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INTANGIBLE INVESTMENT BY PUBLISHERS

Addendum to previously published report

This note is an addendum to the report titled "The Contribution of the Publishing Industry to the UK Economy", written by Frontier Economics for the Publishers Association and published in 2017. It corrects a figure quoted in the report which was labelled as the total amount authors received in 2016 from advances, royalties and income from secondary licensing and rights. The figure originally quoted (£161m) does not in fact include the advances publishers pay to authors and as such a more accurate figure would be roughly £350m.

Background and context

In the economic contribution report published December 2017, we noted that the publishing industry invested £545m in 2016. Of this figure, £168m was invested by publishers in physical assets (across book and journal publishing) and £377m in copyrighted artistic originals, a form of intangible asset. Corresponding to this investment by publishers in artistic originals is the ‘authors share’ of investment, at £161m. This note explains the origins of these numbers, and corrects a labelling error made in the report and the annex.

The intangible investment numbers above are based on work that Dr Peter Goodridge published in 2013,[1] which has since been adopted as part of the official measurement of the UK National Accounts. It is also similar to the OECD’s methodology of measuring investment in intangible assets. Goodridge set out to improve the UK’s method for measuring investment in artistic originals across most of the creative industries (Film, TV, Radio, Music and Books), but here we focus on his method and data as it relates to book publishing.

We have interpreted Goodridge’s calculations based on subsequent correspondence with him, and updated his results to reflect the subsequent growth of the sector as estimated by the Office for National Statistics (ONS).

[1] Goodridge, P., 2013. Film, television & radio, books, music and art: estimating UK investment in artistic originals. *Measuring the Contribution of Knowledge.*

Methodology

Goodridge took a ‘revenue approach’ in his work, since it is difficult to measure intangible investment in other ways, such as the cost of inputs or production costs. When economists face this issue, they often use the returns to an investment as a proxy for the investment itself, since over time, these should be more or less equal.[2] So, the revenue that the publishing industry makes from its intangible assets – its intellectual property – is assumed to be equal to its investment in these assets.

Goodridge brought together four different types of revenue for this exercise:

1. Advances paid by publishers to authors, which are a proxy for the future revenue expected by publishers.
2. Royalties received by authors, which account for the authors’ revenue from sales.
3. Licensing and secondary rights income, which is part due to publishers and part due to authors.
4. The cost of own-account writing and editing by publishers, for instance editing of books and textbooks and investment in in-house software, which complete the expectation of publishers for future revenues.

Data on (1), (2) and (3) was collected by the UK Intellectual Property Office (who funded the research) through collecting societies, namely the Authors Licensing and Collecting Society and the Publishers Licensing Society. Data on (4) was collected largely through a survey of half of the top 11 UK publishing houses. This was then scaled up to represent all of the top 11 (but not the smaller publishers).

Summing all those four together gave Goodridge’s estimate for the total investment of the publishing industry, which leaves the issue of separating the investment of authors from that of publishers. Using the primary data he collected, Goodridge estimated that publishers account for about 70% of the investment (and receive 70% of the revenue) and authors account for the remaining 30%.

In investment terms, these 30% include the author’s own effort, skill and ideas that contribute to the creation of their intellectual property. In revenue terms, these 30% account for the royalties UK authors receive from the sales of their books (both domestically and abroad), and their share of the secondary licensing and rights income.

In our correspondence with Goodridge, he gave us his results up to 2010. We then took those numbers and extrapolated them to 2016 using the nearest official ONS figures for the wider relevant sector.[3] Goodridge confirmed in our correspondence that this was the best available source for extrapolation, and in any case, the ONS figures showed that investment was nearly flat between 2010 and 2016, so our figures ended up close to the 2010 estimates. Goodridge indicated that the 70/30% split between publishers and authors also remained stable over time in his data.

[2] Fundamentally, the value of an asset – and therefore, the investment required to produce it – is the lifetime value of the stream of revenues that the asset will produce over time.

[3] Section J of UK SIC Codes 2007, Information and communication.

Results and clarifications

Taking all this together, we can clarify that:

- The total investment that the publishing industry as a whole made in artistic originals (i.e. intangible assets) in 2016 was £538m: £377m by publishers and £161m by authors. This excludes the £168m invested by publishers in *physical* assets.
- In revenue terms, we estimated that authors in 2016 received at least £161m in royalties and income from secondary licensing and rights. This figure:
  - does *not* include advances, as they are counted as part of the publishers' share and not the authors' share;[4]
  - *does* include royalties from overseas sales of books by UK authors; and
  - includes royalties received in 2016, whether for new titles or the sale of existing backlist titles.[5]
- The £161m figure primarily covers authors in consumer publishing, since journal and textbooks authors are largely remunerated in other ways.
- Part of the data (revenue stream 4) accounts for only the top 11 publishing houses and not the full market, and therefore is a conservative estimate. However, this relates only to the 'publishers share', and does not affect the £161m figure.
- The data available does not allow us to robustly estimate the total flow of royalties *and* advances to authors, and further primary evidence is required for this. However, Goodridge has indicated that advances account for approximately half of the £377m 'publishers share', suggesting that the total flow of payments received by UK authors in 2016 is roughly £350m.
- Notably, it is our understanding that the ONS is currently in the process of improving these estimates with an updated methodology and potentially new primary data, to be published in 2019. While the figures presented in this addendum represent our best estimates at the moment, subsequent ONS publications will provide more accurate data.

[4] This corrects the error made in the December 2017 report.

[5] This is based on a simplifying assumption Goodridge makes. In an ideal world, royalties from each year will be measured separately. However, data is more readily available for total streams of royalties; it is possible to show that under some assumptions, over the long run ('in equilibrium'), the annual investment in new work is equal to the snapshot of annual payments for all work, new and old.