

THE CHAPTERS EFFECT ON BRITISH COLUMBIA-BASED
LITERARY PUBLISHERS

by

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ABSTRACT

The restructuring of the Canadian bookselling industry—the effect on that industry of the creation of superstore bookstore chains Chapters and Indigo, their subsequent merger, and the parallel decline of the independent bookstores—is an area of heightened importance to the publishing industry in British Columbia (B.C.). This enquiry begins with the merging of three bookstore chains (Coles, SmithBooks, and The Book Company) to form the Chapters phenomenon in 1995. The period of enquiry ends with the newly merged Chapters/Indigo superstore mega-chain in 2001. The aim of this project is to document the events from 1995 to 2001 as they related to B.C.-based publishers; specifically, how Talonbooks, a Vancouver-based independent literary press founded in 1963, weathered the radical and sudden changes in the Canadian book marketplace.

Keywords: Chapters book stores; indigo books music & more; Talonbooks; New Star Books; book publishing

Subject Terms: Publishers and publishing – British Columbia; Booksellers and bookselling – Canada; Book industries and trade – Canada; Book industries and trade – British Columbia;

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PREFACE

My analysis of the Coles/SmithBook merger, the creation of Chapters, the Indigo acquisition of Chapters, and its effect on the B.C. publishing and, in particular, on Talonbooks is wholly my own. While Karl Siegler, Talonbooks' CEO and President, reviewed a late draft of this paper and provided valuable feedback—much of which I have cited directly—his view of the “Chapters Effect” on B.C. publishers and on his own company differs in many ways from mine, thus the reader is cautioned that the opinions expressed in project report are not necessarily that of Karl Siegler or of Talonbooks. And although I have deferred to Karl Siegler numbers and dates where applicable, I am, of course, responsible for any errors in fact.

OUR LITERATURE

Literature is not only a mirror; it is also a map, a geography of the mind. Our literature is one such map, if we can learn to read it as our literature, as the product of who and where we have been. We need such a map desperately, we need to know about here, because here is where we live. For the members of a country or a culture, shared knowledge of their place, their here, is not a luxury but a necessity. Without that knowledge we will not survive.¹

In 1972 Margaret Atwood wrote the seminal criticism of Canadian literature with *Survival: A Thematic Guide to Canadian Literature*, in which she argued that victimization was the central trope of Canadian writing and survival was the chief paradigm of Canadian culture, an argument which tapped into the nationalistic fervour of the late 1960s and early 1970s. *The Globe & Mail* declared *Survival* “the most important book that has come out of this country.”² The book was an instant success, and a source of controversy.

Atwood’s metaphor for survival explicitly referred to the content of Canadian-authored books and implicitly acknowledged the role of a Canadian-owned publishing industry. Her survey of CanLit included the chapter “How to Use This Book,” which drew the readers’ attention to “A Short List” and “A Long List” of books at the end of each chapter and to the appended “Fifteen Useful Books.” Fitting with Atwood’s predisposition, “much of the books focus was not on Canadian literature generally but on writers published by House of Anansi, the publisher of *Survival*; 42% of the titles in Anansi’s 1972 catalogue were recommended by Atwood in *Survival*’s various reading lists.”³ However, a survey of the other titles listed reveals the vast majority of “our literature” was being published by us: House of Anansi, McClelland and Stewart (M&S), M&S’s New Canadian Library, New Press, Ryerson, and the University of Toronto Press.

¹ Atwood, Margaret. *Survival: A Thematic Guide to Canadian Literature*. Toronto: Anansi, 1972, p19.

² Grosskurth, Phyllis. “Truth—and a major talent.” *The Globe & Mail*. October 28, 1972, p. 33. Review of Margaret Atwood, *Survival*.

³ Davey, Frank. *Margaret Atwood: A Feminist Poetics*. Vancouver: Talonbooks, 1984, pp. 153-154. The New Canadian Criticism Series.

A brief sample of industry statistics shows the phenomenal growth of CanLit and Canadian publishers in the thirty years since the publication of *Survival*: 610 Canadian-controlled publishers added over 3,500 new titles—72.2% Canadian authored—to the nearly 100,000 in print in 2000–2001; a market worth about \$970 million annually.⁴ Yet the Canadian book publishing industry is in perpetual crisis, characterized by chronic under-capitalization, pressure to relax foreign ownership regulations, increased consolidation of foreign and domestically owned publishers, a fragile supply chain, and monopolization of the Canadian book trade.

Thus, thirty years after Margaret Atwood’s treatise, most Canadian publishers still had a tenuous hold on survival. Crises threaten the industry so regularly as to appear cyclical, with patterns of stability that ebb and flow about every five years. Nearly every five years, a federal budget changes the funding structure for publishers. About every five years, a (usually) wealthy business person (such as Bollum, Duthie, Stevenson, or Reisman) attempts to (finally) succeed in creating a successful book retail chain or large-format book superstore—often only to overestimate the market, sink, and take a few more publishers and independent bookstores down with them. Every five years, a Canadian author is hailed as a “break-out” on the international scene—usually by winning a prestigious, non-Canadian award compensated with hard currency, or by being discovered by Hollywood—as if we are unable to validate our own literature. And speculation ensues about who will be next—which lucky writer, which savvy publisher—and whether this time, finally, Canada will shed its colonial culture-coat and get the recognition it deserves. Or whether with the next crisis, cultural protectionist laws and treaties will collapse, flooding Canada with American big-box retailers and foreign branch plants.

A case in point: while Margaret Atwood has become the doyenne of Canadian fiction, *Survival* has passed from Anansi to branch plant interests “The Canadian

⁴ Canada. Statistics Canada. *Survey of Book Publishers and Exclusive Agents; Book publishers and exclusive agents* (data tables). [Ottawa] November 2003.

Publishers,” McClelland & Stewart.⁵ Paperbacks of Atwood’s bestsellers have been published by Seal Books, a joint venture of M&S and Bantam Books (a division of Random House). Chapters and Costco superstores sold *Oryx and Crake* at deep discounts independent bookstores could not compete with, and *The Blind Assassin* is reportedly soon to be Hollywood feature film (her third book to make it to the big screen). Anansi barely escaped the fall of General Distribution Services and was sold to venture capitalist Scott Griffin in 2002. When Heritage Minister Sheila Copps commented on the demise of the Stoddart empire, the threat to independent Canadian literary presses, and her government’s apparent reluctance to enforce the foreign ownership and competition laws in the culturally protectionist spirit intended, without irony, she cited Margaret Atwood as a Canadian publishing success story: “If you’ve got authors like... like the Margaret Atwoods, the Margaret Laurences, the Rohinton Mistrays, the Michael Ondaatjes, who are known around the world, obviously we must be doing *something* right.”⁶ Is this the measure of a successful Canadian publishing industry? Are we America’s farm team? Is this survival? As Atwood herself asked thirty years ago, “If so, what happens after survival?”⁷

B.C.-Based Publishing

For B.C.-based publishers, survival is even more precarious than for the Toronto-based publishers that dominated Atwood’s book lists in 1972, and who represent the Canadian publishing epicentre today. And just as the distinct voice of West Coast writers may not conform to the tropes of Atwood’s argument or disposition, B.C. publishers’ work is also

⁵ Avie Bennett, chairman and president of McClelland & Stewart, donated 75% of the shares in M&S to the University of Toronto and sold the remaining 25% to Random House Canada, a division of Random House USA, a division of Bertelsmann AG of Germany, the largest publishing company in the world. Random House Canada’s control over M&S’s marketing and sales department has many within the book publishing industry arguing de facto control is Random House’s.

⁶ Sheila Copps. [Trouble in the Canadian Book Industry.] Interviewed by Sandra Abma. The House [radio program]. August 17, 2002. Produced by the Canadian Broadcast Corporation, Toronto. [emphasis added] Heritage Minister Sheila Copps was responding to Karl Siegler’s question “...are you still serious about the intent and the application of this regulatory framework, or have you just given up and conceded?”

⁷ Atwood, Margaret. *Survival: A Thematic Guide to Canadian Literature*. Toronto: Anansi, 1972, p 246.

unique. Publishing on the West Coast is thematically, geographically, economically, and historically distinct from publishing in Central Canada, while remaining a vibrant, viable, and culturally important industry both regionally and nationally.

Possibly the paramount and most easily discernable role of B.C. publishers is that of an advocate for local writers. In *Publishing on the Edge*, written in 1993, Roy MacSkimming reported that 70% of new titles and 83% of backlist titles produced by the 21 B.C. publishers surveyed were written by resident authors.⁸ Certainly a substantial proportion of these titles would be considered regional—primarily concerned with the history, culture, people, and geography particular to the province—but regionalism represents a paradox for B.C. publishers. On the one hand, regional titles are central to the shared knowledge of ourselves that Atwood propagates in *Survival*; they consistently dominate the B.C. bestseller lists, and are a staple for many thriving local firms. Some critics contend that *Survival* does not apply to B.C. writing at all: the themes of home, family, and harmony with the environment are primary to West Coast writing.⁹ As *BC Bookworld* publisher Alan Twigg dryly stated, the “best way to win a B.C. Book Prize is to write about Indians. Or trees. Or preferably both.” But many B.C. publishers are wary of the regional publisher label and its hobbyist, farm team connotations. As Jane Fredeman (editor at UBC Press from 1973–1990) wrote, while it is “tempting to focus exclusively on the many regional books published locally, discussing the categories into which they fall and highlighting the bestsellers... to do so would be to fall into the eastern trap, seeing Toronto publishers as national and all others as regional. It would also be to ignore the size, diversity, and maturity of the industry that has grown up in the province.”¹⁰

B.C.’s geography not only influences the themes of the province’s literature, but also the nature of the publishing community. Western alienation is a recurrent theme

⁸ MacSkimming, Roy. *Publishing on the Edge: A Cultural and Economic Study of Book Publishing in British Columbia*. Prepared for the Association of Book Publishers of British Columbia, November 1993, p 8.

⁹ Pritchard, Allan. “West of the Great Divide: A View of Literature of British Columbia,” *Canadian Literature* no. 94 (1982), pp 96-112.

¹⁰ Fredeman, Jane. “Book Publishing in British Columbia, 1990: More Than a Regional Enterprise,” *Journal of Canadian Studies*, Vol. 25, no. 3 (1990): 124-130.

politically and across disciplines: B.C.-based publishers are acutely aware of their physical separation from Canada's publishing hub. Many major conferences (Book Expo Canada), national organizations such as the Association of Canadian Publishers (ACP), Literary Press Group (LPG), Association for the Export of Canadian Books (AECB), and government bodies, including the Canada Council for the Arts, the Department of Canadian Heritage (DCH), Bureau of Competition Policy (BCP), and, of course, the head offices and buyers for major chains are based in Toronto or Ottawa. And despite British Columbians' proclivity for reading, the major population—thus readership—in Canada is three time zones away. At the most pragmatic level, this distance creates additional expenses for B.C.-based publishers, such as telecommunications, couriers and transportation charges, and travel costs. Extra effort is required to remain top-of-mind and establish a visible presence in Central Canada: of the 439 companies in Canada whose primary business activity is publishing (according to Statistics Canada), only 67 (15%) are based in B.C.; 243 (55%) are located in Ontario.

In terms of contribution to the Canadian publishing industry, British Columbia trails far behind Ontario, publishing only about 11% of the country's indigenous English-language titles, compared to the 68% produced by Ontarian publishers, although B.C.'s production has been steadily increasing. B.C. lags behind Ontario and even prairie-based publishers in terms of average revenue per title too.¹¹ One of the primary reasons for this disparity is funding. Government assistance remains a necessity, as most publishing firms do not operate profitably before grants, nor do they have enough retained earnings or access to capital to fund growth and development. Funding fluctuates with the economy and political climate, but at the time of Roy MacSkimming's 1993 report, *Publishing on the Edge*, "the B.C. industry has the third-lowest average provincial support per firm, as well as the third-lowest level (6.5 per cent) of total grants as a percentage of revenues."¹²

¹¹ Canada. Statistics Canada. *Survey of Book Publishers and Exclusive Agents; Book publishers and exclusive agents* (data tables). [Ottawa] November 2003.

¹² MacSkimming, Roy. *Publishing on the Edge: A Cultural and Economic Study of Book Publishing in British Columbia*. Prepared for the Association of Book Publishers of British Columbia, November 1993, p 50.

MacSkimming also noted that the “Alberta, Ontario, and Quebec, for example, offer not only block grants to offset production and other publication costs, but loan guarantees, marketing and distribution support, and assistance with investment in new technology. Manitoba, although its publishing industry is small, also offers support across a spectrum of block grants, marketing assistance and professional development. Alberta, Nova Scotia, and even tiny Prince Edward Island are beginning to expand their support of book publishing with additional resources from federal/provincial cultural agreements. Saskatchewan is also embarking on an expanded policy of support for its growing publishing industry.”¹³

But in the past decade, funding in British Columbia has improved, and concordantly, production and profitability have grown. Production has nearly doubled, resulting in revenues jumping to nearly \$110 million. The percentage of profitable B.C. firms rose to 61.1% as profit margins increased to 6.3% of revenues (still a lower margin than the national average of 7.7% and the average of 8.9% in Ontario.)¹⁴ In most years between 1992 and 2000, growth in B.C. book sales outpaced all other regions.¹⁵ B.C. publishers’ success in exporting books quantifiably refutes any residual parochial claims: exports of B.C.-published books have tripled in the last decade, amounting to \$22 million in sales in 2000–2001.¹⁶ Further security has been provided by the provincial government’s Book Publishing Tax Credit, introduced in February 2003, which grants qualifying publishers tax credits equal to 90% of their federal Book Publishing Industry Development Program (BPIDP) Aid to Publishers grants.¹⁷ This new funding will aid an industry already fortunate to develop in a market that boasts the highest per capita book

¹³ Ibid, pp 49-50

¹⁴ Canada. Statistics Canada. *Survey of Book Publishers and Exclusive Agents; Book publishers and exclusive agents (data tables)*. [Ottawa] November 2003.

¹⁵ Evans & Company Retail Consultants Inc. *Retail Market Study: A Review of the Canadian Book Industry*. Prepared for the Association of Canadian Publishers, February 2001, p. 23.

¹⁶ Canada. Statistics Canada. *Survey of Book Publishers and Exclusive Agents; Book publishers and exclusive agents (data tables)*. [Ottawa] November 2003.

¹⁷ BDO Dunwoody. “2003 British Columbia Budget Report.” February 18, 2003. <http://www.bdo.ca/en/library/publications/taxpub/budgetreports/bcfeb03.cfm>

expenditures in the country, the highest percentage of book readers in Canada, and a wealth of inspiration, talented writers, and scholars.¹⁸

Also key to B.C. publishers' success is a robust independent book trade. In 1995, Vancouver had 166 book retailers (21 Coles and SmithBooks locations and 145 other book retailers, including used book stores); it was the only major metropolitan market studied in the Evans & Company report for the ACP to grow between 1995 and 1999, adding another 12 retailers to the market (three of which were Chapters locations; four Coles/SmithBooks locations were closed but seven superstores were opened). Vancouverites were also the most likely to shop at independent bookstores, with esteemed retailer Duthie Books garnering 16.5% of the market, and Book Warehouse, 15.5%.¹⁹

Talonbooks

Vancouver-based independent literary press Talonbooks (legally Talon Books Ltd., and also known as Talon) was founded in 1963 as a high school poetry magazine and in 1967—five years prior to the publication *Survival*—Talonbooks published its first titles.²⁰ Now presided over by owner and publisher Karl Siegler and his partner, Christy Siegler, Talon's publishing program includes literary fiction, poetry, and drama, as well as non-fiction that focuses on social and literary criticism and ethnography. Many outstanding and renowned Canadian writers have been published by Talon, including Bill Bissett, Robin Blaser, George Bowering, Sally Clark, Frank Davey, Timothy Findley, David French, David McFadden, Daphne Marlatt, Mavor Moore, John Murrell, bpNichol, Howard O'Hagan, Morris Panych, Rick Salutin, Audrey Thomas, Jane Rule, George

¹⁸ Evans & Company Retail Consultants Inc. *Retail Market Study: A Review of the Canadian Book Industry*. Prepared for the Association of Canadian Publishers, February 2001, p. 23.

Fredeman, Jane. "Book Publishing in British Columbia, 1990: More Than a Regional Enterprise," *Journal of Canadian Studies*, Vol. 25, no. 3 (1990): pp. 124-130.

¹⁹ Evans & Company Retail Consultants Inc. *Retail Market Study: A Review of the Canadian Book Industry*. Prepared for the Association of Canadian Publishers, February 2001, p. 30.

²⁰ For an extensive history of Talonbooks from its beginning to 1991 see Michael Hayward's "Talonbooks: Publishing from the Margins" online at <<http://www.harbour.sfu.ca/~hayward/talon>>. Talonbooks' history is also archived at the Simon Fraser University Library.

Ryga, George F. Walker, and Phyllis Webb. Talonbooks is the pre-eminent publisher of Quebec literature in translation, with works from Michel Marc Bouchard, Marie-Claire Blais, Daniel Danis, Michèle Mailhot, Jovette Marchessault, and Michel Tremblay. The press has been the authority in Canadian drama since the first ever Canadian-authored drama title published in Canada, Beverley Simons' *Crabdance*, which was followed by James Rainey's *Colours in the Dark* in 1969 and George Ryga's *The Ecstasy of Rita Joe in 1970*. All three titles remain in print on Talon's backlist; *Crabdance* has been reissued as a new format reprint and Ryga's play is the second-best selling book in Talonbooks' history and the fourth most popular title sold in 2000. In August 1984, Talonbooks canonized the Canadian drama titles they had become known for—a genre they had almost single-handedly created—with *Modern Canadian Plays: Volume 1*. Together with *Modern Canadian Plays: Volume 2* (which first appeared in 1994), these drama anthologies have sold over sixteen thousand copies and are now recognized as “the primary textbook in Canadian theatre and literature courses around the world”²¹ and are now being published in their fourth editions. Talonbooks has also published significant non-fiction titles, ranging from literary criticism to international politics, First Nations' issues, and the environment, largely due to the interests and expertise of the publisher. Talonbooks has refined its editorial focus, remaindered popular cookbooks and commercial titles published in the eighties (despite their success), moved away from mainstream titles, and returned to publishing fine, intellectual Canadian literature and socially significant, often politically-charged non-fiction. By 1994 Talonbooks had over 160 titles on its backlist, including major award winners and internationally recognized authors, and was publishing an average of fourteen new titles a year. In 1996, venerable publisher Coach House Press closed its doors and Talonbooks purchased 21 of its literary titles, including the works of renowned playwright George F. Walker. With over 120 authors in print and a backlist of over 300 titles, Talonbooks is now the “largest independent and exclusively literary press in Canada,” according to Siegler. But even with its solid editorial niche, enviable backlist,

²¹ A review of Jerry Wasserman, *Modern Canadian Plays, Volume I*, in *The Ottawa X-Press*, as cited in Talonbooks' fall 2001 catalogue.

and its pre-eminent position in the Canadian literary marketplace, Talonbooks' survival is continually at risk.

Throughout the history of publishing in B.C., publishers like Talonbooks have faced and surmounted numerous and persistent challenges to create a culturally significant, economically viable, regionally diverse industry that has become the map and geography of the mind for British Columbians. Its sustainability remains perilously balanced on a thriving independent book trade, loyal readership and authors, culturally protectionist legislation, and continued local, provincial, and federal support. In recognition of this precarious composure, the restructuring of the bookselling industry—the creation of superstore bookstore chains Chapters and Indigo, their subsequent merger, and the parallel decline of the independent bookstore—is an area of heightened importance to the publishing industry in B.C. This enquiry begins with the merging of three bookstore chains (Coles, SmithBooks, and The Book Company) to form the Chapters phenomenon. The period of enquiry ends with the newly merged Chapters/Indigo superstore mega-chain. The aim of this project is to document the events from 1995 to 2001 as they related to B.C.-based publishers; specifically, how Talonbooks—and, to a lesser extent (largely for comparative purposes), New Star Books—weathered the radical and sudden changes in the marketplace. This case study highlights the superstore effect on B.C.'s pre-eminent literary publisher, and on its survival.

1995: THE EMERGENCE OF THE SUPERSTORE

In the early nineties, consumer debt rose to staggering heights, the Canadian dollar plummeted, leisure hours shortened, and Canadians were deep into a recession, but the mood in the book industry—particularly in retail—was one of optimism.²² The B.C. book retail market, in particular, was booming. Music retailer A&B Sound began carrying books at its downtown Vancouver location in the spring of 1995 and in its Victoria location in the fall. Zebra Books opened its doors in Yaletown, while Blackberry Books closed its West 4th Avenue location (leaving its flagship Granville Island store and a store in Kitsilano) after Duthie Books opened a new 3,200-square-foot location across the street in October of 1993. September saw Black Sheep Books open in Vancouver, followed by a new Simon Fraser University Bookstore at the downtown Harbour Centre campus in December. The overall growth in book retailing is reflected in *Quill & Quire's* annual “Retail Roundup,” which found “shutdowns outnumbered by start-ups offering coffee, couches....”²³ The book trade was also exceptionally positive toward opportunities to expand markets and new technologies. Vancouver’s Duthie Books—at its peak, a vibrant chain of ten stores—launched a virtual bookstore on the burgeoning World Wide Web. Though not yet enabled for electronic commerce, the site allowed book lovers to browse the store shelves virtually. Enabled by new technologies to keep substantial database files, the Canadian book trade launched into customer loyalty programs.

The Coles/SmithBooks Merger

The mid-nineties also marked the beginning of the superstore phenomenon in Canada, which started with the expansion of the Renaud-Bray chain outside of Montreal and the announcement of Bolum Books, a 23,000-square-foot store in downtown Vancouver. In May 1994, Pathfinder Capital, created by Lawrence (Larry) Stevenson in 1993, and

22 Statistics Canada. 2001 d. *Income Trends in Canada, 1980-1998*. Ottawa: Statistics Canada (Catalogue No. 13F0022XCB).

23 “Retail Roundup.” *Quill & Quire*. Vol. 64, no. 1 (January 1995), pp. 8-9.

Canadian General Capital (CGC) purchased SmithBooks' 253-store chain for \$21.5 million. In August, Pathfinder Capital and CGC proposed buying the 181-store Coles chain, owned by Federal Industries and presided over by Tom Bryden. The purchase and merger would create a 434-store chain under the leadership of Larry Stevenson, who, while the proposal was under review by the Bureau of Competition Policy, maintained, "two Canadian chains would not have been able to survive in this competitive marketplace."²⁴ Many publishers objected to the merger and relayed *their* concerns about the impact of a monster chain and superstores, and their worries about how a dominant player might leverage co-op dollars and extended payment terms. Siegler, publisher and owner of Talonbooks, was adamantly opposed to the merger, and argued that Larry Stevenson's "straw man of a threat of a possible simultaneous bankruptcy of both Coles and SmithBooks" was highly unlikely and that a laissez-faire approach would have "allowed the industry as a whole to carry out the 'necessary rationalization' of the chain business by reducing the number of chain stores... but it also would have strengthened, not weakened the independents."²⁵ Rolf Maurer of New Star Books was more optimistic: "One of the implicit criticisms that Stevenson was making in creating the merger and announcing these new stores called Chapters was that, at that point, the Canadian consumer was underserved by the book trade. There were not a lot of good book stores, though some cities were better served than others. Ironically, the best bookstore in the country at the time was World's Biggest in Toronto, and the second biggest was Coles on St. Catherine's in Montreal. So when Stevenson came along and said, 'Canada needs big-box book stores,' I agreed with him, and I was hopeful that that would be what we would be getting."²⁶ As the events of the next five years would show, Chapters did not fully disclose its strategy for dominating the book trade in Canada. Had the company revealed

²⁴ Lorinc, John. "One Big Bookseiler: 434-store strong Smith-Coles faces competition review." *Quill & Quire*. Vol. 60, no. 10 (October 1994), p. 4.

²⁵ Siegler, Karl. Re: "Draft Consent Order" of April 18, 2001, in the matter of Chapters/Indigo/Trilogy, filed with your Tribunal on that date by the Commissioner of Competition [letter]. May 8, 2001. Filed as article 17a by the Registrar of the Competition Tribunal, Ottawa. (The collected documents of the Tribunal are available online at: www.ct-tc.gc.ca/english/cases/ct-2001-003/trilogy.html)

²⁶ Interview with Rolf Maurer, August 2004.

its strategic plans (or even the possibility) of creating a wholesale/distribution division, expanding beyond bricks-and-mortar locations, or entering the post-secondary book retail market, the BCP may have ruled against the merger. However, Stevenson successfully lobbied on the fanciful platform that the merged entity presented no threat to the Canadian book trade, and, as a minority player, the company would resurrect two doomed chains and grow the market for everyone. The BCP rejected the doomsday prophecies of independent bookstores and publishers and approved the merger in the spring of 1995; the official acquisition took place April 15. The new, merged chain, which encompassed the Book Company, Chapters, Classic Books, Coles, Librarie Smith, SmithBooks, and the World's Biggest Bookstore brands, was renamed Chapters Inc. Stevenson named himself CEO and appointed former Ontario premier David Peterson (and brother of Federal Liberal Secretary of State Jim Peterson) to the post of chairman of the board, and the company immediately quit the Canadian Booksellers Association.

In November, Chapters opened its first superstore, a 20,000-square-foot giant in Burlington, Ontario, which was soon followed by Chapters Metrotown (Burnaby, B.C.) and plans to roll out 50 more stores. CBA executive director John Finlay prophesized “the independents cannot look at doing business the same way they’ve always done it.... And certainly there will be some that will not survive.”²⁷ As they prepared themselves for the challenge of a power player in book retailing, most independent bookstores expressed confidence that Canadian readers would discern the difference between their expertise, special orders, and service record and Chapters’ American big box retail concept. Shortly after the unveiling of the first superstores, independent bookstores began to shift their strategies. Bollum’s, for example, began discounting hardcover best sellers by 20%, while Duthie’s offered 20% off an entire category of books each month (such as cookbooks or travel). All the time bookstores were jockeying for position, they continued to make confident buys for fall 1995, albeit with a closer eye to those books which distinguished

²⁷ Bert Archer. “Waiting for the Wave: Independent bookstores brace for the beginning of the superstore era.” *Quill & Quire*. Vol. 61, no. 12 (December 1995), p. 9.

them from their superstore neighbours. These events occurred against a bleak retail outlook: between 1989 and 1996, demand in Canadian retail (measured in after-tax disposable income) dropped 11%, while supply (measured in retail square footage) increased by 40%.²⁸

The optimism of the independent book trade in the West slipped as the year ended, with key independent trade accounts closing their doors as “aggressive book discounting by Price Club/Costco and Wal-Mart” and “the struggle with the chains for business in the busy Christmas season”²⁹ put the squeeze on small stores. In Toronto, independents were meeting the challenge head-on. Mini-chain Lichtman’s News and Books “expanded one of its branches and experiment[ed] with new initiatives to maintain and improve its customer base;”³⁰ Books for Business did the same. However courageous or noble the independent book retailers’ struggle, Chapters’ comprehensive, sophisticated, and well-capitalized strategy had only begun to unfold. With both the independent and chain bookstore sales growing and the book retail industry poised for expansion, the question was how many more books are Canadians going to buy, and from whom?

Talonbooks’ Distribution and Sales Representation Shift

As Karl Siegler states:

In 1991-92, as president of the ACP, Talon CEO [I] had negotiated the return of the former DoC’s, (now the DCH’s) sales-based funding program for Canadian-owned publishers, the BPIDP, at a much more substantially funded level than had previously been the case between 1980 and 1991, (a level of funding that the Federal government had warranted to the industry would stay in place for the BPIDP’s next five-year term, 1992

²⁸ Stevenson, Lawrence N., Joseph C. Shlesinger and Michael R. Pearce. *Power Retail: winning strategies from Chapters and other leading retailers in Canada*. McGraw-Hill Ryerson, Toronto: 1999, p. 8. [using figures from Statistics Canada’s Centre for the Study of Commercial Activity (CSCA)].

²⁹ Allentuck, Andrew, et al. “On the Block: Stores being sold, closed predominate in this month’s retail roundup.” *Quill & Quire*. Vol. 62, no. 1 (January 1996), p. 11.

³⁰ *Ibid.*

through 1996), along with a parallel DCH-guaranteed loan program called the “Cultural Industries Development Fund” (CIDF) administered by the FBDB (now the BDC). Talon saw these two interrelated Federal support programs as an opportunity to finally shed what it felt was its unjustified “regional” and “academic” reputation and to attain its true stature as a “national player” in the Canadian book trade. [I] quickly calculated the degree of annual increased profitability the newly re-financed BPIDP would deliver to Talon over the five-year period of its commitment to Canadian-owned publishers, totalled it up and borrowed that sum (\$96,000.00) in two instalments from the CIDF, based on a business plan that would see Talon acquire commissioned trade sales representation from a national sales organization (rather than through the patchwork of independent representatives it had been using since the 1970s), increase its marketing efforts and expenditures across the country and especially in central Canada, and to add a number of more “trade-oriented” titles (topical and hardcover “coffee-table” books) to its list of 10 to 12 more “difficult” (in trade marketing terms) titles annually.

Based on this new, aggressive, more trade-oriented business plan, Talonbooks was riding a wave of success in its 1992 fiscal/calendar year, ironically with a huge regional full-colour hardcover bestseller, *Vancouver a Visual History* on its list, and its new-found national profile on its hands....

In June of 1992... [Talon] bought [“silent partner” David] Robinson out, and gave Robinson’s 50% share in Talon to Christy Siegler, who had been working with him as a full-time employee since 1986. Already stretched to the limit of operating capital borrowing from the CIDF, however, Talon had to borrow the \$50,000 to buy out David Robinson from private sources, eventually increasing the company’s total long-term debt burden to \$146,000.³¹

In October 1993, Talonbooks published *They Write Their Dreams on the Rock Forever: Rock Writings in the Stein River Valley of British Columbia* by ’Nlaka’pamux elder Annie York, Richard Daly, and Chris Arnett. The regional non-fiction title was published at the height of both national and international environmental protests against logging in the Stein Valley, and contributed to the establishment of the Stein Valley as a protected

³¹ Karl Siegler, editorial addendum to this report, September 2006. [In the editorial addendum text excluded by the ellipses, Karl Siegler referred to David Robinson as his “silent partner.”]

wilderness area by publicizing the cultural and ecological plight of the Stein. The cloth-bound book with red-ochre drawings and black & white and colour photos retailed at \$34.95 and sold over 1,600 copies within a year. Repositioned with an ambitious publishing program, Talonbooks published an impressive fifteen new titles in 1994—including Bryden MacDonald’s Governor General’s Award Winner for Drama *Whale Riding Weather*, John Gray’s popular *Lost in America: The Imaginary Canadian in the American Dream*, and a new edition of Talonbooks’ perennial best-seller *Forever Yours, Marie-Lou* by Michel Tremblay. As an extraordinary testament to the quality of the Talonbooks list, fully one-third, or five of the 15 eligible titles from Talonbooks’ list were nominated for Governor General’s Awards in 1994.

Newly represented in 1993 by the Vancouver-based but nationally active commissioned sales representatives Kate Walker & Co., Talon’s total net sales dropped precipitously to \$363,387 in that year—a 15.5% decline from the \$430,317 it had achieved with its old patchwork of commissioned sales reps across the country in 1992. Clearly, something about Talon’s business plan was not working, and relations between Talon and Kate Walker & Co. became strained. On January 1, 1994, Talonbooks had made a strategic move and began a distribution arrangement with GDS. “While [our] former distributor, UTP had a reputation as a good, reliable supplier to the academic and institutional markets in Canada, its service to the retail book trade was somewhat wanting.”³² Talonbooks had initiated this move months beforehand, in consultation with and on the advice of Kate Walker & Co., in an effort to align themselves with a more commercial distributor so as to get a bigger bite out of the retail market, a strategy that failed to have any immediate impact on Talon’s trade sales. Even with a change of Talon’s distributor from UTP to the more trade-oriented GDS, and Talon’s hiring, for the first time in its history, of a sales manager for three months in the crucial fall season, total net sales for the year only managed to grow negligibly to \$367,571, a mere 1.1% over its 1993 results. One year later, and on much shorter notice to Kate Walker & Co.,

³² Karl Siegler, editorial addendum to this report, September 2006.

which, as its national sales force for the years 1993 and 1994 had failed to maintain, much less improve on Talonbooks' largely "self-generated" trade sales success of 1992, Talonbooks changed both its list and its commissioned sales force, turning to the Literary Press Group (LPG) for sales representation, starting on January 1, 1995. Talonbooks was already a member of the LPG, a co-operative project of Canadian owned and operated literary book publishers as well as an advocacy group, but had not previously engaged the LPG's trade sales representatives. But in December 1994, at its sales conference for the spring season of 1995, Talonbooks presented only four new titles to its new sales representatives at the LPG—and only one title, *Too Good to be True*, was to make it to press that season.

Canadian-Owned Publishers Destabilized

Early in 1995, the pendulum had begun to swing within the publishing industry, signalling a widespread shift in the industry's previously optimistic mood. On February 27, 1995, utterly without warning, Finance Minister Paul Martin unveiled the new Liberal federal budget, which unexpectedly slashed funding to publishers. The Book Publishing Industry Development Program (BPIDP) was lopped off at \$16.3 million, 33.5% less than the \$24.5 million disbursed in the previous fiscal year. The fledgling Publications Distribution Assistance Program (PDAP), begun in June 1993 to replace the "book rate" postal subsidy, had its funding decreased by more than 70%, from \$20.7 million to just \$6 million. The Canada Council, directed by writer Roch Carrier from 1994–1997, had its overall budget depleted by \$1.9 million. The total and instantaneous loss to publishers amounted to over \$23 million dollars.³³ While there were clear economic indicators that the Canadian economy was faltering and budget restraints were inevitable the extent of the cuts to publishing shocked most publishers and threw them into turmoil. "Paul Martin had promised Canadian taxpayers cuts to 'grants to industry' of 65% over two years, The reason the Liberal cuts came as such a surprise to Canadian

³³ Archer, Bert. "Meaner, Leaner Times: The feds take a big bite from book industry grants; publishers cry foul, calling budget 'death knell' for Canadian firms." *Quill & Quire*. Vol. 61, no. 4 (April 1995), p. 4.

publishers is that in order to capture grants to publishers with his promise to taxpayers of cuts to ‘grants to industry,’ Martin had re-classified ‘publishing’ from a cultural activity to an industrial activity without ever consulting publishers and/or their professional associations before doing so.”³⁴

The expectation of certain annual Federal funding levels (the Department of Canadian Heritage had after all, in 1992, committed to a five-year cultural funding program) and the relative commercial success of their previous three years had encouraged most publishers to commit themselves and their resources to ambitious publishing plans, as well as increased future and ongoing projects and new author development. Now, many companies were forced to overhaul their lists and lay off staff in order to remain in business. Already working with reduced cash flow because of the failure of its business plan to produce its anticipated sales increases, with these grant cuts, Talonbooks lost 55% of the grant monies for which they expected to be eligible in 1995.³⁵ The company underwent a dramatic restructuring in order to remain solvent: half of Talonbooks’ (already inadequate) four person staff was laid off, leaving only Karl and Christy Siegler; the company vacated the small office space and mini-warehouse they occupied on Cordova Street and moved into a cavernous, windowless office inside GDS’s western warehouse; all publishing activities to pre-press were moved in-house; and the planned 1995 list was reduced to an exclusively literary selection of just seven titles, only one of which was published that spring. Talonbooks did manage to secure \$15,000 in emergency funding from the Canada Council, but with the caveat that the Block Grant committee would determine if the funds were a loan to be repaid in their future assessments. As it turned out, Talon had to repay this amount by having \$3,000 deducted from its Canada Council grants over the next five years.

Most publishers cut their lists in the fall of 1995 and spring of 1996, publishing “fewer new writers, fewer reference books, and a lot less drama and poetry... in an effort

³⁴ Karl Siegler, editorial addendum to this report, September 2006.

³⁵ Based on Siegler’s calculations using the previous year’s funding levels.

to keep up with the deep reductions in federal and provincial grant money.”³⁶ But for fall 1995 Talonbooks published exclusively drama and poetry, including poetry titles *Aurora* by Sharon Thesen, Bill Bissett’s *th influenza uv logik*, David McFadden’s *There’ll Be Another*, and *Cartouches* by Lola Lemire Tostevin, and drama titles *The Weekend Healer* by Bryden MacDonald, and a revised edition of *Canadian Drama and the Critics*, edited by L.W. Connolly.³⁷ March 1996 saw the implementation of the second phase of the budget cuts announced in February 1995. Though several titles were announced for spring of 1996, Talonbooks did not manage to get any new books to press that season.

Talonbooks’ Trade Sales by Category

The cuts to Talonbooks’ federal grants (which resulted in fewer new titles for 1995–1996) dealt a devastating blow to the company’s 1995–1996 revenues: net sales to the independent book trade in Canada plummeted in 1995 by 47.7%, (in direct proportion to Talon’s cut in new title output of 46.7% in that year) while Talonbooks’ total net retail trade sales for the 1995 fiscal year were a crushing 57% lower, according to Karl Siegler, “primarily due to an 86.3% decline in net sales to the newly merged chains. Net sales to chain stores (Chapters) declined far more precipitously in 1995 than those to the independents, not only because Talon had published significantly fewer frontlist titles (the chains—first Coles and SmithBooks, then Chapters—have not traditionally ordered much backlist, either from Talonbooks or from anyone else) but primarily because Talon had made the explicit decision, particularly after its disastrous flirtation with ‘going more commercial’ with its marketing infrastructure and title selection in 1993 and 1994, to ‘return to its roots’ and publish only literary titles, and specifically not the kinds of populist titles that are most suited to chain store sales.”³⁸

Talonbooks’ post-secondary sales were somewhat insulated from the effects of its

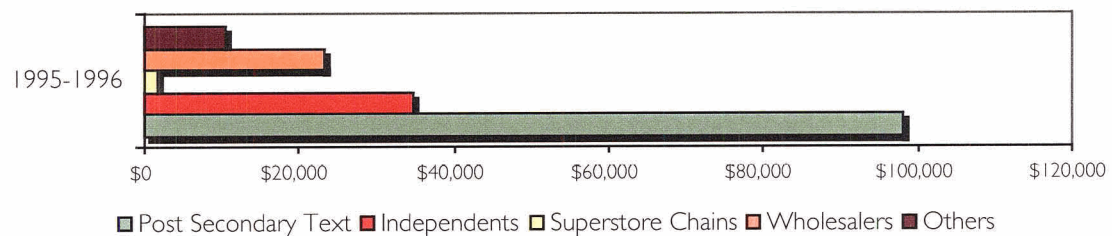
³⁶ Elashi, Anita “Grant-slashing Reshapes Lists: Belles lettres vs. bottom line? No contest.” *Quill & Quire*. Vol. 62, no. 1 (January 1996), p. 10.

³⁷ Lead title and non-fiction/social issues title *Bleeding to Death* by Jill van Dijk was cancelled.

³⁸ Karl Siegler, editorial addendum to this report, September 2006.

drastically reduced 1995 frontlist. Post-secondary course adoption is nearly entirely responsible for the sale of Talonbooks' backlist titles. This is consistent for literary publishers, as academia traditionally mines backlists for Canadian classics, established writers, and Canadian literary history. Instructors also need time to prepare course materials before introducing a new title to the curriculum. Thankfully, Talonbooks' academic clients seemed to have no problems making the shift to the new distributor either, as post-secondary sales increased by 8.9% in 1995. Gross sales to post secondary institutions were \$139,103, representing 58.8% of total gross sales, a larger percentage of Talonbooks' revenue than any years previous or immediately following. Returns in post-secondary sales in 1995–1996 were \$40,849—or 29.7% of post-secondary sales (about average for the period of study). Thus net Canadian post-secondary sales for the period were \$98,254 (or 58.3% of total net sales), more than two times higher than sales to independents and chains combined, and a higher percentage of total sales than in any year to date.

Figure 1. Talonbooks' Canadian Net Sales by Category, 1995–1996



Commissionable Versus Non-Commissionable Sales

Another way to analyse sales effects is by comparing commissionable sales, or those sales that are attributed to the efforts of the sales force, which includes all sales to independent bookstores, superstore chains, wholesalers, retailers carrying books, and miscellaneous trade, with non-commissionable sales, which includes most post-secondary textbook sales, direct library sales, and special sales (including individuals and mail order, ELHI, and corporate sales), as the sales representatives do not actively solicit these markets. Commissionable sales represent, on average, 47% of Talonbooks' net sales.

As table 2 demonstrates, Talonbooks' non-commissionable net sales remain fairly consistent (varying, at most, by 25% over the period of study), while commissionable sales vary more widely and by as much as 60%: the variance in commissionable sales for 1995–1996 and 1999–2000 is nearly \$100,000. It is understandable there would be a decrease in sales following Talonbooks' "reduction of both annual new title output and its adamant decision to publish only titles of the highest literary value, making no concession whatsoever to the Chain's ever increasing demand for more populist titles, to the extent that in 1999, Talon even remaindered its still popular cookbooks in order to more clearly define its exclusively literary market niche in the new millennium, increasingly important in its new active website positioning and marketing initiatives."³⁹ Talonbooks would not achieve the same level of commissionable sales as with Kate Walker & Co. in 1993–1994 until 1999–2000, only to see sales levels drop again dramatically in 2000–2001.

Table 1: Trade Sales by Sales Representation

Sales Representation	Fiscal Year	Commission-able Sales	Non-Com/ales	Commission-able Sales (as percentage of total sales)	New titles published ⁴⁰	New sales per new title ⁴¹
Kate Walker & Co	1993/1994 (averaged)	\$148,755			15.5	\$9,597
LPG	1995–1996	\$62,995	\$105,583	37.4%	9.5	\$6,631
LPG	1996–1997	\$94,636	\$124,632	43.2%	11.5	\$8,229
LPG	1997–1998	\$113,486	\$124,482	47.7%	15.5	\$7,322
LPG	1998–1999	\$129,093	\$118,539	52.1%	20.0	\$6,455
LPG	1999–2000	\$162,275	\$140,271	53.6%	18.5	\$8,772
LPG	2000–2001	\$101,669	\$135,388	42.9%	15.5	\$6,559
Average for the period of study (1995–2001)		\$110,692	\$124,816	47%		

With respect to the table above, Karl Siegler comments:

³⁹ Karl Siegler, editorial addendum to this report, September 2006.

⁴⁰ Karl Siegler, editorial addendum to this report, September 2006.

⁴¹ Karl Siegler, editorial addendum to this report, September 2006.

As can be clearly seen on Table 1, Talonbooks' commissionable trade sales per new title published were significantly different only between the years 1993/1994 [\$9,597], when the company was actively courting more commercial titles and markets (publishing more populist books specifically designed for the Chain store market), and 1995/1996, when Talon abandoned that kind of commercial title, the sales force and the type of retail outlet associated with it, and returned to its literary roots and a sales force more suited to its original mandate—that of the LPG—[\$6,631].

Even the anomalous periods of *apparent* increase in dollars per new Talon titles published, 1996-1997 and 1997-1998 can be explained by the fact that the dire predictions concerning the harm Paul Martin's grant cutbacks of 1995 would visit on the Canadian-owned publishing industry were correct. Coach House Press fell victim to those cutbacks, closing its doors in 1996 and offering its entire catalogue to remainder houses and recyclers, while other publishers sought to trim their lists of what they considered to be unprofitable titles in similar fashion. Talon was therefore able to initially acquire 17 literary titles from the Coach House Press list and later four more, in addition to one from Blizzard Publishing and one from Playwrights Canada Press, by paying these publishers \$1.00 per unit of their inventory of these titles, plus GST, and to begin selling them in the Talon catalogue, not as "new titles published" by Talon, but as "titles new to Talonbooks." Most of these titles were acquired in 1997, the balance in 1998, representing "new product for sale from Talon," and therefore invisibly "inflating" Talon's "sales per new Talon title(s) published" in both 1997 and 1998. By 1998/1999, after this period of "new product acquisition" from its competitors, Talon's net sales per own new title published returned to 1995/1996 levels, [\$6,455].

In addition, the anomalous period of Talon's apparently much improved net sales per new title published, 1999/2000 [\$8,772] (the very year that Larry Stevenson was improving his share values in preparation of the "hostile" takeover of Chapters by Indigo, returning books to publishers like they were literally going out of style), can easily be explained by the fact that Talon's *net* sales during this period were significantly overstated. Its distributor GDS, facing bankruptcy, artificially overstated its sales statistics (and those of its clients) during these two years by ignoring and refusing to process returns from Canadian booksellers, especially from the chains, by the semi-trailer-load. Proof of GDS's failed attempts at manipulating its sales statistics can be found in the fact that *alleged returns of Talon titles during this period were apparently only 24.1%*, but in the year before this period, 1997, they were 29.0%, and in the year following this period, 2001, they were 36.5%. By 2000/2001, Talonbooks' net sales per own new titles published had returned to a level "normal" for purely literary titles [\$6,559], almost identical to the figure at the beginning of this period, 1995/1996 [\$6,631]. It is immediately after this period, on January 1, 2002, that Talon left GDS just prior to its bankruptcy, and returned to

UTP as its North American distributor.

It is perfectly clear from the data displayed on Table 1 that Talon's commissionable sales over this historical period had everything to do with the number and type of new titles Talon was publishing annually, and almost nothing to do with changes to Talon's distribution, sales and marketing infrastructure in the years covered by the Table.⁴²

Left to explain are the reasons Talonbooks took such a relatively long time to recover and rebuild from the Federal grant cutbacks of 1995.

I expected regional distribution to alter because of the shift from Kate Walker & Co. to the LPG, as Kate Walker & Co. were based in B.C., and, in 1993/1994, representing notable B.C. publishers Douglas & McIntyre, Raincoast Books, and Harbour Publishing, and with a greater presence of sales representatives in B.C. than any other province, while the LPG represented publishers nation-wide, and with a sales force distributed representatively across the country. But the sales distribution of the titles sold by the LPG by region is fairly consistent with its predecessor; the decrease in Talon's sales was not due to regional factors. Academic sales show that the impact of moving distributors from UTP to GDS in 1994 was also likely negligible. Thus the 1995 reduction in federal grants and Talon's resulting commensurate decrease in frontlist title publication coupled with a change in the type of title published are the likeliest reasons for this dramatic decline in its net sales in 1995/1996.

Table 2: Trade Sales by Region

	B.C.	Alberta	Man/Sask	Ontario	Quebec	Atlantic
Kate Walker & Co. 1993–1994	41.9%	6.1%	4.4%	39.9%	6.0%	1.7%
LPG 1995	44.3%	2.4%	2.5%	43.9%	5.8%	1.2%
Variance	+2.4%	-3.7%	-1.9%	+4%	-0.2%	-0.5%

⁴² Karl Siegler, editorial addendum to this report, September 2006.

Siegler calculated that “in 1993–1994, about 230 titles in our backlist generated commissionable sales of \$63,997.88” and “publishing 14 frontlist titles annually, our frontlist sales were \$84,757.12.”⁴³ Thus of total averaged sales (\$148,755) for 1993 and 1994, 57% of commissionable sales came from the frontlist. If, for the sake of argument, this percentage represented the average contribution of the frontlist to commissionable sales, then with half as many titles in 1995—all other things being equal—Talonbooks could have foreseen a drop in commissionable sales for 1995–1996 to \$106,367 (approximately \$63,998 in backlist sales plus \$42,378 in frontlist sales) and for commissionable sales to have rebounded slightly in 1996–1997 (as Talonbooks published 11 titles in the fall, though none in the spring) to \$130,592. While speculative, these figures give a sense of how the federal grant cuts and the resulting decrease in title production affected sales. The same formula applied to total net sales would have forecast a minimum overall loss of 13.4% (if commissionable sales, on average, represent 47% of sales and the vast majority of non-commissionable sales are backlist titles). However, commissionable sales for 1995–1996 were \$62,995 (41% lower than what might have been projected) and \$94,636 (27.5% lower) in 1996–1997, implying the change in sales force might have been more costly than anticipated. Karl Siegler opposes this analysis, citing the change in types of titles published radically altered Talonbooks’ mix of frontlist and backlist commissionable sales.⁴⁴

Table 3: Canadian Trade Net Sales, 1992–1996

Year (representation)	Total Net Sales	Change
1992	\$430,317	
1993 (Kate Walker & Co.)	\$363,387	-15.6%
1994 (Kate Walker & Co.)	\$367,571	+1.2%
1995–1996 (Literary Press Group)	\$168,558	-54.1%

⁴³ Siegler, Karl. Commissionable Canadian net trade sales plan [photocopied letter]. January 26, 2000. Letter to Literary Press Group Sales Manager Linda Palmer. 1993 and 1994 were averaged to reduce variables. Sales are organized by calendar year in the appendix.

⁴⁴ Karl Siegler, editorial addendum to this report, September 2006.

New Star Books' Experience

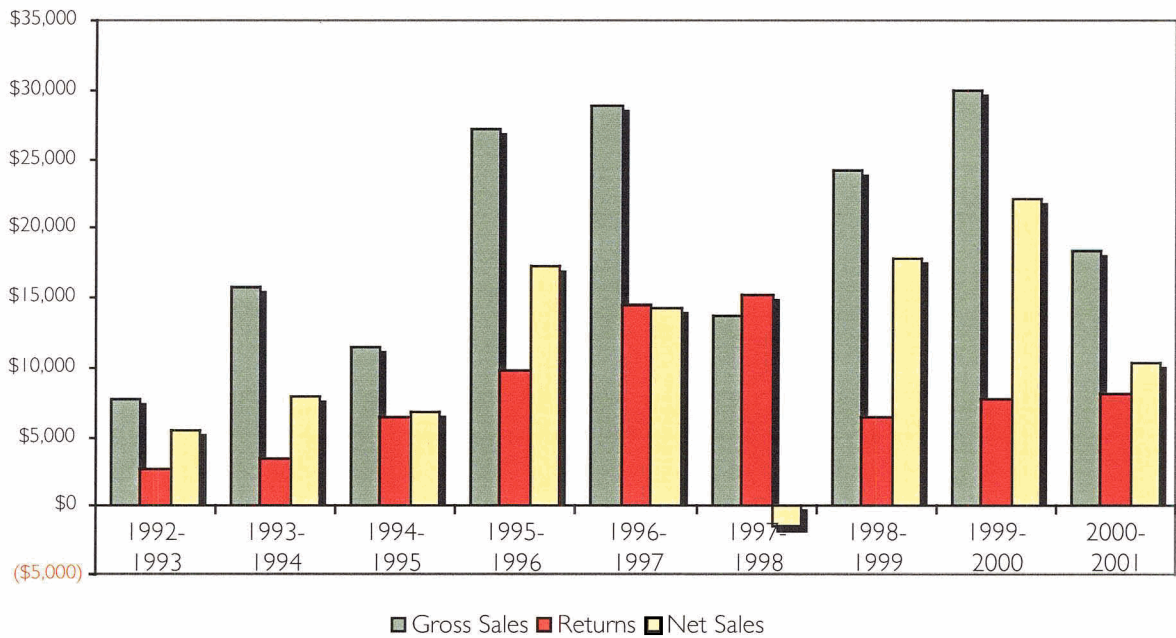
Those publishers who survived and managed to get books to press despite the February 1995 federal grant cuts were able to capitalize on both the increased marketing by independent booksellers and the initial stock purchases of big box retailers. Over the same period of time that Talonbooks saw sales figures drop, Vancouver-based literary press New Star Books experienced a remarkably different effect on sales to trade bookstores. Maurer recollects: "Most of my time and energy at the time of the grant cuts was taken up not wondering about how we would do with the granting agencies, but wondering how we would do in the marketplace given these new changes. By far the biggest issue in the mid-'90s was the creation of Chapters, and in the States the creation of Barnes and Noble, and the fallout that that had on the whole industry."⁴⁵ With New Star Books' focus on the new superstore chains (Coles and SmithBooks until 1995 and Chapters thereafter), their net sales to the chain sector jumped from \$6,839 in 1994–1995 to \$17,288 in 1995–1996, while sales to independents plummeted from \$19,745 in 1993–1994 to \$12,179 in 1994–1995 (a decrease of 38.3%), only to rebound in 1995–1996 to \$27,982 (an increase of 43.5%).⁴⁶ "Initially, Chapters made significant buys of most new books. We would have a typical order of two to four hundred books for a Chapters store, in some cases it was over five hundred," said Maurer. "It should be noted that those kinds of initial orders were not untypical for a new book. We would typically have five hundred to one thousand orders from independents. It's not like all of a sudden we had Costco-type thousands of quantity units ordered, we had modest orders, especially modest when you think of them as replacing the independent orders that we used to have."⁴⁷ New Star Books was also represented by the LPG and distributed by GDS, though it had been a client since 199, a few years longer than Talon.

⁴⁵ Interview with Rolf Maurer, August 2004.

⁴⁶ Maurer, Rolf. Letter of opposition to the Chapters/Indigo Merger [photocopied letter]. March 21, 1996. Private collection. Used with permission of Rolf Maurer, publisher, New Star Books.

⁴⁷ Interview with Rolf Maurer, August 2004.

Figure 2. New Star Books' Superstore Gross Sales, Returns, and Net Sales 1992–1993 to 2000–2001



(*2000–2001 figures represent a partial report—eight of twelve months.)

Talonbooks' net sales to Chapters (both superstores and small-format stores) in 1995–1996 appear to have been only \$1,796—only one tenth of their colleague's sales—although sales to independents were on par with previous years. Rather than profit from the growth in chain bookstores and the optimism of the independent bookstores as other publishers experienced, Talonbooks missed the wave (which would turn out to be fortuitous).

“However,” says Siegler, “it must be remembered that Talon's results here (1995-1996) are a combination of relatively high returns from the Chain in this 12 month period, and its publication of practically no titles suitable for chain sales during this precise period. Talon's Chain sales in these years are more realistically calculated (in comparison to those achieved by its colleagues/competitors also distributed by GDS and sold through the LPG sales force) by referring to Talon's fiscal year, which is calendar-based. Thus, while Talon's net Chain sales for its fiscal/calendar 1995 were a mere \$3,081.58, a precipitous decline from the previous year's net Chain sales of \$22,418.07,

by 1996 Talon's net Chain sales were already showing a pattern of recovery, with an increase to \$15,066.78, but this time with a purely literary (and a significantly smaller) list."⁴⁸

⁴⁸ Karl Siegler, editorial addendum to this report, September 2006.

1996: THE SUPERSTORE STRATEGY

Chapters' president Larry Stevenson co-authored *Power Retail: Winning strategies from Chapters and other leading retailers in Canada*, with Joseph Shlesinger (Bain & Company), and Michael Pearce (Richard Ivey School of Business at the University of Western Ontario). The work offers insight into the strategies that guided Chapters' business practices while underscoring some of the flawed concepts and unfulfilled objectives that initiated the chain's eventual demise (and Indigo's successful takeover). There were four guiding principles to Chapters' business development strategy:

- Deliver a customer-driven superior retail value proposition
- Achieve the leadership position in geographic markets, categories, and channels
- Execute better than competitors in the area of people, technology, and costs
- Lead change by continually reinventing the organization.⁴⁹

Chapters' business development strategy presented both opportunities and threats to B.C.'s publishers. The primary marketing concept—the customer-driven superior retail value proposition (RVP)—started with “a huge selection of books, magazines, CD-ROMs, and music. Convenience is offered through the accessible locations, extended hours, and knowledgeable staff. An appealing buyer experience is delivered through numerous events such as book readings and music performances, as well as through the décor and the refreshments of the onsite Starbucks café, which encourages customers to browse the merchandise comfortably in couches or armchairs with a cup of coffee and biscotti at their elbow. Finally, Chapters builds customer loyalty with programs of discounts, rewards, special offers and invitations.”⁵⁰ Chapters did extensive customer

⁴⁹ Stevenson, Lawrence N., Joseph C. Shlesinger and Michael R. Pearce. *Power Retail: winning strategies from Chapters and other leading retailers in Canada*. McGraw-Hill Ryerson, Toronto: 1999, pp. 14-28.

⁵⁰ *Ibid.*, p. 27.

surveys in 1994–1995, using the services of Bain & Company—a retail consultant company and Stevenson’s former employer—to ascertain the importance of convenience, price, service and ambience, and selection to customers of each of the four store types acquired in the Coles and SmithBooks merger: airport/Central Business District stores, mall stores, street-front small stores, and large format stores.⁵¹ For the large-format stores with which Chapters would focus its expansion, convenience was the lowest priority (10% of the points allocated by importance to the customer), preceded by price (20%), service and ambience (25%), and, most-importantly, selection (45%). Chapters further segmented its customer base into boutique buyers, impulse mall shoppers, browsers, and bargain hunters. Coles and SmithBooks dominated the market on impulse mall shoppers—characterized by their desire for convenience and location, and not service-driven—so understandably Chapters did not want to cannibalize their market share by appealing to this market in their expansion plans. In fact, the company planned an extensive “rationalization of the traditional bookstore business.” The bargain hunter—characterized by the importance of price above all—was the smallest and least lucrative of the customer segments. Already served by Wal-Mart, Costco, and others, this group of “very bargain-sensitive shoppers rarely patronized retail bookstores,”⁵² thus was not the target market either. The largest and most profitable audience was the “boutique buyer,” who was driven by ambience/image, selection, and location/service indicators.

The large, lucrative “boutique buyer” group frequented existing Chapters-owned locations less than any other group, thus attracting this market segment to the big-box locations would not significantly cannibalize sales from the mall stores. Sixty percent of this customer group bought from Canada’s existing independent bookstores, while 20% bought from Coles or SmithBooks, and 20% from other outlets. Said Maurer, “Their model was to directly attack the leading independents, often by building places not too far

⁵¹ At the time, Chapters owned two large-format stores, including the flagship Coles store in Toronto and one in Montreal.

⁵² Stevenson, Lawrence N., Joseph C. Shlesinger and Michael R. Pearce. *Power Retail: winning strategies from Chapters and other leading retailers in Canada*. McGraw-Hill Ryerson, Toronto: 1999, p. 54.

from the independents, and by offering, initially, the same thing that the independents had, which was a wide selection and service. They were competing head-to-head with the Duthie Books, the Sandpiper Books, the Mary Scorer-type of independent bookstores—and with great success.”⁵³ Chapters’ extensive surveys and research showed that boutique buyers “preferred smaller stores but we interpreted this to be a desire for superior selection and service.”⁵⁴ *Power Retail* claims that small stores could not “fill the fundamental gap that existed in the book-retail universe,” so Chapters aggressively expanded with large-format stores. In 1998, each Chapters store carried (on average) 105,000 titles, while other large-format stores carried about 72,000 titles.⁵⁵ Small street-front stores obviously carried substantially less: at the time, Rolf Maurer estimated the big-box stores carried 75,000–125,000 titles, with some stores carrying as many as 150,000 titles; independents stocked between 20,000 and 50,000 titles (Duthie’s carried approximately 35,000); and mall stores had between 2,000 and 5,000 titles. In terms of shelf-space, Chapters carried more books per square foot than other stores by steering away from non-book merchandise. This RVP strategy was how Chapters developed its business from the merger of 434 SmithBooks and Coles Bookstores to 77 super stores and 230 mall stores—less stores, but more titles, greater square footage, and a unique selling proposition (USP) to distinguish it from other retailers.⁵⁶

A 1997 survey by Roger Barnes and Rowland Lorimer on book buying habits in Canada revealed that at least 60% of all book-buying decisions were made in-store. The same survey also showed that 34% of literary book purchases were of titles unknown to

⁵³ Interview with Rolf Maurer, August 2004.

⁵⁴ *Ibid.*, p. 53.

⁵⁵ *Ibid.*, p. 86.

⁵⁶ “These figures would seem to lend a great deal of credence to [my] allegation to the Competition Tribunal that Stevenson’s merger of SmithBooks and Coles should never have been approved, “allowing the industry as a whole to carry out the necessary ‘rationalization of the chain business’ by reducing the number of chain stores...also strengthen[ing], not weaken[ing] the independents.” By this time, Stevenson had already closed 204 of those original mall stores (referred to by Chapters as their “traditional stores”), and the 77 superstores that he had started up were competing head to head not with his remaining mall stores, but head to head with the major Canadian independents.” Karl Siegler, editorial addendum to this report, September 2006.

the reader prior to seeing the book in-store.⁵⁷ Thus with independent presses' small marketing budgets, many readers would not have had occasion to see the limited advertising or read a review, particularly with the number of venues for literary book reviews on the decline. Without every title of each publisher's frontlist and backlist stocked in each appropriate book retail outlet at all times, publishers would miss occasions for sales. Chapters could positively influence sales through greater bookstore presence and resulting impulse purchases.

Selling to Chapters

By 1997, Chapters' mandate to provide the largest selection of titles resulted in expanding Talonbooks' and New Star Books' market reach by stocking their titles in more locations than before. Significantly, however, Chapters made no claims about being able to sell more books to Canadians, only to sell books in a different way (through their superstores and online). Says Maurer: "Initially, the Chapters model was to have a serious bookstore set up to have the widest possible selection. The idea was if you walked into a Chapters, they would maximize the chance for you to find something that you wanted and to make sure that they have it in stock. That was the initial promise of the 'big box' model, and it was that particular promise that I thought had possibilities and that I welcomed."⁵⁸ Most small presses have neither the financial ability nor interest to pursue commercial publishing, which can have much higher returns on investment than literary publishing but involves substantial outlays for printing and marketing, thus a higher element of risk. The risk is compounded by the book industry's unique business model, a consignment system developed during the Depression as a means of enabling book retailers to afford stock, which continues to allow retailers to return unsold titles. After seeing the astonishing returns figures from the Chapters small-format stores, most small presses approached sales to the new superstores cautiously. As Scott Anderson, editor of *Quill & Quire*, noted at the time: "chain stores have always elicited mixed feelings from small

⁵⁷ Barnes, Roger and Rowland Lorimer. *Book Purchasing in Canada: 1997 In-Store Survey* (Draft Report). Roger Barnes Market Planning, 1998, p 16.

⁵⁸ Interview with Rolf Maurer, August 2004.

presses. On the one hand, publishers will do almost anything to have their books displayed prominently in stores across the country. On the other hand, they recognize the risk of filling an order that may, in large part, be returned to them unsold... In Canada the problem has not been as severe [as in the U.S.], and may never be, if Chapters continues to order prudently...⁵⁹ Accordingly, neither Talonbooks nor New Star Books increased any of their print runs to serve Chapters, nor did they pressure their sales representatives to “oversell” to Chapters. New Star Books actually decreased many of their print runs: “We changed our print runs, but not specifically to cater to Chapters. It was part of a longer-term trend that had to do with technological change in book production, and a trend in book publishing to print smaller print runs initially, which was financially a bit more feasible than it had been in the ’80s.”⁶⁰

Talonbooks did not see Chapters as an incentive or driver to publishing different kinds of books either. Talonbooks’ fall 1997 catalogue highlights this decision by stating that after the grant cuts Talonbooks began “rededicating ourselves to our literary roots. While most of our colleagues have scrambled to become more ‘commercial,’ we adamantly continued, even sharpened our editorial search for the finest writing in Canada within our community of discourse: the four genres of poetry, fiction, drama and belles lettres, from the anglophone and our many founding nations in translation.”⁶¹ The publisher continued to rely on independent bookstore, including small street-front stores, mini-chains like Duthie’s, and the few large-format independents like Bollum Books, which represented just over 20% of Talonbooks’ net sales, with sales of nearly \$35,000 in 1996–1997. Chapters’ small-format stores represented just 1% of sales, a meagre \$1,796. Though just over \$10,000 worth of books was sold to Chapters’ small-format stores, a whopping 83.5% of that amount was received in returns. Clearly, the impulse mall shoppers Coles and SmithBooks targeted best did not represent Talonbooks’ or New Star Books’ target market. And Talonbooks very rarely sold into stores like Wal-Mart and

⁵⁹ Anderson, Scott. “Small-Press Showcase.” *Quill & Quire*. Vol. 63, no. 2 (February 1997), p. 6.

⁶⁰ Interview with Rolf Maurer, August 2004.

⁶¹ Siegler, Karl and Christy Siegler. “Publishers Message.” *Talonbooks 30th Anniversary Catalogue*. Burnaby: 1997, p. 1.

Costco, nor appealed to bargain hunters with remaindered titles. The threat Chapters represented to Talonbooks was its business development plan, particularly, its marketing strategy focused on raiding customers currently shopping at independent bookstores. Chapters' strategy would test the fabled ability of independents to hand-sell from their expertly selected and small-press friendly inventory—and whether Talonbooks' titles would sell through in the big-box “boutique” marketplace as well as they did with independents.

1997: BIG-BOX RETAILERS RAMP-UP

The second principle in Stevenson's *Power Retail* was to "achieve the leadership position in geographic markets, categories, and channels." By 1997, it was evident to the book industry that Chapters' aim was to "dominate their markets (by) playing number two to no one, and investing to outflank the current or expected future competition."⁶² Compared to its American cousin (and 20% stakeholder) Barnes & Noble,⁶³ Chapters' expansion in Canada was cautious. From the initial merger of Coles and SmithBooks, Chapters created two new large format stores. These first two big-box Chapters superstores opened in 1995, followed by seven more stores in 1996 and Chapters' successful initial public offering. In 1997, Chapters began to ramp up operations, closing more unprofitable mall stores, opening 18 more superstores, and making a bid to enter the campus bookstore arena, beginning with McGill University Bookstore in March of 1998. The slower approach was due to the BCP, which had analyzed consumer prices, market share, and competition prior to approving the merger between Coles and SmithBooks and subjected the merger to a three-year monitoring period wherein Chapters submitted quarterly audits detailing payment terms and discounts, co-op advertising rates, and lease agreement information.

In 1995, the BCP determined Chapters controlled about 40% of retail book sales in Canada and, in 1997, *Quill & Quire* estimated that its market share had remained fairly constant because of Chapters' limited revenue growth.⁶⁴ By 1997, Chapters was posting \$390 million in revenue from 346 stores, with an average of 3,613 square feet per store, thus an average of \$312 in sales per square foot. While revenues for the chain had grown since 1996 by just over \$10 million, and the average store size had grown by 600 square

⁶² Stevenson, Lawrence N., Joseph C. Shlesinger and Michael R. Pearce. *Power Retail: winning strategies from Chapters and other leading retailers in Canada*. McGraw-Hill Ryerson, Toronto: 1999, p. 91

⁶³ Canadian General Capital sold a 20 percent stake in Chapters to Barnes & Noble in 1996. Two Barnes & Noble executives joined Chapters board at that time, while two senior Barnes & Noble managers joined Chapters' management team in 1995.

⁶⁴ Lorinc, John. "Does Chapters wield too much clout? What happens when Ottawa stops monitoring the chain is anyone's guess." *Quill & Quire*. Vol. 63, no. 11 (November 1997), p. 6.

feet, the chain had closed more stores than it had opened, and the revenues per square foot had actually dropped, even with the closure of the least profitable mall stores and the addition of the first big box “Power Retail” locations.⁶⁵ The big box stores had yet to prove themselves capable of generating revenues on par with their size. Yet Chapters’ studies of the marketplace revealed loftier ambitions, claiming: “Canada can support 150 superstores—10% of [a] Wall Street analyst’s prediction for the U.S. saturation point of 1,500 stores.”⁶⁶ In response, Maurer stated, “It is certainly true that there was room for large new bookstores. Indeed, in many Canadian cities the new Chapters was the best bookstore in the community,” but virtually no one outside the Chapters enterprise believed Canada could sustain 150 superstores.⁶⁷ Many, including Maurer, believed Chapters had “failed to account for the geographic and demographic differences between Canada and the U.S.”⁶⁸ The monitoring period was “a chance for independent bookstores to reconsider their own operations... [and] to give some thought about how to market themselves,” said CBA president Richard King at the time of the merger.⁶⁹ As the monitoring period drew to a close, no independent bookstore had made any considerable effort to become a credible threat and, indeed, some independents had already succumbed in the volatile, low-margin trade bookstore market. Publishers reluctantly acclimatized to the new retailer too, including adjusting to heavy returns, longer payment terms, and the repositioning of key accounts. While the market had undergone “a rapid superstore roll out, [1996’s] returns crisis, the demise of a pair of mini-chains [Bollum Books and Edwards Books & Art], the closing of dozens of mall-based chain stores, and a highly successful public offering of Chapters shares,” all the events were the result of

⁶⁵ Chapters Inc. 1999, *Annual Report 1998-1999*, Chapters Inc., Toronto.

⁶⁶ Lorinc, John. “Returns Rising: Books are being sent back at an alarming rate, and everyone’s got a theory as to why.” *Quill & Quire*. Vol. 63, no. 2 (February 1997), p. 6.

⁶⁷ Maurer, Rolf. Letter of opposition to the Chapters/Indigo Merger [photocopied letter]. March 21, 1996. Private collection. Used with permission of Rolf Maurer, publisher, New Star Books.

⁶⁸ Lorinc, John. “Returns Rising: Books are being sent back at an alarming rate, and everyone’s got a theory as to why.” *Quill & Quire*. Vol. 63, no. 2 (February 1997), p. 6.

⁶⁹ Lorinc, John. “Merger to Makeover: With the Smith-Coles deal approved, Larry Stevenson gets down to the nitty-gritty of revolutionizing Canadian bookselling—while a U.S. chain also eyes Canada’s potential.” *Quill & Quire*. Vol. 61, no. 5 (May 1995), p. 5.

varying factors that the BCP did not unequivocally link to Chapters' presence in the marketplace, and the chain effectively skirted trouble during the monitoring period, even after raising co-op rates (the advertising and marketing funds required to participate in joint advertising and marketing activities) and adding more placement fees (for prime location displays, such as in windows, on prominent tables, and next to the point-of-sale). It seemed certain that Chapters would achieve the leadership position it sought unfettered by the BCP or serious competition.

Indigo Books

There was competition on the horizon. Heather Reisman, former Cott Corp. executive and married to Gerry Schwartz—multi-millionaire and CEO of Onex Corp.—and her company, now! industries, had formed Borders Canada with the Second Cup's Michael Bregman, Edwards Books & Art, and, of course, U.S. book retail goliath Borders Inc. Their proposal to enter the Canadian big-box book-retailing ring with Chapters was thwarted by Industry Canada in 1996, with the help of significant lobbying efforts by Chapters CEO Larry Stevenson.⁷⁰ Reisman responded by founding Indigo Books & Music later that year with the help of seven executives headhunted from Chapters.⁷¹ In September 1997, the first Indigo book superstore opened in Burlington, Ontario—home of the first Chapters superstore. Operating with a similar business strategy as Chapters, the first Burlington store offered about 200,000 books in a swanky decorator store by renowned designer Bruce Mau and architecture firm Kuwabara Payne McKenna Blumberg. Its location in the Burlington Power Centre was chosen with the same geographic marketing principles Chapters applied to its roll out.⁷² Aside from contrasting colour schemes—Chapters trademark tomato red versus Indigo's cool blue—the only significant differences apparent to the consumer might be Indigo's pro-CanLit slogans

⁷⁰ Lorinc, John. "Borders Skirmish: Industry rallies against imminent invasion of U.S. superstores." *Quill & Quire*. Vol. 62, no. 1 (January 1996), p. 1.

⁷¹ Lorinc, John. "Reisman to head new superstore chain." *Quill & Quire*. Vol. 62, no.9 (September 1996), p. 7.

⁷² Lorinc, John. "Large-format independents challenge Chapters at its own game: Western retailers rethink everything from location to merchandising in preparing superstore debuts." *Quill & Quire*. Vol. 62, no.10 (October 1996), p. 8.

“The World Needs More Canada” and Indigo’s 15,000 music titles (like Borders outlets in the U.S.). Chapters avoided the highly competitive music market and had previously withdrawn from selling toys, videos, and stationery in its mall stores to “purposefully build upon the company’s category dominance in the selling of books and other related items,”⁷³ such as magazines and proprietary publishing, as part of its second principle—to be the market leader by category. Chapters would soon face stiffer competition in its bid to be the market leader by markets, category and channels: in early 1997, Indigo acquired independent book retailer Printed Passage Books in Kingston, Ontario, and announced plans to open 25 Indigo stores over the following three years.⁷⁴

Chapters’ strategy, and now Indigo’s, to become the book retail market leaders from coast to coast and city to city, presented serious threats to the stability of the book business in Canada, both in book retailing and publishing. With both retailers poised to spend their way to market dominance, publishers were susceptible to increased instability and risk. Further, as a privately held company, Indigo’s strategy was secretive, but Riesman’s partner, Gerry Schwartz, had a well-founded reputation for hostile takeovers followed by the “rationalization” of corporations by breaking them apart and selling their assets off piecemeal. The high-stakes rollouts of both chains were set to proceed in earnest in the fall of 1998.

The First Superstore Returns Crisis

While independent presses welcomed competition to Chapters, the superstores had, up to 1997, undermined publishers’ viability. During 1996’s returns crisis, publishers saw returns climb well beyond the industry standard of 15–20%. Various explanations for the surge in returns were offered, including online bookselling and overly ambitious print runs, but the overwhelming target of criticism in the trade press was the “massive

⁷³ Stevenson, Lawrence N., Joseph C. Shlesinger and Michael R. Pearce. *Power Retail: winning strategies from Chapters and other leading retailers in Canada*. McGraw-Hill Ryerson, Toronto: 1999, p. 108.

⁷⁴ Indigo Books & Music Inc. “About Our Company.” chapters.indigo.ca [online]. [Cited November 12, 2001.] <<http://www.chapters.indigo.ca/article.asp?artcode=chaptersinc&Section=home&Cat=&Lang=en>>

restructuring in book retail: computerized inventory management, the superstore revolution, and new competition from mass merchandisers like Wal-Mart [that had] radically altered the market.”⁷⁵ Some of the biggest publishers reported a returns average of more than 30% over 1995 and 1996, and Craig Laudrum, executive director of the LPG, complained, “The highest returns we’re seeing are from Chapters.”⁷⁶

Such was not the case for Talonbooks: returns dropped across all major categories, from 28.8% of gross sales in 1995–1996, to 22.1% of gross sales in 1996–1997. Returns from Chapters totalled \$6,741 in 1996–1997; not only a drop of \$2,222 (24.8%) over 1995–1996, but, at 21.2% of Chapters’ gross sales, a slightly lower rate of return than that of independent bookstores (21.9%). Talonbooks’ net sales to the chains jumped to \$25,108; still significantly less than sales to independent bookstores, but a whopping 1300% jump over the previous year’s sales to chain stores.

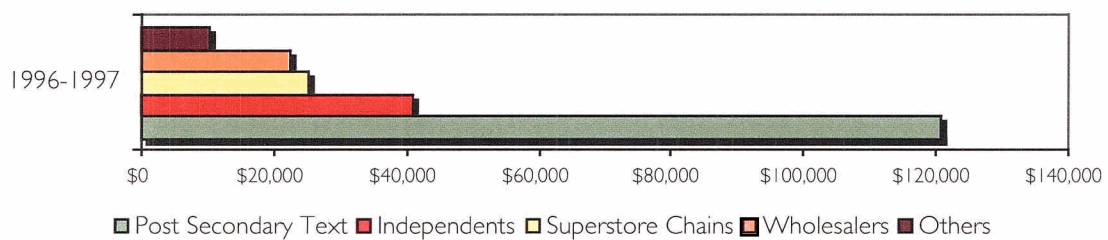
Thirty years after Talonbooks published its first title, the press had not only survived but was thriving, expanding its list aggressively as other publishers struggled. In the spring of 1997, Talonbooks acquired 23 titles from other publishers: 21 from Coach House Press, which had closed its doors the year prior, one from Blizzard Publishing, and one from Playwrights Canada. Two of the titles were revised and reprinted as Talonbooks titles within the year: Joan MacLeod’s *Amigo’s Blue Guitar* and Guillermo Verdecchia’s *Fronteras Americanas*, and a new collection of plays by the newly acquired author, George F. Walker, *Suburban Motel* appeared as his first Talon-published title. Most of these titles Talonbooks acquired from other publishers not only proved to be successful, but also added several significant literary names to Talon’s list, including the current and future works of George F. Walker, Joan MacLeod, and Sharon Thesen. The addition of these titles boosted post-secondary sales for 1996–1997, as some of the titles were on course textbook lists but hadn’t been available for at least a season. Five of the titles immediately

⁷⁵ Lorinc, John. “Returns Rising: Books are being sent back at an alarming rate, and everyone’s got a theory as to why.” *Quill & Quire*. Vol. 63, no. 2 (February 1997), p. 1.

⁷⁶ *Ibid.*, p. 10.

appeared in the top thirty of Talonbooks' 1997 best-selling titles. Post-secondary sales jumped by nearly 23% to \$120,812 for 1996–1997. Independent bookstore sales also rebounded as booksellers bought into Talon's relatively substantial acquisitions of these new titles and authors as well, and as they prepared themselves for the battle with Chapters. Net sales to independents in 1996–1997 reached \$40,723, up 14% over the previous year; net sales to the chains accounted for \$42,511 of sales, up 93% over the previous year.

Figure 3. Talonbooks' Canadian Net Sales by Category, 1996–1997



Talonbooks' gamble on twenty-three acquired literary titles, rededication to its own literary roots, and strategy for dealing with the emerging superstore chain paid off. Growth in post-secondary, independent, and chain bookstore sales restored the company to profitability in 1997. In the fall of 1997, the company produced its thirtieth anniversary catalogue, complete with another ten of its own new titles. Efforts were rewarded by not only an increase in net sales to the trade book retail market but also with a Governor General's Literary Award for Sheila Fischman's translation of *Bambi and Me* by Michel Tremblay, and the Association for Asian American Studies Outstanding Book Award in Poetry for *Pacific Windows: Collected Poems* of Roy K. Kiyooka, edited by Roy Miki. Just two fiscal years after the grant cuts and change of its sales force, Talonbooks had not just survived, but was entering its thirtieth year of publishing with renewed vision and optimism.

The superstore strategy would present a challenge to Talonbooks yet. The publisher had managed to stave off Chapters' huge returns, but that was largely attributable to the negligible quantity of titles Talonbooks had published and the chain

had managed to order in the previous year—gross sales in 1995–1996 were \$10,732; gross sales in 1996–1997 were \$31,849. Further, Chapters’ entry into the post-secondary textbook market, starting with the McGill bookstore, represented a serious threat. Talonbooks derived a significant portion of its income from selling to campus bookstores—45% of net sales in 1996–1997. Part of their success lay in their wealth of backlist drama and literary titles, but Talonbooks had also capitalized on the post-secondary market by securing smaller discounts on backlist books ordered in quantity. To comply with the “like quality and quantity” provisions of the Competition Act, booksellers’ orders of 11 or more of a single backlist title were sold at a 25% discount off the list price (compared to 40% off the list price for orders of less than 10 units of a title)—the same discount textbook publishers traditionally offer to university and college bookstores. Chapters had the market clout and the will to circumvent such small publishers’ discount schemes and ensure maximum profit margins. If Chapters fulfilled course textbook orders—or any store orders, for that matter—through a wholesale division (a strategy used by the American chains Chapters’ business strategy mirrored), the retailer would be entitled to a 46% discount on all titles. The threat that Chapters could undo thirty years of literary survival based in very large part on Talon’s ability to obtain shorter discounts for its college course adoptions of its backlist titles was real and, possibly, imminent.

1998: RETAIL GROWTH AND DIVERSIFICATION

In the fall of 1998, Statistics Canada released *The 1996–1997 Survey of Book Publishers and Exclusive Agents*, which revealed some surprising information about the book business in Canada. Contrary to what most publishers and the book trade press had been reporting but consistent with Talonbooks' experience, net sales to independent bookstores grew between 1995 and 1997, from an average of 19% of sales to 22% of sales. Talonbooks' sales to independents grew from 20.68% in 1995–1996 to 23.71% in 1997–1998.

However, it is understandable that some publishers were surprised by the results of *The 1996–1997 Survey of Book Publishers and Exclusive Agents*; at about the same time the report was published, the once-flourishing Duthie Books announced the family-owned company was selling a 51% stake of the venerable independent mini-chain of 10 stores to a group of investors. Celia Duthie was selling control as a means to “weather increased competition from Chapters, make capital improvements and consider expansion in 1999.”⁷⁷ By mid-November, Duthie's had rejected the “obnoxious takeover bid,”⁷⁸ to the relief of some who did not want to see control given to a non-book trade entity, while raising concerns about how the company might restructure itself to succeed. To begin with, Duthie Books announced that their Arbutus Village store would be closing, and the company was reportedly trying to sell the MacNeil Library Services division. By May 1999, Duthie Books had resorted to filing for bankruptcy protection while it worked on a restructuring plan. Finally, in August 1999, Duthie Books announced it would close all but one of its stores.

As one of Western-based small presses' biggest accounts and strongest supporters in the independent book trade faded, Toronto's Albert Britnell Book Shop held a surprising “Extinction Sale.” The 106-year-old institution was closing because owner Mary Britnell-Fisher had decided to leave the book retail business and, with little hope of

⁷⁷ Snyders, Tom & Scott Anderson. “Duthie Books sells stake in chain.” *Quill & Quire*. Vol. 64, no. 12 (December 1998), p. 5.

⁷⁸ *Ibid.*

selling the store, simply closed up shop after Christmas 1998. Britnell-Fisher denied that Chapters had any effect on her decision, but “the alarm bells [which] have been sounding off for independents since day one”⁷⁹ of Chapters’ entry into the book retail trade certainly seemed to ring louder with the demise of Britnell’s and the depreciation of Duthie Books.⁸⁰

There was very little news about Indigo in 1998, as it made quiet inroads into the book retail market. It opened four new stores in the fall of 1998—in Toronto, Richmond Hill, Calgary, and Montréal—bringing the chain’s total to seven stores. The company also teamed up with the International Festival of Authors in Toronto (which had previously cooperated with independent David Mirvish Books) as part of its embarkation into a stronger marketing strategy, with the hopes of increasing the chain’s exposure.⁸¹ The focus of the book trade media remained fixated on Chapters.

Chapters Goes Online

Part of the Chapters strategy was to dominate not only by geographic markets but also by channels. The initial merger gave the company dominance in the mall bookstore channel, and was fast becoming the market leader in large format stores, but the buzz in the book business in 1997 questioned the bricks-and-mortar approach and set in motion another upheaval of the book trade in Canada. In order for Chapters to achieve the dominant position in all channels, they had to jump on the virtual bandwagon. The hugely successful initial public offering of Amazon.com in May 1997 highlighted the business world’s confidence in the potential of online retailing and brought yet another area of opportunity and threat to the consciousness of the Canadian book industry. Areas of concern included “the unknown fate of territorial rights, the issue of virtual versus

⁷⁹ Toller, Carol. “The rest is history; After more than 100 years, Toronto’s Albert Britnell Book Shop calls it quits.” *Quill & Quire*. Vol. 65, no. 3 (March 1999), p. 1.

⁸⁰ Anderson, Scott. “Not-So-Distant Warning.” *Quill & Quire*. Vol. 64, no. 9 (September 1998), p. 5.

⁸¹ Lahey, Anita. “Indigo teams up with IFOA: Fledgling chain hopes for greater exposure this fall.” *Quill & Quire*. Vol. 64, no. 9 (September 1998), p. 5.

'terrestrial' competition, the time and energy consumed by even the most rudimentary online venture, and the perennial questions about the Canadian book industry's place in this rapidly developing market."⁸² Canada could brag about its wired status, with a greater proportion of the population online than in the U.S., and already independents like Duthie's and Librairie Paragraphe Books in Montreal had a dedicated online presence, but nothing that could compete with Amazon.com or Barnes & Nobles' virtual bookstores in terms of scope and marketing prowess. Publishers mostly steered clear of online retailing directly, conceding they would not be able to generate enough sales to make the venture viable. Though there was very little public discussion, it was hard to deny that many Canadian publishers whose business involved significant exclusive Canadian territorial rights to the distribution of foreign titles in Canada wished that Chapters would launch their own online store, alleviating some of the pressure for deeper discounts offered to Canadian retailers by American wholesalers and ebbing the flow of American editions being shipped illegally to Canadian customers and USA-based Amazon.com's direct sales of those foreign titles to Canadian readers.

Late in the spring of 1998, Chapters announced that it would launch a website co-operatively with *The Globe & Mail* in the fall of 1998. The virtual location, www.chaptersglobe.com, would feature over a million titles and offered customers 20 years of the newspaper's book reviews. Press releases from Chapters estimated revenues of \$5–\$10 million by the end of the first year of operation and projected that online bookselling would account for 15% of the total book retail market by 2001. Once announced, of course, opponents to Chapters' geographic and channel domination resurfaced, fuelled by criticism for the controversial new alliance between Chapters and *The Globe & Mail*, and renewed worry about Chapters' monopsonistic intentions. In order to facilitate this new enterprise, Chapter leased a 300,000-square-foot distribution centre in Brampton, Ontario. The online store concept fit with Chapters' retail value

⁸² Lorinc, John. "Land of the Giants: Canadian bookstores up against Amazon, B&N as online sales ignite." *Quill & Quire*. Vol. 64, no. 4 (April 1998), p. 8.

proposition (RVP) and gave the company another advantage: “The Internet shares many of the front-end costs with the large Chapters stores, such as brand-building and customer relationships. All three businesses share money costs at the back end (e.g., finance, systems, and construction), and this serves to improve Chapters’ cost position and, hence, profit performance. Most importantly, all businesses [mall stores, large format stores, and the online venture] share fulfilment, which gives Chapters sales and cost advantages over its competitors.”⁸³ Chapters most often ordered new literary titles, drama, and poetry in ones and twos. Re-orders on slower-moving titles were rare, owing in part to the disconnect between point-of-sale and inventory databases. Of course, sales representatives feared overselling to the chains (and indeed, any retailer) because of the distinct possibility of returns. An attempt by the retailer to finally control the avalanche of returns and place reorders for titles with more modest sales would have been warmly welcomed, yet reducing the waste inherent in returns and streamlining operations only addressed one aspect of Stevenson’s cost management strategy. The other: margin erosion.

Chapters’ Pegasus Wholesale Division Takes Wing

The most serious of Chapters’ efforts to reduce costs was the launch of a new distribution centre in the fall of 1998, followed by the formation of Pegasus Wholesale (82% of which was owned by Chapters) based in that centre in May—in other words, immediately after the BCP conditions on its 1995 approval expired and the merger of SmithBooks and Coles had become unassailably permanent in April of 1998. The huge facility in Brampton, Ontario was created to be the hub from which all books would travel to the stores and to customers who placed orders on Chapters’ website, the idea being that the warehouse would reduce costs by garnering larger wholesaler discounts from publishers, allow for just-in-time shipping, and manage bibliographic data information. According to a report in *Quill & Quire*, “the new distribution centre represent[ed] the culmination of an information technology project that dates back to the formation of the company itself: the

⁸³ Stevenson, Lawrence N., Joseph C. Shlesinger and Michael R. Pearce. *Power Retail: winning strategies from Chapters and other leading retailers in Canada*. McGraw-Hill Ryerson, Toronto: 1999, p. 112.

implementation of an effective point-of-sale inventory control system that can be used to reorder books on a just-in-time basis, thereby reducing stock levels and costs associated with returns due to overly aggressive ordering.”⁸⁴ That is not to say that Chapters had solved the technology problems required to reach this panacea: the company “acknowledged to publishers that it will likely take about 18 months to de-bug the new technology and then phase in the system to the point where all shipments can be sent directly to the new facility.”⁸⁵

The new warehouse was the subject of huge consternation amongst publishers and independent bookstores because “just as independent booksellers were recovering from the news that there’s really nothing they can do under Canadian law to prevent Chapters from negotiating even-better discounts from their suppliers, they learn that Chapters is negotiating with some of its suppliers for higher discounts.”⁸⁶ The larger discounts were based on the assumption that Chapters’ new warehouse facility, operating as Pegasus Wholesale, would qualify for wholesaler rates, which, in the case of Talonbooks, was 46% off the cover price (versus 40% for bookstores). Chapters used its market dominance to leverage its position, in essence threatening publishers to agree to a substantially bigger discount or not have their titles ordered by Pegasus, thus not have their titles represented in Chapters’ stores. Yet again, the BCP examined Chapters’ business practices, and yet again determined that the company did not contravene the Competition Act.

Perversely, if publishers and distributors collectively negotiated for lower discounts to the chain and its wholesale operations, the publishers and distributors would be acting illegally. With Chapters’ market clout, small publishers had little leverage, and the representative associations (like the ACP) were loathe to get involved over fears of price-

⁸⁴ Ibid.

⁸⁵ Ibid.

⁸⁶ Anderson, Scott. “Not-So-Distant Warning.” *Quill & Quire*. Vol. 64, no. 9 (September 1998), p. 5.

fixing accusations.⁸⁷ When Firefly books refused to sign on, Chapters returned \$1 million in Firefly and their distributed presses' inventory. Likewise, when Key Porter threatened to have author Allan Fotheringham denounce the chain publicly in *MacLean's* magazine because there were none of his books in stores for his cross-country tour, Stevenson countered with the promise "he'd return every Key Porter book in his possession."⁸⁸

The Superstore Effect on Talonbooks

Talonbooks dealt with warehouse structures similar to Pegasus in the U.S. for retailers like Barnes & Noble, and Talonbooks had a complicated U.S. discount structure to match: in Canada, sales to bookstores were discounted at either 40% (for all frontlist titles and for backlist orders of less than 10 per title) or 25% (for backlist orders of more than 11 copies of a title), but for the U.S., retail sales were discounted by 45%, while the chains received 45% for drop shipments or 48% for discount warehouses or distribution centres. Canadian wholesalers received a 46% discount, whereas U.S. wholesalers received 50%. Talonbooks could afford this relatively more generous discount structure to the American book trade because of the high Canadian exchange rate for the U.S. dollar. However, if Chapters' new warehouse were to demand the same discounts as its U.S. counterparts, Talonbooks would have seen its already slim Canadian profit margin all but disappear. (Following the significant decline in the value of the Canadian dollar, Talonbooks amended its discount and pricing in its spring 1999 catalogue, posting only the Canadian discount scheme and no U.S. prices, only a notation "For U.S. prices, deduct \$3.00 from listed prices.")⁸⁹

Talonbooks' catalogue offered a shortened list of titles in the spring of 1998 due to

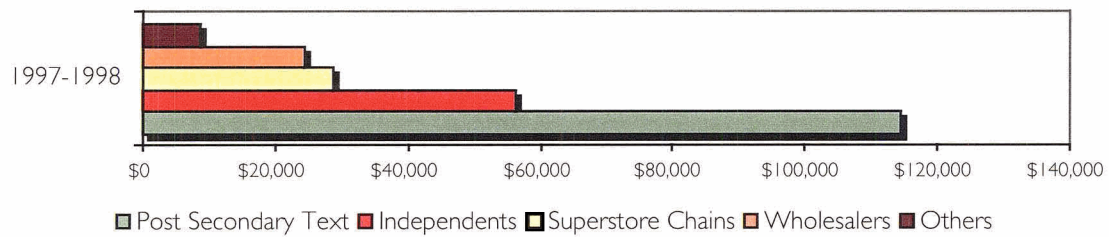
⁸⁷ "The LPG was not yet taking positions; it had just become legally separate from the ACP. All LPG members belonged to the ACP, so that's where we were doing our political advocacy work. Arguably, the ACP's position on Chapters deepened the divides between the organisations and led to greater political independence on the part of the LPG." Rolf Maurer, editorial addendum to this report, November 2006.

⁸⁸ MacSkimming, Roy. *The Perilous Trade: Publishing Canada's Writers*. McClelland & Stewart Ltd., Toronto: 2003.

⁸⁹ The Canadian dollar reached an all-time low of US\$0.6311 on August 27th, 1998, compared to an average of US\$0.73 for the mid-1990s.

ongoing staff shortages, but its otherwise steadily increasing new title production and their trade sales were encouraging. While sales to the academic and post-secondary market had a minor slip—down 5.3% to \$114,413—sales to independents soared. Despite the demise of the Bollum mini-chain in B.C., the Edwards Books & Art mini-chain in Ontario, Sandpiper Books in Calgary, and Duthic Books’ drastic reduction of its mini-chain from 10 stores to one, net sales to independents grew by over \$15,000 to \$56,419: up 38.5% over 1996–1997 and 61.8% over 1995–1996, “mirroring almost exactly an increase in Talon’s own new title production of 63% since 1995-1996, an its ‘invisible’ acquisition of the Coach House Press, Blizzard and Playwrights Canada Press titles during this period.”⁹⁰ Independents were not reclaiming their market share from the superstores though; net sales to the chains had increased by only 15% to \$28,889, with half of that growth coming from the emerging Indigo venture because Talonbooks no longer primarily published for, nor catered to the chains.

Figure 4. Talonbooks’ Canadian Net Sales by Category, 1997–1998



Aided by advances in desktop publishing technology, Karl and Christy Siegler were perhaps the most productive of all literary presses in Canada during this period, and had even managed to post a company website in the fall of 1996. Karl Siegler also spent a considerable amount of time and effort lobbying the government and was an active participant in the Literary Press Group, working on policy issues in an attempt to restore a higher level of funding to Federal programs in support of Canadian-owned publishing,

⁹⁰ Karl Siegler, editorial addendum to this report, September 2006.

with some, but limited, success. The overworked staff of two owner-managers focused on the editorial, publishing, and financial management of the company until September 1999, when Talonbooks was finally able to add another full-time staff member to its roster to assist with sales and marketing management. “[We] not only rebuilt [our] company’s new title production back up to its previous high of 15.5 titles [in the Kate Walker & Co. years of 1993-1994] by 1997-1998, [we] even exceeded this level of activity by 1998-1999, publishing 20 new titles in each of those two years. [We] did this alone, with no staff assistance, and with a purely literary list within four years of the disastrous Federal funding cuts and the establishment of Chapters in 1995. Even more incredible is that [we] were able to hire [our] first new staff person because [we] had also managed to repay all of [our] \$146,000 in long-term loans to both the CIDF and [our] private lender in this four year period—by November of 1999. One can only speculate how much faster [our] recovery would have been had [we] not been saddled with this debt, premised as it was on a false commitment by the federal Liberals on a ‘guaranteed’ level of funding over the five-year period 1992 through 1996.”⁹¹

Karl Siegler maintains that the threat of decreased profit margins and the decline of Duthie Books, which had been Talonbooks’ single largest independent trade bookstore account prior to the creation of Chapters, were not inhibiting factors for growth. Nevertheless, Duthie Books had sold Talonbooks’ frontlist titles well, and returns were a smaller percentage of gross sales than most other accounts. While Duthie Books (and other independent booksellers) could not blame their woes entirely on Chapters, with Chapters’ new warehousing scheme, Pegasus, independent booksellers were competing with the Chain on increasingly uneven ground—most publishers’ discounts to the chain were escalating and payment terms were being extended, benefits those publishers were not extending to the chains’ independent competitors. No one with the clout to confront Chapters could or would do so—not the branch plant publishers, not the ACP, not the thriving independents and their professional association, the CBA, and not the BCP. The

⁹¹ Karl Siegler, editorial addendum to this report, September 2006.

virtual demise of Duthie's was ominous for other independent bookstores and seemed so also for Talonbooks. Duthie's represented the fabled independent book hand-seller, champion of local authors and the independent press, with scrupulously selected stock and extraordinarily knowledgeable booklovers as staff—the independent mini-chain's bankruptcy was the symbolic demise of an era in Canadian bookselling.

1999: MERGERS AND ACQUISITIONS

Mergers, acquisitions, and big business agendas were defining characteristics of the 1990s in the book trade and in the waning months of the decade—indeed, the century—and the trend showed no signs of abating. In June 1999, Renaud-Bray acquired the Champigny and Garneau mini-chains in Quebec and Rupert Murdoch’s News Corp. purchased the Hearst Book Group and merged its Canadian operations with HarperCollins. A retrospect of the decade in the book trade from *Quill & Quire* declared, “While the story for publishers in the first half of the 1990s was about recession and downsizing, the second half concerned market growth and expansion. The superstore phenomenon drove sales up, but international consolidation left fewer publishers sharing in the profits. Curiously, the merger trend didn’t trickle down to smaller companies... Canadian-owned publishers remained fiercely independent.”⁹² Fiercely independent, but at serious risk.

As the events of latter part of 2000 would show, very few proposals or intervention attempts were successful in engaging the government in its role of protecting a diverse, viable, and Canadian-owned book trade. One of the few signs of relief throughout the entire decade was the long-awaited revisions to the Canadian Copyright Act, which went into effect in September 1999, and requires booksellers to place orders with Canadian suppliers, assuming the publisher or distributor meets service guidelines. The regulations meant Chapters and other stores could not legally engage in the practice of “buying around,” though the problem persists. In the meantime, the book trade saw the demise of more venerable independents in 1999–2000: Lichtman’s, the largest central Canadian independent book chain with nine stores declared bankruptcy on March 31, 2000, and Vancouver lost many small independents, including Mallard Books, East End Book Co., Mystery Merchant, Zerafa Books, and Amber Books.

⁹² Anderson, Scott. “They must be giants: The Canadian book industry goes global.” *Quill & Quire*. Vol. 66, no. 1 (January 2000), p. 18.

Chapters' Strategy Unravels

By the fall of 1998, Chapters had shed the shackles of the BCP and became accountable solely to its shareholders, though widely scrutinized by the public and the Canadian book industry. With 52 locations secured by the end of 1998, Larry Stevenson's strategy addressed the most public aspects of the company's practices by aiming to "execute better than competitors in areas of people, technology, and costs." This principle involved three elements:

- Investing in people to achieve customer loyalty
- Managing information technology for strategic breakthroughs
- Cost management to minimize margin erosion

Chapters' success in these three "critical components of execution" was debatable.⁹³

Chapters' Investment in People Principle

In order to hire the right people, Chapters had an elaborate candidate selection process that sometimes involved joint interviews with six to eight applicants. Many of the stores' floor management were lured from non-book retail, while some top management members were hired from Barnes & Noble or were part of the Coles/SmithBooks management structure. At one point, Chapters' expensive human resources strategy seemed to pay dividends: customer satisfaction surveys consistently ranked Chapters very highly. In 1997, 1998, and 1999, the Kubas Customer Survey rated Chapters the best all-round retailer, and even industry trade publication *Quill & Quire* rated Chapters tops.⁹⁴ Larry Stevenson infamously sent 160 managers on a free trip to Paradise Island in the Bahamas for three days in June 1999 as a reward for meeting targets, but Chapters was top-heavy and underwent significant restructuring through 1998–1999.

⁹³ Stevenson, Lawrence N., Joseph C. Shlesinger and Michael R. Pearce. *Power Retail: winning strategies from Chapters and other leading retailers in Canada*. McGraw-Hill Ryerson, Toronto: 1999, p. 116.

⁹⁴ Toller, Carol. "Indies vs. Chains: Q&Q's fourth annual store survey finds independents resisting pressure to discount." *Quill & Quire*. Vol. 64, no. 3 (March 1998), p. 1.

Some of Chapters' problems were inherited from the Coles/SmithBook merger and still more were created by the ambitious company expansion. The management structure had "superstore staff reporting to as many as four different bosses (general manager, lead, product manager, and operations manager)" while "some stores... didn't have a manager on duty during all opening hours... [and] each outlet had its own public relations person."⁹⁵ As part of the company's cost-saving measures, it streamlined management and reduced labour costs by benchmarking store efficiency; that is, matching labour with customer traffic patterns. In terms of "investing in people to achieve customer loyalty," it's hard to imagine a high employee morale environment with the management issues Chapters was dealing with. The policy that "if a member of the Chapters team leaves to join a direct competitor, the doors are closed against coming back" hints at the damage done by key executives' moves to Indigo.⁹⁶ And while Chapters may have invested in people, its technological infrastructure did not support its front-line workers.

Chapters' Information Management Principles

The disastrous state of the Chapters' information systems was another limiting communications factor and frustration for publishers, for the book buying public, and for Chapters' own management and staff. At the time of the SmithBooks and Coles merger "one chain had information systems that tracked what was selling, but not what was it had on the shelf. The other chain had a system that tracked what was on the shelf, but not what was selling."⁹⁷ Nor was that the worst of it. Rather than a standard three-part retail information system (point of sale, inventory, and back-end/office system), "information was so compartmentalized between the two chains that, rather than having

⁹⁵ Lorinc, John. "Leaner, faster, stronger: Is Chapters unbeatable?" *Quill & Quire*. Vol. 65, no. 6 (June 1999), p. 18.

⁹⁶ Stevenson, Lawrence N., Joseph C. Shlesinger and Michael R. Pearce. *Power Retail: winning strategies from Chapters and other leading retailers in Canada*. McGraw-Hill Ryerson, Toronto: 1999, p. 137.

⁹⁷ Stevenson, Lawrence N., Joseph C. Shlesinger and Michael R. Pearce. *Power Retail: winning strategies from Chapters and other leading retailers in Canada*. McGraw-Hill Ryerson, Toronto: 1999, p. 164.

the standard three systems, there was a total of 14.”⁹⁸ The addition of chaptersglobe.com in 1998 and chapters.ca in April 1999 added more layers to the IT mess, as did adding a music section “Hear Music” in the summer of 1998 and entering the college bookstore market. When publishers got their first peek at *one* of Chapters’ information systems after the company made it public with the chaptersglobe.com site, many quickly identified serious errors of fact and spelling throughout the online database. Chapters’ spokesperson Helena Aalto was reported as saying errors occurred “when several databases were merged to create a single database of 2.9 million titles.... During the merging process, U.S. bibliographic information overwrote Canadian information in many cases.”⁹⁹ Right up until the end of chapters.com (which superseded chaptersglobe.ca and, in turn, was superseded by indigo.ca after the takeover), dozens of Talonbooks and New Star title listings on the site remained erroneous. Incorrect title spellings and title prices were the most common error, followed by titles completely missing from the database, in-stock titles listed as not yet published, out-of print, or currently not available, and titles attributed to the wrong publisher. The state of the other 13 systems undoubtedly impacted sales too.

Misinformation and disinformation was a bugaboo for customers too. Case in point: a customer special-ordered a title after not being able to find it on the shelves of the Langley store, nor listed in-stock on Chapters self-serve in-store computer terminals. The sales associate, using a different computer terminal and database program at the special order desk, processed the request and advised the customer that the book would arrive in no more than two to three weeks. After four weeks, the customer returned to the store, where the special-order clerk advised her that that book had still not arrived. After a quick perusal of the store, the customer came across an entire end-cap display of the book. Perturbed, she complained to the special order desk and was countered with apologies and excuses about Chapters’ computer systems. While the customer didn’t

⁹⁸ Ibid.

⁹⁹ Toller, Carol. “Chapters working to fix online retail glitches.” *Quill & Quire*. Vol. 64, no. 12 (December 1998), p. 5.

place any special orders with Chapters after that, the accumulated benefits on her store loyalty card kept her coming back.

Chapters' affinity program was the one aspect of "managing technology for strategic breakthroughs" that reaped rewards. Chapters had two programs, Avid Reader for the mall stores and Chapters One for the big-box locations, which together represented "the largest paid loyalty program in Canada... with close to 700,000 members."¹⁰⁰ From the introduction of the Avid Reader program in 1995 with 125,000 cardholders, membership skyrocketed to 625,000 members by 1999 (each of whom pays \$15 to join and \$10 per year after that to remain a member, in exchange for 10% off all purchases and a point program).¹⁰¹ (While membership numbers for the Chapters One program are not directly cited in *Power Retail*, if the company had nearly 700,000 loyalty program members and 625,000 held Avid Reader cards, then Chapters One members numbered less than 75,000.)

Chapters' "Anticipation" Strategy

Not content to maintain the status quo, which garnered Chapters number one ranking in the prestigious Major Market Retail Report by Kubas Consultants for four consecutive years (1997, 1998, 1999, and 2000), and unabated by the BCP and the Standing Committee on Canadian Heritage, Chapters continued its onslaught on the book trade. The fourth and final strategy of *Power Retail* was to "anticipate to lead change."¹⁰² As the opening paragraphs outlining this concept indicate, reinventing a company to outpace competitors is the most difficult of the principles Stevenson proposes:

Abiding by the first three principles does not guarantee that a retailer will successfully implement this fourth principle. Retailers clearly need to develop a winning retail value proposition (RVP), establish clear market

¹⁰⁰ Stevenson, Lawrence N., Joseph C. Shlesinger and Michael R. Pearce. *Power Retail: winning strategies from Chapters and other leading retailers in Canada*. McGraw-Hill Ryerson, Toronto: 1999, p. 167

¹⁰¹ Ibid..

¹⁰² Stevenson, Lawrence N., Joseph C. Shlesinger and Michael R. Pearce. *Power Retail: winning strategies from Chapters and other leading retailers in Canada*. McGraw-Hill Ryerson, Toronto: 1999, p. 219.

leadership, and execute superbly. But, ironically, the retailer who religiously follows the first three principles for success is more likely to violate this last one, because changing a successful organization is often more difficult than changing one that is in turmoil. It is perhaps the most difficult principle to follow—yet without a strategy for leading change, the retailer will in fact be the victim of change.

The Power Retailers lead change. They know that while historical success is no guarantee of future success or even survival, change is a certainty. They embrace change, they know where the organization is going, when to bring new players onboard, and how to stay focused while responding to change—and sometimes this means reinventing themselves before the deck is on fire.¹⁰³

To continue outperforming competitors and stave off encroachment on their market share by retailers like Costco, Wal-Mart, and Indigo, Chapters continued extending itself. The expansion of its big-box stores well underway, the new warehouse/wholesaling concept Pegasus more or less in effect, and with Chapters posting record earnings, the company's focus shifted back to the Internet. President of Chapters Internet Rick Segal proclaimed, "the Internet will fundamentally change everything in retail,"¹⁰⁴ as Chapters entered the their third business transition. ("The first successful transition was the original 1995 merger. The second was the launch of book superstores and the transformation from a mall-based business to a destination store business. The third transition [at the time *Power Retail* was written, in 1999] has just begun as Chapters launches itself full steam onto the Internet."¹⁰⁵)

The company spent millions to ensure the success of their online venture, guided by the notion that "red ink will not flow forever" in e-commerce.¹⁰⁶ However, Chapters' online success was reliant on an IT infrastructure knot that had yet to be untangled, and dependent upon the efficiency of Pegasus to fulfil orders quickly when the warehouse had proven to be nothing more than a bottleneck. Larry Stevenson and Chapters did not

¹⁰³ Ibid.

¹⁰⁴ Ibid., p. 221.

¹⁰⁵ Ibid., p. 226.

¹⁰⁶ Ibid., p. 221.

anticipate the cost of leading change online, nor the changes 1999–2000 would have upon them, and by the end of the fiscal year, the lead they had established was quickly and permanently narrowing. And this third transition was substantively different than the previous two: this time, there was serious competition. Perhaps Stevenson—*Report on Business* magazine’s “Man of the Year” for 1999—was aware of the challenge facing his company: he cashed in one-third of his Chapters holding between August 1998 and February 1999, worth over \$5.5 million.¹⁰⁷

Indigo Expands

The biggest threat to Chapters’ market share was Indigo. While other retailers like Wal-Mart and Costco focused on mass-market best sellers and remainders, Indigo was targeting the same lucrative “boutique buyers” as Chapters. Indigo mirrored Chapters’ strategy in other areas too: chapters.ca was launched April 1999 and indigo.ca was launched mere months later, in July 1999; when Chapters online division acquired the gardening website gardencrazy.com in January 2000 and began selling the home and garden products later in the year via its villa.ca site, Indigo followed suit with the purchase of the mail-order garden institution Cruikshanks in March 2000, with the intention of integrating the garden production into Indigo’s online venture. Indigo ramped up its operations again in July 1999 with a revamped website that boasted more content and bigger discounts, a huge branding campaign led by the slogan “Blue Your Mind,” and six new stores for the fall (bringing the chain’s total to 14 bricks-and-mortar locations). Though Indigo executives denied they were squaring off against chapters.ca, indigo.ca offered a 50% discount off their top 100 titles plus free shipping for the summer. Most publishers were pleased with Indigo’s performance, noting that “sales to Indigo have grown beyond the start-up orders required to stock new stores... (as) reorders are coming in and returns are low.”¹⁰⁸ The company’s movement spawned rumours that it

¹⁰⁷ *Report on Business Magazine*. Vol. 16, no. 4, (October 1999).

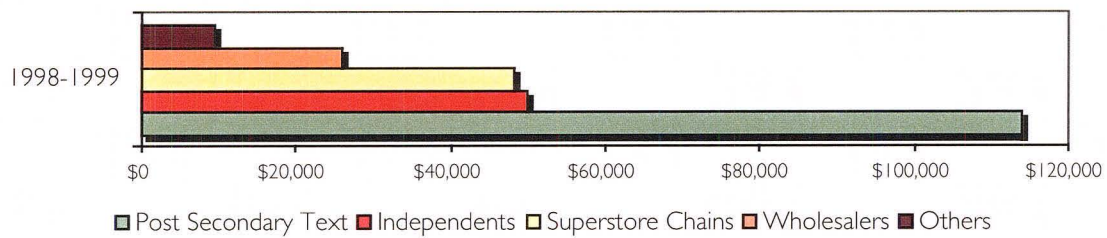
¹⁰⁸ Lorinc, John. “The Indigo way: Stylish and savvy, Canada’s number two chain marches to its own beat.” *Quill & Quire*. Vol. 66, no. 2 (February 2000), p. 22.

would be going public sometime in 2000, as Chapters had done with its online division in September 1999.¹⁰⁹

Talonbooks' Returns Crush

The growth of the Indigo chain was not necessarily welcome news at Talonbooks. The publisher's gross sales and net sales numbers for 1998–1999 look good at first glance—gross sales continued to climb another 5.3% in 1998–1999 and net sales sustained growth of 4.1% over 1997–1998 net sales—but they hid an alarming development. Returns shot even higher, to \$91,813 in 1998–1999, up 15.8% from 1997–1998 and nearly 26% higher than 1995–1996. Over 25% of Talonbooks' returns were from the superstores, which, even as they continued rapid expansion, represented less than 20% of Talonbooks' sales. Another way of parsing the numbers: the superstores returned \$23,287 worth of books in 1998–1999, nearly half of all gross sales to superstores in the previous year. The heavy volume of returns felt across the industry caused a cash crunch for distributors and cash flow concerns for publishers, compounded by Chapters taking up to 140 days for payment.¹¹⁰

Figure 5. Talonbooks' Canadian Net Sales by Category, 1998–1999



B.C.-based publishers became increasingly concerned with the big-box strategy when Chapters' management restructuring eliminated store-level ordering and moved to

¹⁰⁹ Indigo announced plans to go public early in 2000, but withdrew because of a "soft market."

¹¹⁰ Lorinc, John. "Leaner, faster, stronger: Is Chapters unbeatable?" *Quill & Quire*. Vol. 65, no. 6 (June 1999), pp. 18-19.

leaner, more centralized (i.e. Toronto-based) buying. The move made it more difficult for publishers outside Toronto to have ongoing communications with Chapters' buyers, encourage regional titles, or have store-level champions of their works. It also meant that if the central buyer passed on a title, it was nearly impossible for Talonbooks, New Star, or others to have the book represented in the majority of the retail market share Chapters held. And with its tangled IT systems, it was unlikely that a buyer in Toronto would know what stock moved or remained on the floor in Vancouver. *Power Retail* maintains that Chapters achieved "a retail operation that knows what it sells, knows what is on the shelf, knows what needs ordering, and is in its best in-stock position ever,"¹¹¹ but the experience of Talonbooks, New Star, and their colleagues and customers shows how far Chapters fell from this ideal. As Maurer pointed out, "Chapters operated as a retail giant, where it tried to collect large amounts of data and then see if it comes up with any findings that could be applied universally. I don't think that works all that well with books. The return rates are evidence of that."¹¹² And many publishers, including New Star and Talonbooks, did not believe that Chapters could turn their information glut into the utopian Internet sales universe they proselytized. E-commerce's reliance on clean code and seamlessly integrated point-of-sale, inventory, and delivery systems was beyond the capabilities the company had thus far demonstrated. Even Amazon, with its head start, global brand-name recognition, team of innovators, and Time's "Man of the Year" for 1999 at the helm, bled \$115 million in red ink in 1998, and was having little effect on American book sales (capturing only 3% of the U.S. book retail market share).¹¹³ Chapters' forays into online threatened to be another "transition" that delivered truckloads of returns to publishers.

¹¹¹ Stevenson, Lawrence N., Joseph C. Shlesinger and Michael R. Pearce. *Power Retail: winning strategies from Chapters and other leading retailers in Canada*. McGraw-Hill Ryerson, Toronto: 1999, p. 164.

¹¹² Interview with Rolf Maurer, August 2004.

¹¹³ Harmon, Steve. "Book 'Em: Barnes & Noble Follows Amazon's Plot," internetnews.com, August 21, 1998. <http://www.internetnews.com/bus-news/article.php/57931>

2000: BRICKS VERSUS CLICKS

After much speculation and hype, the Internet finally began to make an impact on book sales in 1999–2000, for some. Many book publishers approached online selling cautiously after the failed technological promises made by CD-ROMs, e-books, and other high-tech innovations that purported to revolutionize the book. For many publishers, the proof of the Internet's potential came during the Christmas season of 1999. The post-Christmas edition of *Quill & Quire* reported huge gains as “Internet sales skyrocket,” with Chapters carving a \$12.2 million portion of the online book sales pie for the quarter ending January 1, 2000—“20 times more than the site’s inaugural 1998 Christmas season... [and] third quarter revenues were 90% higher than those of the previous quarter.”¹¹⁴ Chapters’ strategy was ceremoniously vindicated by the Retail Council of Canada awards for Innovative Retailer of the Year, Excellence in Retailing Award for Retail Marketing, and, for its online efforts, the Excellence in Retailing Award for Online Retailing. Indigo kept its figures quiet, with Indigo.ca president Ted Boyd simply commenting “we’re absolutely delighted.”¹¹⁵

With both Chapters and Indigo using lavish marketing budgets to attract online buyers—Chapters spent \$2.3 million in the first quarter of 1999—as well as deep discounts and free shipping incentives, the sustainability of online giants became questionable as they duelled for market share.¹¹⁶ On June 1, 2000, Chapters posted revenues of \$17.2 million, an increase of 67%, but the cash influx was due to a large-scale sell-off of shares in Chapters Online (with an IPO on September 21, 1999, the company generated \$46 million by selling 3.4 million shares at \$13.50 per unit) and Pegasus (Canadian General Capital, which owned 16% of Chapters, purchased a 15% share in

¹¹⁴ Lorinc, John. “Internet sales skyrocket: Chapters Online revenues soar 90% over previous quarter.” *Quill & Quire*. Vol. 66, no. 2 (February 2000), p. 24.

¹¹⁵ *Ibid.*

¹¹⁶ Weiler, Derek. “Indigo launches round two of expansion: New stores, Internet campaign mark chain’s renewed growth as competition with Chapters intensifies.” *Quill & Quire*. Vol. 65, no. 6 (September 1999), p. 9.

Pegasus for \$7.5 million) worth \$42.7 million.¹¹⁷ The balance sheet would have shown a staggering net loss of \$25.5 million without the cash injection.

On the bricks-and-mortar bookselling side of Chapters' business, revenues for both the big box and mall locations fell from \$12.7 million to \$9.1 million. The start-up distribution/wholesale enterprise Pegasus accounted for a \$9.5 million loss. The razzle-dazzle of Chapters Online burnt up the most revenue: the "anticipate to lead change" strategy that motivated Chapters Online resulted in a loss of \$25 million, compared the division's loss of \$2.4 million the previous fiscal year. CEO Larry Stevenson "assured investors the three businesses provide a solid foundation for long-term strength and growth" and further defended speculation that the company was in financial difficulty by launching a lawsuit against the *National Post*, which had reported Chapters was having serious financial trouble.¹¹⁸

Chapters' Cost Management Principle

In the Canadian bookselling industry, gross margins declined from 37% in 1993 to 33% in 1998, an event driven by three pressures.¹¹⁹ Number one was the general growth of bestseller discounting and loyalty programs, which effectively meant that the most frequent book purchasers were getting discounts in bookstores across the board, including in the smaller bookstores. During the same period, large-format stores were on the upswing, operating at a 4 to 5% lower gross margin than the small stores. Finally, substantial share gains were made by deep discounters of books—companies such as Costco, Wal-Mart, and the grocery chains. As these outlets gained share at a lower gross margin, bookstores had to find cost savings of 4% of sales just to stay even on a

¹¹⁷ Weiler, Derek. "Pegasus makes progress with publishers: HarperCollins comes to verbal agreement, Raincoast, Thomas Allen sign on." *Quill & Quire*. Vol. 65, no. 12 (December 1999), p. 4.

¹¹⁸ CBC News Online. "Chapters posts profits of \$17.2 million." CBC News [online], June 1, 2000. [Cited November 12, 2001.] <cbc.ca/cgibin/templates/view.cgi?category=Business&story=/news/2000/06/01/chapters00060>

¹¹⁹ Canada. Statistics Canada. *Survey of Book Publishers and Exclusive Agents; Book publishers and exclusive agents* (data tables). [Ottawa] November 2003.

profitability basis.¹²⁰ Of course, Chapters began with the merging of two wholly unprofitable bookstore chains, which, by Larry Stevenson's account, were both doomed to bankruptcy without a merger.

The final element of Chapters' *Power Retail* strategy, "cost management to minimize margin erosion," had a significant impact on B.C.-based publishers. While Dan Soper, Senior Vice President of Large-Format Operations, is quoted as saying: "Chapters added more square footage to the retail book sector in just one year [1998] than Coles Bookstores had built in forty years of operations,"¹²¹ Chapters had also closed more bookstore locations that year than it had opened. By 1999, the company had closed 190 of their 440 mall bookstores, primarily because of high rent-to-sales ratios. The bulk of Chapters' revenues had been quickly shifting to the big-box locations: the 35 Chapters superstores opened by the end of the first quarter of fiscal 1999 accounted for 48% of all revenues. Yet the average sales per square foot dropped again, from \$312 (in 1997) to \$262.¹²² To succeed in generating profit from fewer locations, with more square footage, and lower sales per square foot, Chapters would have to lower operating costs in proportion, thus by 22%, just to remain profitable at 1996 levels. But from Chapters' perspective, it was necessary not simply to be profitable, nor simply more profitable than small bookstores or mini-chains, but to compete on a profitability basis with some of the world's largest retailers.

The Chapters rollout was ebbing well short of the 150 stores the company believed the market could bear, with only seven stores slated for opening in fiscal 2001 (compared with sixteen during the previous year), as Chapters was in a precarious financial position. Shares hovered around the \$9 mark, versus their one-time high of \$35 in mid-1999. Revenue was growing, but not at a rate high enough to counter capital expenses, debt, and overhead, so Chapter's owner Larry Stevenson started making drastic

¹²⁰ Ibid., p. 187.

¹²¹ Ibid., p. 27.

¹²² Lorinc, John. "Murphy's Law: Chapters enters new era: New retail CEO plans sweeping changes to buying and merchandising strategy." *Quill & Quire*. Vol. 66, no. 7 (July 2000), p. 4.

moves to safeguard his book empire and ward off a hostile takeover. In May 2000, the company's new head of retail announced: "the time has come to reduce our dependency on the book category in our stores."¹²³ In an effort to increasing flagging share values, Chapters began a restructuring program that saw the diversification of products entering the stores, namely gift items such as picture frames, seasonal toys, and greeting cards. The plush couches that welcomed browsers and their (sometimes spilled) Starbucks cappuccinos were quietly removed. Some stores saw cyber or web cafes open, other stores, particularly the largest locations, began stocking music CDs. No part of the enterprise was exempt: in the fall, Chapters began to look for a buyer for Pegasus and, in mid-November, Chapters Online announced plans to lay off nearly 20% of its staff—a total of 73 employees. Chapters' RVP was no longer centred on its claim of having over 100,000 titles in store, which faded into memory along with the stock. The purchase order windows were reduced to four weeks, and retail floor space was divided into sections with their own fixed budget based on past revenues.¹²⁴ Poetry and drama sections were depleted. Further emphasis was placed on best-selling titles, and remaindered titles and bargain books began to fill the front of the stores.

Chapters' Restructuring, and Returning

The Chapters restructuring program resulted in the largest volume of returns publishers had ever seen. Linda Palmer, the sales and marketing director for the LPG in 2000, predicted that initial orders from Chapters' buyers would shrink by up to 80%, and with Pegasus in the game, tracking reorders was impossible.¹²⁵ The return rate reached astronomical proportions as Chapters returned about \$70 million in books to publishers between March and July 2000 and, according to CFO Tamara Lawson, planned on returning a further \$25 million by March 2001.¹²⁶ Unprecedented truckloads of

¹²³ Ibid.

¹²⁴ Ibid.

¹²⁵ Ibid., p. 6.

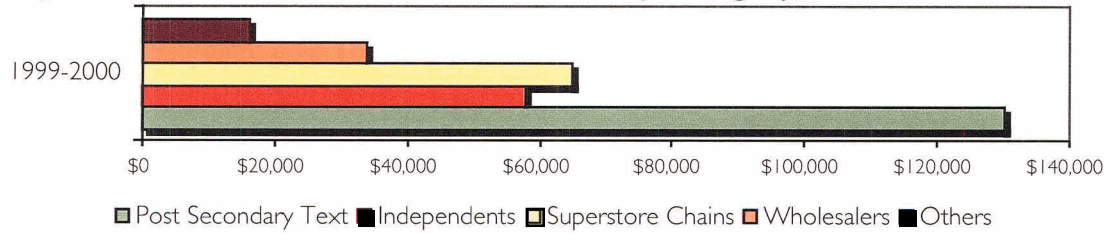
¹²⁶ Lorinc, John. "Indigo eliminates management layer: Lay offs point to cost-cutting at chain." *Quill & Quire*. Vol. 66, no. 8

inventory, mostly backlist titles, were returned to distributors in an effort to lower the value of receivables and boost stock prices; that is, improve their financial statements by lowering inventory and payables without actually selling books. Many publishers experienced consecutive months of net negative sales. The payments for books that Chapters and Pegasus did keep were late—even beyond the already generous payment terms demanded by the chain and extended by distributors. As for the distributors, they had more returns than they could process, and the returns from independents began to get held up. In many cases, returns went to the wrong distributor. Disputes began between distributors and publishers when the nature of some of the returns was discovered: distributors had accepted damaged titles and ineligible returns, and the amount of returns was being held against receivables. While the book industry in Canada had frequently and almost consistently been in crisis, there was no doubt that the industry was deeply into a crisis the likes of which hadn't been felt since the drastic cuts to federal grants in 1995. For some publishers, including Talonbooks and New Star Books, it was even worse.

Talonbooks' sales figures for 1999–2000 reflected changes in the bricks-and-mortar marketplace: for the first time, net sales to chain bookstores seemed to eclipse net sales to independent bookstores. Chapters represented the majority of Talonbooks' net sales to chain bookstores, with \$43,770 in sales to the big-box stores and a further \$12,763 to Chapters small-format stores. Net sales to Indigo grew by a further \$1,940 or 31% in 1999–2000, which still represents substantial growth, but not like the 226% growth of 1998–1999, and still leaving Indigo with only about 13% of Talonbooks' overall net sales to superstore chains. Combined, Talonbooks' Canadian Net sales rebounded from 1995–1996's low of \$168,578 to \$302,546 in 1999–2000, as net sales to the chain bookstores reached an all-time high of \$64,789.

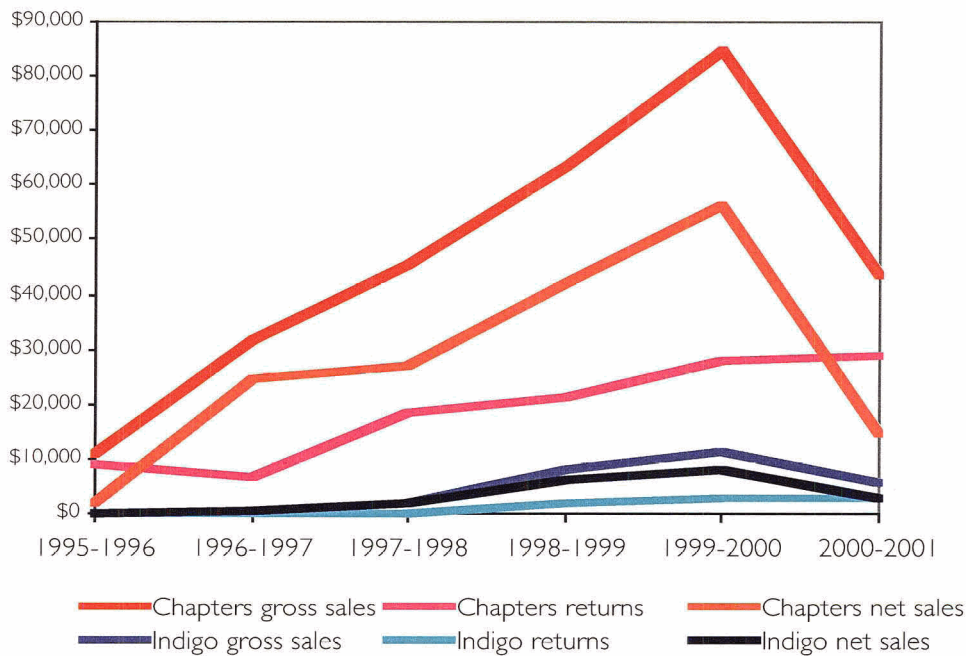
(August 2000), p. 4.

Figure 6. Talonbooks' Canadian Net Sales by Category, 1999–2000



But while the big box stores may appear to have increased sales, debilitating return rates from the chains threatened the stability of all the players in the supply chain. Returns from Indigo were \$1,744 (or 22% of gross sales) for 1998–1999, and \$2,999 (or 27% of gross sales) for 1999–2000, well below the return rates for Chapters and Chapters small-format stores, which returned 28% of gross sales and 130% of gross sales in 1998–1999. In 1999–2000, Chapters big-box locations returned \$26,598 worth of Talonbooks—an increase of 62% over 1998–1999 and 38% of gross sales.

Figure 7. Chapters and Indigo Gross Sales, Returns, and Net Sales Comparison



Talonbooks certainly didn't see twenty times more books being ordered online to make up for any losses on the chains' bricks-and-mortar front. The company continued to struggle with Chapters' databases, and many of Talon's key titles were erroneously listed as unavailable or not yet in print throughout the Christmas season. However, the potential of online sales confirmed by other publishers, Talonbooks made efforts to improve its side of the operation and develop a plan to create a database-driven website capable of e-commerce in order to capitalize on the special-order gap created with the demise of key independent bookstores. New Star Books didn't see twenty times more books being ordered online during the Christmas 1999 season either. Nor did publisher Rolf Maurer believe they would: "Amazon replaced mail order; they've never been a significant portion of book retail sales, and they'll never be more than 10 or 15%. In fact, I don't think that all online book retailing will ever be more than 10 or 15% of sales."¹²⁷

The biggest sales impact came, surprisingly, from the diminishing category of Chapters' small-format stores, dozens of which had been closed since the merger. From net-negative sales in 1998–1999, Talon's sales to small-format stores exploded in 1999–2000 to \$12,763—representing the largest percentage of sales to the superstore chains at 20% of net sales. The difference was primarily due to Talonbooks' 20-title list for 1999–2000, which included *Lions Gate* by Lilia D'Acres and Donald Luxton. The combination of high production values, historical photos, architectural insight, and the intriguing stories surrounding this iconic, historic landmark made *Lions Gate* a bestseller, and for the first time since the Coles/SmithBook merger, Talonbooks had produced a title suitable for the mall-format stores and equally appealing to independent bookstores. That is not to say that Talonbooks had shifted its editorial focus in order to appeal to the "new economy" of the book trade: Talonbooks had previously published many diverse regional titles (such as *A Guide to B.C. Indian Myth & Legend* by Ralph Maud, *Too Good To Be True: Alcan's Kemano Completion Project* by Bev Christensen, and *Vancouver: A Visual History* by Bruce MacDonald), as well as several photographic titles (including *Bridges of Light: Otto*

¹²⁷ Interview with Rolf Maurer, August 2004.

Landauer of Leonard Frank Photos, 1945–1980 and *An Enterprising Life: Leonard Frank Photographs 1895–1944* by Cyril E. Leonoff, and *Hidden Cities: Art & Design in Architectural Details of Vancouver and Victoria* by Gregory Edwards). At \$29.95, the cloth-bound *Lions Gate* was a good fit for the mall and airport locations of Chapters' contract stores in B.C. The book made a big impact on Talonbooks' bottom line during troubling times; Talonbooks sold over 1,200 copies in less than six months. The profile of the best seller was further augmented by its win of the City of Vancouver Book Award. Unfortunately, because of looming hidden factors at Talonbooks' distributor, GDS, the success of *Lions Gate* in 1999-2000 did not parlay into security, even temporarily, for Talonbooks.

2001: COMPETITION AND MONOPOLIZATION

Late in the summer of 1999, the Federal Government announced its plan to make the DCH responsible for reviewing foreign investment in Canadian cultural industries. But first the DCH had to address home-grown concerns. In February 2000, the DCH formed a committee to review the book publishing industry in Canada. The Standing Committee on Canadian Heritage was convened to address the allegations from independent bookstores that Chapters was attempting to put them out of business and the concerns of publishers, bookstore owners, and authors that Pegasus was using strong-arm tactics to monopolize Canadian book wholesale and distribution channels. Over 60 people and organizations appealed to the Committee during the seven months of research and hearings,

“...one of the most interesting of which, according to the all-party members of the committee, consisted of a brief called *The Emperor’s New Clothes* which [I] had written and presented to the Committee for the LPG—a brief which contained much of the same business analysis of Chapters as that presented in this paper; remained critical of the BCP for having approved the merger of Coles and SmithBooks; and presented the committee with dire predictions for the future of the Canadian book trade unless something were immediately done to regulate Chapters.”¹²⁸

In June of 2000, the Standing Committee on Canadian Heritage submitted their findings and recommendations to Heritage Minister Sheila Copps in a 109-page document, *The Challenge of Change: A Consideration of the Canadian Book Industry*. The report suggested 25 recommendations to strengthen the Canadian book trade and acknowledged that “the issue that probably generated the most heat during the Committee’s hearings was the relationship between the book retailer Chapters and the book wholesaler Pegasus,” but believed that the concerns of the witnesses fell under the jurisdiction of the BCP.¹²⁹

¹²⁸ Karl Siegler, editorial addendum to this report, September 2006.

¹²⁹ Canada. Standing Committee on Canadian Heritage. *The Challenge of Change: A Consideration of the Canadian Book Industry*. [Ottawa] Canadian Heritage, 2000. Committee chair was Clifford Lincoln. [Cited November 12, 2001.] <<http://www.parl.gc.ca/InfoComDoc/36/2/HERI/Studies/Reports/heri01-e.html>>

Regarding “The Chapters/Pegasus Question,” the report states:

When asked about [an amendment to the Competition Act setting out a review of any structural features in an industry that would diminish the opportunities for small and medium-sized firms to operate and the Canadian Bookseller Association’s recommendation that the government force Chapters to divest itself of Pegasus] a senior official from the Department of Heritage responded:

‘I would say that the argument that there’s a need to break-up or tear down or do something about Chapters or Pegasus has not been made. And my own view is that if there is anti-competitive or anti-consumer behaviour, the existing Competition Act can deal with it.’

The Committee notes, however, that it has neither the tools nor the authority to determine if these companies are in contravention of the Competition Act. Indeed, as one Committee member indicated in response to this matter:

‘It is not for the committee to say or declare whether anyone in the book industry is guilty of unfair competition... because we have neither the authority to do so nor the authority to conduct an investigation.’¹³⁰

Elsewhere in the document, the report states that while “the Committee appreciates and understands the many concerns witnesses have voiced with regard to the issue of competition, market share and vertical integration in Canada’s book industry... it agrees with the position of the Department of Canadian Heritage and reminds the reader that the Department does not focus on issues of competition.”¹³¹ In other words, the BCP had already decided upon Chapters’ fate, and the DCH was woefully unequipped and unwilling to do anything about helping publishers survive “the challenge of change.” It was a huge disappointment and setback, and it occurred (or failed to occur) just as Talonbooks was on the cusp of its greatest challenge.

Both the issues of ownership and of industry consolidation are ongoing concerns with Siegler, who has been actively involved in public policy work on behalf of his industry organizations (the ACP and the LPG) since 1975. As two-time president of the

¹³⁰ Ibid. [Chapter Six: Considerations for the Future, section D: The Chapters/Pegasus Question]

¹³¹ Ibid. [Chapter Three: Distribution: Wholesale and Retail, section B: Relevant Legislation, part ii: Vertical Integration]

ACP and co-founder and much more frequent president of the LPG, Siegler has consistently pursued the issues of consolidation, market dominance, and ownership in the Canadian book trade on behalf of all Canadian-owned publishers, and especially on behalf of its 40 Canadian-owned literary publishers collectively, as well as independently as the president and publisher of Talonbooks. Unfortunately, now in the midst of one perilous industry situation, Talonbooks was forced to deal with a very specific manifestation of that issue: the downfall of General Distribution Services.

The Fall of General Distribution Services

In a letter to publishers in February 2000, Jack Stoddart explained that in January, “Chapters debited back returns of \$4.3-million rather than paying its bills. At the same time, returns from independents exceeded ‘any year in memory.’ In total, returns ‘have been nothing short of astonishing.’”¹³² In addition, GDS’s financial backer, the Finova Group, sought bankruptcy protection and GDS lost access to its credit line. But the troubles for GDS started long before the month of “astonishing” returns in 2000, and were more than the effects of a bullish superstore chain. In an industry that survives on the tiniest of margins, GDS failed in a flurry of major logistical and tactical errors initiated when Jack Stoddart apparently staked his companies’ success on that of Chapters. In 1998, GDS moved from an 85,000-square-foot warehouse space (which it owned and sold) to a new 300,000-square-foot leased warehouse in Toronto in an effort to position itself for dominance in the Canadian book distribution industry, but it never filled the extra space it had acquired through this move. Even after that Toronto debacle, GDS also moved its Vancouver warehouse to new facilities in 2000 (which weren’t operational until months later due to run-ins with city bylaws and building regulations), only to have to close them permanently in April 2002. There were computer problems with the system GDS spent \$2 million to upgrade, while the company was still being sued

¹³² Anderson, Scott. “Heritage may help GDS clients through cash crunch: But at least one publishing executive is calling for a longer-term solution.” *Quill & Quire*. Vol. 67. no. 4 (April 2001), p. 4.

for payment to ready their systems for Y2K.¹³³ An affidavit filed by Stoddart reveals the tally of GDS's fall: billing \$87-million in 2001, and reaping \$6.5-million, or 7.5%, in profit. So while profitable, GDS was unable to maintain operations without sustainable cash flow, either from its credit providers, or from clients like Chapters, or both.

Pegasus, the wholesale operation with heavy investment from Chapters, received a chilly reception when it was announced in the fall of 1998, not only from publishers and booksellers—and the attention of the Standing Committee on Canadian Heritage—but from Canadian distributors, retailers, and librarians. With the wholesale/distribution arm of Chapters continuing its incursion, bulk orders and increased discounts changed the competitive environment in Canadian book distribution, which already operated on margins as slim as that of publishers. GDS began aggressively signing distribution agreements with smaller Canadian presses in the summer of 1999 in an attempt to maximize his newly expanded warehouse space with its newly unionized staff, and the processing capacity of this substantially larger (and much more costly) facility they had acquired.¹³⁴ *Quill & Quire* identified GDS's predicament in July 1999: "the distributor that may be most squeezed [by Pegasus] is General, which has long refused to offer smaller Canadian wholesalers the standard 50% discount, but now finds itself with little choice but to do business with a very large one. Asked whether his terms may change now that Pegasus has entered the scene, Jack Stoddart said that his company does an annual review in July. Until then Stoddart's wholesale discounts will remain at 48%. 'I'm not saying we will change or we won't, but we can't offer them 50% until we review. And if we do change, we'll have to offer the new discount to everyone.'"¹³⁵ Negotiations with Pegasus regarding discounts and a limit on returns were at a standstill with many publishers during 1999–2000, but slowly publishers began to sign on at the 50% discount demanded by Pegasus. Very few opted out completely, choosing not to have their profit

¹³³ Anderson, Scott. "Days of Reckoning for General Publishing: Distribution business will be jettisoned, sources say." *Quill & Quire*. Vol. 68. no. 6 (June 2002), pp. 5-6.

¹³⁴ Lorinc, John. "The Pegasus Effect: How the new national wholesaler will change the face of the trade." *Quill & Quire*. Vol. 65, no. 7 (July 1999), p. 8.

¹³⁵ *Ibid.*

margins further depleted, but it appeared none had successfully negotiated a limit on returns. The negotiating power of GDS's client publishers was diminished when in the fall of 1999, astonishingly, Stoddart signed on his publishing houses, Stoddart and General Publishing, with Pegasus.¹³⁶ What's more, GDS reduced warehouse fees to client publishers who dealt with Pegasus, purportedly because, Stoddart stated, "it's a reduction in costs to us, so we're passing that on."¹³⁷ The final factor for many hold-outs was Pegasus' threat: "This week [early October 1999] we're beginning to segregate the merchandise we're preparing to return," stated Pegasus' Dennis Zook, alluding to the company's decision not to purchase Chapters' stock returns from companies that are unwilling to do business through Pegasus.¹³⁸ The next month, *Quill & Quire* reported that holdouts Raincoast Books, Thomas Allen & Son, and HarperCollins Canada had agreements in place, leaving very few publishers unsigned and Pegasus' success in dominating the wholesale book business virtually assured.

General Distribution Services couldn't blame its woes on Pegasus alone. Arsenal Pulp Press gave the distributor notice after a year of "slow and incomplete order fulfilment, inaccurate sales and inventory-level reports, and concerns over a new clause in distribution contracts relating to returns," and the move to a new 300,000-square-foot warehouse that "wasn't smooth, and glitches related to a new phone system led to a rocky Christmas season marred by inconsistent customer service and missed orders...a successful unionization drive...[and] high turnover caused by the move."¹³⁹ The fear for the client publishers that remained, including Talonbooks, was not only whether GDS could restore its customer service to an acceptable level, but concerns over "new returns-reserve arrangements that would have allowed General to factor the anticipated cost of returns into his monthly sales payments by deducting an average amount based on his

¹³⁶ Weiler, Derek. "Pegasus in standoff with publishers over terms: Trade balking at wholesaler discount." *Quill & Quire*. Vol. 65, no. 10 (October 1999), p. 5.

¹³⁷ Weiler, Derek. "Pegasus standoff continues: Publishers brace for shipments of returned stock." *Quill & Quire*. Vol. 65, no. 11 (November 1999), p. 4.

¹³⁸ *Ibid.*

¹³⁹ Toller, Carol. "GDS distribution woes prompt publisher outcry: Chairman Jack Stoddart vows service is improving." *Quill & Quire*. Vol. 66, no. 5 (May 2000), p. 5.

previous year's returns."¹⁴⁰ The arrangement would have client publishers assume part of the fiscal responsibility for returns which, according to Jack Stoddart, became necessary because "distributors need to watch their own cash flow more closely now that Chapters holds so much inventory and can send back a flood of returns with no warning."¹⁴¹ In 1992, publishers with the LPG had arranged a group distribution deal with GDS, Canada's largest distributor at the time. Incensed by Stoddart's new demands, the LPG discussed the issue with Jack Stoddart present at their annual general meeting in June of 2001, and again, without Stoddart present, at a Special General Meeting the LPG called specifically on this issue on December 9, 2001. The heated debates of these meetings concluded with the agreement that members, including Talonbooks, would have to explore other distribution arrangements—something that Mike O'Connor of Insomniac Press had begun on the LPG's behalf prior to moving to Publishers Group West (PGW) as of June 1, 2000. On December 18, 2001, Talonbooks gave official notice of termination to GDS, citing non-payments of their accounts, and signed a new distribution agreement with UTP, to begin January 1, 2002. While this move protected Talon's inventory held in the two GDS warehouses by having it transferred to UTP in January 2002, it still left Talon vulnerable to some \$114,000 in uncollected accounts receivable for its 2001 net sales from GDS that it would lose completely when GDS was finally officially declared bankrupt in August of 2002. A month earlier, in November of 2001, New Star Books had given notice to GDS, effective May 1, 2002, but it was caught in a situation where its distribution agreement expired. Although New Star was then able to do their own distribution, it had no access to their stock, which was tied up in the GDS warehouse during the bankruptcy proceedings, and also got hit with a double whammy of returns when clients returned New Star books directly to them because it was changing distributors—all this along with receiving ongoing high returns from Chapters as the company tried to improve its financial position. The GDS extended bankruptcy proceedings seriously and almost fatally interrupted the cash flow of Talonbooks and New

¹⁴⁰ Ibid.

¹⁴¹ Ibid.

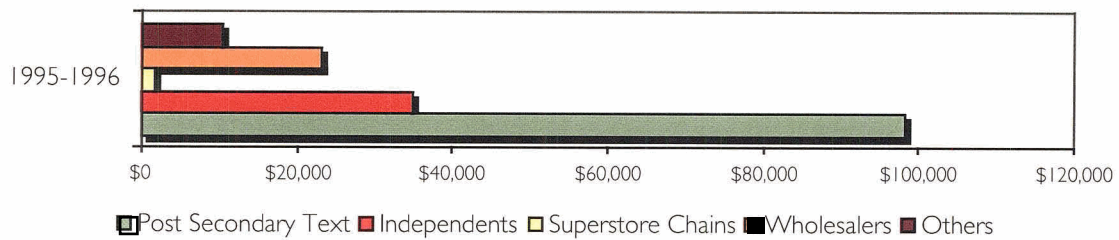
Star Books. By the end of the 2000–2001 fiscal year, small presses were left in a precarious state, again. In this era of mergers, acquisitions and big business, where would 40 small, literary presses find a home—in which bookstore, via which wholesaler, through which distributor, and when—and would the margins remaining in their new circumstances be sufficient for their recovery and survival?

Talonbooks Downsizes (Again)

Talonbooks continued to occupy the windowless concrete offices in GDS's Vancouver warehouse from 1996 until June of 2000, where it maintained a very good relationship with Jack Stoddart and GDS. However, the returns epidemic not only caused a crisis of confidence in the book trade, but a severe lack of cash flow to GDS clients also ensued. GDS withheld payment from publishers while it attempted to clear its backlog of unprocessed returns and resolved (or ignored) disputes regarding illegal returns. The relationship between Talonbooks and GDS deteriorated irrevocably. Karl and Christy Siegler moved from their home in Burnaby to Powell River (five hours' drive from Vancouver), relocating their editorial office, though not yet their inventory, from the GDS warehouse in Burnaby. Their sole employee, Shyla Seller, now maintained the company's sales and marketing department in a 100-square-foot space within the offices of Arsenal Pulp Press and *Geist* magazine in downtown Vancouver, taking over Talonbooks' top trade accounts, selling and billing them directly around GDS in order to maintain Talon's liquidity in a situation where its monthly payments from GDS became increasingly delayed.

In the midst of the chaos, a normally stable customer category, post secondary gross text sales increased to \$179,226 in 2000–2001, up 4.6% in 1999–2000, and, like in other customer categories, returns increased too. Returns from the college sector amounted to \$53,185, representing more than half of all returned books (\$105,496) for that year and 29.7% of gross sales. In terms of a percentage of gross sales, returns had remained fairly consistent over previous years, (29.4% in 1995–1996, 26% in 1996–1997, 29.7% in 1997–1998, and 29.4% in 1998–1999 and 24.1% in 1999–2000), but in terms of volume, \$53,185 was an astounding amount to process.

Figure 8. Talonbooks' Canadian Net Sales by Category, 2000–2001



“After having provided Talonbooks with five years of continuous growth, independent bookstores *appear* to have decreased their orders by 26.3% in 2000-2001, but this is an illusion. In response to the clearly visible coming disaster of the GDS bankruptcy and its early-warning signs of ever slower and delayed payments to its clients, Talonbooks had been reducing their new title output by 22.5%, moving from 20 titles in 1998-1999, to 18.5 titles in 1999-2000, to 15.5 titles (once again) in 2000-2001.”¹⁴² The returns from independents however also decreased to the lowest point during the period of this study, down 35.8% from 1999–2000 to a mere \$10,461. Talon’s resulting net sales to independents were down 23.6% from \$57,702 in 1999–2000 to \$44,071 for 2000–2001, which, Karl Siegler points out, “mirror[s] almost exactly, (once again) Talonbooks decline in new title output in this period.”¹⁴³

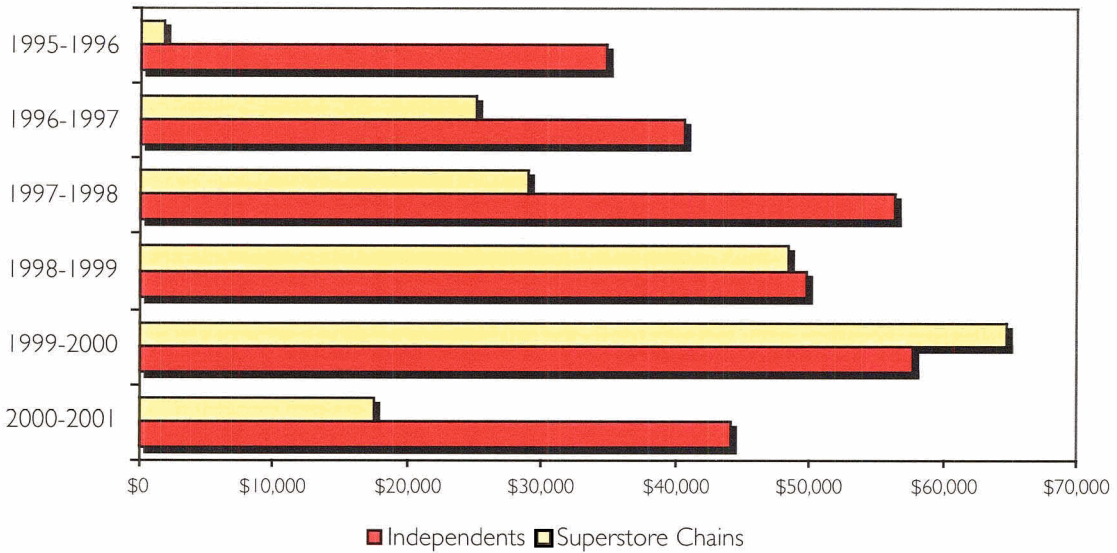
Overall, however, Talonbooks’ returns from independents decreased 33.7% and net sales increased 26.4% over the entire period of this study. When one considers the dramatic decline in the number of independent bookstores since Chapters first entered the marketplace in 1995, these remarkable figures attest to the strength of those independents remaining and their ability to scull-through to their readers Talonbooks’ literary list. “They also attest to Talonbooks’ abiding faith that there would always be a market for quality Canadian literary work,” said Karl Siegler, “No matter what upheavals and dislocations the retail structure of the Canadian marketplace might experience from

¹⁴² Karl Siegler, editorial addendum to this report, September 2006.

¹⁴³ Karl Siegler, editorial addendum to this report, September 2006.

time to time.”¹⁴⁴

Figure 9: Talonbooks’ Canadian Retail Net Sales, 1995–1996 to 2000–2001



Gross sales to the superstore chains sank from \$95,913 in 1999–2000 to \$49,006 in 2000–2001, but that is not to say that the superstores found less to return: another \$31,432 in returned books made their way back to the warehouse, 64.1% of gross sales.¹⁴⁵ Accordingly, Talonbooks’ net chain sales plummeted to \$17,574 in 2000–2001 (from the all-time high of \$64,789 in 1999–2000). Chapters’ vertically integrated wholesale unit, Pegasus, wreaked havoc on the wholesale sector: gross sales reached a high of \$40,611 in 2000–2001, but returns increased accordingly, up to 15.3% of gross sales. While that does not sound astronomical, it is an extraordinary hike for this normally stable customer category. Wholesalers prior to the creation of Pegasus posted return rates of only 8% in 1995–1996, 5% in 1996–1997, 6.3% in 1997–1998, 5.6% in 1998–1999 and 7.8% in 1999–2000 for Talonbooks’ titles. In less than three years, Pegasus had managed to precipitate the downfall of Talonbooks distributor and, simultaneously, send the publisher

¹⁴⁴ Karl Siegler, editorial addendum to this report, September 2006.

¹⁴⁵ Karl Siegler maintains that these gross sales figures were heavily overstated by GDS.

the highest rate of returns ever seen from a wholesaler. It seemed the fears publishers and booksellers had presented to the DCH in 1999 and to the Standing Committee on Heritage in 2000 had been well founded, albeit ignored. Ironically, Pegasus was less the winged horse ridden to fight the Chimera in Greek mythology than it was an aspect of the Chapters chimera; but in the end even Chapters began circumventing its own wholesaler, Pegasus, asking publishers to ship directly to stores.

The Indigo Takeover

With the survival of many publishers riding on a successful fall and Christmas season, anxiety dominated in 2000, as highlighted *Quill & Quire* articles like: “The fate of the fall season: Chapters’ shift in retail strategy has publishers guessing,” and “Pegasus problems cast shadows over Xmas season: Publishers ask to ship directly to Chapters stores.”¹⁴⁶ It didn’t appear that Indigo was going to provide any relief either. Seemingly in an effort to keep pace with Chapters, Indigo made adjustments to its business practices, first by eliminating a management layer. As the company had not yet gone public, most of the business’s strategy was subject to conjecture: an article in *Quill & Quire* speculated that “while Indigo recently raised \$30-million in a private placement and plans to use the funds to open two new superstores this year [2000] in Vancouver and Edmonton and re-launch its website at the end of the summer, such highly visible cutbacks, together with a bevy of other organizational changes, suggest that the cash crunch afflicting Chapters may be sweeping over its smaller rival. Some publishers have noticed, for example, that Indigo is holding up payments.”¹⁴⁷

Publishers were desperate for something to dramatically change the retail marketplace, but perhaps few had anticipated the events that began to unfold when, on

¹⁴⁶ Chapters itself asked publishers to by-pass Pegasus, requesting that HarperCollins Canada, Random House of Canada and H.B. Fenn ship directly to stores beginning in September. (Crawley, Devin. “They shoot horses, don’t they? New questions raised about the fate of Pegasus, as publishers continue to bypass the struggling wholesaler.” *Quill & Quire*. Vol. 67, no. 1 (January 2001), p. 5.

¹⁴⁷ Crawley, Devin. “Industry divided on returns issue: Not our problem, say independents.” *Quill & Quire*. Vol. 66, no. 9 (September 2000), p. 4.

November 28, 2000, Trilogy Retail Enterprises, a private limited partnership headed by Heather Reisman and Gerry Schwartz, made an unsolicited bid for Chapters, offering \$63.5 million for 50.1% of Chapters (it already owned 9.5% of Chapters' shares). In a conference call, "Schwartz told analysts that combining and 'right-sizing' the operations of Indigo and Chapters is the only way to turn a profit. He said that some stores that are currently losing money would be profitable without competition between the two chains."¹⁴⁸ The commentary was reminiscent of Stevenson's claims about Coles and SmithBooks in 1995. Neither Reisman nor Schwartz commented on how such a takeover and restructuring might shake out, nor on the fate of the Chapters brand, Pegasus, or the mall stores. Investors responded quickly: the day of the offer for 4.88 million shares at \$13 apiece, Chapters' stock traded at \$9.10; encouraged by the news, stock jumped by \$2 the next day. Chapters CEO Larry Stevenson was not pleased by the offer, however, and the board of directors of Chapters Inc. released a statement later that day calling the bid "totally inadequate" and saying it "creates substantial uncertainties for shareholders."¹⁴⁹

The publishing community responded quickly too. Some publishers expressed relief, hoping that an Indigo-led mega-chain might be better managed than Chapters and alleviate the stress of returns and late payments. Other publishers believed that the new chain would have too great a hold on the retail market share and would use that power to behave as badly as Chapters, perhaps even worse. According to Trilogy's Gerry Schwartz, the combined retail chain would represent 30% of the total Canadian book market—27% for Chapters, 3% for Indigo—thus would slide under the BCP's 35% ownership threshold and its jurisdiction. However, StatsCan's 2000/2001 survey of the book industry listed the chains' market share as 37% of English-language publishers' sales and *Quill & Quire* estimated "the combination of Canada's two largest book retailers would create a giant with at least 50% of the English-language Canadian retail trade

¹⁴⁸ CBC News Online. "Chapters posts profits of \$17.2 million." CBC News [online], June 1, 2000. [Cited November 12, 2001.] <cbc.ca/cgibin/templates/view.cgi?category=Business&story=/news/2000/06/01/chapters00060>

¹⁴⁹ Ibid.

book market.”¹⁵⁰ With Chapters clearly ailing, speculation that foreign interests—specifically, American—would be considered by Investment Canada sparked fears among many. Amazon.com had already announced intentions of setting up a dedicated Canadian website and, in order to fall within Canadian investment law, established a majority Canadian-owned distribution site arrangement for fulfilment.

On December 8, 2000, Chapters CEO Larry Stevenson announced a \$25.5-million plan to buy back ownership and control of the Chapters.ca online operation from minority shareholders, and Pegasus book distribution from Canadian General Capital Ltd. At the end of the month, the retailer issued a forecast predicting an operating profit of \$60.8 million on revenue of \$770 million by March 2001. Stevenson also unsuccessfully petitioned the Ontario Securities Commission to order Indigo to release its previously undisclosed financial records and warned shareholders that approval of the takeover would require “a giant leap of faith.”¹⁵¹ Meanwhile, Trilogy purchased more shares in Chapters, raising their stake from 9% to 10% (they would shortly increase their holdings to 14%), and raised their bid to \$15 for the outstanding shares they desired. Another player entered the game in mid-January. Supported by the Chapters board and executives, Future Shop bid \$200 million for all of Chapters, either \$16 cash or two Future Shop shares for each Chapters share, with a maximum \$100 million in cash. January 20, Indigo followed by upping the ante, raising the bid to \$17 a share for all of Chapters, worth \$121.5 million. Future Shop bowed out of negotiations, and on January 31, 2001, Chapters gave in to the “hostile” takeover and advised shareholders to accept Trilogy’s offer. On February 1, 2001, Trilogy acquired control of Chapters by adding a further 7,146,000 shares to the 1,641,894 shares already purchased, resulting in ownership of 70.5% of the company’s outstanding shares.¹⁵²

¹⁵⁰ Anderson, Scott. “It’s a chain-eat-chain world: Indigo makes a play for Chapters, while the trade waits and worries.” *Quill & Quire*. Vol. 67. no. 1 (January 2001), pp. 4-6.

¹⁵¹ *Ibid.*

¹⁵² Indigo Books & Music Inc. “About Our Company.” [chapters.indigo.ca](http://www.chapters.indigo.ca) [online]. [Cited November 12, 2001.] <<http://www.chapters.indigo.ca/article.asp?artcode=chaptersinc&Section=home&Cat=&Lang=en>>

Merger Opposition

Some booksellers and publishers were vehemently opposed to the merger. The official avenue and, indeed, the only recourse available to challenge the deal, was the BCP's Tribunal. Of course, the BCP was the same entity that approved Stevenson's merger of Coles and SmithBooks to create Chapters in 1995. While the merger would not be prohibited, on April 18, 2001, the Commissioner of Competition drafted a Consent Order. To ease concerns about a book retail monopsony, or, according to the Tribunal, the "alleged substantial lessening of competition,"¹⁵³ the Consent Order stipulated a code of conduct and directed the divestiture of 13 large-format book superstores, ten mall stores, Indigo's distribution centre, and a portion of Indigo's online assets.

While three parties (Talonbooks, the Book Shelf in Guelph, Ontario, and Tanners Books in Sidney, B.C.) filed official and formal interventions with the Tribunal expressing their deep reservations about the Consent Order, and presses Key Porter, Groundwood Books, Fitzhenry & Whiteside, and Firefly also gave unofficial and anecdotal evidence, the major book industry associations—the ACP and the CBA—supported the Consent Order (albeit the CBA had reservations about divestitures rather than store closings). Many publishers, writers, and booksellers opposed the merger and rejected the terms of the Consent Order—in reading the filings with the Tribunal, there was reasoned, impassioned opposition to virtually every aspect of it—yet only nine submissions from the hundreds of stakeholders demonstrates the degree to which the industry feared Chapters' reproaches and clout or had acquiesced to the new monster book retailer reality. In fact, the overwhelming mood was of eagerness to move on: the letter from the ACP on behalf of its 140 publisher members urged "swift resolution."¹⁵⁴ In response to overwhelming support (or silence), the Tribunal issued the Consent Order on June 6, 2001. Trilogy

¹⁵³ Canada. Competition Bureau. *Commissioner of Competition v. Trilogy Retail Enterprises LP. / Chapters (CT-2001/003)*. (Online). Available <http://www.ct-tc.gc.ca/english/cases/ct-2001-003/trilogy.html> [May 1, 2004].

¹⁵⁴ Karl Siegler notes that "Talonbooks, the only publisher in Canada who had filed a formal intervention with the Competition Tribunal, had not been a member of the ACP since 1998, in part because the ACP, presided over at the time by its president Jack Stoddart, had refused to ask the BCP for an extension to its three-year conditional approval of the Coles SmithBooks merger that had created Chapters in 1995."

officially and legally merged Chapters and Indigo on August 14, 2001.

SURVIVAL REDUX

Combined, the Chapters-Indigo chain represented 92 of 96 Canadian book superstores, 231 small-format bookstores, and the only two Canadian online book retailers of significance. While the deal was approved, the BCP conceded that the mega-chain would lessen competition, thus subjected the merger to several provisions agreed to by the parties in the Consent Order. Requirements included the divestiture of nine Chapters and four Indigo superstores, ten small-format mall bookstores, the Indigo distribution centre, and the indigo.ca online store, which the BCP believed would “encourage expansion or new entry by other booksellers, thereby maintaining choices for consumers and competition in the book industry.” Further, Trilogy had to adopt a mandatory five-year code of conduct that stipulated fair trade practices with publishers. Could the newly merged Chapters-Indigo book behemoth finally stabilize the industry, as supporters of the \$122 million deal hoped, or would the shift from oligopsony to virtually monopsony further exploit Canadian independent publishers’ vulnerabilities?

The Failure of the Consent Order

Those worried by the deal recalled Reisman’s initial attempts to enter the big-box book business hand-in-hand with mega-chain Borders, and worried Reisman could use her recently purchased market clout to open the doors to American book retail interests. In the years following the merger, Siegler, Maurer, and other concerned publishers noted with dismay—but not surprise—that Indigo failed to meet the requirements of the Consent Order. Siegler clearly and vehemently opposed the code of conduct, characterizing it as a charade devoid of any means of enforcement.¹⁵⁵ As Siegler’s submission to the BCP stated:

¹⁵⁵ Siegler, Karl. Re: “Draft Consent Order” of April 18, 2001, in the matter of Chapters/Indigo/Trilogy, filed with your Tribunal on that date by the Commissioner of Competition [letter]. May 8, 2001. Filed as article 17a by the Registrar of the Competition Tribunal, Ottawa. (The collected documents of the Tribunal are available online at: www.ct-tc.gc.ca/english/cases/ct-2001-003/trilogy.html)

The ‘divestiture’ order issued by the BCP involving 13 superstores and 10 mall stores of the newly merged Indigo/Chapters/Trilogy organization, along with the order to sell its “distribution facility” (the former Pegasus) does nothing but attempt to virtualize the marketplace conditions which existed prior the Bureau’s approval of this merger. Each of these 13 superstores was either not profitable and/or redundant pre-approval because of the ongoing head-to-head competition between Chapters and Indigo.... Whom, exactly, does the Bureau think it’s fooling in its pretence that any credible, competitive buyer will ever be found for these unprofitable and/or redundant superstores; these unprofitable and/or redundant mall stores; and this unprofitable wholesaler? And in the absence of such a credible buyer, what will happen to these operations? Market forces will dictate that they eventually be closed. And all competition for Chapters will have been eliminated and its hegemony in the retail marketplace will have been re-enforced with the assistance of the Competition Bureau. It would be difficult for the average Canadian citizen, much less a participant in the Canadian book trade, to imagine a more perverse inversion of the mandate in any federal government agency which the conditional approval of this merger by the Competition Bureau manifests.¹⁵⁶

Trilogy’s search for a buyer was unsuccessful, as was that of the trustee who assumed responsibility for the sale as per the Consent Order (who had reportedly approached 288 prospective buyers).¹⁵⁷ The assets on offer clearly represented the least appealing of Indigo’s stores and brands: “an important contribution to the lack of interest from Canadian purchasers was the Bureau’s decision not to insist on a larger divestiture package in order to create a competitor with the critical mass to compete effectively against Chapters/Indigo. Indeed, during the Consent Order approval process, the Bureau actively rebuffed the submissions of intervenors [including Siegler] who argued that the assets in the divestiture package were ‘unlikely to be sufficiently profitable to be attractive to a purchaser.’”¹⁵⁸ Despite Indigo’s claims at the outset of their hostile takeover

¹⁵⁶ Siegler, Karl. Re: “Draft Consent Order” of April 18, 2001, in the matter of Chapters/Indigo/Trilogy, filed with your Tribunal on that date by the Commissioner of Competition [letter]. May 8, 2001. Filed as article 17a by the Registrar of the Competition Tribunal, Ottawa. (The collected documents of the Tribunal are available online at: www.ct-tc.gc.ca/english/cases/ct-2001-003/trilogy.html)

¹⁵⁷ McMillan Binch LLP. *Canadian Antitrust Report*, “Chapters/Indigo: A Failed Divestiture Remedy.” March 2002, [Online] [Cited November 25, 2005]. http://www.globalcompetitionforum.org/regions/n_america/canada/CAR_Chapters_Indigo_Spring%202002.pdf.

¹⁵⁸ McMillan Binch LLP. *Canadian Antitrust Report*, “Chapters/Indigo: A Failed Divestiture Remedy.” March 2002, [Online]

that there wasn't enough room for all of Chapters' and Indigo's stores in the Canadian book retail market, the failure to find a buyer was fodder for Reisman's protestations about the culturally protectionist laws prohibiting foreign ownership of book retailers and distributors.

The Consent Order also stipulated a limit on returns, albeit at 42% for the first 12 months after the Consent Order took effect and 30% thereafter. But with store closures and Indigo's diminishing reliance on books as a part of its marketing mix, the company would rely on heavy returns often exceeding these guidelines. In her report to shareholders in the fall of 2004, Reisman announced her "plan for the bookstore megachain's solvency is to transform it into a chain of 'cultural furniture stores'. Books will occupy no more than 65% of the floor space and will account for about the same percent of sales—or less, if possible. That's down from the current 80–85%. Insider intelligence suggests that a key element in the plan is to reduce the number of titles per store to 15,000. No doubt some marketing genius has mathematically demonstrated that this is the right number of titles to have in stock for maximum turnover and profit."¹⁵⁹ Siegler had predicted this in his letter to the BCP, stating:

"Given that the pre-merged Chapters had already started a process of 'product diversification' in its superstores into 'non-book items' in the third quarter of 2000; and given further the repeated public statements by the CEO of the newly merged Chapters/Indigo/Trilogy that it is her ambition not to operate these superstores primarily as bookstores but as 'cultural supermarkets,' it is very clear that the newly merged chain will contain not just books and periodicals, but also CDs and DVDs, possibly new and alternate media, and, specifically, 'flowers.' This will create a situation in which these superstores will evolve much like the big-box 'drugstore' chains have. The sale of books, the original 'purpose' of these stores, will be increasingly marginalized in these stores until their book sections are not significantly larger than the mall chain stores which the

[Cited November 25, 2005].

http://www.globalcompetitionforum.org/regions/n_america/canada/CAR_Chapters_Indigo_Spring%202002.pdf.

¹⁵⁹ Lockheed, Gordon. "Translating Heather;" Dooney's Café [Online] [Cited November 25, 2005]

<http://www.dooneyscafe.com/modules.php?op=modload&name=News&file=article&sid=391&mode=thread&order=0&hold=0>

same organization operates. Within the ten years since 1995, the current Consent Order of the Competition Bureau will have effectively stripped the Canadian book trade of the diversity of selection among book product available to Canadian consumers prior to the Competition Bureau's first merger approval in the matter of Chapters in 1995."

The imposed code of conduct also established fixed payment terms of a generous 110 days for the first 12 months of the Consent Order, 100 days for the next 24 months, and 90 days thereafter for the five-year period during which the Consent Order was valid. As Siegler responded, "Given the BCP's complete failure to either investigate or take action against the 'unlimited returns' policy Chapters has clearly granted itself for the past nine months, in contravention of the terms of trade under which it acquired its product, what credible reason does the Bureau have for granting to Chapters (and, by extension of its own rules, the entire Canadian retail book sector) payment terms which exceed by twenty days for the first year, and by ten days in the second year, the date by which any player in this sector can return to its suppliers any and all unsold product in lieu of payment? Given that Chapters has already reduced its inventory (and therefore its risk) well beyond the point allowed by its current suppliers' terms of trade, why are these 'extra' 20 and 10 days for payment 'needed' by the newly restructured and merged Chapters/Indigo/Trilogy?"

The Consent Order was breached in spirit—if not in practice—in other aspects too. A year after the Consent Order, the Western Canadian College Stores Association lodged a complaint with the BCP, alleging Indigo's violation of the agreement which ordered the company not to expand its retail chain until 2003. Chapters Campus Bookstores, in co-operation with U.S. chain Barnes & Noble, had been marketing to campus bookstores, encouraging them to turn over the management of their stores to Chapters.¹⁶⁰ The futility of the BCP and their inability to instate any regulation that would benefit the consumer or Canadian publishers creates uncertainty for the trade. As Maurer commented, "I think what we have to do is convince the government of

¹⁶⁰ McMaster, Geoff. "U of A bookstore joins complaint against Indigo," *Express News*, January 15, 2002. [Online] <http://www.expressnews.ualberta.ca/article.cfm?id=1718>

Canada—and that also means the people of Canada—that it’s a good thing that we have competition rules, and it’s a good thing that we have foreign investment rules, especially in the area of culture. We have to have rules in those areas and we have to enforce those rules, and that will begin to create a situation where there can be at least what we can call a level playing field for Canadian consumers as well as publishers and booksellers.” Under the auspices of regulation imposed by the BCP, it seemed it was business as usually for Chapters and Indigo.

The Indigapters Strategy

The only aspect of the superstore strategy which had represented any credible opportunity for independent publishers like Talonbooks was the stores’ ability to offer an huge selection of titles, thereby increasing the publishers’ market reach; that aspect had been dropped from Chapters’ strategy by their third year of operations, and never manifested itself credibly in Indigo’s plans. Chapters’ business development strategy was premised on delivering a customer-driven superior retail value proposition; achieving the leadership position in geographic markets, categories, and channels; executing better than competitors in the area of people, technology, and costs; and lead change by continually reinventing the organization.¹⁶¹ Indigo’s strategy, publicly, is to “provide a service-driven, stress-free approach to satisfying the booklover,” promising to be customers’ “most complete and trusted resource for books, music, gifts and much more.” This is not a new strategy by the company, which had named its first location Indigo Books, Music & More. Their statement goes on to assert “in the very beginning that we wanted to create a true booklovers’ haven—a place to discover books, music and more that might, in the rush of life, have gone undiscovered. A place that reflects the best of a small proprietor-run shop bundled with the selection of a true emporium.”¹⁶² Thus Indigo’s strategy varies

¹⁶¹ Stevenson, Lawrence N., Joseph C. Shlesinger and Michael R. Pearce. *Power Retail: winning strategies from Chapters and other leading retailers in Canada*. McGraw-Hill Ryerson, Toronto: 1999, pp. 14-28.

¹⁶² Indigo Books & Music Inc. “About Our Company.” [chapters.indigo.ca](http://www.chapters.indigo.ca) [online]. [Cited November 25, 2005.] <<http://www.chapters.indigo.ca/article.asp?artcode=chaptersinc&Section=home&Cat=&Lang=en>>

little from Chapters', except in one significant way: it openly and unabashedly positioned Indigo as "more" than a book store, but also a music and gift retailer with a heavy emphasis on a boutique shopping experience despite its superstore presence. And "nowhere in its current Consent Order did the Competition Bureau mandate a permanent, minimum degree of book selection in these superstores, at a level at least as broad as that available in the Canadian book trade prior to 1995, as a condition of approving this merger."¹⁶³ In pursuit on the big-box bookstore panacea, "Indigapters" has decimated the independent book trade; according to Maurer, "The number of independents that we could sell our books to collapsed in the 1990s. Studies were done that indicate that the number of book stores hadn't declined, but those studies included things like used book stores, and any place that sold books, or listed book selling as one of its functions. But practically speaking, in terms of ongoing businesses that are independent booksellers that we could make sales presentations to and get our books into, my sense is that the number of those out there that are available to us throughout B.C. in general and in Vancouver in particular has declined significantly in the last 10–20 years."

Will Indigo, now with six times as many superstores and 231 new small-format stores in its portfolio along with far more generous payment and returns terms, be more able to make the business model work than Larry Stevenson had been? Indeed, is the big box store a business model that could work for books in Canada at all? If the mega-chain business model fails or abandons books as its primary concern, Indigo will leave a literary market wasteland in its ashes, ripe for American book retailers to exploit. And there will be virtually no grounds left on which to exclude them, as there is no government will strong enough to prohibit them. The Indigo future looks bluer and bleaker than the Chapters past, as the chain has secured itself an effective monopsony in the Canadian retail book trade, unencumbered by any meaningful regulation, and has, in the process,

¹⁶³ Siegler, Karl. Re: "Draft Consent Order" of April 18, 2001, in the matter of Chapters/Indigo/Trilogy, filed with your Tribunal on that date by the Commissioner of Competition [letter]. May 8, 2001. Filed as article 17a by the Registrar of the Competition Tribunal, Ottawa. (The collected documents of the Tribunal are available online at: www.ct-ct.gc.ca/english/cases/ct-2001-003/trilogy.html)

managed to further undermine the stability of Canadian independent publishers, thus condemning New Star Books, and other Canadian-owned publishers to survival redux. “But perhaps, just maybe, not Talonbooks,” says Karl Siegler.

Having lost over \$114,000 of its unrecoverable net sales revenue in the GDS bankruptcy of 2001 (at the end of which it moved its distribution back to UTP), Talon once again surged back from the brink, increasing its new title production to 17, and posting a record before-tax profit in its fiscal/calendar year 2002 of \$191,410—68% more money than it had lost to GDS the year before. This remarkable and almost instantaneous recovery allowed Talonbooks to continue to revitalize its publishing program to the present day. By sticking purely to its principles and publishing only books of the highest literary calibre, Talonbooks had rebuilt its list to 21 new titles and its net sales to over \$400,000 by 2004, a level not seen since 1992, the year before it had begun its brief and disastrous two-year flirtation with a more populist sales approach and infrastructure, with Kate Walker & Co. as its sales representatives.

In its most recent fiscal year, 2005, Talonbooks, now distributed by Raincoast Books and sold by PGC in Canada, and distributed to its many export markets by Northwestern University Press using the world-wide services of the University of Chicago’s Distribution Centre, again published 21 new titles and showed growth in every one of its domestic and foreign market sectors except for the university and college book market. In the current year, 2006, Talon is publishing 20 new titles, but perhaps even more importantly, it is reprinting 26 of its enduring backlist titles—2 poetry, 21 drama, 1 literary fiction and 2 works of ethnography—this in a market environment where Canada’s “One Big Chain” currently accounts for approximately 70% of the Canadian retail book trade, but only 4.5% of Talonbooks’ total net sales annually.

In as much as it is true that Canada’s one big retail chain is an ongoing unfair competitive threat to all other booksellers, it is also clear that its threat to Canadian-owned publishers only remains real if those publishers cater to it and restructure their lists, their infrastructures and their terms of trade to primarily service Indigo/Chapters, and not primarily the readers of books.

As Talonbooks has so convincingly demonstrated from the outset about “The Chapters Effect,” Canada’s regulatory agencies and its book trade should just stick to the rules and the responsible traditional business principles of dedication to producing a good product for its citizens and its customers—*readers, not retailers*. Only when publishers return to working for and with their communities of discourse, rather than for speculative and manipulative venture-capitalists, yielding to the corporatist siren call of the kind of “power retailing” that MBA graduate Larry Stevenson and

socialite Heather Reisman so love to indulge in, all of the negative effects of The “One Big Chain” may well eventually regulate themselves out of the book trade.¹⁶⁴

¹⁶⁴ Karl Siegler, editorial addendum to this report, September 2006.

APPENDIX

Talonbooks' sales figures in this study are taken primarily from year-end reports from GDS, which have been categorized by customer group and by province. Sales figures are divided amongst customer categories to reflect the different markets that Talonbooks serves. The customer categories are based on the nine major categories established by the distributor. Post Secondary Text includes sub-categories for university text course adoptions, college text course adoptions, college and university library sales, and miscellaneous post-secondary sales. Independents includes anglophone independents and francophone independents—a misnomer carried over from the distributor, which refers to all independent bookstores in the province of Québec, not simply those that are primarily French language booksellers. The Superstore Chains category includes Chapters, Chapters' contract stores (Coles, SmithBooks, and The Book Company), and, after 1996, Indigo. Wholesalers are subdivided into general wholesalers, Pegasus, institutional jobbers, and specialty wholesalers. The remaining categories are Retailers Carrying Books, Libraries—Direct (the small number of library orders not placed through a wholesaler, thus primarily special orders), Individuals and Mail Order (later to include online sales from Talonbooks' website), ELHI (elementary and high school direct orders), and Corporate Sales. As Karl Siegler points out, “It is important to recognize that the Talonbooks financial year is based on the calendar year and is not synchronous either with the GDS financial year, July 1 through June 30; nor with the financial year for all of its granting agencies, which run from April 1 through March 31. The only year in which this re-categorization of Talonbooks' Canadian sales through GDS is misleading is in Talonbooks' highly anomalous calendar/fiscal year 1995, and this anomaly has been noted in the text for the reader. It goes without saying that none of Talonbooks' export sales are tabulated here, since ‘The Chapters Effect’ is an exclusively Canadian phenomenon.”¹⁶⁵

¹⁶⁵Karl Siegler, editorial addendum to this report, September 2006.

New Star Books' sales figures are compiled from the interview held with publisher Rolf Maurer and from a letter the publisher sent to the Mergers Branch of the BCP regarding the proposed Chapters and Indigo merger, submitted March 21, 2001.

Figure 10. Talonbooks' Canadian Gross Sales, 1995–1996 to 2000–2001

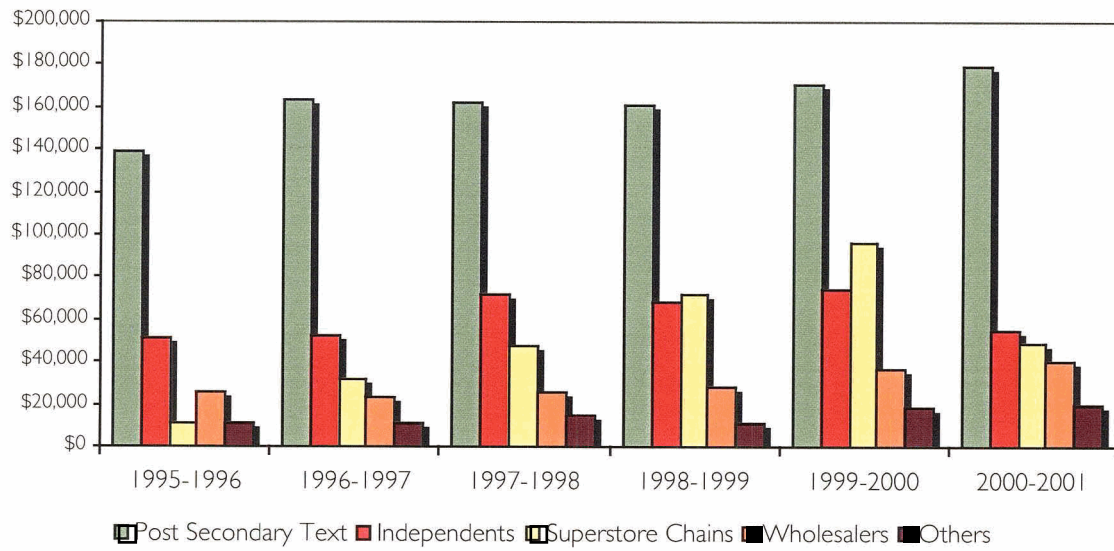


Figure 11. Talonbooks' Canadian Returns, 1995–1996 to 2000–2001

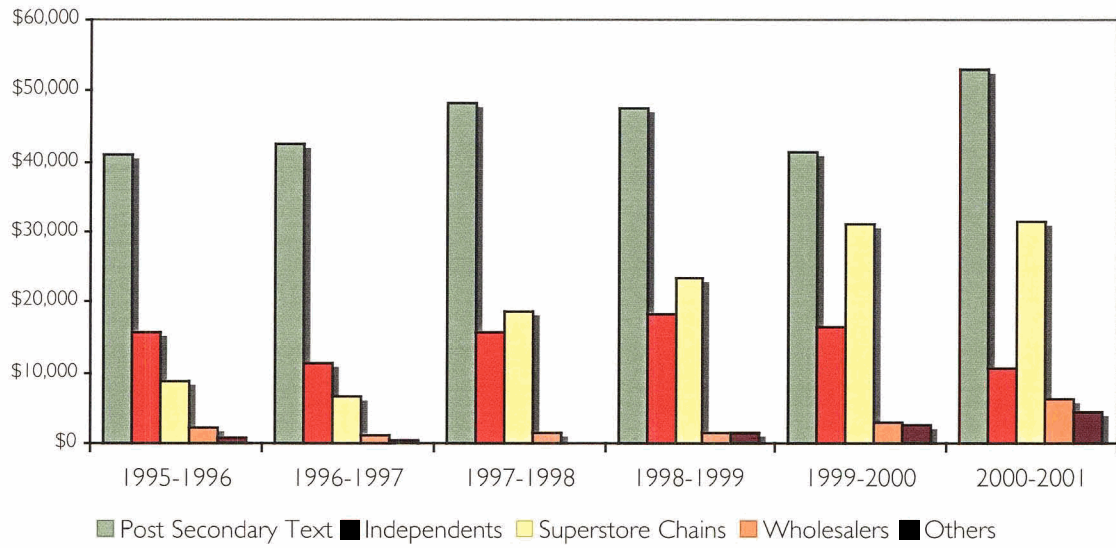


Figure 12. Talonbooks' Canadian Net Sales, 1995–1996 to 2000–2001

