader that weighs about 6.13 ounces with E-Ink screen technology. The Cybook reads many file formats including the Mobipocket secured ebook format and offers access to a wide range of digital documents such as PDFs and images. The Cybook runs Linux as its underlying operating system; however, the firmware is not open source. This could be due to the support for DRAM protected eBooks, which probably requires third party libraries. To a host computer the Cybook functions as a typical USB mass storage device, which allows for easily copying of books from most computers. As a result, it is supported on most operating systems. A Secure Digital card slots allows for expanded storage, which currently limited to a 2 gigabyte SD card [12]. In addition, MP3 files are supported for users to easily listen to music or audiobooks, making Cybook more than just an eBook reading device.

EXHIBIT 13: LIST OF DEVICES THAT USE E INK TECHNOLOGY

Current eBook Reader Devices that Use E Ink's Technology

• Sony Reader PRS-700: Released to market 4th quarter of 2008, uses touchscreen.
• Sony Reader PRS-505: Released to market in October 2, 2007.
• Bookeen Cybook Gen3: Released for sale at the end of October 2007.
• iRex Digital Reader: is the largest electronic ink reader to date. It optionally includes a touch screen.
• iRex iLiad: is the 2nd largest electronic ink reader to date. It includes a touch screen.
• The Jinke/Hanlin: Makes several models for direct sale and via OEM's. Some have a second screen area for input.
• Amazon Kindle 2: The 2nd generation Kindle is available from their web site (not sold outside of the USA). Released to Market February 24 2009.
• Amazon Kindle DX: The Kindle DX is a 9.7" screen display device. It is available from their web site (not sold outside of the USA). Released for orders May 7, 2009
• Ganaxa GeR2: Released September 2007, for Les Echos daily newspaper.
• Soribook: Released to Korean domestic pre-orders only in May 2008.
• Readius: Projected release date Autumn 2008 in Italy. Uses a rollup electronic ink display.
• Hanvon N516 - A Chinese reader that uses a 5" electronic ink screen with the same number of pixels as the current 6" screens which increases ppi to 200.

EXHIBIT 14: EBOOK VALUE NET

Activity	Create Content	Layout/ Typeset Book	Create Digital eBook File	Distribute/Sell Inventory of eBooks	Read eBook	Print eBook

Players	• Author
	• Illustrator
		• Author
		• Publisher
		  - Graphic artist
		  - Typesetter
			• Author
			• Publisher
			• Distributor
				• Author with website
				• Online publishers (e.g., iUniverse.com)
				• Online bookstores (e.g., Amazon.com)
					• Customer
					  - consumer
					  - professional
					  - student
						• Customer
						• 'On-demand' professional printer

Tools	• Software
	  - word processing
	  - illustration
	  - digital imaging
		• Page layout software (e.g., Adobe InDesign, QuarkXPress)	• eBook Formats
			  - PDF
			  - Microsoft Reader (.LIT)
			  - HTML
			  - OEB
			  - Proprietary
			• Conversion software (e.g., Adobe Acrobat, Overdrive)
				• Digital rights management systems (e.g., Adobe PDF Merchant)
				• Content server service providers (e.g., Lightning Source)
					• Dedicated eBook device (e.g., Rocket eBook)
					• PDA with reader software (e.g., Palm Pilot or Pocket PC device)
					• Desktop or notebook PC with reader software (e.g., Acrobat Reader, Glassbook Reader, Microsoft Reader)
						• Laser printer
						• 'On-demand' printing system

Source: Tripas, Mary. "Adobe Systems Incorporated." Harvard Business School. 13 Nov 2001.

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Charles Lin

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Fletcher McCombie

Vincent Mei

George Michelogiannakis

Nicholas Moe

Ryan Mullins

Michael Munie

Abhilash Nair

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