

# BANKRUPTCY INSIDER

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## Lower the volume

Will Tower Records end up in the for-sale bin?



In the two years since its emergence from bankruptcy, there has been much speculation among bankers and industry observers that **Tower Records Inc.**'s new owners will sell the West Sacramento, Calif., retail chain, probably the earliest music megastore.

"Would it surprise me if [Tower] traded hands this year? No, not at all," says **Lloyd Greif**, president and CEO of **Greif & Co.**, the investment bank that facilitated Tower's ownership change during its bankruptcy. "If I were the bondholders, I'd be itching to sell. It's a very strong mergers and acquisitions market right now."

The bondholders to which Greif refers—**Barclays Bank plc**, **Highland Capital Management LP**, **MG Global Investment Corp.** and **MW Post Advisory Group**—took over 85% of the company when it came out of bankruptcy in March 2004, a near-record 35 days after its filing. Tower's founder **Russell Solomon** and his family held onto the other 15% of the 88-store company.

Tower officials have been tight-lipped about its rumored sale as well as the company's financial status since emerging from Chapter 11. A spokeswoman for the firm said the company does not want to discuss its finances.

But Greif, like others familiar with the situation, believes Tower's debt-for-equity swap during its short stay in Chapter 11 allows it to control its own destiny.

"I think the purpose of [Tower's] bankruptcy was to put the company back on solid footing," Greif says. "They had to get out of \$122 million in junk bonds, and their bankruptcy took it down to \$30 million. They also got out of some bad leases."

Greif said parting with the company may be a difficult decision for the new

ownership because Tower is an "iconic brand," with a loyal consumer base. But its place in today's music market seems to be fading, so selling may be the new owners' only option.

Tower, whose New York stores with red-orange neon lights were once a destination for upstart rock bands who wanted to show off their music, now has to contend with such mass merchants as **Best Buy Co.** and **Wal-Mart Stores Inc.** At the same time, digital music, such as **Apple Computer Inc.**'s iTunes, gains steam every year.

For example, Apple sold 8.5 million iPods in the quarter that ended on April 1, up from 5.3 million iPods a year earlier.

Barry Sosnick, president of record industry consulting firm **Earful.info**, believes music specialty stores such as Tower are "ill prepared to compete" with this new competition.

At the same time, Tower is losing market share in two important areas of its in-store business.

The retailer continues to lose sales on new releases and Top 100 albums, formerly their bread and butter, to mass merchants who sell CDs at a lower price just to get consumers in their stores, hoping they'll also buy accessories such as headphones or speakers.

Tower is also selling less "catalog product," or albums more than a year old and no longer in the Top 100, Sosnick says, adding that today's consumers are more apt

to buy older recordings from online retailers.

"Tower is in the most dangerous spot you can be in from a market position," Sosnick says.

Greif adds that Tower is still smarting from a 2002 decision to shed its Japanese outlets.

"They sold off one of their crown jewels, and I'm not sure they've recovered," he says. "Tower Japan was a clear home run."

Tower, however, is developing new initiatives such as a new Podcast Web service launched last month, to help it keep up with competitors. This service is designed to drive more business to the store's Web site and compete with the popular Podcasts on iTunes.

Podcasting—distributing audio and video programs over the Internet—"is an excellent way to differentiate Tower," says Sosnick.

The Podcasts planned by Tower will emphasize lesser-known music from independent record labels, giving customers something they can't get from mass merchants.

While Podcasts alone may not be enough to keep the music retailer afloat, Tower may not have trouble finding a buyer because it's a well-known brand with a loyal consumer base. Also, having shed its debt in bankruptcy, Tower is much more stable.

Tower's suitor may, surprisingly, not be a private equity firm looking in the bargain bin, but a mass merchant.

Such a transaction with a mass merchant would have to happen by late August, however, so Tower's new owners will have enough time to get ready for the holiday retail season. ■

—John Blakely

### TIMELINE OF TOWER RECORDS BANKRUPTCY

1960	Tower Records opens for business in Sacramento, Calif.
Feb. '04	MTS Inc., parent of Tower Records, files for bankruptcy
March '04	MTS exits bankruptcy

Source: www.BankruptcyInsider.com