McTevia Quoted About Borders Financial Troubles in article on Daily Finance

On April Fool's Day, Will the Joke Be on Borders?

By SARAH WEINMAN

Borders (BGP) has seen so much trouble in the last few years that its very existence suggests the book retailer has nine lives. But this Thursday, April 1, when a critical $42.5 million loan from its majority stakeholder, Pershing Square Capital Management, comes due, the publishing industry will find out if the company has used up all of its good luck karma -- or if Borders has yet another life left to live.

Big Trouble in 2009

At this time last year, Borders was getting ready to report some seriously grim fourth-quarter earnings. Stock was trading below $1 a share and the NYSE threatened to de-list it. George Jones had been replaced as CEO by Ron Marshall, who proceeded to lay off 136 employees at the company's corporate headquarters in Ann Arbor, followed by a larger layoff of 742 store-based employees. Analysts had whipped themselves into a frenzy of speculation that the retailer was doomed to enter Chapter 11. Jim McTevia, managing partner of Bingham Farms-based McTevia Associations, told the Detroit Free Press last year, "Depending on their ability to get debtor-in-possession financing, they could easily file for Chapter 11.... It is much easier to facilitate the sale of a troubled company under bankruptcy protection."

But bankruptcy didn't happen. Pershing Square extended its loan, which it had already done two previous times before. An even larger loan backed by Bank of America (BAC) had its payback deadline confirmed for July 2011, buying Borders a little more time to come up with the $360 million that would be due. The stock was not de-listed and now hovers around $2 a share. The store still had the power to make or break bestsellers, such as Heather Gudenkauf's debut novel The Weight of Silence and, more recently, the paperback edition of Chris Cleave's Little Bee. And Pershing Square CEO William Ackman made the confident claim that bankruptcy was a "low-probability" event.

Instead of going the Chapter 11 or 7 route, Borders began what is known internally as "Project Phoenix" for handling the $562 million in leases it must pay for the 513 superstores it operates. Stores designated with this moniker are those whose locked-in leases, negotiated when the economy was riding high, are now so prohibitive that even if they make money on books, can never be profitable -- making them the retail equivalent of an underwater mortgage. If a company came knocking and wanted to take over these stores and negotiate with landlords directly, Borders would hardly stop them. But as long as the economy recovers at a pace slower than a snail, then Borders is stuck with these never-profitable

Project Phoenix stores, punished with inferior stock, slower re-orders, and a cap on the amount of office supplies (stories have circulated on internal message boards of Projejct Phoenix stores getting their supplies through the charity of profitable stores over-ordering and sending along their surplus.)

2010: The Bad News Continues

So far, 2010 has followed last year's script of personnel changes, layoffs and negative speculation almost to the letter. Ron Marshall exited the company in January to become the CEO of the Great Atlantic and Pacific Company, and Michael Edwards was promoted to take his place until a more permanent replacement can be found; 164 people were laid off at the corporate level -- cutting the overall roster in half to a mere 650 -- and even though the numbers have still not been confirmed, hundreds more store employees were let go earlier in March. The company also closed 150 of its smaller, mall-based Waldenbooks stores, slashing that division in half. Borders still employs more than 22,000 people, but that's down from the 27,000 employed a year ago.

That has Jim McTevia bringing up the prospect of bankruptcy anew. "Borders is a classic example of a company that is struggling for survival," McTevia told the Ann Arbor News. "I would say that if somebody doesn't buy Borders and merge them into an operation that Borders will probably fail and liquidate."

The biggest red flag as to why this bit of deja vu might actually signify something more drastic for Borders is that there is still no date scheduled for when the retailer will release its fourth quarter earnings. The Associated Press reported last week that the quarterly report would be issued Monday, but Borders spokesperson Mary Davis told DailyFinance that the AP's report "inaccurate" and stressed, "We never announced a date for the 4th quarter release or the conference call."

One possible reason for holding back on the earnings report is that with news so bad of late -- like the nearly 15% drop in holiday sales for stores open at least a year -- there's no reason to rush on releasing even gloomier news. But the probable truth is no laughing matter: if Borders and Pershing Square don't figure out how to keep the loan afloat, then it has a ripple effect on the larger, Bank of America-backed loan, which may also need to have its deadline extended, assuming the bank can come to an agreement with various investors.

Why Borders May Not Be Down for the Count

On March 10 the company's' board of directors approved retention bonuses for the top five executives, and claimed in a March 16 SEC filing that they would develop a business plan for the second half of 2010.

The company is shaping up to enter the e-books market in a much more focused way than they ever have before, what with a recent spate of job listings for its digital division. Though Borders sells the Sony (SNE) Reader, they've never had an e-bookstore like the juggernaut Amazon (AMZN) or brick-and-mortar competitor Barnes & Noble (BKS). This summer, Borders plans to sell a $149 e-reader manufactured by Kobo, a company spun off from Canadian bookstore retailer Indigo, and the Alex Spring Design e-reader, priced at $399. Both have pros and cons -- the Kobo e-reader's price is attractive and its software also works on a variety of other devices, such as Apple's (AAPL) iPhone and upcoming iPad -- but eating into the massive market share of the Kindle or competing with B&N's e-reader, nook, might be a tall order at this point.

All that distress puts Borders on equal footing with some other troubled local retailers, as turnaround expert Ken Dalto told the Free Press: "[Borders is] doing what GM and Chrysler were doing at this time last year," Dalto said. "They will either do a workout with creditors or do a formal bankruptcy."

Depending on what happens, Borders will either breathe a sigh of relief come April 1, however temporary, or will experience a very sad April Fool's Day.