Malone's Barnes & Noble bid a bet on the Nook

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In this June 8, 2010 file photo, a customer enters a Barnes & Noble in Bethel Park, Pa. Barnes & Noble Inc. on Thursday, May 19, 2011 said that online retail, media and communications conglomerate Liberty Media Corp. offered to buy the book seller for $17 per share in cash. That amounts to about $1.02 billion, based on the number of shares it had outstanding as of March. (AP Photo/Gene J. Puskar, File)

Why buy a bookstore? John Malone, who made a fortune in cable television, is offering $1 billion for Barnes & Noble - trying to jump into a business so sick that its No. 2 competitor, Borders Group Inc., is on life support.

The difference is that Malone and his Liberty Media conglomerate aren't betting on the books-and-mortar past, analysts say, but the promise of the electronic future.

Barnes & Noble's Nook electronic reader now accounts for 28 percent of the market for those devices. And the Nook has the potential to go beyond books to deliver all types of digital products, including music, magazines, TV shows and movies. That makes it a competitor not just to Amazon.com's Kindle but also to Apple's iPad.

"This deal is all about the device," said Sherif Mityas, a partner in the retail practice of global management consulting firm A.T. Kearney. "As Apple proved, you need to have the content and the device. Malone has the content, and Barnes & Noble has the device. You're not buying the stores; you're buying the Nook."

Malone's empire, Liberty Media Corp., operates three publicly traded companies - Liberty Interactive Inc., Liberty Starz Group and Liberty Capital Group - through which it runs home-shopping network QVC and movie channel Starz. It also holds stakes in numerous other online, media and communications companies. Some believe that QVC could be used as a marketing vehicle for Barnes & Noble's Nook.

With the backing of a media conglomerate, Barnes & Noble's digital business would be able to compete better with Amazon, Apple and others, said Gary Balter, a retail analyst at Credit Suisse.

Barnes & Noble's 700 stores may appear to be an albatross. But they could be transformed into places that highlight mostly digital devices and content and mimic Apple's successful stores. Barnes & Noble has already cleared space at the front of its stores to display the Nook and push e-books.

"You don't want the old-fashioned bookstore customer who goes in and sits and reads a book for two hours. You want people going in there who are hungry for experience," said Richard Hastings, a consumer strategist with Global Hunter Securities.

Barnes & Noble's shares surged almost 30 percent on Friday and passed Liberty's bid of $17 a share in cash, closing at $18.33. The companies haven't yet signed an agreement, and the deal is still subject to closing conditions, including one that founding Chairman Leonard Riggio keep a stake in the company and remain in a management position, Barnes & Noble said.

Barnes & Noble reiterated Friday a committee of its board is evaluating the offer.

Barnes & Noble had put itself up for sale in August in response to pressure from billionaire activist shareholder Ron Burkle, but the company didn't find much interest.

Traditional book sellers have been facing increasing competition from online retailers like Amazon.com and discounters like Wal-Mart Stores Inc. And heavy readers are quickly embracing e-books.

Right now, though, Simba Information senior trade analyst Michael Norris estimates there are still at least five print book buyers for every e-book buyer.

Still, the industry thinks e-books are the future. Amazon.com said Thursday that, after less than four years of selling electronic books, it's now selling more of them than printed books. Stores have cut shelf space devoted to printed books by 15 percent over the past year, estimated Mike Shatzkin, CEO of Idea Logical, a book consulting company. Last year, he predicted that it would take five years for stores to cut space for printed books by 50 percent; now, he believes it will only take about three.

The shift has already rocked Borders Group, which filed for bankruptcy court protection in February. It has been closing stores and is reportedly in talks to sell more than half of those that remain.

While Barnes & Noble has done better than Borders, its quarterly results have been weighed down by large investments in its online and e-reader businesses. Barnes & Noble reported growth in its online store in the most recent quarter, and said both that and its bricks-and-mortar stores were helped by sales of its Nook e-reader.

Last month, Barnes & Noble added an app store and an e-mail program to its Nook Color e-reader. That brings the $249 device closer to working like a tablet computer like the iPad, which sells for twice as much. Barnes & Noble is expected to announce a new version of the Nook next week, though it hasn't said what features it will include.

Clearly, there are concerns. Norris says he would like assurance from Liberty that it's not going to look at the Nook in "a vacuum" and get rid of the stores.

"Its success has been (tied) with the physical bookstores because people are not giving up physical books," he added.

No one know knows exactly what Malone, 70, has in mind. He has typically been a pure investor, like Warren Buffett or a private equity firm, who buys companies when they are cheap and on the brink of financial ruin.

Malone doesn't have a history of putting together grand technological schemes, said Wedge Partners analyst Martin Pyykkonen. He called Malone a "financial engineer" who demands excellent returns, keeps management in place and reaps rewards when the business returns to health.

It could be there is no grand plan with Barnes & Noble, either, besides closing unprofitable stores and otherwise improving profitability. One thing that is similar with other Malone investments is Barnes & Noble's big share of its market, which could get bigger if Borders Group closes or sells more stores.

"Malone's style is to very quietly, very patiently look and watch, and when things get to his threshold level, then make his move," Pyykkonen said. "But he makes his move in a generally quiet, friendly, cooperative way, because he actually wants management to stay in there and keep running the company."

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