

Books, Music, and Movies

INDUSTRY OVERVIEW

After declining for several years, sales of physical books finally seem to have stabilized and are actually trending up slightly. Sales have been driven by improved merchandising efforts coupled with a stable/improving market for physical books, particularly for children's and young adult books with movie tie-ins. Digital album and track sales are now on the same downward trajectory as physical CDs and DVDs, as more and more consumers opt for streaming services.



TREND TRACKER

Three month NOLVs	Consistent/ Decreasing ↓
Sales Trends	Mixed ⇕
Gross Margin	Consistent
Discounting	Consistent

NOLVs: NOLVs for books have been flat for most companies; however, NOLVs for music and movies have declined.

Sales Trends: Sales of physical books are up slightly. E-book sales continue to increase, but at a slower pace than in past years. College textbook sales continue to decline on a dollar basis, as rentals grow in popularity, while K-12 sales are rebounding due to recent adoptions. Physical CD and DVD sales are still plummeting and digital track and album sales are declining in favor of streaming services.

Gross Margin: Gross margin has been relatively flat to slightly up for most companies. Companies have been strategic in their promotions and relying on in-store events and experiences to drive traffic and compete with online sellers.

Discounting: Discounting has remained relatively consistent, with thoughtful, targeted promotions.

KEY INDUSTRY DRIVERS

- In-store experience:** Brick-and-mortar book stores have been pushing in-store marketing events to drive traffic and offer an experience that online giants can't replicate. During the holiday season, Barnes & Noble enlisted the help of 100 popular authors including Dan Brown, EL James, and Hilary Clinton to sign nearly 500,000 copies of their books (combined). These books were only available for sale in the retail stores. Retailers also continue to expand non-book categories like toys, games, and gifts, which are generating increased comparable store sales.
- E-books:** E-book sales have stalled on a dollar basis, but are still increasing on a unit basis. Comparisons are being impacted by lower e-book prices since the 2012 price settlement and the mix of books being sold, as 2012's bestsellers were heavily skewed toward e-books. In November, Amazon and Hachette finally reached a compromise to their pricing dispute whereby Hachette will set e-book prices, but the publisher will receive "financial incentives" from Amazon if it chooses to lower prices to consumers. This gives publishers greater control over pricing, but opens the door for Amazon to discount e-books if it can incentivize its publishers appropriately.
- Struggling NOOK business:** During the holidays, Barnes & Noble's NOOK sales decreased 55.4% compared to the prior year, with device and accessories sales down 67.9%. The company now outsources tablet manufacturing to Samsung and announced that its agreements with Microsoft and Pearson were terminated. It also changed its decision about spinning off the NOOK business, instead opting to spin off its college bookstore business by the end of August.
- Textbook rentals:** In the college segment, there is now more competition than ever for online rentals, causing several companies to experience a decline in the average rental price. In response, companies are becoming smarter with their rental pricing. Companies like Chegg are also focusing on the service side of the business to connect with students and build customer loyalty. Some book stores are also collaborating with Amazon.com to store the inventory in Amazon's warehouse and rent it through Amazon's website. Amazon has also opened its first physical on-campus location at Purdue and has two others planned for fall. Under this arrangement, Amazon manages the contract for the school. While three locations is not enough to have a significant impact, industry players are keeping a close watch on Amazon's growth in this sector.



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KEY INDUSTRY DRIVERS

- **Digital textbooks:** Students still prefer hard copies to digital, especially when rental prices are often cheaper than the price of digital versions. However, publishers are making efforts to enhance digital offerings to make them more appealing.
- **Improving K-12 market:** K-12 sales have been up due to improvements in the market from recent large-scale adoptions, but have varied by company based on which programs were adopted by which state. Digital penetration has been increasing, though still remains small. The recent Texas adoption, which is a bellwether for the industry, was particularly strong in terms of digital sales. However, costs and school infrastructure concerns are still major roadblocks for expansion of digital.
- **Declining CD and DVD sales:** Music sales are down across the board, including both physical and digital product, as consumers gravitate toward streaming services. Streaming revenue reached close to \$1.5 billion in 2013. Vinyl has been the one bright spot, with sales up 52% over 2013. However, this is a small piece of the industry and its longevity is unclear. DVD sales are also down, though Blu-ray sales have fared slightly better, and digital movie sales continue to grow.

SALES TRENDS

The following table illustrates comparable store sales trends for major public book retailers (Represents the most recent fiscal quarter sales reported):

	Most Recent Quarter	Prior Quarter	Two Quarters Ago	Three Quarters Ago
Barnes & Noble ¹	1.7%	0.5%	(0.4%)	(1.9%)
Books-A-Million	1.8%	0.1%	(2.5%)	(1.8%)

Note(s): Represents core comparable bookstore sales and excludes sales of NOOK products.
The most recent quarter for Barnes & Noble ended January 31, 2015; Books-A-Million ended November 1, 2014.

The following table illustrates physical CD album sales in units, per year, as well as the change versus the prior year, as reported by Nielsen SoundScan:

Year	CD Album Sales in Units (in 000s)	Change versus prior year
2008	360,617	(19.7%)
2009	294,924	(18.2%)
2010	236,956	(19.7%)
2011	223,507	(5.7%)
2012	193,378	(13.5%)
2013	165,407	(14.5%)
2014	140,850	(14.9%)
YTD February 15, 2015	15,591	(5.9%)



OUTLOOK

Retailers will continue to manage book, CD, and DVD inventory levels while also using other categories and in-store events to drive traffic. Sales of physical product will continue to decline and those retailers that stock the right depth of key titles will fare the best.

Experience

GA is one of the largest liquidators of retail inventory and has been involved in a variety of liquidations, ranging from the disposition of excess inventory and the closing of underperforming stores, to full-scale liquidations of national retailers with hundreds of stores. GA has experience with full and partial liquidations of companies throughout a variety of retail sectors, some of which are detailed below:

Target Canada	Cache	Office Depot/Max	Circuit City
Macy's	Fashion Bug	Mervyns	Tower Records
Fortunoff	Frederick's of Hollywood	Eddie Bauer	RadioShack
Linens 'N Things	Naartjie	Whitehall Jewelers	Borders
Jo-Ann Fabrics	Boot Town	A&P	Movie Gallery

These experiences, in addition to numerous others, provide GA with valuable insight into the market trends and the consumer response that can be expected in a liquidation. They give us an understanding as to recovery values that can be achieved for retailers within these industries. In addition to this liquidation experience, GA has worked with and appraised numerous retailers, including industry leaders within each sector. While our clients remain confidential, GA's extensive list of appraisal experience includes:

- Leading book retailers, including one with over 700 store locations and sales of upwards of \$4.5 billion.
- Two of the top textbook publishers within the K-12 segment, brick-and-mortar retailers of college textbooks, online renters and retailers of college textbooks, and textbook distributors.
- Several e-commerce and multi-channel retailers, as well as flash sale websites and auction websites. In particular, GA has appraised 74 of the top 500 e-commerce companies as reported by *Internet Retailer*.
- Numerous retailers of apparel and accessories, including major department store retailers and a variety of specialty retailers that are found in malls throughout the country.
- Leading off-price retailers of apparel and accessories, including major national and regional chains.
- Retailers of consumer electronics, including smaller, more localized chains, as well as regional, national, and international retailers with close to 4,500 store locations.
- Many jewelry retailers, including one of the largest in the United States, with locations throughout the country.
- Major national and regional discount and dollar stores, including one of the country's largest chains, with over 10,000 stores.
- Sporting goods retailers that specialize in a number of products, including those for outdoor sports, recreational ball sports, hunting, camping, and fishing, and a variety of other equipment for outdoor enthusiasts.
- Major regional grocery store chains including one with a store base of close to 400 and net sales of nearly \$8.0 billion, as well as smaller local grocery store retailers and pharmacies.

In addition to our internal personnel, GA maintains contacts within the retail industry that we utilize for insight and perspective on recovery values.

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