Don’t Judge a Book By Its Cover

November 9, 2006

Pershing Square
Capital Management, L.P.

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Borders Group

BORDERS.

Ticker: **BGP**

Recent price: **$21**

Note: BGP fiscal year ends on January 31. Presentation based on a Calendar year.

- **2nd largest U.S. book retailer**
  - 13% of U.S. retail book market (versus Barnes and Noble at 17% and Amazon at 10%)
- **2006E Rev of $4.1bn and EBITDA of $235mm**
- **Year-end Enterprise Value of $1.6bn and Equity Value of $1.1bn (1)**
  - EV / '06 EBITDA: **6.9x**
  - EV / '06 EBITDA – Maint. Capex: **8.8x**
  - P / '06 EPS: **27.2x**

Forward estimates based on Pershing estimates.

(1) Based on management's guidance for Net Debt and shares outstanding at year end 2006. Assumes a $21 current stock price for BGP throughout this presentation.

What is Borders?

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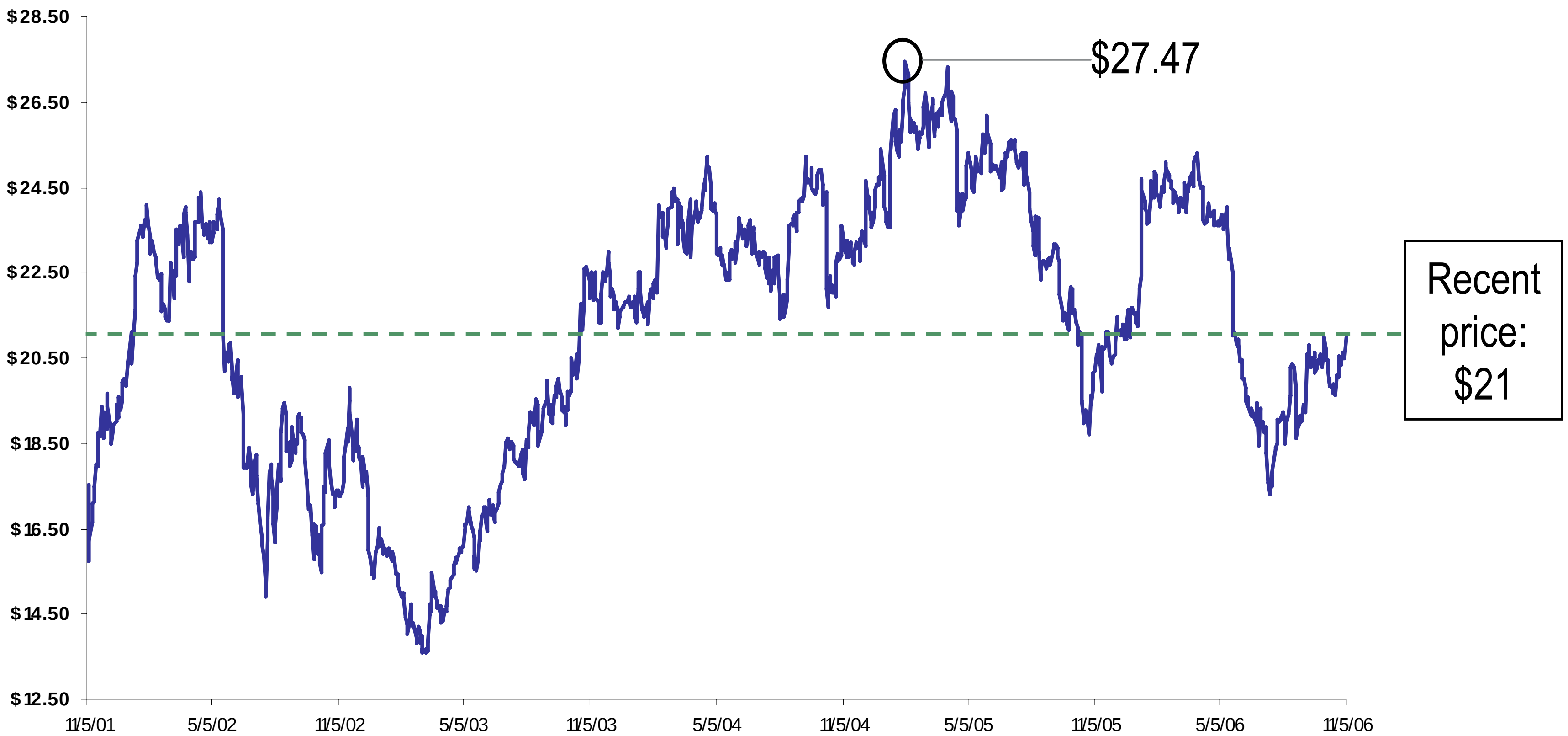
Superstores	Mall Stores	International
Large format (25,000 sq ft) Large selection 476 units Most profitable segment Positive sales trends	Waldenbooks Small format, mall-based Limited selection 600 units Negative sales trends and declining profitability	U.K. and Australia 90 units / mix of large / small format stores Declining profitability

% LTM Rev.	*68%*	*17%*	*15%*
% LTM EBITDA	*92%*	*5%*	*3%*
% LTM ROA	*10%*	*-1%*	*-2%*

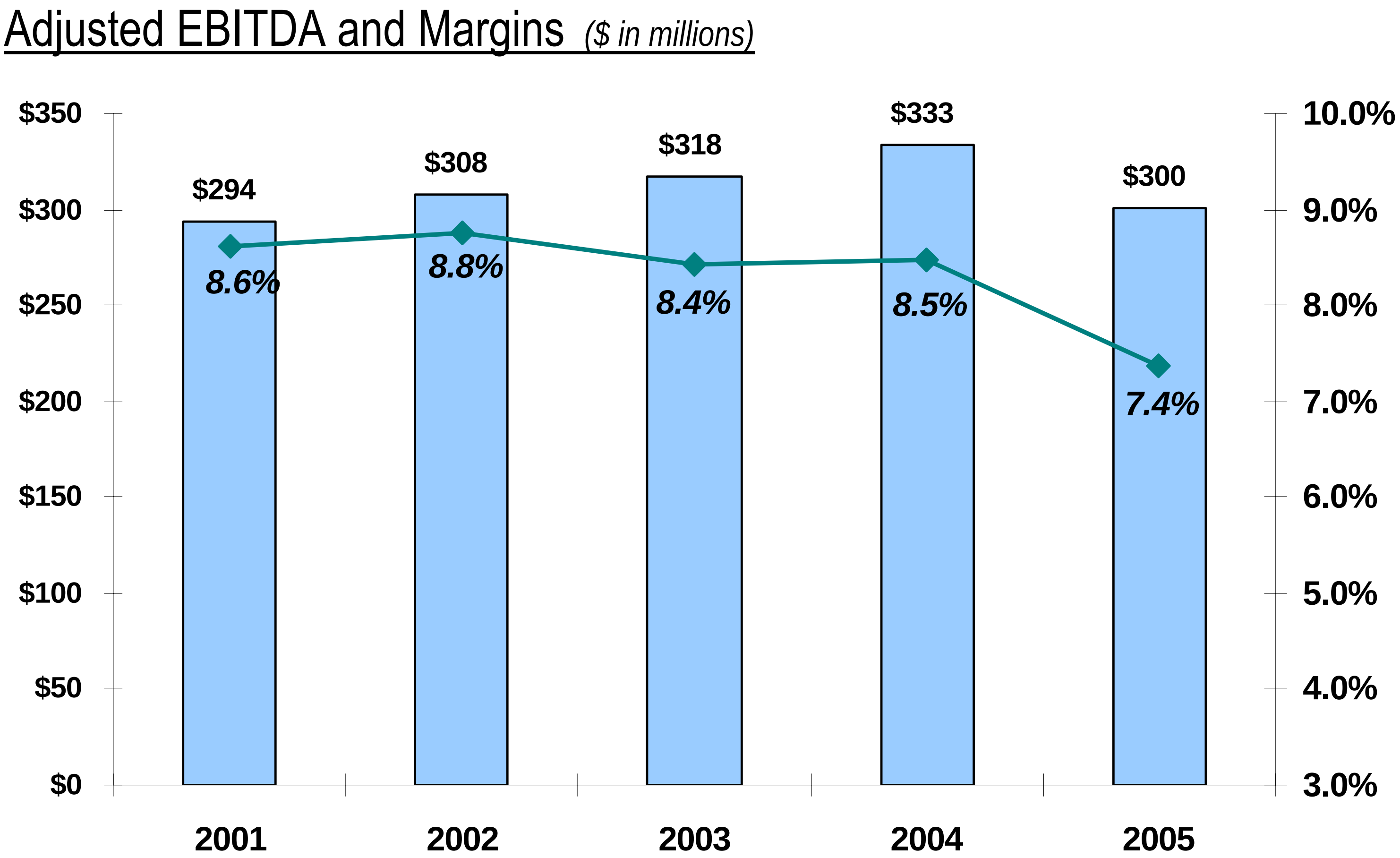
Five Year Stock Price Performance

Borders was trading at approximately $27.50 per share in February 2005 but has since traded down primarily due to weakening margins and same store sales trends



Borders Historical Financial Performance

In 2005, Borders' consolidated Adjusted EBITDA margins fell to 7.4% from the previous four-year average of approximately 8.6%



Traditional Sentiment on Borders

- **Unattractive industry**
  - “Amazon risk”
  - Consumer interest in books is declining
  - Difficult SSS comparisons with *Harry Potter*
- **Second place operator behind Barnes and Noble**
  - More exposure to declining Music category
  - Worse execution (lower working capital turns and sales / sq.ft.)
  - Low margin, legacy mall stores
- **Limited free cash flow due to large, recent cap ex initiatives**
  - Consolidating distribution centers
  - Significant store remodel program

Why Do We Like Borders?

Why Do We Like Borders?

1. The book superstore industry is misunderstood

- “Amazon risk” is largely exaggerated for superstores
- Book superstores are valuable franchises
- Minimal inventory risk because inventory is returnable at cost
- Maintenance capital is significantly less than depreciation because long-lived leasehold improvements are depreciated over initial lease term

Why Do We Like Borders?

2. Borders is a mix of high-quality businesses and several low-ROI, money-losing businesses which are in the process of being rationalized

- **Value of core Superstores business is obscured by declining profitability in the Mall Stores and International Stores**
- **In addition, within the Superstores segment, value is being masked by a declining category as well as several recent management initiatives**
  - Rapid decline of Music sales (music was 22% of sales in 2001, now roughly 11%)
  - Recent initiatives, including (1) Remodel program, (2) Rewards program, and (3) Distribution center consolidation, have reduced reported Superstores profitability

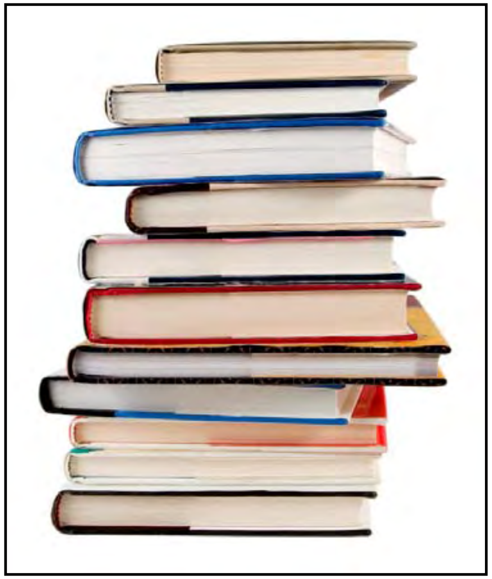
Why Do We Like Borders? *(cont'd)*

- **Superstores are healthy, growing and improving**
  - Stable EBITDA margins (9.5% - 10+%) with high ROIC
  - Expected annual square footage growth of ~6%
  - Remodeling program will reduce Music category exposure
  - Opportunity to increase working capital turns
- **Mall and International segments are low ROIC businesses that can be monetized with minimal disruption**
  - Estimated ~$200mm of Net Working Capital on an estimated ~$15mm of EBITDA contribution
  - Potentially "worth more dead than alive"
  - New Management is focused on rationalizing business

Why Do We Like Borders?

3. Extensive share repurchase program and newly hired CEO should help drive value creation

- **~$500mm of share repurchases in the past 2.5 years**
  - Common shares outstanding reduced by ~ 20%
- **Company is repurchasing ~14% of market cap in the second half of 2006**
- **New CEO George Jones joined in July**



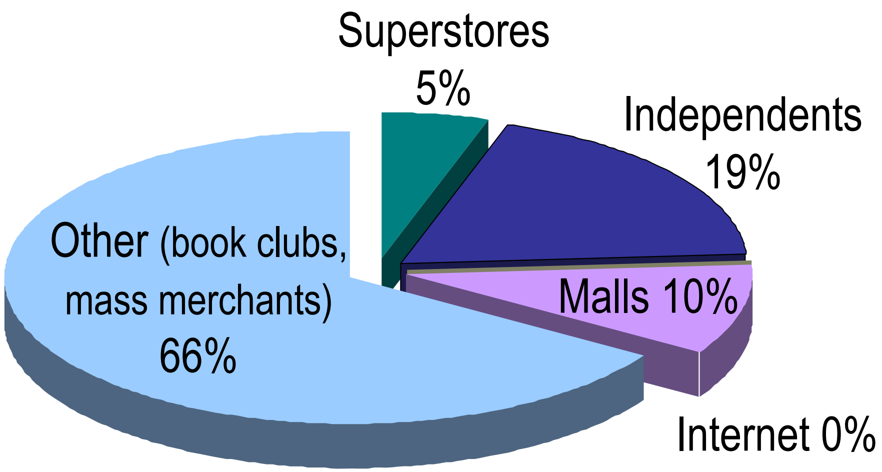
1. “Misunderstood Industry”

"Amazon Risk?"

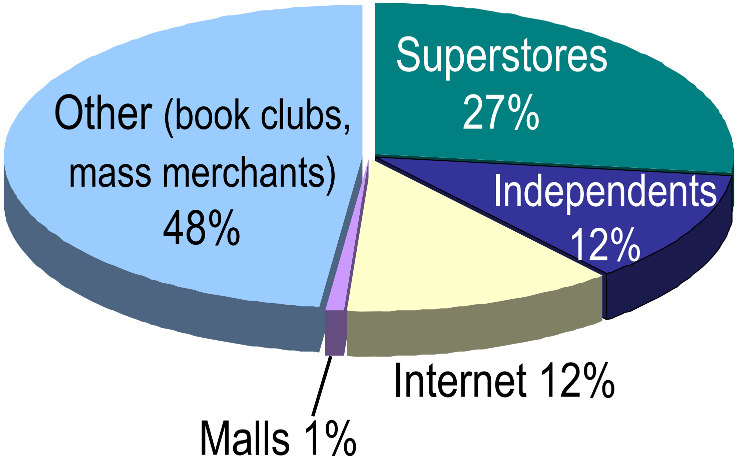
Superstores have increased share in tandem with Amazon by focusing on selection and quality of experience

Losers have been Independents, Mall stores, Mass Merchants and Book Clubs with limited selection

U.S. Consumer Book Industry <u>1993</u>



U.S. Consumer Book Industry <u>2005</u>



Source: Borders Group management presentation.

Books Superstores Are Valuable Franchises

- **Book Superstores are attractive “anchor” tenants**
  - Favorable customer demographic – book buyers are well-educated, high-income customers
  - Superstores are “Mini Malls” with books as the anchor
- **High-quality customer experience**
  - Borders ranked #2 in Overall Quality for Retailers in 2006 Harris Poll
  - Not just a book store: café, community events, meeting place
  - Customer spends an average of one hour in the store
- **Opportunity to sell more than books**
  - Barnes and Noble is the second-largest retailer of coffee in U.S.
  - Borders achieving success with Seattle’s Best and Paperchase

Gross Margin Stability at Superstores

- **Best sellers are ubiquitous and extremely price competitive, yet they represent less than 5% of typical superstore sales**
- **Nearly all (~97%) book inventory is returnable to the publishers at cost**
  - Increases gross profit margin stability
- **Book inventory is non-perishable and generally has limited "fad" risk**

Industry Maint. Capex is less than Depreciation

Reported earnings for Book Retailers understates true cash flow

- **Book retailers depreciate store assets over initial lease term ~ typically 10-15 years**
- **Maintenance capital requirements are lower than depreciation expense**
  - Fixed assets (book shelves) last longer than lease terms
  - Maintenance costs typically limited to paint and carpeting

Borders Group ($ in mm)	**2006E**
D&A	$130
Maintenance Capex	50
Difference	80
Net Income	$43
Maintenance FCF (after-tax)	$123
Price to Earnings	**27.2x**
Price to Maint FCF (after-tax)	**9.4x**

Maintenance FCF = NI + D&A – Maintenance Capex

Based on Pershing estimates. Assumes a $21 stock price for BGP.

Superstores

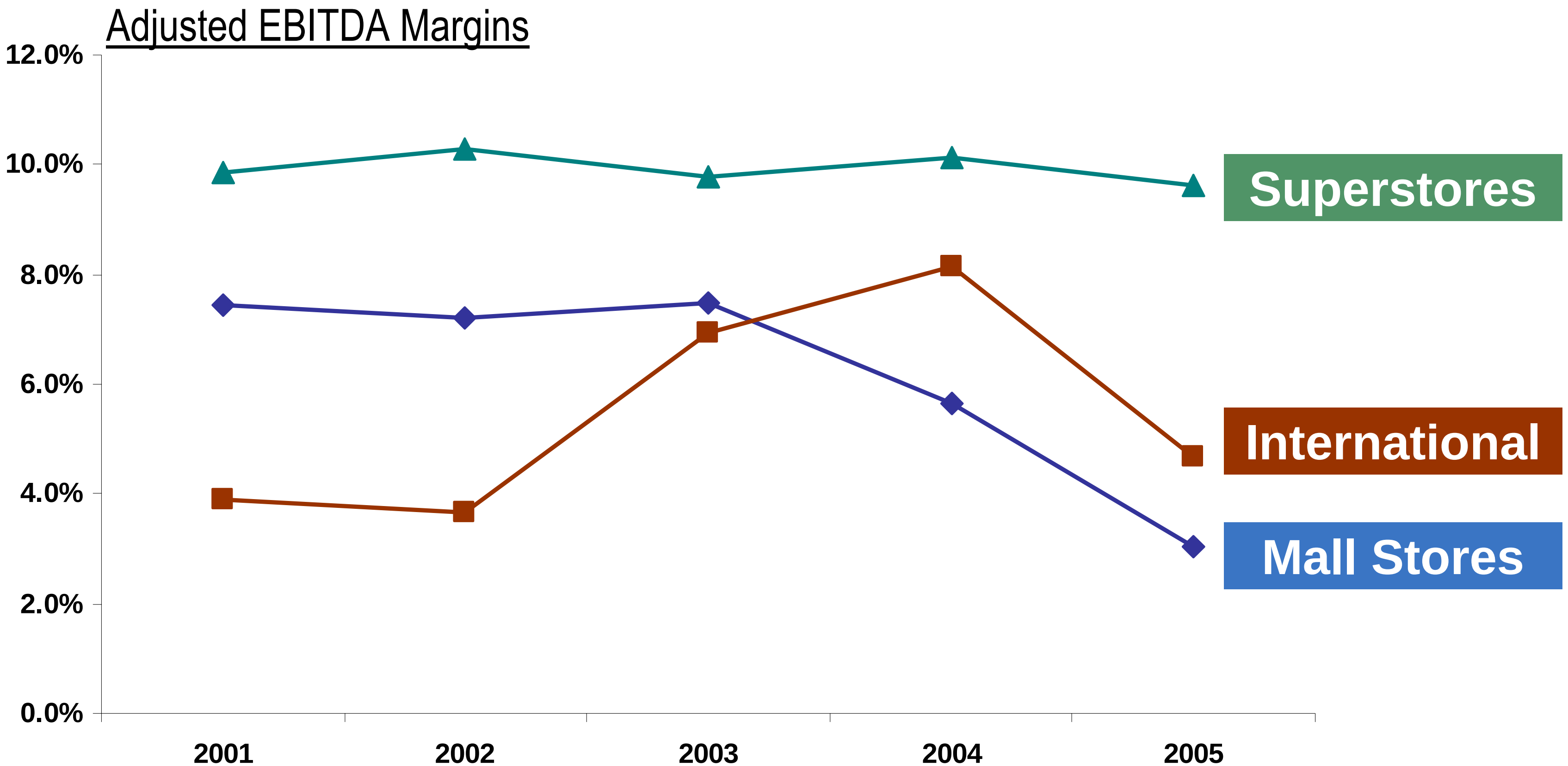
Mall Stores

International

2. High-Quality Businesses Obscured by Money-Losing Businesses

Healthy Superstores Obscured by Bad Businesses

Superstores profitability and stability have been obscured by the Mall and International businesses, which are currently being rationalized



Note: EBITDA Adjusted for non-cash asset impairment associated with store closures.

Within Superstores, there is Opportunity…

Superstores performance has also been masked by declining music sales and certain one-time costs in 2006

- **Company has initiated a Store Remodel Program**
  - Reduce exposure to declining Music sales
  - Increase high-margin Paperchase and Coffee sales
- **Newly launched Rewards program and several one-time expenses have created noise in reported 2006 financials, obscuring results**
  - Expenses for consolidating distribution centers, launching rewards program and remodeling store base
- **Superstores EBITDA could increase by 40+% by 2008 as result of improved product mix, unit growth and elimination of these one-time expenses**

Borders Superstores

Superstores: “Mini Mall” with several “Tenants”

Books	“Anchor tenant.” Stable business
Café	Seattle’s Best. “Mini-Starbucks.” High margin + growing
Paperchase	Specialty paper like *Kate’s Paperie*. High margin + growing
Music	Deteriorating rapidly
DVD	Growth slowing

Superstores: Operating Data

- **Typical store has 25,000 sq. ft**
  - Up to 200,000 titles of books, music, movies plus a Cafe
- **Attractive unit growth**
  - 476 superstores
  - Current plan is to grow 30 units / year (~6% annually)
- **Unit economics:**
  - $2.4mm of invested capital ($1.2mm of fixed assets, $1.2mm of NWC)
  - Average unit sales of $5.7mm
  - Avg. 4-Wall EBITDA – Maint. Capex contribution of ~$700k
  - ~29% "stabilized" unlevered ROI

$$\frac{\$700}{\$2{,}400} = 29\%$$

Based on Pershing estimates.

Superstores Historical Financials

Over the last five years, the Superstores segment has generated steady Adj. EBITDA margins between 9.6% - 10.3%

($ in millions)	2001	2002	2003	2004	2005
Operating Data:					
Units	363	404	445	462	473
Growth		*11.3%*	*10.1%*	*3.8%*	*2.4%*
Reported SSS	*2.0%*	*-1.2%*	*1.2%*	*0.6%*	*1.1%*
Financial Data					
Sales	**2,234**	**2,319**	**2,470**	**2,589**	**2,710**
Growth		*3.8%*	*6.5%*	*4.8%*	*4.7%*
Adj. EBITDA	220	239	242	262	261
Margin	***9.8%***	***10.3%***	***9.8%***	***10.1%***	***9.6%***
Growth		*8.5%*	*1.2%*	*8.6%*	*-0.6%*

EBITDA adjusted for non-cash asset impairment associated with store closures.

Music Category Exposure Has Hurt

Excluding Music sales, Superstores same store sales ("SSS") trends have averaged 1.5% more than average reported comparable sales, based on our estimates

	2001	2002	2003	2004	2005	
Reported Superstore SSS	**2.0%**	**(1.2%)**	**1.2%**	**0.6%**	**1.1%**	**Avg. 0.7%**
Estimated Music SSS	(4.0%)	(8.0%)	(11.4%)	(12.0%)	(12.0%)	
Music % of Sales	22.0%	17.0%	16.0%	15.0%	11.0%	
Music Impact on Reported SSS	(0.9%)	(1.4%)	(1.8%)	(1.8%)	(1.3%)	
Est. Superstore SSS (ex-music)	**2.9%**	**0.2%**	**3.0%**	**2.4%**	**2.4%**	**Avg. 2.2%**
Difference	**0.9%**	**1.4%**	**1.8%**	**1.8%**	**1.3%**	

Remodeling: Improving the Superstore

Remodeling program will reduce Music category exposure by ~50% and improve Coffee and Paperchase sales

- **Reducing Music category exposure and replacing with high-margin Paperchase category**
  - Music margins are ~20% versus Paperchase margins of ~50%
  - Paperchase has higher sales per square foot than Music
- **Upgrading Café offering to Seattle's Best Coffee (Starbuck's subsidiary)**
- **Significant financial benefits in Year 1**
  - Estimated storewide 2.6% sales lift
  - 40bps of margin improvement due to mix shift to higher-margin products with minimal maintenance capital requirements
- **Remodels one year after conversion continue to outperform**

Remodeling: Attractive Use of Cash Flow

Based on the first year of remodel activity, the New Format Superstores should have over 22% return on remodel cap ex

$ in thousands	Old Format	New Format	Commentary
Revenue	$5,700	$5,848	
Sales Lift (Year 1)		2.6%	
Incremental Sales		$148	
Contribution Margin		35.0%	**Note: 40% current contribution margin**
Profit on Incremental Sales		**$52**	
Margin Benefit from Mix (Year 1)		40 bps	**Seattle's Best Coffee / Specialty Paper**
Margin Increase from Mix		**$23**	
Combined Margin Benefit		**$75**	
Remodel Cost (net of W/C reduction of $15k)		**$335**	
ROIC (Year 1)		**22.5%**	

Based on Pershing estimates and management guidance.

Rewards Program Creating "Noise" in Financials

Newly launched Rewards Program has created noise in Superstores financials

- **What is the Rewards Program?**
  - 5% of all purchases (triggered at $200 per Rewards customer) are credited towards a Holiday Spending Account
  - "Use it or lose it"
- **What is the impact?**
  - Accrual assuming 100% redemption
  - Launch and accrual expenses have reduced YTD Superstores segment EBITDA compared to prior years
    - Rewards accruals of $8.4mm
    - Advertising and payroll for launch of $4.2mm
    - Reduced YTD EBITDA by 18%

Rewards Program Creating “Noise” in Financials

What will be the impact of Rewards going forward?

- **Q3 reported earnings will feel the most impact**
  - Accrual amount likely to accelerate as larger member base exceeds $200 spending level
  - Q3 is historically the weakest quarter, usually breakeven to slightly negative earnings
- **We expect that Q4 will see a positive impact from Rewards**
  - We believe Q4 guidance conservatively assumes high redemption rate and no incremental sales
- **Prior year test markets showed positive impact**
  - Comparable sales in test markets were higher – implying incremental sales
  - Avg. ticket w/ rewards credit was 2x avg. ticket w/o rewards credit

One-Time Costs Expected in 2006E

Redundant distribution center costs: YTD $7.8mm

Launch of Rewards: YTD: $4.2mm

One time P&L impact of Remodels: YTD $2.5mm

Superstores Segment Financials

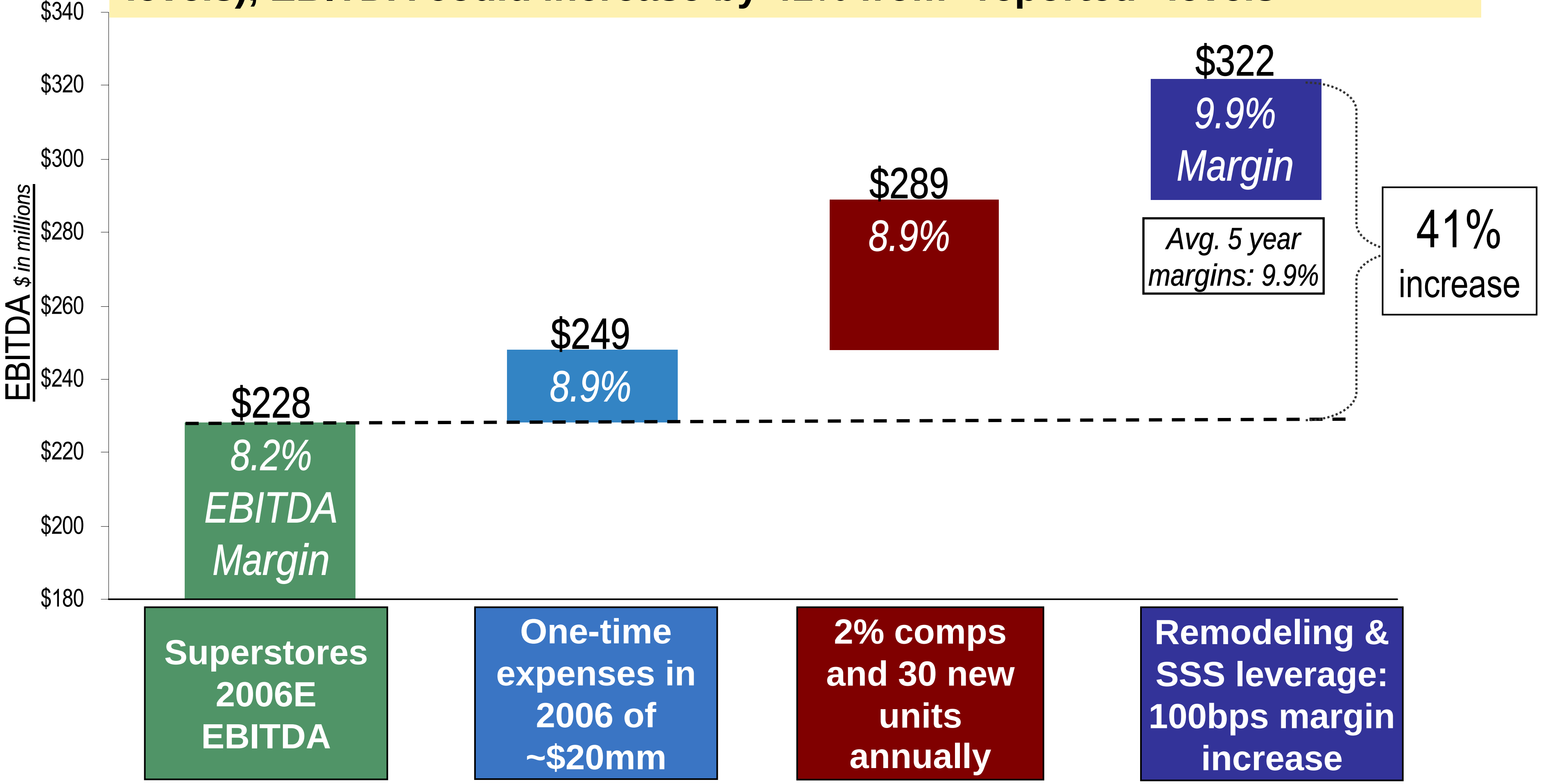
($ in millions)

	2005A	2006E
Same store sales	*1.1%*	*0.0%*
Revenue	**$2,710**	**$2,795**
EBITDA	**261**	**228**
Margins	*9.6%*	*8.2%*
One time costs:		
Redundant Distribution Center Costs		$10
Advertising / G&A for Launch of Rewards		5
Impact of Remodels		5
Total		**$20**
Pro Forma EBITDA		**$249**
Pro Forma Margins		**8.9%**

Based on Pershing estimates.

What Could Superstores EBITDA be in 2008?

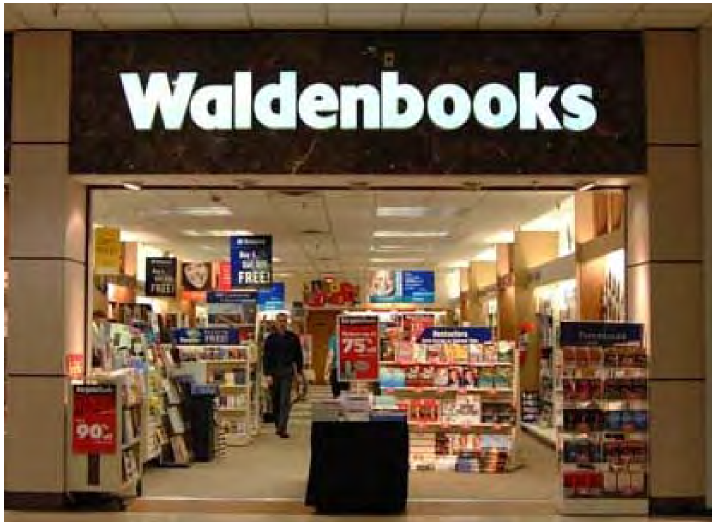
Assuming 2% comps and the Company's unit growth plan, if EBITDA margins were to improve 100bps by 2008 (returning to 5-year average levels), EBITDA could increase by 41% from "reported" levels



Working Capital Opportunity

Potential for $130mm of cash flow generation (or ~12% of the current equity market value) through working capital improvements at Superstores over the next 2 years

- **Net Working Capital at Superstores currently at ~$550M**
- **Company can reduce working capital by 10-15% near term and 30-40% in the long term**
  - Consolidating distribution centers and new merchandising system
  - Increasing “face outs” / decreasing stock
- **Current Superstores inventory turns of ~1.7x**
- **We have assumed Superstores segment achieves inventory turns equal to 2.2x, a discount to Barnes and Nobles at ~2.4x**
  - Equals approximately ~$130mm of free cash flow generation



Mall Stores

Mall Stores: Obsolete Format

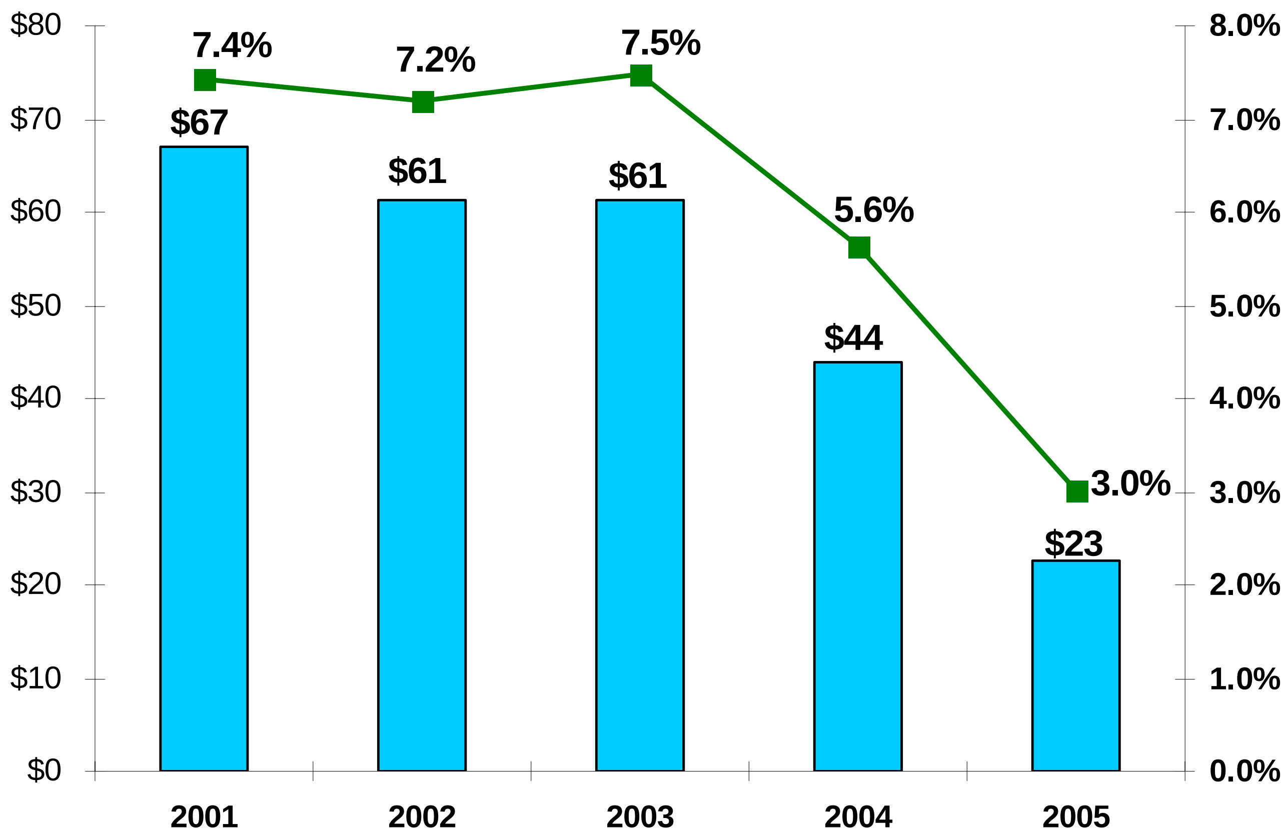
<u>Obsolete Format:</u> Mall stores have difficulty competing with Mass Merchants on price and with book superstores on selection / "experience"

- **~600 Waldenbooks stores**
- **Typical store has 3,000 sq. ft and 30,000 titles**
- **Best sellers are a higher % of sales**
- **Weak margins / deteriorating business**
  - 2006E Revenues of $615mm and EBITDA of $5m
  - Seasonal Calendar Kiosk business is the main EBITDA contributor
- **Barnes and Noble has exited nearly all mall locations…**

Mall Stores: Deteriorating Business

Mall segment Adjusted EBITDA margins in 2005 were 3%, having fallen ~60% since 2003

Adjusted EBITDA
($ in millions)



Adjusted EBITDA Margins

Note: EBITDA Adjusted for non-cash asset impairment associated with store closures.

Mall Stores: Rationalization Plan

- **410 Mall Stores (~70% of total) have leases expiring in 2006**
- **Management says that 200 are profitable, 200 are marginal, and 200 are losing money**
- **Plan to close unprofitable stores as leases expire**
- **Remaining stores negotiate rent reductions with 1-year renewals**

Mall Stores: “Worth More Dead than Alive”

Assuming $150,000 of Net Working Capital on average per Waldenbooks store, we believe there is $90mm of total Net Working Capital trapped in the Mall segment

Waldenbooks Total Units	600
Net Working Capital per store ($000)	$150k
Total Net Working Capital ($ in mm)	**$90mm**

2006E EBITDA	~$5mm

BORDERS®

U.K. Australia

International

International Stores

- **U.K. stores**
  - 37 Borders Superstores
  - 31 Books, Etc. (small format)
  - 90 Paperchase
- **Australia / New Zealand:** 18 Superstores
- **2005 EBITDA margins of 4.3%**
  - Significantly lower than 2005 Superstore margins of 9.6%
  - We estimate International 2006E EBITDA margins of 1.5% (assuming revenue of $650mm and EBITDA $10mm)

International May Be Sold if Not Fixed Soon

Management has indicated it would sell the International business (franchising) if it can’t be fixed in a timely manner

- **International Segment has seen dramatic deterioration**
  - UK Business is struggling
  - Books, Etc. (small format) stores are obsolete and have negative EBITDA
  - UK Superstores challenged, contributing <$10mm of EBITDA
- **Aus/NZ business is healthy, contributing ~$10mm of EBITDA**
- **Management sees no synergy to operating international markets, has ceased additional development**

International: Worth More Dead than Alive?

Based on our assumptions, we believe there is approximately $110mm of Net Working Capital in the International Stores

	NWC / Store	# of Units	Net Working Capital (mm)
UK Superstores	$2.2mm	37	$80
Books, Etc. (small format)	$285k	31	9
Australia / NZ Superstores	$900k	18	16
Other (Puerto Rico, Singapore, etc…)	$1.2mm	4	5
Total (in mm)			**$110**

2006E International Stores EBITDA (mm)	**~$10**

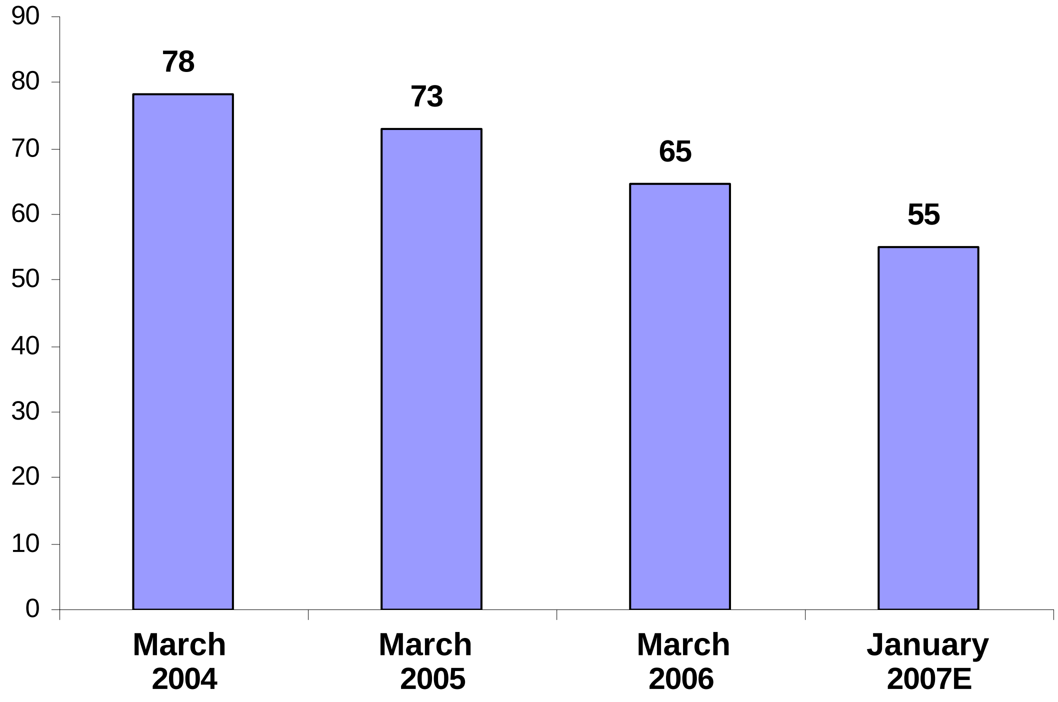
BORDERS®

3. *Other Factors:* Share Repurchase Activity and New CEO

Strong Share Repurchase Focus

Borders management guidance implies ~55mm common shares outstanding by January 2007. This is an approximate 30% reduction from its common share count in March 2004 of 78mm.

Borders common share outstanding



New CEO: Focused on Returns

- **New CEO, George Jones**
  - Joined in July
  - Purchased ~$1mm of stock
  - Retail merchandising and operations expertise (Target, Warner Bros., Saks)
  - Renewed sense of urgency
  - Fixing / rationalizing the business
  - Emphasis on returns

Valuation

Valuation Assumptions

We believe our valuation assumptions are conservative

- **No EV / EBITDA multiple expansion**
- **Mall and International Segments value based on NWC**
  - The least these segments are worth
  - Upside at International segment -- it was generating $40mm of EBITDA in 2004 (versus ~$10mm in 2006E)
- **Reduced share repurchase rate**
  - Current rate of ~$250mm/year
  - We assume $80mm/year (proceeds from Superstores net working capital improvements and FCF after capex)
  - No incremental leverage to fund share repurchases

Borders Group: What's It Worth?

With no multiple expansion, Borders could be worth $36 in the next 18 months, a 72% premium to the current price (of $21).

Segment	Methodology			Commentary	Value
Superstores	**7.0x**	'08E EBITDA of	$322	Assumes no multiple expansion	**$2,257**
Mall Stores	Value of Net Working Capital			The least it's worth	**90**
International	Value of Net Working Capital			The least it's worth	**110**
Unallocated G&A	**7.0x**	'08E EBITDA of	($25)		**($175)**

Enterprise Value	**$2,282**
Less: Net Debt expected at Year End 2006	(450)
***Equals:* Equity Value**	**$1,832**
FD shares outstanding expected at year end 2006	55
Less: Shares repurchased using $130mm from NWC improvement at Superstores, net of options [(1)]	(4)
***Equals:* FD shares outstanding**	**51**
Share price	**$36.17**
Premium to current price	***72.2%***

$ in millions,
except per share data

(1) Assumes $130mm of proceeds from Net Working Capital improvement and $30mm of FCF generated between 2007 – 2008 used to repurchase shares at $30 per share. Fully diluted calculation based on the treasury stock method and assumes ~7mm of options outstanding by FYE 2008.

Trading Multiples at Target Valuation

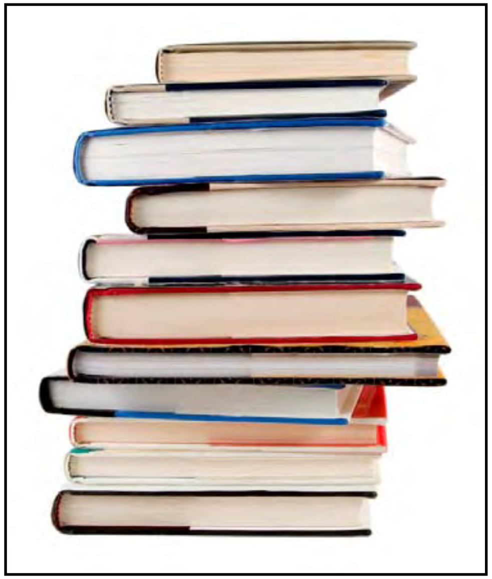
At a $36 share price (adjusting for ~$4 of equity value ascribed to the NWC at the Mall and International Stores), Borders would trade at 7x ’08E EBITDA, 7.5x ’08E EBITDAR and approximately 11x ’08E Maintenance Free Cash Flow

BGP Trading Multiple	2008E
EV / EBITDA	**7.0 x**
EV / (EBITDA - Maint Capex)	**8.4 x**
Adj EV / EBITDAR	**7.5 x**
Price / Earnings	**14.7 x**
Price / Maint Free Cash Flow	**10.9 x**

Recent LBO Leverage Levels

At a $36 price, Borders would trade at 7.5x ’08E EBITDAR, only a slight premium to 6.8x, the average of total leverage levels used in several recent retail LBO transactions

Transaction:	Purchase Price EV / EBITDA	Total Leverage Adj. Debt/ EBITDAR
Linens 'n Things	7.7 x	6.2 x
Burlington Coat Factory	7.4 x	6.5 x
The Sports Authority	7.7 x	6.8 x
Michael's Stores	11.0 x	7.8 x
Average	**8.5 x**	**6.8 x**



Concluding Thoughts

Concluding Thoughts

Borders is similar to other investments where we have had success

- **Value of high-quality segment obscured by performance of low-return segments**
- **Traditional sentiment on the Company is "negative" or neutral at best**
- **Market is more focused on consolidated same store sales rather than the underlying business quality**
- **New CEO is focused on making changes to fix the business**

Concluding Thoughts…

Investment requires a long-term view…

- **Near-term performance impacted by current business structure and initiatives (Rewards, Remodeling, etc…)**
- **Near-term risk is somewhat mitigated by an upcoming slate of strong book releases**
- **We believe it will take time for management to realize full opportunity**

BORDERS®