LUISS

Department of
Business and Management

Chair of Equity Markets & Alternative Investments

Private Equity Investments in the Sports Industry.
E1 Series: How the First-Ever Electric Powerboats Championship Can Attract Funds' Interest.

Prof.

Marco Morelli

SUPERVISOR

Prof.

Guido Traficante

CO-SUPERVISOR

ID: 722731

Lorenzo De Spirito

CANDIDATE

Academic Year 2020/2021

Page intentionally left blank

Page intentionally left blank

Questa volta a Voi,
Perché ve lo meritate,
Perché mi supportate.

TABLE OF CONTENTS

Introduction.

Private Equity funds are always seeking for new, untapped investment opportunities in order to generate abnormal return for their investors. The Sports Industry is attracting more and more interest from private investors, as the sports ecosystem usually offer huge opportunity materializing in extraordinary returns. The aim of this research is to investigate the trend of Private Equity investments in the Sports Industry, to then assess the potential of the first-ever electric powerboats championship, E1 Series, and suggest a dashboard of key actions to implement in order to attract PE funds' interest.

In the first chapter, "Overview of Private Equity Funds", we are going to deep dive into the most important characteristics of PE funds, as well as the impact the global pandemic has had on their activity and most recent trend, in particular ESG investing.

Throughout the second chapter, "Overview of the Sports Industry", we will analyze this very heterogenous industry through the Porter's five forces analysis, in order to understand who are the key forces that shape the Sports Industry. Moreover, we will conclude the analysis by looking at the main trends and key challenges that are impacting sports organizations.

In the third chapter, "Financial of the Sports Industry", we will understand what the key economics and financial forces impacting the Sports Industry are. Then, we will analyze different ownership structures, both in US and Europe, in order to understand what the consequences are in terms of the sports organization performance, both from a sportive and a financial point of view. To conclude this chapter, we will review the main principles of capital budgeting in the context of sports organizations, ending the analysis with an assessment of key emerging revenue sources in the Sports Industry.

Throughout the fourth chapter, "Private Equity & the Sports Industry. The Formula 1 Case", we will review the investment opportunities in the sports arena and assess the investment thesis of past Private Equity investments in sports organizations. To conclude the chapter, we will go through a business case: CVC/Liberty Group deal involving the ownership transfer of Formula 1, the most famous Motorsports championship in the world.

Lastly, in the fifth chapter, "E1 Series: How to Maximize Value and Attract Private Equity Funds' Interest", we will analyze the first-ever full electric powerboats championship, set to kick off its first season in 2023. We will first go through the business proposition, understanding its business model as well as it key revenue drivers. Then, based on the analysis carried out in the first four chapters and the main findings, a dashboard of three key actions to implement to attract PE funds' interest will be presented.

Chapter One – Overview of Private Equity funds

1.1 Introduction

Capitalism have seemingly increased the pace of changes for the economic framework where corporations live in. Notably, one of the most disruptive changes in the global economy took place during the 1970s and 1980s. In those years, a wave of deregulation and liberalization forced conglomerates and monopolies to focus by breaking up into smaller entities: smaller companies that have been created were useful to address changing and emerging needs.

If on the one hand the size and scope of action of major corporations changed, on the other hand the related sources of financing didn't adapted: whenever a company needed financing, two solutions only were available: the stock exchanges and bank loans. This was true before the liberalization wave, but also after it took place. However, not every company had and nowadays have access to these two sources of financing: the stock market provides access to new capital only for medium and large-sized companies meeting specific criteria regarding their financials and track record; on the other hand, due to regulatory constraints, commercial banks only issue loans to those companies and projects respecting tight requirements. More recently, after the 2008 financial crisis and the consequent Basel III Agreements, banks have been forced to further tighten their financing policies, resulting in the so-called "credit crunch".

All these factors together paved the way for the birth of non-banks finance companies, operating through direct lending. In particular, thanks to new developments in financial markets, companies have been given access to private capital: private equity, private debt and private real assets.

In particular, private equity supports companies at every phase of their life cycle: from the idea-originating process, through the seed financing, to early, mid and late-stage development, through the venture capital and growth capital, during transfer of ownership in leveraged buyouts (LBOs), and lastly restructuring, through the turnaround capital.

Private equity represents the bulk of private markets, with 60% of the documented private market funds activity, private real assets representing 25% and private debt 15%[1].

---

[1] C. Demaria, *Introduction to Private Equity, Debt and Real Assets: From Venture Capital to LBO, Senior to Distressed Debt, Immaterial to Fixed Assets*, 3rd edition, 2020, p. 14.

1.2 Private Equity funds structure.

The term Private Equity (PE) stems for the investment activity in the risk capital of unlisted companies. Historically, this type of investment has always been classified as opposed to liquid investments, typical of regulated financial markets. PE funds are not passive investors, in addition to providing companies with new capital they also take a sit in their boards in order to manage the corporate strategy to reach specific goals, generating the desired return on the investment.

Depending on the jurisdiction where PE funds are incorporated, they can take on different corporate and contractual characteristics. For the sake of this analysis, we will refer to two main models: the Investment Company (see the Italian case where the role of Investment Company is entrusted to the SGR, manager of the fund) and that of the Limited Partnership, a very common model in the United States and in Anglo-Saxon countries.

Although these two models show profoundly different characteristics, it is interesting to highlight that the principles governing the relationship between managers and investors are common to both the Investment Company and Limited Partnership. In particular, we can observe the use of specific incentive schemes to stimulate the performance and align the interests of both actors involved, for example: the protection of the equity interests of investors with privilege clauses in the return on invested capital and in the minimum yield; the managers' remuneration occurs in a significant part through performance commissions, so that their interests are aligned to the ones of the investors, only investing in companies deemed to be profitable; lastly, a final example in favor of what has been said can be identified in the investment, albeit minimal, in the fund by the same managers in this way doubling the sources of returns: on the one hand, investing own monetary resources entails the need to remunerate adequately the investment, while on the other hand by directly investing managers show to potential investors their personal commitment and risk sharing throughout all the process, from companies selection to divestures.

In the most common model, the Limited Partnership, the starting point is represented by a limited number of people incorporate a Limited Liability Partnership (LLP), raising the capital to be invested from a pool of investors. The LLP has a limited life, typically corresponding to a decade, and is substantially a closed investment fund. Within a LLP there are two key type of players: the investors, also known as Limited Partner (LPs), and the managers, also known as General Partners (GPs). LPs include all the subjects who, on the basis of their financial capacity, can invest in the fund, such as: pension funds, banks and insurance companies. GPs can deliver returns in two ways: by charging periodic fees to the fund in the form of management fees, or other fees on the capital they manage such as the so-called carried interest, a remuneration scheme recognized to managers when they meet certain profitability targets. In general, after the fund has returned the initial invested capital to the investors, earned profits are divided so that 80% go to the LPs and 20% to the GPs.

The advantages of a Limited Partnership are to be identified in its organizational structure, as it is considered the most effective formula to offer investors the best contractual conditions, emerging in a pro-active management style. This is an important differential aspect as compared to the European framework and its Investment Company structure: it is noted that, in this second case, a reactive style is much more frequent, more similar to that of fund managers in general.

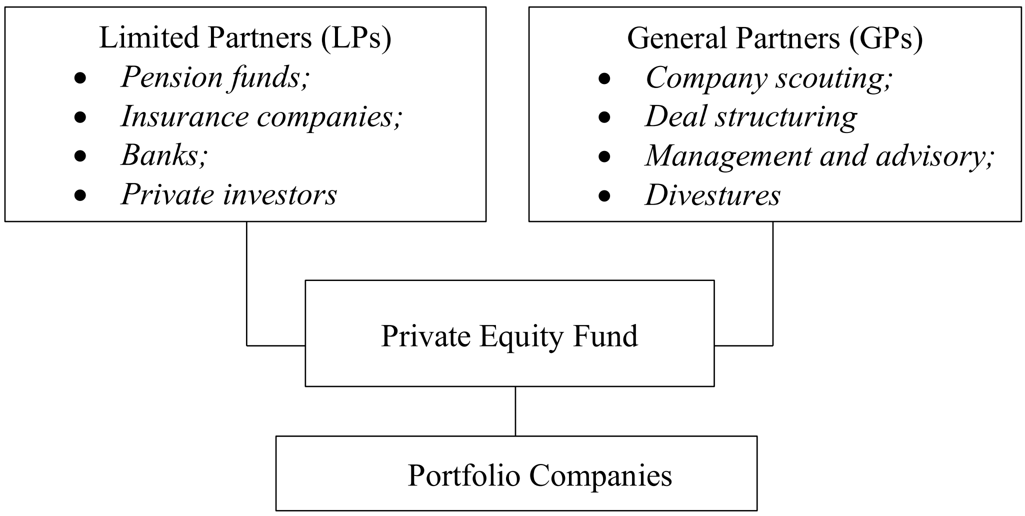

Figure 1.1 – Limited Partnership structure

The second most widespread organizational model that a PE fund can take on is the closed-end funds scheme, typical of the Italian framework, which is shown below through figure 1.2. As it can be seen from the diagram below, it is evident how a management company which promotes and manages the funds themselves is necessary. Managed funds will have different characteristics in terms of investment focus, whereby each fund will have its own portfolio of target companies. Investors who choose to join a fund promoted by a specific management company can decide where to direct their investments on the basis of the prospectus provided before the subscription phase, where the main characteristics of the fund are described.

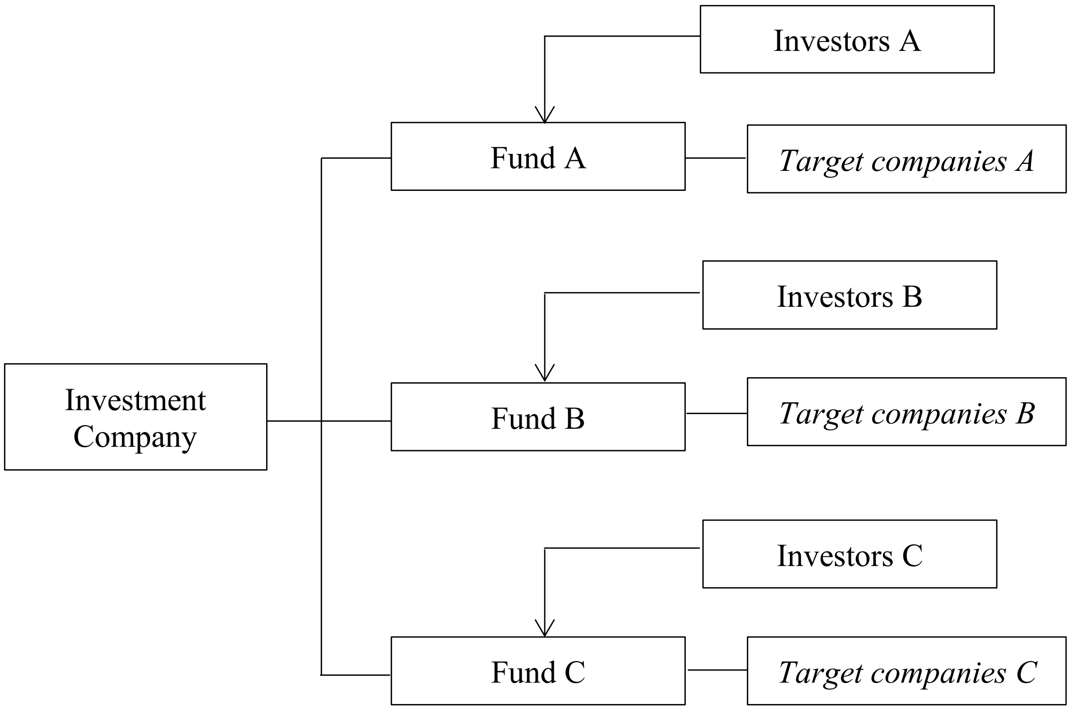

Figure 1.2 – Investment Company structure

The main difference between the first and second model concerns the clear separation between the capital of the management company, that of the funds and, within each of them, of each investor. While in the Limited Partnership the investors enter the fund assets as limited liability shareholders, in the case of an Investment Company at the time of capital subscription, the investors are allocated a number of shares and, on the basis of the shares held, the percentage of membership of the fund is determined.

The Investment Company may, in turn, be an investor in the fund promoted by itself. The commission scheme is similar to what has already been seen in the case of an LP, but in this case the management fees are withdrawn from the fund in favor of the Investment Company, and the same thing can be said for the performance-related fees. In this way, investors are paid a percentage of the capital gains of the fund equal to 70-80% similar to what happens to the LPs. In this second model, the Investment Company is not obliged to enter the fund's capital, which is, however, implicit in the first model; certainly, as already mentioned, the participation of the Investment Company itself increases the credibility of the objectives indicated in the prospectus.

Irrespective of the organizational structure of the PE fund, potential investors who have been presented with an interesting investment opportunity will start an in-depth analysis phase which, generally, starts with the evaluation of the investment team. According to the AIFI

(*Associazione Italiana del Private Equity, Venture Capital e Private* Debt), with regard to the investment team, the main variables under investigation can be summarized as follows:

- Experience and track record;
- Level of team cohesion;
- Personal and ethical qualities of key people;
- Mix between financial and business skills;
- Balancing of seniority within the team;
- Structure of the decision-making process;
- Involvement of key players in management activities;
- Motivation of team members.

The analytical skills of the investment team is one of the central points for any investor in a PE fund, and therefore it is the due diligence phase to which the most time is devoted. Potential investors will meet most or all the people who are part of the team through both group and individual interviews, with the aim of evaluating previous experiences of key members by examining the operations carried out and their investment style. Moreover, great attention is usually paid to understanding the internal dynamics between team members, to ensure that there is a good degree of cohesion within the group, and that complementary skills coexist. A not negligible risk, in fact, is that the key people of the management company have valid qualities individually taken and significant management experiences, but that it is then difficult to harmonize the group as a whole. Attention should also be paid to the personal structure of the team, which must present the right mix of seniority and an adequate presence of junior people who can, over the usual ten years of life of a fund, grow and if necessary, replace a senior member who for any reason leaves the team, ensuring an adequate generational change to the whole structure[2].

In recent years, PE funds' investors have gradually increased their focus not only on the investment team analysis, but also on the structure supporting the operations. In particular, major areas of concerns regarding the support structure are[3]:

- Internal compliance structure;
- Outsourced functions;

[2] G. Campanella, W. Ricciotti, *L'investimento in un fondo di private equity: guida al processo di selezione e due diligence*, AIFI, 2012, pp. 17.
[3] G. Campanella, W. Ricciotti, *L'investimento in un fondo di private equity: guida al processo di selezione e due diligence*, AIFI, 2012, pp. 18.

- Back office and portfolio evaluation process;
- Custodian bank quality;
- Completeness of control procedures;
- Risk management procedures;
- Reporting structure.

According to the AIFI, for these aspects it will be necessary to pay particular attention to the excesses of formalization by verifying the substantiality and effectiveness of the control systems.

1.3 What do Private Equity funds do?

The objective of the active PE investor is to invest in the risk capital of companies having great potential, and to enhance their assets aiming at divesting within a medium-long term horizon. The goal of this type of investments is to generate a return that, weighted for the embedded risk, is profitable for the investors, once the investments have been liquidated. In most cases, PE investors don't receive periodic dividends as for "classic" equity stakes, but rather they cash in the increase in the value of the share of capital held. To monetize that increase in value, i.e., the capital gain, PE funds must wait for the transfer of the assets in their portfolio, which is why in almost all cases the return on the investment is achieved in the medium to long term.

On the other hand, from the companies' founders' point of view, opening up the risk capital to PE investors generally denotes the willingness to grow thanks to the guidance of professionals in the sector, sharing with them any realized capital gain. Other times, especially during the early stages of a company's life, this type of investment is the only way of raising new capital that can be implemented by young companies having no structured track records, which therefore would not obtain financing from standard financial institutions, such as banks.

Within the PE macro-class, we can distinguish three different main sub-classes: Venture Capital, Growth Capital and Leveraged Buoyout (LBO).

Venture Capital can be defined as any investment aimed at supporting the birth of a new entrepreneurial initiative, whether it is still in the idea-stage or in the start-up phase. From the demand of capital point of view, the request for intervention from specialized investors is generally attributable to an entrepreneur, or aspiring ones, willing to develop a new invention, or to improve an existing product or production process. Beside new capital, what the bearer of a new business idea often needs is a contribution in terms of entrepreneurial ability and managerial skills. In start-up or early-stage deals, entrepreneurs often need help in defining the entrepreneurial formula and in assessing their competitive positioning. At the same time, the investor must necessarily have trust not only in the potential of the business, but also in the team who will lead it with him. Venture Capital configure itself as a high-risk investment, as such generating high return whenever the entrepreneur and specialized investors manage to transform the business idea into a structured and profitable company.

On the other hand, Growth Capital represents a minority investment in the risk capital of companies seeking new funds to finance their growth strategies, where the return on the investment is mainly driven by a consistent EBITDA expansion[4]. Companies looking for growth capital are typically more structured than the ones financed through venture capital. Growth Capital target companies are able to generate revenues and profit, but they are generally unable to deliver a sufficient liquidity level to finance their business expansion. Growth Capital deals are usually structured as privileged capital, even if in some cases investors rely on hybrid financial instruments, such as mezzanine debt.

The last sub-class in the PE cluster, the Leveraged Buyout, consists in acquiring a majority/hundred per cent stake in a target company by financing the acquisition with a higher-than-average debt level. The debt is usually financed by one or more financial institutions organized as a consortium (usually banks) and is generally secured through the company assets, then it is paid back during the investment period through the free cash flows (FCF) generated by the target company; on the other hand, the PE fund act as a sponsor by providing the risk capital in the acquisition. A typical LBO deal can be seen as an investment process structured in four different steps: the first phase involves the collection of the necessary funds (both debt and equity) and the creation of a management incentive scheme; the PE fund, also known as financial sponsor, usually contributes with 30-50% of the transaction price, with the remaining portion being financed through debt; during the second phase, the financial sponsor buys all or the majority of the target's stocks; in the third phase, under the guidance of the sponsor, the target management team implement growth strategies to improve the company valuation; lastly, during the fourth phase the financial sponsor, that is the majority shareholder of the company, look for exit strategies in order to divest and, possibly, realize a capital gain. PE funds that decide to invest in target companies through LBOs generally aim at exiting from the investment within 3-5 years (exit strategies will be analyzed in the following pages).

[4] R. Ippolito, L. L. Etro, *Private Capital. Principi e pratiche di private equity e private debt*, 2019, pp. 127.

A typical LBO candidate is a mature company having the following characteristics[5]:

- Stable free cash flows: the ability to generate significant, resilient and predictable FCF is the key driver of any LBO candidate. This imply that companies belonging to regulated, mature or niches industries with high barriers to entry, having consolidated and long-term partnerships with their clients are the typical LBO candidate. In addition to that, companies having low capex needs are usually preferred.
- Consolidated positioning in the market: injecting high levels of debt into mature companies with lower investment needs is a simpler and safer task. Moreover, in mature industries the company assets have higher market values as secondary markets for those assets are more efficient with respect to less mature industries, and this increase the target ability of issuing secured debt.
- Market leadership and competitive advantage: a relevant market share implies the existence of a consistent client base, a strong brand or better cost conditions; all these key success factors increase the FCF stability and predictability.
- A strong asset-base: valuable assets can be used as collateral to issue secured debt at a lower interest rate, reducing the counterparty risk for the financial institutions.
- Management team with a good track-record: industry knowledge, the ability to manage a heavily indebted company and the achievement of ambitious performance targets are key elements for a successful management team during an LBO. A good practice during LBO deals is to make the management team committed to the achievement of the set performance target by investing directly in the company, in this way aligning managers objective with those of the company.

We have seen how the PE family is a fluid cluster, adapting to each one of the company's life cycle.

[5] R. Ippolito, L. L. Etro, *Private Capital. Principi e pratiche di private equity e private debt*, 2019, pp. 151-153.

1.4 The life cycle of Private Equity funds.

1.4.1 Capital raising process.

Regardless of what services the PE fund provides to the target companies and the amount of capital it invests in them, the fund relies on investors who are willing to commit substantial capital, for extended periods of time, in high-risk activities[6]. Private Equity investors typically belong to the cluster of institutional investors (not retail ones); among all:

- Pension funds, collecting large amounts of capital to be invested in a long-term horizon, having no liquidity constraints in the short-term;
- Family offices;
- Banks and insurance companies;
- Foundations, from banks to universities above all, which are able to collect a huge amount of money from donations.
- Funds, which invest in other funds, the so-called "funds of funds".
- Financial holding companies.

The capital raising can be undertaken in two ways. On the one hand, it can take place through the management team in the vest of promoter, looking for investors who are willing to commit their financial resources in the fund; on the other hand, the needed capital can be raised by hiring an placing agent, who has a broader market vision, with specific advisory skills and usually having a strong network of potential investors. Once the investors enter into the selection process, they receive an information memorandum containing all relevant information to carry out a proper evaluation of the fund and its management team: achieved returns, management team track-record and past experiences. Besides the information on the fund itself and the management team, the information memorandum contains all the terms and conditions of the proposed investment. If the investor decides to invest in the fund, he/she commits himself/herself in providing the fund with the subscribed capital whenever it would be asked to do so. Once the fund achieves a predetermined amount of subscribed capital, the process stops, and the next phase starts.

[6] E. Talmor, F. Vasvari, *International private equity*, 2011, pp. 30-34.

1.4.2 Company scouting and investment processes.

The next step corresponds to the portfolio companies' selection process. This process should always start with a careful analysis of the investors' objectives and constraints. Three key aspects should be taken into consideration. First, the amount that is deemed appropriate to be invested considering total capital subscribed by the investors. Second, the temporal sustainability of the investment, since the PE investment is carried out over a medium-long term horizon and it cannot be easily liquidated, even if in recent years a secondary market has developed quite lively (i.e., operators who buy shares subscribed by previous investors during the life of the fund). The third element that must guide the scouting process is the expected risk-return profile[7].

At first, the fund starts the selection process by gathering public information on a large pool of companies (hundreds), usually belonging to those industries where the management team has specific knowledge and skills, respecting other constraints too, such as the life cycle phase they are in[8]. After having gathered public information on the selected panel of companies, the selection process starts with the aim of reducing the number of selected companies to a smaller number. Once interesting companies have been assessed, the fund signs a so-called Non-Disclosure Agreement (NDA) to collect private information, such as: last three years balance sheets, existing contracts with customers and suppliers, companies' competitive positioning and their management team. To carry out standing selection process, the funds analyze all that private information through a business plan, representing a picture of the company, both in terms of track-record and forecasted performances. If this preliminary research shows that the objectives of the entrepreneur and those of the fund's management team are aligned, the fund proceed with a deeper analysis. In this phase, the analysts working for the fund carry out a first preliminary due diligence, much less expensive and demanding than the final one which, as we will see, will be carried out at a later stage. This consists in the analysis of the documents provided by the company to the fund; here, the purpose of the fund is to identify potential sources of risk, defining mitigating strategies and possible solutions.

If the preliminary due diligence process ends up with a positive outcome, then a non-binding offer is sent to the company. Depending on the specific characteristics of the company being analyzed, the fund can decide to look for co-investors that are willing to invest in that

[7] G. Campanella e W. Ricciotti, *L'investimento in un fondo di private equity: guida al processo di selezione e due diligence*, AIFI, Commissione rapporti con gli investitori istituzionali, 2012, p. 14.
[8] E. Talmor, F. Vasvari, *International private equity*, 2011, pp. 88-90.

company, usually looking for funds focused in specific industries in order to reach a higher level of knowledge. Preliminary information contained in the non-binding offer, such as the offered price, are to be confirmed after the full due diligence process has been taken, gathering all the necessary information to carry out a proper company evaluation. The non-binding offer is contained in the so-called “Letter of intent” (LoI), aimed at formalizing the commitment between the selling and buying parties to define the main terms of the agreement.

Here the execution phase begins, where the fund runs the full due diligence and at the same time the draw up of the sale contract with which the transaction will be formalized after the due diligence starts. The first due diligence to be carried out is the business due diligence followed by accounting one, carried out by professional accountants, usually auditing firms. The purpose of these due diligence is to confirm key business elements contained in the business plan, and to assess potential risks, hidden liabilities or critical areas. This are not only very important information to evaluate the company, but also serves to identify the corporate culture and possibly bring out the most hidden problems. At this stage, the fund starts structuring its own idea of the company and of its future management process, and the value of the company is gradually assessed to guide the fund in offering the right price in the final contract, including any clauses the fund may wish to include to cover potential risks.

Besides the business and accounting due diligence, the funds also analyze the company by looking at its industrial, fiscal, legal, environmental, IT and insurance characteristics, running a due diligence for each of those areas. All these analyses are carried out as a risk mitigation tool in order to identify any possible risk: some risks may have consequences on the final offered price, others may even lead to the failure of the transaction.

The industrial due diligence is aimed at assessing the current state of the company assets, such as any plant and machinery, in order to check whether any investment is needed to run the core business of the company.

The fiscal due diligence, usually carried out by external advisors, is needed to ensure that all taxes prior to the acquisition have been paid, as an investment in the risk capital also implies consequences on the new shareholders if irregularities rise. In addition to the payment of specific taxes or fees, it is also a question of checking whether there are existing disputes underway with the tax administration that must be evaluated to identify possible negative repercussions.

On the other hand, the legal due diligence is carried out by large lawyers’ firms, analyzing existing contracts with strategic partners, authorizations granted to the company, violation of any rules on contracts with customers, suppliers, workers and, finally, the existence of possible disputes in progress.

Gaining more and more importance in recent years, the environmental due diligence verifies that the company is not exposed to pollution risks, and that it meets all the regulations on noise, chemical agents and urban profiles.

As well as the environmental due diligence, in recent years the IT due diligence too increased its relevance. The increased complexity of IT systems adopted by most of the company is requiring an additional level of scrutiny when performing a full due diligence.

Lastly, the insurance due diligence is carried out to assess what is intended to be insured after the acquisition takes place and how it translates in terms of costs.

Once all the risks have been assessed and the full due diligence has been carried out, the investment proposal is sent to the board of directors or to the investment committee. Then, if they approve the transaction, managers start collecting the capital subscribed by the investors and, in parallel, they also submit the investment proposal to banks and financial institutions to finance the acquisition.

1.4.3 Investment management.

After having analyzed how a PE fund raises capital to be invested and then choses the portfolio companies to invest in, we are about to deep dive into the investment management process. This step starts with the fund providing the needed capital to the company and the managers implementing any operational activity to increase the company value.

In the investment management process a key decision concerns human resources: a fundamental step is to choose the right management team that will be responsible for the company strategy and its operations. Human resources are of central importance for a company that wants to reach certain performance targets. Successful companies are typically led by a successful team of highly skilled managers, who create an added value over competitors. Given the relevance of the human resources working within a portfolio company, one of the PE fund priorities is to assess the existing employees already working there and, if that is the case, replacing them with more skilled personnel. In this assessment process, the starting point is the CEO, as he/she plays a key role in increasing the value of the company, covering a pivotal role between the company and the PE fund during the investment horizon. For this reason, if the current CEO is not considered to be adequate for the role and linked responsibilities, a PE fund will usually decide to hire a new one belonging to its network. Moreover, during the investment management process, in order to increase the company value and generate positive returns, it is of key importance that the company and CEO interests are as much as possible aligned. To ensure this, it is typically required that the CEO shares some risk with the company and the PE fund by investing his/her own money in the shares of the company. After having assessed the CEO, the next step is managers' level: the objective is to understand whether they have adequate skills to lead the company towards given performance targets. A well-structured management team is fundamental to successfully implement the business plan after the acquisition. The management team will be considered successful if the company will achieve the performance objectives within the required time frame, increasing its value by the end of the investment period. This means that managers must be able to make the company react as quickly as possible to its competitive environment and to any changes in it. Then, after having properly assessed the managers, the analysis continues at lower levels by assessing other employees to understand if the organization as a whole is sufficiently skilled and experienced to guide the company towards growth and value creation.

Once the PE fund has carefully analyzed and chosen the human resources that will lead the company, the management team enters the core of the investment management process. We will now analyze what the new managers do to make the company grow and to deliver outstanding returns for the fund's investors.

The first step is usually a deep dive into the company industry. One of the main objectives is to assess the current state of the industry in terms of recent trends, competition and growth opportunities. Then, another area of analysis involves establishing possible commonalities with similar industries to assess further competitors offering a similar product/service deemed to be substitute. From this analysis, managers can also evaluate possible entries in new markets or new channels.

A useful tool usually implemented by managers to frame this analysis is the Porter's 5 forces model. According to Porter, the 5 competitive forces intervening in a given industry are: threat of new entrants, threat of substitutes, bargaining power of customers, bargaining power of suppliers and competitive rivalry[9].

Studying deeply the industry is also useful to make a 360 degrees assessment of the product/services the company is offering, everything leading to check whether the company is delivering high or low margins. Once identified the current margins, the management team can look for strategies to implement them by analyzing carefully the value chain. First, the attention

[9] M. E. Porter, *How Competitive Forces Shape Strategy*, Harvard Business Review, 1979.

is on primary activities, like operations, marketing and sales, then on support activities, like HR management and IT. A PE fund, through the chosen management team, must be able to identify which phases of the value creation chain are considered to be core, and as such to be internalized, and which ones are to be externalized, in this way creating efficiencies and, possibly, cutting costs.

Overall, the management team has to build strategies to increase revenues or cut costs, possibly both. On the one hand, to increase revenues managers have to understand whether and where growth opportunities lie, both internally and externally. Usually, managers' focus is on the company's core business, as developing parallel revenues streams is sometimes resource-consuming and more consistent with long-term plans, usually exceeding a PE fund investment horizon. On the other hand, to cut costs it is necessary to analyze the cost structure and make it more efficient looking for possible alternatives and best-practices in the market.

1.4.4 Exit options.

When PE funds invest in portfolio companies, their objective is to maximize their value within a 3–5-year time window, and then exiting from the investment. Of course, in doing this the final aim of PE professionals is to meet investors' expectations by delivering outstanding returns. This will help the PE fund in building a strong track-record that will make it easier to raise new capital from new investors. Considering this, it can be said that exit strategies are as important as the investment management process, as they both contribute to the PE fund value creation. The company value maximization at the exit stage depends both on internal and external factors: mainly operations growth and de-leveraging on the one hand, and market conditions on the other hand. In fact, for example, if the company has grown over the years by organic growth, it could happen that at the exit period market's multiples are depressed, and so the company valuation.

Above all, a PE fund that wants to exit from an investment has different options. We can distinguish between two clusters: private and public transactions. On the private side, a PE fund can sell its stake in a company to a strategic buyer (usually a competitor) or to another financial sponsor (secondary buyout); on the other hand, a PE fund can tap the public financial markets and sell its stake through an Initial Public Offering (IPO). We are going to deep dive into each one of these three exit options.

1.4.4.1 Sale to a strategic buyer.

A very common exit option corresponds to the PE fund selling its stake to a competitor belonging to the same industry of the portfolio company. This is usually the most wanted outcome for a PE fund, as the strategic buyer can in most of the cases benefit from synergies arising from the acquisition, and as such it can offer a higher price as compared to other types of buyers. On the other hand, with the acquisition, the management team of the portfolio company run the risk of being fired, given that the acquiring company already has its own, and so internal conflicts of interests would often arise.

To exit through selling to a strategic buyer, the PE fund usually hire an external advisor (an investment bank) to look for potential buyers. In the best scenario, the investment bank identifies multiple potential buyers and set up a competitive process, through an auction, to sell the PE stake. This process would be likely to push the final price up, not only for the abovementioned synergies, but also for the competitive process itself.

1.4.4.2 Secondary buyout.

A secondary buyout takes place whenever a PE fund sells its holding in a portfolio company to another financial sponsor or investment fund. In this framework, every business aspect takes a back seat in favor of purely financial considerations.

To run a successful secondary buyout some conditions must be verified. First of all, at the exit date, the company has to be in a good financial status, meaning that the debt originally issued by the selling PE fund should be totally (or at least in part) paid back, so that the buyer can finance itself the transaction through leverage. So, a key condition to sell a stake through a secondary buyout is deleveraging.

In most of the cases, the financial resources raised during the primary buyout are directed toward operational expansion, instead during the secondary buyout any issued debt is usually intended to finance strategic plans to cut costs, creating economies of scale, and making the organization more efficient overall.

As opposed to the sale to a strategic buyer, in a secondary buyout it could happen that the new shareholder, i.e., the new financial sponsor, decides to let the existing management team leading the company. This can happen as the existing management team has a deep knowledge of the company and is already familiar with reporting to a PE fund and its investors, so it could be not necessary to hire new managers.

1.4.4.3 Initial Public Offering.

As an alternative to private transactions, a PE fund can decide to sell its shareholding by tapping the public financial markets, by selling the company's shares through an IPO. This exit strategy is largely adopted in those jurisdictions where the stock market is developed and well-structured.

What is interesting about an IPO as a possible exit strategy is the fact that in this process the interests of the PE fund and those of the management team are aligned. In fact, in most of the cases after the IPO the management team stays in their sits, so it is in the best interest of both the parties to maximize the company's value at exit. On the other hand, an IPO is a very time and resource-consuming process, where to the management is asked an extraordinary commitment, both to interact with investment banks and other external advisors, both to take on the so-called "management roadshows" to meet with potential investors and run marketing activities.

Not every company can have access to the stock exchange. In fact, formal and informal prerequisites exist. For example, it is asked that the company has to be transparent in communicating with financial markets, and that for example it undertakes structured auditing processes to certify its balance sheets. Moreover, in order for an IPO to be successful, the company needs to show an outstanding track-record and growth path, it has to build trust with potential investors by sharing strong and achievable business plans.

1.5 Covid-19 impact on the Private Equity industry.

Different events taking place in 2020 have put the PE industry, and the whole world economy, to the test. Last year has been tumultuous from various points of view. First of all Covid-19 came in, first in China, then spreading all over the world, impacting every shade of the society. But bad news did not end at healthcare level. Many other events undermined global stability: months of left-sided groups' protests against police, the US presidential elections ultimately leading to an unprecedented mob assault on Capitol Hill, tensions between Iran and the US and oil prices plummeting.

Despite all this bad news, dealmakers did not stop their activity, continuing closing deals while, on the other hand, exits and fund-raising fell in line with five-year averages[10]. As it happened across the global economy, PE activity fell down during April and May 2020, as both buyers and sellers took a step back amid the initial shocks caused by Covid-19 countermeasures undertaken by governments. As a matter of fact, immediately after Covid-19's global spread, few were willing to make buy and sell decisions due to the high uncertainty. However, the trend flipped soon after central banks (both in the US and Europe) decided to flood the economy with trillions, avoiding liquidity to be a concern for companies and financial intermediaries. Stimulus measures implemented by central banks had different effects: first, they boosted confidence that the economic downturn would have been temporal; then, a direct consequence has been the interest rates lowering, making cheap debt available to finance transactions. Moreover, available liquidity making assets prices rising, together with the fears of a capital gain tax increase in the US, made sellers put their portfolio assets on sale.

If, on the one hand, deal count remained depressed all over the year, on the other hand, deal and exit values reverted back vigorously in Q3. In terms of resources invested, H2 ended up being as strong as any second half in recent PE history. If one thinks about PE funds' main characteristics, a strong performance even during economic disruptions is not a surprise: for example, economic downturns typically offer PE funds huge investment opportunities in distressed companies.

In following pages, main characteristics of 2020 investments, exits, fund raising, and returns will be analyzed.

1.5.1 Investments.

Having rebounded impressively from a dismal second-quarter performance (North American deal value alone was off 85% from the same quarter a year earlier), the global industry sprinted to the finish in 2020, generating $592 billion in buyout deal value. That was an 8% jump from 2019's performance and 7% higher than the five-year average of $555 billion. Conversely, Covid-19 had a pronounced negative impact on global deal count, as the number of buyouts fell 24% to around 3,100 in 2020, from 4,100 in 2019. With the exception of the technology and telecom sectors, the number of deals slumped across the business landscape

[10] *European PE Breakdown*, Pitchbook, 19th January 2021.

compared with the five-year average. The retail, consumer, and media and entertainment sectors were among those taking the biggest hits. The reason total deal value rose in 2020 while volume slipped was a 24% increase in average deal size to $776 million[11].

2020's figures are consistent with the ongoing concentration trend characterizing the PE industry, where bigger funds have to close bigger deals to attract investors' interest. An additional factor boosting this trend has been banks willingness to concede financing to larger, more structured deals as compared to smaller one, as they involved more secure and established players.

1.5.2 Exits.

PE funds' exit activity in 2020 followed a similar pattern as compared to investments. As soon as Covid-19 hit, financial sponsors stopped looking for potential routes to be followed to exit their investments. Then, during the second half exit value picked up, with the number of total exits below 2019's figures, but thanks to larger deal sizes, global exit value reached $417 billion in 2020, in line with last five-year average.

Once again, strategic buyers provided the largest exit channel. Sponsor-to-sponsor deals held up well, and initial public offerings increased by 121% to $81 billion as public equity markets soared. Firms also leaned heavily on partial exits, as GPs sought to keep a stake in attractive assets rather than have to hunt down new prospects in a highly competitive deal market. Overall, the median holding period for companies exited in 2020 was 4.5 years, slightly higher than in 2019 but in line with the five-year average[12].

1.5.3 Fund-raising.

One of the main areas of concern regarding economic downturn's consequences on PE funds was a slowdown in the fund-raising activity. Nevertheless, total resources raised during 2020 represent the third-highest total in history, reaching $989 billion, a slight decline from 2019's all-time high of $1 trillion. This confirms that LPs continues seeing PE as a good vehicle to invest their money. In particular, surveys show that around 80% of LPs are confident PE will continue its outstanding performance during 2021, almost 40% of them say they are under

[11] *Global Private Equity Report 2021*, Bain & Company, 2021, p. 9.
[12] *Global Private Equity Report 2021*, Bain & Company, 2021, p. 17.

allocated to the asset class, and lastly the vast majority plan to either increase or maintain their commitments in PE funds during 2021[13].

1.5.4 Returns.

As well as investments, exits and fund raising, PE returns too soared in 2020. A key contributor to the PE funds outstanding performance has been the fact that GPs were ready to face an end to the record-breaking, decade-long recovery that took place after the global 2008 financial crisis. As compared to thirteen years ago, the main difference is the amount of liquidity that flooded the financial markets to overcome the pandemic.

Although PE funds exited fewer investments during 2020, those disinvested generated multiples on invested capital of around 2.3x, slightly more than the last five-year average[14]. Above all, what the global pandemic made evident is how variable the PE funds' returns across sectors and sub-sectors. For example, in 2020 Technology and Business Services outperformed the market, while Consumer, Healthcare, Industrials and Natural Resources have not meet expectations[15].

1.6 Recent trends: the ESG case for PE funds.

ESG (Environmental, Social and Governance) is a broad term that still miss a standard definition and time-tested methodologies to measure either factors' impact or their return on investments. This, of course, brings in some skepticism around the theme by Private Equity investors.

There is always an exception confirming the law: the TPG case. TPG, a leading global private investments firm, has been a pioneer in ESG investing and implemented ESG principles both in its organization and within portfolio companies. TPG is a leader also for having launched ESG impact funds dedicating specialized human resources to drive the change: for example, in January 2021 TPG announced that former US Treasury Secretary Mr. Hank Paulson would join the fund as executive chairman of TPG Rise Climate, a climate-focused fund[16].

---

[13] *Perspectives 2021. Tracking LP sentiment in turbulent times*, Private Equity International, 2021.
[14] CEPRES Market Intelligence.
[15] CEPRES Market Intelligence via DealEdge.

[16] A. R. Sorkin, *Henry Paulson Returns to Finance, to Run Climate-Focused Fund*, New York Times, 6th January 2021.

ESG performance indexes suggest that portfolio companies owned by US-based PE funds are behind those owned by European players by 12 points, and yet even in Europe there is room to improve the ESG performance. For example, looking at sustainability factors, most EU-owned portfolio companies haven not launched impactful initiatives yet. Moreover, another interesting evidence is that PE-owned companies and corporations are not far from each other in terms of ESG scores, both in the US and Europe[17].

Private equity has always focused on governance risk and increasingly sees the value in cutting costs through sustainability. What is changing is firms' growing awareness that environmental, social and governance issues are highly interrelated and that the biggest benefits over time accrue to companies that balance efforts between all three. The desire to contribute to a better world is certainly a motivator, but the rationale is all business. These firms recognize that consumers, regulators, employees and sources of capital are energized by the notion that investors can and should use their economic clout to address the many existential crises we face as a society. Each of these groups is ramping up demands for change and, in many cases, rewarding it[18].

For example, consumers are directing towards companies that they believe act in a responsible way, and this is especially true for millennials and post-millennials. As suggested by Net Promoter Score, ESG factors are becoming a key driver to build customer loyalty too. For example, Capgemini recently published a survey of 7,500 consumers and 750 executives showing that a significant majority of consumers (79%) are changing their purchase preferences based on sustainability. This contrasts sharply with the 36% of organizations who believe consumers are willing to make this change in their choices based on social or environmental impact. Such a gap represents a risk of ~6% of brands and retailers' revenue if unaddressed[19].

On the other hand, especially in Europe, ESG factors are being demanded by a growing number of LPs: globally, 88% of LPs are using ESG performance indexes to make investment decisions, while 87% of them said they are rewarding those company that are reducing their short-term return on capital to reallocate resources to ESG initiatives[20]. One of the reason why LPs are paying more attention to ESG principles is that, on the bankers' side, sustainable and more socially responsible companies are considered to be less risky, and as such PE firms manage to lower their cost of capital by monetizing their ESG strategies.

---

[17] *Business Sustainability Risk and Performance Index 2020*, EcoVadis, 2020.
[18] *Global Private Equity Report 2021*, Bain & Company, 2021, p. 31.
[19] *How Sustainability is Fundamentally Changing Customer Preferences*, Capgemini Research Institute, July 2020.
[20] *Edelman Trust Barometer Special Report: Institutional Investors*, Edelman, November 2020.

Finally, one of the reasons why European PE firms, instead of US ones, are plotting the route towards ESG investing is because of regulators. The European Commission recently established the EU Taxonomy, taking effect in December 2021, a classification system establishing the conditions an economic activity has to meet in order to be qualified as environmentally sustainable[21]. It is one of the key pillars to scale up sustainable investments and to implement the European Green Deal, and it will force EU asset managers to disclose their share of taxonomy-compliant investments, as such creating an incentive in raising the share to be competitive on the market.

[21] Sustainable finance taxonomy - Regulation (EU) 2020/852.

CHAPTER TWO – OVERVIEW OF THE SPORTS INDUSTRY.

2.1 Sport Industry Overview.

Despite its relevance in today's world economy, there is not yet a standard definition of what the Sport Industry is and what their boundaries are. It is perceived as one of the most heterogeneous industry, both for its composition and for the business models of the key players shaping the market.

To start analyzing this industry it is crucial to identify some boundaries that delimit the spectrum of potential players acting within it. A good approach is to take institutional classifications of economic activities and refer to the definition contained in them. The North American Industry Classification System (NAICS) and the *Nomenclature statistique des Activités économiques dans la Communauté Européenne* (NACE, issued by the European Commission), respectively define the Sport Industry as:

- NAICS: "This U.S. industry comprises professional or semiprofessional sports teams or clubs primarily engaged in participating in live sporting events, such as baseball, basketball, football, hockey, soccer, and jai alai games, before a paying audience. These establishments may or may not operate their own arena, stadium, or other facility for presenting these events"[22].
- NACE: "This class includes the activities of sports clubs, which, whether professional, semi-professional or amateur clubs, give their members the opportunity to engage in sporting activities. This class includes operation of sports clubs: football clubs, bowling clubs, swimming clubs, golf clubs, boxing clubs, winter sports clubs, chess clubs, track and field clubs, shooting clubs, etc."[23]

Although these definitions are a good starting point, we cannot limit here the definition of the Sport Industry: in recent years, this market saw an exponential growth of key players involved in the value creation chain, such as national and international sport federations, Committees, leagues and championships owners.

Today, the Sport Industry can be considered a wide-reaching business spanning the field of play, ranging from clubs their players and media rights, to food and merchandising stands at the stadium. From a broader point of view, the Sport Industry consists in selling sports services and related contents by teams, clubs and athletes offering the audience a show to be enjoyed.

---

[22] NAICS 711211 – Sports Teams and Clubs, NAICS Association.
[23] NACE 9312 – Activities of Sports Clubs, Eurostat.

Talking about some key financial metrics, the global Sports market is expected to grow from $388 billion in 2020 to $441 billion in 2021 at a compound annual growth rate (CAGR) of 13.5%, with growth being mainly driven by the companies rearranging their operations and recovering from the COVID-19 impact, while the market is expected to reach $600 billion in 2025 at a CAGR of 8.0%[24].

Rights owners define the structure of professional sports around the world. They set the rules, organize the events and take responsibility for generating revenues from matches, media and marketing rights. The Sports value chain is structured around four pillars:

- Properties: the intangible assets managed by rights owners that stimulate fans' interest and cash flows. They comprehend a wide range of parties, including leagues (such as the English Premier League), pro tours (golf 's PGA Tour), teams (the Manchester United FC) and athletes (Roger Federer, Lionel Messi, Louis Hamilton).
- Rights management: professional sports nowadays strictly depend on media and marketing rights monetization, making up a big slice of the revenues pie.
- Events: effective rights management materialize on operating live events too, and an live experience to be enjoyed by fans create key revenues streams.
- Content: stadiums and arenas can only host a limited number of fans attending the live events, and for this reason creating contents that fit to broadcasters' and sponsors' needs is a key part of the value creation process in modern Sports.

Structured around these four pillars, the sports value chain becomes a virtuous circle. Shaping a property can help increase its value through tailored rights management, and content packaging can make it more attractive. For example, when cricket organizers created "Twenty20" cricket in 2003, shortening the typical game from several days to a few hours, they shaped a format better suited to live broadcasting[25].

---

[24] *Sports Global Market Report 2021: COVID-19 Impact and Recovery to 2030*, Research and Markets.
[25] P. Zygband, H. Collignon, N. Sultan, C. Santander, U. Valensi, *The Sports Market. Major trends and challenges in an industry full of passion*, A.T. Kearney, 2011.

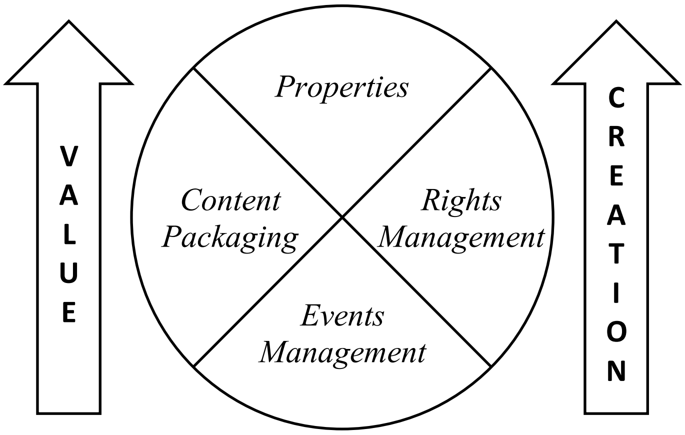

Figure 2.1 – The four pillars of the value creation process.

2.2 From a Playful Practice to the Sport-Business.

The practice of Sport, in its most complete meaning, has faced over time a huge process of evolution and innovation to the point of assuming today's economic and social relevance. It is important to highlight at least the fundamental stages of this evolutionary path, which from a simple playful practice, has led Sport to become one of the fastest-growing industries.

First of all, archaeological evidence show that sporting practice already existed in pre-classical time: some archaeological finds testify that physical activities were already practiced at the time of the Maya and the Sumerians. Then, Sport assumed an increasingly important role within society, becoming a real unifying factor for the populations, who, through playful activities, were able to carve out valid brackets from daily efforts. It is with the Greek civilization that the sporting discipline undergoes a first and profound mutation, through which firsts competitive disciplines were born. So, at that time there has been a shift from Sport almost exclusively linked to social and playful practice, to an essentially competitive practice. A further step in the transition from a playful practice to the today's Sport-business is the Middle Ages: Sport took on a more violent guise, physical confrontation becomes a central element of sporting activity, an essential core around which every type of sport revolves. It is no coincidence that the most violent sports practices still practiced today find their birthplace precisely in this specific historical moment. The awakening from the dark medieval period that accompanies the slow process of civilization of the entire human activity certainly does not spare the practice of sports which, at this stage, feels the need to control violence through the definition of rules: during the Enlightenment period, Sport became an important pedagogical and educational tool. Between the end of the eighteenth century and the beginning of the nineteenth century, the importance Sport gained, led it to be recognized as a discipline aimed at developing team spirit, a sense of discipline and respect for opponents, entering schools for the first time, and presenting itself as the precursor of the modern concept of sporting activity.

The evolution process that has profoundly changed the face and role of sports in society ends with the meeting between Sport and Business. With the birth of the modern economy, the focus definitely shifted from Sport being a mere playful practice to a new perception of Sport, that is increasingly integrated with economic principles and best practices. This process started with companies beginning to be interested in Sport, spotting huge opportunities: from financial gains to social recognitions, for example. It was in the early twentieth century that flashy advertising billboards of well-known companies began to appear where important sports meetings took place, and the images of great champions began to be associated with those of consumer products. At that time, the industrial world took the opportunity to indirectly attract the interest of the general public through Sport and its famous athletes. The relationship between Sport and companies became firmer with the advent of mass media, fully delivering the potential from a media point of view of the Sport industry and most famous athletes. The relationship was initially bilateral: the media represented for Sport a sort of free promotional tool, while Sport represented for the mass media a tool through which attracting a broader audience and increasing the interest of the general public. In this way, Sport became a promotional tool through which on the one hand companies, and on the other mass media, conveyed their image by multiplying it according to the number viewers who followed a given sporting event. In this period, the first forms of sponsorship were born. Nowadays, the practice of sponsorship is considered one of the most effective communication techniques.

Concluding, it is possible to affirm that today's Sport industry is the result of a slow process of evolution through which simple playful practices have evolved into one of the most flourishing market in today's economy.

2.3 Key Players and Forces Shaping the Sport industry.

The Sport industry is very peculiar even when it comes to frame it according to some of the most used models to assess the potential of a given industry. In the next pages we are going to assess the attractiveness of the Sport industry according to the Porter's five forces model[26].

[26] M. E. Porter, *How Competitive Forces Shape Strategy*, Harvard Business Review, 1979.

2.3.1 Competitive Rivalry: Clubs, Leagues and different Sports.

Starting from competition, we can assess it from three different points of view: between clubs belonging to the same league, between leagues belonging to the same sport, and between different sports. Starting from the competition between clubs belonging to the same league, it is in the nature of the leagues themselves to make clubs competing against each other. Clubs are in competition for different reasons that can be grouped into two clusters: increasing the heritage and track-record of the clubs (i.e., building "brand awareness"), and increasing their financial performance. These two drivers are strictly linked, because it is usually the case that when a club is building brand awareness, it happens on the back of winning the championship, and this of course will benefit the financial performance of the club too. The relationship between building brand awareness and increasing the financial performance of the club can be seen as a virtuous cycle, for example thinking about a Football: when a club starts winning matches and championships its financial performance will improve thanks to the increased revenues streams (for example from sponsorships), this in turn will allow the club to buy top players that will improve the brand prestige and will make it more likely for the same club to win the championship next year, and so on. We can say that if on the one hand clubs belonging to the same league are competing among them for those reasons, their goal is also to protect the league they are in from outside threats. Stepping into the competition at leagues level, it is of course in the best interest of each of the leagues belonging to the same sport to increase their prestige to attract an ever-growing share of interests and consequent investments. For example, thinking about Football there are five main leagues (English Premier League, Italian Serie A, Spanish La Liga, French Ligue 1 and German Bundesliga) competing against each other: every measure they take is with the aim of increasing the revenues for the league owners and clubs, and this can be done by increasing the interest from the general public that, in turn, will increase the media rights revenue stream, for example. Lastly, the third layer of competition within the Sport industry is at different sports level: Football is king among all sports, with almost a 50% share of the global Sport Event market, followed by US football, Baseball, Formula 1, Basketball, Hockey, Tennis and Golf[27]. Overall, the competition at different sports level is

[27] *The Sports Market. Major trends and challenges in an industry full of passion*, A.T. Kearney Paris, 2011.

mainly driven by the media rights, ticketing and merchandising revenues stream: the larger the fan base of a given sport, the larger the slice of the global Sport market pie will be.

2.3.2 Threat of New Entrants: Meritocracy vs Financial Resources Availability.

Continuing with the analysis, the potential threat from new entrants into the Sport industry takes a different meaning as compared with other, more standardized industries. As mentioned in the section *Sport Industry Overview*, we are analyzing a very heterogeneous industry, making it difficult to elaborate standard considerations applicable to any player in this market. For what concerns the potential threats of new entrants, it is not possible to analyze the Sport industry as a whole, instead we should go one step ahead and analyze each sport and related leagues separately. For the sake of this study and to analyze two very different cases, the focus will be on European Football and Motorsport (mainly Formula 1 and MotoGP). The potential threat of new entrants in the Football industry is very limited: any league has a limited number of spots, so every year a limited number of clubs can participate and if a new club wants to enter the top league it would have to start from the lowest league (in Italy the so-called Serie C) and, year by year, it will have to climb up to the major league by winning titles. So, for what concerns Football, it is a very meritocratic process limiting the threat of new entrants at a minimum level. On the other hand, Motorsport has a very different functioning as compared with Football: when referring to Motorsport, in each championship there are usually two competitions and related titles, one for pilots and the other for constructors, so competition is both at pilots and constructors' level; at this stage, the constructors' point of view will be taken. Major Motorsport championships rules make the entrance of new teams not linked to meritocracy, as it happens with Football, but instead to the availability of licenses and related financial resources to afford them. For what concerns Formula 1, according to the eighth Concorde Agreement (the contract signed between FIA, Formula 1 owner and the ten teams regulating the championship), from 2021 new teams willing to enter the championship will have to pay $200 million to the existing teams (ten teams, $20 million each) as part of a prize-money dilution fund. A similar process applies to MotoGP.

2.3.3 Bargaining Power of Suppliers: Athletes and Broadcasters Threating Club Owners.

Even when analyzing the bargaining power of suppliers, we should go one step ahead and make specific considerations that applies to the Sport industry. First of all, to start analyzing this force we have to define who suppliers are in the context of Sport. Among the others, we can focus our attention on two main clusters:

- Athletes: they are at the core of the Sport industry and can be regarded as “content provider”, providing clubs and teams with their skills and reputation in order to attract and retain fans.
- Media and broadcasting companies: they can be considered as the mean through which the content created by sport entities is brought from playing fields and stadiums to home televisions and streaming platforms.

2.3.3.1 Bargaining Power of Athletes: the US and EU cases.

Starting from athletes, clubs have faced over the years an increase in their bargaining power especially in the form of salary and benefits increase, both in the US and Europe. Starting from the US case, athletes from Baseball, Basketball, American Football and Hockey throughout the years have joined their forces to increase their bargaining power against clubs' owners. Baseball players started gathering in 1885 under the Brotherhood of Professional Baseball Players, not only with the aim of increasing their salaries, but to reduce the clubs' owner control over their careers. Thanks to the union, in mid 1900, they managed to increase their minimum salary from $6,000 to $10,000, a very small figure as compared to 2021 $4.17 million average salary[28]. Talking about Hockey, before the foundation of the National Hockey League Players Association in 1967, players received an annual salary usually ranging from $10,000 to $15,000, having no pension and healthcare benefits and being forced to have summer jobs to support their families. Thanks to the union work things have changed significantly over the years, with more and more benefits being recognized and salary increased up to today's minimum wage fixed at $750,000[29].

Passing from the US to the EU case, the bargaining power of athletes takes a different strength depending on the Sport we are analysing: on the one hand EU Football players' salaries and

[28] *Average MLB salary at $4.17 million, down 4.8% from 2019*, ESPN, 16th April 2021.
[29] *Hockey Central. The Original Six, 1942-43 to 1966-67*, National Hockey League

benefits have skyrocketed throughout the years, as their ability to produce revenues for the teams has skyrocketed too; on the other hand, athletes from minor sports face poorer working conditions and lower benefits.

We now dive deep into the analysis of the bargaining power of athletes other than football players. As anticipated, professional athletes face a different reality as compared to football top players, given poorer working conditions, lower wages and reduced benefits. An analysis financed by the European Commission examined the working conditions of professional athletes from ice hockey, rugby, handball and basketball. Main findings raise a number of serious issues about the life of professional athletes, calling for an action from EU institutions. For example, of the 566 professional athletes interviewed many reported the following:

- Still many players are without a contract, bringing in many issues such as security of employment and the application of proper legislation to protect their rights at work.
- In many countries, regardless of the type of sport, interviewed athletes reported consistent delays in receiving their salaries.
- Many professional athletes reported lack of pension provisions, raising serious question about their life after the sporting career.

The research raises serious weaknesses in the regulation of employment in the Sport sector and the negative effects this has on the working lives of professional players. While these issues are not insurmountable and, in some cases, relatively simple actions would deliver significant improvements to the lives of players, needed improvements will require a multilateral approach, involving the European Commission and its parallel institutions, player associations, employers and the bodies regulating the leagues of each sport across all member states[30]. Hence, the bargaining power of professional athletes other than football players does not represent an issue for the EU Sport industry, but some countermeasures from players associations and EU institutions are to be expected.

Continuing the analysis with EU Football, one clear distinction must be made between the "superstars", hence players whose salaries are tremendously high but represent a minority (ex. the Argentinian Lionel Messi, Portuguese Cristiano Ronaldo, or French Antoine Griezmann), and the rest of players, whose salaries are well below those of superstars, but still very high if compared to the average EU GDP per capita. There are three main reasons why Football players' salaries are so high: the "law of supply and demand", the limited time of their careers

[30] *An analysis of the working conditions of professional sports players*, UNI Global Union, European Commission, 2011.

and players having become "brands". The first and most direct explanation is the liberal "law of supply and demand": superstar players are very rare, and as such they are very expensive; the Football market is characterized by a huge imbalance between demand of top-players and their supply, being populated by plenty of Football teams and just a handful of superstars. Second, Football players' career is very limited if compared to a "normal" worker's career, usually lasting for an average of twenty to twenty-five years: high salaries constitute a kind of guarantee for them for their life after retirement. Lastly, besides having unique skills making it easier for the teams to win matches and championships, superstars have become brands whose images are being exploited by Football teams in order to increase their revenues, mainly in the form of higher sponsorships, ticketing and merchandising revenues.

2.3.3.1.1 Juventus FC and Cristiano Ronaldo: Top Players Threatening the Industry.

An interesting case is the 2018 transfer of Cristiano Ronaldo from Real Madrid CF to Juventus FC. Cristiano Ronaldo is one of brightest superstar in the modern football, contending for the throne with Lionel Messi. Differently from the Argentinian top-player, what makes Cristiano Ronaldo unique is his off the pitch performance, making him a brand of his own. After spending many years at the Spanish football club Real Madrid CF, on July 10th 2018 he officially passed to the Italian team Juventus FC for a total sum of €117 million: €100 million for the transfer fee, €5 million payable as FIFA solidarity payments and €12 million as transfer commissions to the player's agent Jorges Mendes[31]. Following the transfer, Juventus and Cristiano Ronaldo signed a four-year deal according to which the football player is going to earn, net of taxes, €30 million per year, equivalent to a €55-56 million expense for the football club. As said before, what makes Cristiano different from other superstars is his non-sportive performance: according to Forbes, his net income for the 2020/2021 season amounted to about $120 million. In fact, apart from being a Football superstar, Cristiano produces revenues from many other sources: sponsorship (ex. Nike, Electronic Arts, Herbalife), his own brand (CR7), and hotels among the others. His performance is outstanding also on the social media field, becoming in February 2021 the first person reaching 500 million followers across Facebook, Instagram and Twitter. So, it is clear that by acquiring Cristiano Ronaldo, Juventus FC has not only bought his extraordinary football skills, but a new brand bringing the unique opportunity of leveraging on his massive fan base, both from a communication and commercial perspective.

---

[31] *Accordo Con Il Real Madrid Per L'acquisizione Definitiva Del Calciatore Cristiano Ronaldo,* Juventus FC press release, July 10th 2018.

An analysis carried out by KPMG Football Benchmark[32] shows that although the acquisition of Cristiano Ronaldo posed some risks, he could have been an accelerator to boost the visible growth Juventus FC has been undertaking since Andrea Agnelli presidency. Considering the abovementioned costs linked to the Cristiano Ronaldo acquisition, according to the study Juventus FC had some key drivers to deliver a positive ROI[33] from this investment: matchday, broadcasting and commercial revenues, coupled with social media and branding implications. Apart from matchday and broadcasting revenues, the real growth opportunity for Juventus to leverage on Cristiano Ronaldo was in the commercial space: indeed, while matchday revenues are limited by stadium capacity (and ticket pricing limits), and media income is generated through agreements set at league/international levels, Juventus needed to strongly capitalize on the acquisition of Ronaldo, especially in merchandising and sponsoring. The club lagged behind the main European superpowers in this area. In 2016/2017 Manchester United FC, Barcelona FC, Real Madrid CF and FC Bayern München recorded €320 million, €288 million, €280 million and €344 million, respectively, more than twice as much Juventus FC's figure of €120 million. Such a gap is even clearer when comparing the jersey value figure for the 2017/2018 season. In particular, Juventus FC get €17 million/season from their main shirt sponsor, Jeep, and €23 million/season from kit supplier Adidas, making for a total of approximately €40 million. On the other hand, Manchester United FC, Barcelona FC and Real Madrid report a total jersey value of €156 million, €140 million and €95 million, respectively. According to the KPMG Football Benchmark study, the investment in CR7 might have provided Juventus with sporting, media, branding and economic benefits that might have well outpaced the related costs, allowing the club to increase their revenues, profitability and, ultimately, enterprise value.

Anyway, Juventus FC does not seem to have capitalized on the growth opportunities that could have been unlocked by the Cristiano Ronaldo affaire. In fact, recent news reported his transfer to the English Premier League club Manchester United FC, for €15 million, thus resulting in a €14 million loss on the 2020/2021 fiscal year (even if savings on his salary will have a positive effect on fiscal year 2021/2022)[34].

As the Juventus and Cristiano Ronaldo case showed, increasing bargaining power on football players' side represents a serious threat for football clubs and their shareholders. Proper

[32] *From Madrid to Turin: Ronaldo Economics*, KPMG Football Benchmark, 2018.
[33] Return on Investments.
[34] *Accordo con il manchester united per la cessione definitiva del calciatore Cristiano Ronaldo*, Juventus FC press release, August 31st 2021.

management is needed in order to carry out full assessments of possible transfers *vis a vis* sky-rocketing players' salary. But, as it happens for any threat, through proper management devices football teams can be able to turn it into an opportunity to increase operating revenues, as Juventus could have done by leveraging on the CR7 brand.

2.3.3.2 Bargaining Power of Broadcasters: Advertising Tools Becoming Key P&L Drivers.

Media has been for many years a key driver of teams and clubs' financial success, but its role has evolved throughout the years from being a simple mean to attract fans to sport venues, to today's key relevance in a team or league P&L structure. In the following pages we will understand how media has changed from being a tool used by teams to advertise their core products (i.e., the sports event) to attract and retain an always larger number of fans, into a revenue stream escalating teams' value and, as a consequence, players' salaries.

Broadcasters represent a double threat for clubs and leagues owners: on the one hand, the broadcasting of sport events may be seen as a substitute to the sale of stadium tickets, as such directly affecting the ticketing revenues for a team; on the other hand, Sport has become more and more dependent on the media and broadcasting revenue stream, shifting the bargaining power towards broadcasting companies[35].

To understand how the relationship between media and Sports has acquired such a high relevance, it is easiest to proceed by dividing their linkage into three different phases, each one characterized by distinct roles played by teams and leagues on the one hand, and media companies on the other hand.

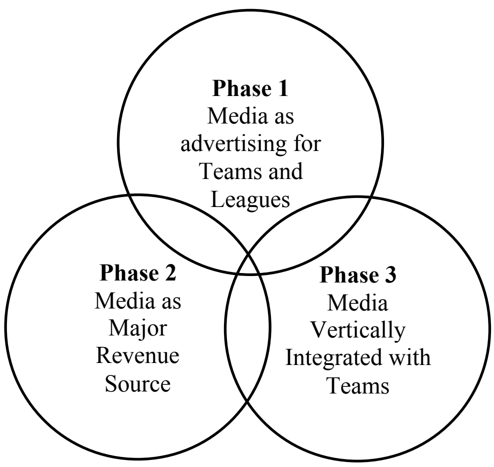

Figure 2.2 – The three phases of the relationship between Media and Sports

[35] P. Downward, A. Dawson, T. Dejonghe, *Sport Economics. Theory, evidence and policy*, 2009, p. 292.

Initially the media were used to advertise teams through stories about the games and players as well as the publication of statistics. Here, the goal for team owners was to ensure that newspapers would deliver exciting stories to readers who should then become fans. At a certain point in time a virtuous circle started, with more and more people being interested in Sports, creating a totally new demand for game and player statistics, as well as insights in team management and affairs. As a consequence, media content providers responded to this growing interest by expanding sports sections on newspapers. The relationship between Sports and media could be seen as of financial reciprocity, being beneficial for both parties: on the one hand, teams needed media to deliver positive messages to people in order to increase the number of fans; on the other hand, as interest in Sports grew, it become more and more important for the profitability of newspapers as it attracted more readers, and with more readers newspapers enjoyed more advertising revenues. From a revenue standpoint, however, Phase 1 involved an indirect relationship between the media and teams. Teams did earn income from the media, but it was through the creation of new fans and their decision to buy tickets that revenues rose. The receipt of money from media distribution services begun in Phase 2, which soon emerged to be a fountain of wealth.

With the radio and then television sets becoming staples in every household, teams began to realize they could essentially have paying fans in the stands and at home. It was here that Phase 2 started, and with it the advent of large amounts of direct revenues for the Sport Industry from the broadcast of games, first through radio transmissions and then on televisions.

This was followed by the complete vertical integration of Sports into team operations. An offshoot from Phase 3 is the rise of merged distribution systems (cable, air wave broadcast, and Internet delivery systems) and advanced media that relies on the Internet to deliver games to millions of fans across the globe in real time. In this context, there is also the emergence of fantasy sports that creates new demand for viewing multiple games and having instant access to statistics on players' performance[36].

Perhaps, COVID-19 crisis marked the start of Phase 4, a new era for the relationship between Sports and media companies. Sport fans are shifting their habits toward Sports and its contents, with a shrinking interest towards traditional pay-tv bundles. This trend is supported by a broader pattern of profits shifting from traditional media companies to digital streaming

[36] J. A. Winfree, M. S. Rosentraub, *Sports Finance and Management. Real Estate, Entertainment and the Remaking of the Business*, 2012, pp. 217-247.

platforms. The revenues implications of this trend are significant, not only for traditional broadcasters but for teams and leagues too, heavily relying on broadcast rights to fund their operations. Some studies estimate that programmers and distributors could see their profits contract by about 10% per year between 2019 and 2024. As their profits decline, programmers will pay less for Sports rights that directly fund teams and leagues. This trend will not fully materialize from day to night and will be gradual. Expectations for the medium/short term are to have a hybrid model, combining both revenues from traditional and streaming content providers. In this, streaming platforms will need to adapt their offer developing direct-to-consumer services, with enough content and price differentiation to set them apart from the traditional broadcasting services. Enjoying most recent technological developments, these direct-to-consumer offerings will be more sophisticated, including access to real time data on players' performances, new betting opportunities, or more interactive and immersive viewing modes. Many media companies already started experimenting expanded media offers, including the following:

- Game packaging: since most fans do not watch entire seasons, distributors are structuring different packaging forms targeting different fans clusters.
- Price differentiation: adapting pricing strategies according to the targeted audience, with "superfans" being more likely to pay higher prices to get the opportunity to enjoy full-content packages.
- Value-added services: including all non-game content shifting to digital platforms to redefine fan engagement.

For sports leagues, teams and broadcasters, the trend away from traditional pay-TV bundles represents a disruptive shift bordering on an existential crisis. But it's part of a trend affecting the entire media landscape. Those who can break down the economics of the content bundle and recreate that value in a hybrid model of linear and streaming distribution will be the ones most likely to maintain their competitive advantage[37].

2.3.4 Bargaining Power of Customers: Fans as the Key Stakeholders.

To start this analysis, it is important who customers are within the Sport Industry. Differently from other industries, here we can define a main, unique cluster of customers: fans. A fan is defined as the person who thinks, talks about and is oriented towards sports even when

[37] D. Mortlock, C. Kim, A. James, *What If Sport Fans Cut the Cord?*, Bain & Company, 13th October 2020.

he/she is not actually observing, or reading, or listening to an account of a specific sport event[38]. In addition, a sport fan is one who shows consistency, dedication and loyalty with the commitment coming in three forms: cognitive, as the consumer builds up knowledge about the sport and team; attitudinal, as the consumer believes strongly in the team and the sport; behaviorally, showing his/her commitment through tangible acts such ticket or merchandise purchasing[39]. From a broader point of view, the term "fan" can include spectators too: individuals following sport events more passively than fans. The primary aim of any sports organization is to attract and retain the highest possible number of fans, as they usually are the ones contributing to big slice of the revenues pie through ticketing, merchandising and media content.

Fans can be grouped into two different groups[40]:

- Regional fans: this group usually grows within the club environment. In some cases, a only one club represents a given city, while in other cases a city can be represented by multiple local teams. Regional fans are usually characterized by a higher degree of loyalty and, in some cases, they can be organized into fan clubs in order to increase their bargaining power against the clubs' owners.
- International fans: they are spread all over the world and can be a strategic asset for clubs and teams, who need to engage them through innovative technologies, helping clubs in reaching every fan with the most customized contents possible, eventually leading to fan monetization.

Throughout the years, it has become more and more important for Sports organizations to structure grounded fan engagement strategies in order to reach a competitive advantage, as engaged sport fans are likely to commit their financial resources to seek interactions with their favorite sport organization or club. In the Sport Industry, money flows according to different paths from fans to clubs and leagues: from fans to pay-tv providers (who, in turn, will pay clubs and leagues for media rights), from fans to ticketing and from fans to merchandising. The more engaged fans are, the more they get loyal to the club and the more they will be likely to feed these flows of money.

[38] J. I. Norris, D. L. Wann, R. K. Zapalac, *Sport Fan Maximizing: Following the Best Team or Being the Best Fan?*, Journal of Consumer Marketing, 2014, pp. 157-166.
[39] B. Stewart, A. C. T. Smith, M. Nicholson, *Sport Consumer Typologies: A Critical Review*, Sport Marketing Quaterly, 2003, pp. 206-216.
[40] E. Coutinho da Silva, A. Luzzi Las Casas, *Sport Fans As Consumers: An Approach To Sport Marketing*, British Journal of Marketing Studies, 2017.

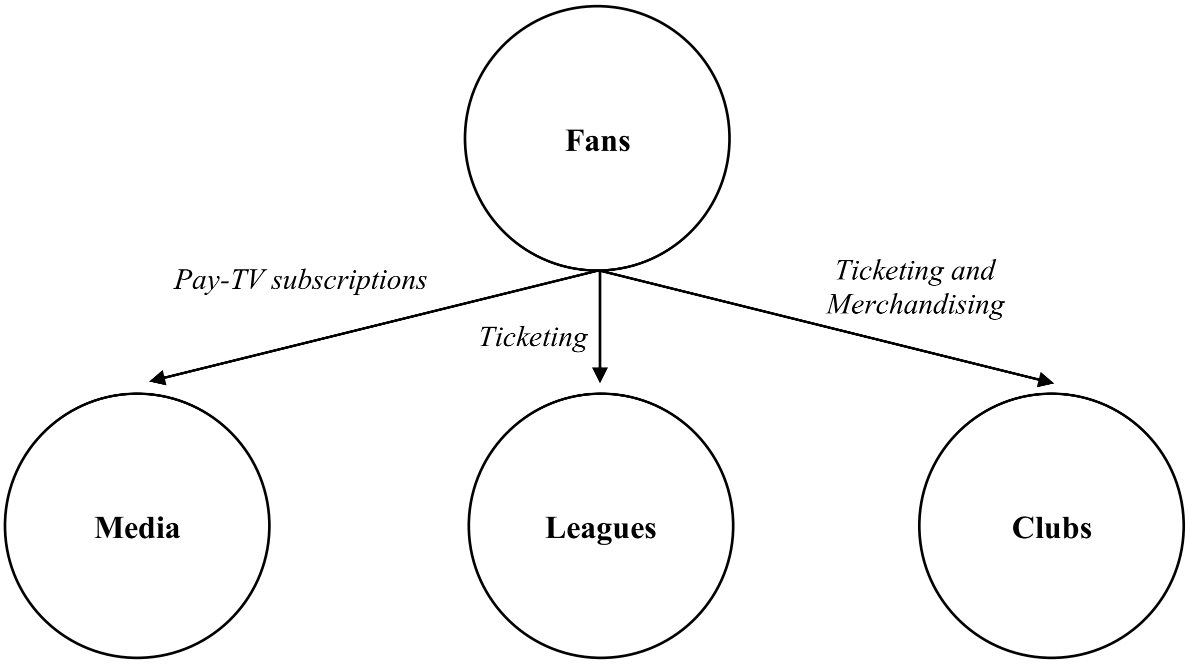

Figure 2.3 – Money flows from Fans to Sports organizations.

Given their high fragmentation, fans do not represent a serious threat for Sports organization. What really matters in this context are fans habits and how they are changing. In this, Sport Industry players must be able to adapt their offering to retain current fans and, possibly, to attract new ones.

2.3.5 Threat of Substitutes: Watch Out to Internal and External Threats.

We can address the threat of potential substitutes in the Sport Industry from two different angles: first, within the Sport Industry itself; then, outside the Sport Industry.

Starting from the threat of substitutes within the Sport Industry, we can tackle this point from two different point of view. Here, the threat of substitutes can come from:

- Within the same sport practice, each league or championship represents a potential substitute for other leagues. Taking European Football as an example, the Italian Serie A can be seen as a substitute to the English Premier League. Again, within Motorsport, the World Superbike Championship can be considered a potential substitute to the MotoGP Championship.
- Within the Sport Industry, each sport practice represents a potential threat for other sport practices. For example, Rugby can be considered as a substitute for US Football.

Considering the peculiarities of the Sport Industry and, in particular, the tight link existing between each sport and their fans, the first one seems to be a more serious threat for Sport Industry players. Taking once again European Football as an example, as analyzed in paragraph

2.3.1, the competition between the main five EU leagues (English Premier League, Italian Serie A, Spanish La Liga, French Ligue 1 and German Bundesliga) is clear. This competition arises from the fact that Football fans consider these leagues as potential substitutes among them: from the very last step of the Sport Industry value chain (i.e., fans), this perception spreads upstream, where each league owner strives to make its own league more appealing than the others in order to attract and retain the highest possible number of fans, as this imply higher revenues for the league and clubs belonging to it, in the form of higher TV rights, merchandising and ticketing revenues.

Continuing the analysis, Sport Industry players have to deal also with the threat of potential substitutes coming from outside the Industry itself. Here, we are referring to practices and activities that are different from Sport, but still are perceived as potential substitutes from Sport fans. Currently, there is one main trend that is threatening the Sport Industry: eSports. In the next pages we will deep dive into the eSports Industry to understand why it represents a threat for the Sport Industry.

2.3.5.1 eSports: from Arcade Competitions in the 1980s to a $ 950 million industry in 2020.

From arcade competitions in the 1980s and LAN parties in the early 1990s to the rise of massively multiplayer online games in the 2000s, gamers have spent decades building the foundations of eSports, defined as a specific subset of online gaming with a focus on the competition between human players (both amateurs and professionals) in a video game with predefined rules[41]. The development of robust computing and graphics platforms, along with the growth of social media and high-speed internet access, has helped enable designers to introduce highly responsive and deeply immersive shared gaming environments[42]. The eSports Industry is grounded on a massive market size, much higher than the one of many traditional sports in terms of both revenues and viewership. Globally, the industry reached $ 950 million in 2020 and is expected to hit the $1.1 billion figure in 2021, with over 75% of the revenues coming from media rights and sponsorship[43]. To play a traditional sport, one typically needs access to an appropriate venue (field, court, etc.), and to be successful, it almost always helps

[41] U. Allenstein, O. Gediehn, S. Lehmann, D. Singer, *Esports as a Sponsorship Asset? What CMOs should know*, McKinsey & Company, June 2020, p. 3.
[42] C. Arkenberg, D. Van Dyke, J.D. Tengberg, N. Baltuskinis, *eSports graduates to the big leagues. Can the industry help media and entertainment companies access a changing audience?*, Deloitte Sports Consulting, 2018.
[43] *Global eSports and Live Streaming Market Report*, Newzoo, 2021.

to be big, fast, strong, or coordinated, or better yet some combination of all four. To play multiplayer video games, all that is necessary is the requisite hardware and an internet connection, and there is a community of millions of players online that are ready to play at any hour of the day. Therefore, professional video game play can be appealing to a massive global audience of people who can watch and learn from professionals and try to improve their own gameplay, something that is not as possible for most traditional sports fans. Moreover, because the distribution of eSports is nearly 100% digital, fans can stream eSports content for free anywhere in the world, unencumbered by traditional TV rights that for most Western-based professional sports leagues have been segmented by geography and are often lumped into an expensive TV subscription[44]. Like traditional Sports, professional eSports championships have been affected by Covid-19 countermeasures, forcing organizers to cancel major live events. Differently from traditional Sports, who have not the same degree of flexibility and adaptability, new formats have allowed to properly manage the crisis and to let professional players streaming their challenges. In fact, many leagues have continued their formats online and this, coupled with the absence of traditional Sports due to restrictions, has made interest in eSports rising: consumer surveys shows that heavy users, defined as people playing more than once a week, increased by approximately 30%[45].

What represents a threat for the Sport Industry is eSports special target audience: it mostly addresses young (on average 26 years of age), male (over 70%), tech-savvy, and highly educated groups[46]. At a first glance, this may not seem to be a threat for traditional Sports like Football, as the above-mentioned study carried out by McKinsey & Company highlights key differences with groups targeted by traditional Sports. Going one step ahead it is clear what eSport target audience implies in terms of revenues, especially the ones from sponsorship: age, educational, and income statistics suggest that eSports fans, on average, are about to start jobs with an above-average salary, making sponsorship an opportunity for companies to advertise their products towards attractive consumer groups. This is one of the main threats that the Sport Industry is facing: eSports leagues and teams may dry resources in the form of sponsorships from traditional Sports organization. While historically eSports sponsors have been limited to closely related industries such as technology hardware, in the past several years we have seen more mainstream sponsors such as insurance, beverage, and car companies enter the fray. As

[44] C. D. Merwin, M. Sugiyama, P. Mubayi, T. Hari, H. P. Terry, A. Duval, *Esports. From Wild West to Mainstream*, Goldman Sachs, 2018, p. 3.
[45] U. Allenstein, O. Gediehn, S. Lehmann, D. Singer, *Esports as a Sponsorship Asset? What CMOs should know*, McKinsey & Company, June 2020, p. 7.
[46] *The eSports Playbook*, Nielsen, 2017.

an example, the North American League of Legends League and the Overwatch League count Toyota, T-Mobile, Sour Patch Kids, Coca-Cola, American Express, and others as non-endemic sponsors (i.e., non-PC/console hardware companies).

An additional threat that eSports is posing to the Sport Industry is the one linked to media rights. In the early years of eSports, there was little organization or infrastructure, and as a result, the massive audience of eSports did not translate into meaningful revenue streams for players and team owners. In 2017, Riot Games created the North American and EU League of Legends leagues, while in January of 2018, Blizzard launched the Overwatch League: these leagues created the requisite infrastructure that will allow eSports to finally start to fill the monetization gap relative to other established sports leagues. In 2017, eSports generated $ 655 millions in annual revenue, including 38% from sponsorships, 14% from media rights, and 9% from ticket revenue. But by 2022, media rights are expected to reach 40% of total eSports revenue, as massive audiences and associated revenue for established online video platforms like Twitch, YouTube, Douyu, and Huya will be able to support a growing pool of media rights fees paid to top publishers for their content[47].

As seen so far, eSports are a threat for the Sport Industry as they can potentially drain financial resources in the form of lower sponsorship and media rights revenues. It is also true that, at the same time, eSports can represent an opportunity for those players of the Sport Industry smart enough to ride the wave to eat a slice of a continuously growing pie. There are many clubs and leagues from traditional sports that have already committed to enter the eSports world: for example, in 2017 both NFL and NBA announced their eSports entry strategy.

2.4 Recent Trends and Key Challenges Impacting the Sports Industry.

During 2020 the global pandemic hit the Sports Industry as no external force had never done before. Countermeasures taken by governments all had strongly affected the ongoing of sports leagues, as well as the financial performance of the clubs playing in them. Different leagues had different reactions to the challenges posed by the pandemic: some of them decided to postpone matches until they could take place under safer conditions, few were terminated with different methods to determine the final standing and winner, and others have been totally cancelled. Each of the solutions taken by leagues had different implications with respect to the relationships they had with commercial partners, such as broadcasting companies and sponsors,

[47] C. D. Merwin, M. Sugiyama, P. Mubayi, T. Hari, H. P. Terry, A. Duval, *Esports. From Wild West to Mainstream*, Goldman Sachs, 2018, p. 4.

many of which tried to re-negotiate the contractual agreements leveraging on substantial changes that have modified the sports products. On turn, the re-negotiations between leagues and commercial partners had a significant impact on clubs' P&Ls[48].

Because of the pandemic, restrictions on event attendance, such as current limits on stadium capacities, are still in place in 2021 and likely to be extended in 2022 seasons. Then, sports organizations' priority is to identify new revenue drivers that can help in stabilizing their cash flows and financial profiles. To understand how urgent this need is, in 2020 National Football League (NFL) teams lost an estimated $5.5 billion of stadium revenues under lower ticket sales, concessions, sponsorships and merchandising[49]. During this challenging time, it is more critical than ever that sports organizations, leagues and teams adapt themselves to the current *status quo*.

On the back of recent trends, the Sports Industry is presented with two key challenges: expanding revenue generating sources, offsetting the loss of "traditional" revenue streams; redesigning the relationship with fans, in order to overcome current limits on stadium attendance and fans' gatherings. To better identify new ways to improve their P&Ls, it is crucial that sports organizations acquire the required digital capabilities to unlock innovative revenue opportunities and new ways of engaging with fans.

2.4.1 Expanding Revenue Generating Sources through Data Monetization.

The challenges posed by the pandemic made sports organizations rethinking the way they do their business, making it clear that it is crucial for them to expand their business models beyond the stadium-related revenue sources.

One of the biggest sources of alternative revenue for sports organizations in 2021 and beyond could be data monetization, particularly in the areas of fan engagement, player and team performance, and sports betting. The market for data-wranglers and aggregators is heating up as organizations increasingly employ data analytics to guide decision-making and support their marketing efforts[50]. Data-driven platforms through the use of artificial intelligence can help organizations in improving their fan-engagement services, especially by sensing their

[48] P. Giorgio, *2021 Outlook for the US Sports Industry*, Deloitte Center for Technology, Media & Telecommunications, 2021.
[49] M. Ozanian, *The Stadium Revenue Each NFL Team Will Lose If Games Are Played Without Fans*, Forbes, May 18th 2020.
[50] P. Giorgio, *2021 Outlook for the US Sports Industry*, Deloitte Center for Technology, Media & Telecommunications, 2021.

sentiment. It is important to create a combination between sensing, data analysis and fan engagement to find new monetization strategies, for example on e-commerce and socially active platforms. Through data analysis, fans can be engaged on social media, team websites, in-stadiums offering like merchandise, and by using hyper-personalized advertising and gamification tools[51]. Moreover, big data is being increasingly used in the Sports Industry to extract insights and key metrics on athletes' performance: as a result, sports data has become a huge business expected to hit nearly $4 billion by 2023, thus a huge opportunity for leagues, teams and clubs[52]. If, on the one hand, data monetization represents a huge opportunity for the Sports Industry, on the other sizable infrastructure investments are required to generate the desired impact.

2.4.2 Redesigning the Relationship with Fans to Unlock Growth Opportunities.

Restrictions put in place to limit the pandemic seems to have had an impact on fans attitude that will last for longer than expected. Hence, new habits put pressure on sports organizations as they need to reinvent the way they engage with their supporters. In doing this, the key to unlock new opportunities resides in digital technologies: the goal is to build year-round, bilateral relationships with fans. The foundation of these relationships has not changed: trust. Trust must be modelled under four lenses: physical, meaning the safety of sports facilities; emotional, meaning the safeguard of emotional and societal needs of sports fans; financial, so that fans' economic and financial concerns are served; digital, relating to the security of their personal data[53].

After establishing a trust-based relationship with fans, sports organizations can unlock unnumbered opportunities in the fan engagement area. To truly maximize opportunities in the area of fan engagement, it's essential that sports organizations truly understand their fan bases—with the ability to segment fan groups (for example, casual fans, those "who love the game," and fanatics). This segmentation allows organizations to strategically target and incentivize different fan groups based on their level of commitment and behaviors. For example, while fanatics might desire daily social media notifications, casual fans could find them annoying. Organizations should strive to find the optimal frequency for communications based on each fan's profile.

---

[51] M. Anis, *Sense, Analyze, Engage: How to Successfully Monetize Your Fan Ecosystem*, Infosys, 2017.
[52] L. Rickwood, *Sports Scores, Stats and Big Data Analytics Bring Whole New Ballgame*, WhatsYourTech.ca, May 23rd 2018.
[53] J. Lee, B. Marquard, B. Sniderman, *Embedding trust into COVID-19 recovery*, Deloitte, 2020.

Through redesigning the relationships with fans, sports clubs can unlock many opportunities for growth, but it is essential for them to invest in those digital infrastructures required to power digital channels, streaming platforms and virtual reality products. Moreover, there is a huge opportunity if clubs and players go beyond traditional broadcasting channels to directly engage with fans, something that has been seldom done so far.

CHAPTER THREE – FINANCIALS OF THE SPORTS INDUSTRY.

3.1 Economic and Financial Forces Impacting the Sports Industry.

The financial performance of the Sports Industry is strictly linked to the current state of the economy as a whole. Sudden macroeconomics changes can heavily affect teams and leagues performance, especially the ones who lack long-term agreements with partners, allowing for revenues stabilization. Usually, sports organization hedge against these shifts in the global economy by diversifying their sources of revenues, for example through real estate developments. Among the different factors influencing the economics of Sports, four of them must be watched out closely: the economic cycle, the television and broadcasting market, the real estate market, and sustainability issues.

3.1.1 The Economic Cycle: a Strong Influence on the Sports Industry.

The economic cycle, made up of four different phases (growth, peak, recession and recovery) and typically lasting from five to six years, has a strong influence on the Sports Industry: as the economy flows through the different stages of growth and contraction, the Sports Industry experiences flourishing periods alternated with downturns.

Economic growth occurs when the economy is growing in real terms (faster than the rate of inflation). Evidence of economic growth includes increases in employment rates, industrial production, sales, personal income, and GDP. During periods of economic growth, the Sports Industry has benefited greatly. Usually new leagues and teams are formed, and teams and athletic departments across countries invest billions constructing new stadiums and arenas.

Then, when the economic cycle hit the recession stage (defined as negative GDP growth for two consecutive quarters, usually lasting for eighteen months), the Sports Industry is affected, as for example it happened during the 2007-2009 crisis in the US: as the economy entered the recession phase in December 2017, spending started slowing down, and many jobs within the Sports Industry got lost, approximately 115,000 between December 2007 and December 2010. The economic downturn not only affected the Sports Industry from a loss of employment point of view, but also leagues ceased operations, teams declared bankruptcy, construction of new facilities slowed down or stopped, and sponsorship revenues dropped[54].

[54] M. T. Brown, D. A. Rascher, M. S. Nagel, C. D. McEvoy, *Financial Management in the Sport Industry,* 2016, p. 43.

The economic downturn impacted the Sports Industry at different degrees depending on the sports organization and the industry segment. The recession main impact has been on sponsorships missed renewals: when the economic cycle starts to contract, especially when coupled with a financial crisis as it happened during the years 2007-2009, main sponsors start to limit their cash outflows, as a consequence limiting sports organizations' cash inflows, and this represents a big issue for the Sports Industry considering the high dependency on sponsorship revenues. Analyzing the US case, the 2007-2009 crisis had evident impact on women's professional sports and NASCAR. Women's professional sports are extremely sensitive to changes in the economic cycle[55], while NASCAR has also proven to be particularly correlated to changing economic conditions, mainly because of sponsorship losses and higher gasoline prices. Just prior to the recession's beginning, a top NASCAR team had to generate between \$20 million and \$25 million in revenues per year, of which \$15 million to \$20 million would come from the team's primary sponsors. When the economy slowed, sponsors became hard to find[56]. At the same time, higher gasoline prices affected NASCAR more than other leagues, as NASCAR fans usually travel long distances to see races, and high gasoline costs affected their ability to get to the races[57].

3.1.2 Broadcasting and Television: Industry Resilience Against Short Term Downturns.

Another important factor in Sports finance is television and broadcasting revenue. It is a guaranteed form of revenue, with long-term contracts in place between leagues, conferences, teams and networks. Fortunately for sports teams and leagues, television revenues somewhat insulate the industry from short-term slowdowns in the economy, such as during the recession of 2007–2009[58].

Post-recession, long-term contracts will likely continue to provide protection to Sports organizations. For example, the English Premier League sold its British television rights for \$7.8 billion for the years 2016 to 2018. These figures do not include revenues from international broadcast rights, the Internet, or satellite/cable league packages[59].

---

[55] M. Kreidler, *State of uncertainty for women's sports*, ESPN, July 24th 2009.
[56] D. Newton, *With Ganassi pulling the plug on a team, question remains: Will it getworse?*, ESPN, July 1st 2008.
[57] B. Klayman, *High gasoline prices pinch NASCAR fans*, USA today, June 30th 2008.
[58] M. T. Brown, D. A. Rascher, M. S. Nagel, C. D. McEvoy, *Financial Management in the Sport Industry,* 2016, p. 46.
[59] M. Scott, *English Premier League sells British TV rights for \$7.8 billion*, The New York Times, February 10th 2015.

3.1.3 The Real Estate Market: a Revenue Diversifier Correlated to the Economic Cycle.

The more Sports has evolved from being simply a playful practice into one of the most flourishing industries, the more leagues and teams have looked for strategies to expand their businesses and to diversify their revenues stream. The development of real estate surrounding stadiums and sport venues has become one of the means through which sports organizations generate additional revenues inflows. The Real Estate market is strictly linked to the global economic cycle, and this also regards the sports venues: several team-owned stadiums constructions were delayed during the 2007-2009 crisis, and as soon as the economy improved, many stopped building projects started to be completed.

One of the most successful examples of the blending between Real Estate and Sports is the L.A. Live. This development, which surrounds the Staples Center in Los Angeles, is made up by complementary entertainment venues, including broadcast studios, restaurants, movie theaters, music clubs, and the Grammy Museum. The Anschutz Entertainment Group owns both the real estate and the Staples Center, as well as the Los Angeles Kings of the NHL and a portion of the Los Angeles Lakers, both of them playing home games in the Staples Center. L.A. Live has long-term leases with ESPN, Ritz Carlton, Regal Theaters, and the Grammy Museum, to name a few[60].

3.1.3.1 Amenities in Sports Facilities: Boosting Revenues and enhancing Fans' Engagement.

Selecting and training the right players and athletes is the core investment of any sports team. Nowadays, of almost equal importance it has become designing and building stadiums and arenas where teams play their matches, as well as where their fans enjoy the amenities offered by the facilities. A major part of the fans' experience is the game itself played on the field, but the full enjoyment of the match is more and more linked to the inclusion of numerous amenities in the stadium, letting fans to enjoy a three hundred- and sixty-degrees experience. These amenities can substantially enhance the revenue a team earns from its investment in players. A large number of fans are willing to pay higher ticket prices for enhanced levels of amenities, more varied experiences, excellent sight lines, and seats placed closer to the field or court. A team failing to offer different amenity packages to the full range of its fans leaves a

[60] T. Van Riper, *Where real estate is whacking sports*, Forbes, July 14th 2009.

great deal of potential income "on the table". If a team fails to capitalize on most or all of its revenue opportunities then, in the long run, a franchise will either be less profitable (and have a lower market value) or spend less for players than teams that offer their fans a full range of revenue generating amenities.

In this context, it is of great importance that team and stadium owners understand the value of luxury. This concept can be better understood by looking at the Automotive industry: people's first need is to have a car as a transportation mean, but once this need is met, most drivers appreciate having some optionals within the car, and this luxury increase manufacturers' bottom-line profits. Similarly to drivers, sports fans wants competitive teams. But once this need is satisfied, they also want a set of additional services (i.e., amenities) that enhance their experience as fans. As those car manufacturers offering the right mix of packages enjoy higher profits, those teams playing in facilities characterized by a set of distinctive amenities will increase their financial performance as compared to those teams not offering these services to their fans. Sport venues have to be considered similar to any real estate project, where owners will offer higher priced accommodations and charge more for retail spaces in some parts of the building, and then offer other buyers (i.e., fans) lower priced seats or locations in other sides of the facility. It has been long realized that some fans are able and willing to pay higher admission prices to secure access to seats that offered the best available sight lines. As a result, seats closer to the field or courts have always cost more than those farther away. Fans also will pay more for more comfortable (or wider seats). Building a facility with more comfortable seats, however, reduces the total number that can be offered (wider seats take up more space)[61].

3.1.3.2 Disneyfication of Sports Facilities.

Talking about sports venues and amenities it is important to analyze the concept of "Disneyfication", i.e., the inclusion of numerous retail outlets and entertainment activities within a facility, and its effects on revenues[62]. The first step towards Disneyfication is building facilities over much larger footprints to have enough space to build the full set of amenities such as restaurants, pubs, retail spaces and other activities that can be enjoyed by attendants during a game day or while taking part to a non-sports event. From being simple sports fields, stadiums and arenas have now become places to be lived and enjoyed by not only sports fans

[61] J. A. Winfree, M. S. Rosentraub, *Sports Finance and Management. Real Estate, Entertainment and the Remaking of the Business*, 2012, pp. 111-112.
[62] *Idem*, p. 112.

all year round, but also by entire communities. By providing facilities with a full set of amenities, teams and stadiums owners objective is to make the fans' spending happening for the biggest part within the facility, and not outside as it happened years ago, resulting in increased revenues streams for a team. Moreover, building facilities with complementary amenities make the fans spending more and more time at the venues, and this has two positive effects on teams' revenues: on the one hand, fans spend their money buying directly at facilities retailers; on the other hand, with fans spending more time at facilities, teams' owners can charge more for advertising and naming rights at the stadium, as there is more time for consumers to be influenced by the advertised messages. Hence, it is clear how adding amenities to sports facilities has a multiplicator effect on team owners' revenues.

Of course, the opportunity to increase revenues does not come without issues. The first and most important one is that to build facilities that can host a full set of amenities (coupled with the sports field) a vast free land is needed. The second issue is more related to logistics and is linked to the convenience of fan access. Here the solution strictly depends on two factors: first, on the type of sports the facility is going to host; second, facility owners need to consider different needs coming from different fans clusters, i.e., the ones who buy luxury tickets and those who buy seats in other sections. In fact, revenues maximization for teams requires finding the optimal solution in meeting the needs of two group of fans. Regarding the positioning of the facility (either in suburbs or in the city center), the ones who buy luxury seats can generally afford extra travel time for a week-end game (week-days games have to deal with working hours and travel time required to get to the location), so in general building facilities in suburban areas do not restrict revenues flow. But again, this analysis would require further investigation depending on the type of sport.

Another key decision a facility owner must take involve the mix between luxury and normal seats, coupled with the overall maximum capacity. There are certain size issues that have become benchmarks relative to sight lines. For example, ballparks with seating for approximately 45,000 have been found to maximize sight lines and offer fans the best range of amenities. Facilities of this size maximize the number of seats between first and third base and then along the foul lines, but beyond the bases. Those ballparks that offer more seating capacity must either place extra seats in a taller upper deck or in the outfield. With reduced sight lines, extra seats will only sustain lower prices. Further, if the team is not as successful, it is likely these seats will remain unsold. While it is usually considered better to play games without too many vacant seats, there is another very important reason not to build too much excess capacity. When fans know that there will always be tickets available, they are reluctant to make advance purchases. This leaves teams dependent on large walk-up crowds on the day of a game and vulnerable to the possibility that at the last moment people might decide not to attend a game. When fans are concerned that good seats for a particular game they want to see may sell out, they are more likely to make an advance purchase[63]. Once the overall capacity as been decided, the next analysis should involve determining the right balance between luxury and normal seats.

3.1.4 Sustainability: Avoiding Waste of Resources and Environment Pollution.

Sustainability is one of the most important themes driving todays' economic policies and interventions, and as such it influences strategies and decisions at Sports Industry level too. In particular, sustainability issues arise when dealing with mega-sporting events like the Olympic Games or the FIFA World Cup, usually requiring hosting countries to invest lots of resources in building new stadiums and arenas that, after the event ends, remain unused in most of the cases.

For example, talking about Olympics, the Chinese case is one of the most evident examples of how the un-sustainable development of venues represents a waste of financial resources and a threat for the environment. To host the XXIX edition of the Olympic Games, the Chinese government invested $ 43 billion; however, many of the venues built for the Games proved to be too big and too expensive for the ongoing hosting of events. The Olympics became an economic disaster for the Chinese, as sport-related infrastructure projects led to little long-term economic growth, opposite to improvements to other infrastructures (airports, highways, and transit systems) that were needed during the Games and that provided long-term benefits[64].

Beijing is not alone in experiencing losses from unused facilities constructed for hosting specific international events and their attendees. Of the ten new stadiums built in South Korea to host the 2002 World Cup, most are unused today. Montréal finished paying for its Olympic Stadium 30 years after hosting the 1976 Games. The facility was largely unused when debt obligations were finally met. Full-service hotels in Lillehammer, Norway, built to handle the influx of visitors for the Games, struggled after the 1994 Winter Olympics[65].

---

[63] *Idem*, p. 125.
[64] V. Matheson, *Caught under a mountain of Olympic debt*, The Boston Globe, August 22nd 2008.
[65] M. T. Brown, D. A. Rascher, M. S. Nagel, C. D. McEvoy, *Financial Management in the Sport Industry,* 2016, p. 48.

3.2 Ownership Structures and Financial Performance.

When analyzing key financials behind a sports team or league it is very important to start by understanding its ownership structure, as it has major implications in tax, economics and legal obligations. Team owners can choose among several structures, including sole proprietorships, partnership, limited liability corporations, governmental and non-profit. At each ownership structure different pros and cons correspond.

Three main business opportunities pushed team owners to review the ownership structures in recent years. First of all, new, large-scale real estate development projects have been anchored by sports facilities. Second, while the revenue stream from telecasts of games exploded in the 1960s and grew robustly for some leagues through the 1990s, the first years of the twenty-first century saw the birth of team and league-owned networks (in the US, for example, the Yankee Entertainment and Sports Network, YES; in Europe, many Football teams added private networks and TV channels to their business, such as Manchester United TV). Third, in the building or remodeling of every sports facility, team owners wanted to enhance and expand the fans' game-day experience through the inclusion of the above-mentioned amenities (see 2.4.1.3.1 and 2.4.1.3.2), leading to an increase in their in-house spending.

These opportunities led to major organizational and managerial changes, making sports businesses as well-structured as any other company operating in a different industry. Hence, while the core business is still represented by the sports area and the organizational structure built around it to allow for athletes and players development, in recent years other parallel business functions have developed, each one overseeing critical aspects of the sports business (such as real estate development and management, media and network operations, sponsorship and commercial operations). While years ago it was not uncommon that the sports business was the principal interest for team owners, the more Sports has evolved into a structured business the more team owners have become either institutional investors or people that have accumulated wealth through other forms of businesses and enterprises, and then add the sports team to their holdings.

In the next pages the US and European cases (with a special focus on Football) will be analyzed, as they present the readers with different peculiarities making it useful to be analyzed separately.

3.2.1 Ownership Structures in the US Sports Industry.

In the US professional sports, most teams are operated as for-profit businesses structured according to various ownership models[66]. The three most common are: private investor, multiple owners and corporations[67].

In the private investor model, a wealthy person owns a team and can either play an active role or delegate the daily management to a pool of managers. The main advantages are low organizational costs, easy decision making and independence, having the opportunity to dispose of the team at his/her discretion. But to high rewards usually correspond high risks: a sole owner has unlimited liability, meaning his/her personal wealth is at risk to pay off team's creditors.

The most common model for team ownership is the multiple owners model. It is the most common for different reasons. First, the value of franchises has risen so high that it is rare for one individual to be able to afford to purchase a franchise on his or her own. Each ownership group is governed by an investment syndicate document, which outlines the decision rights of the owners, including who will represent them in league meetings. Sometimes the ownership group has a dominant individual who appears to be a single owner[68]. The most obvious drawback to having a team owned by two or more people is that there might be disagreements among the owners. The benefit, however, compared to a sole proprietorship is that there is less financial risk for each owner. If a team must raise cash, each partner can contribute, and the inclusion of partners also means people with different ideas regarding revenue generation could be incorporated into the management of the franchise[69].

The third ownership model is corporation model. Corporations are legal entities owned by shareholders who elect a board of directors to manage the team. Its main benefit is the limited liability provided to the owners, meaning that the corporate capital and the private wealth are neatly separated. So, investors' losses are limited to their investment. Some US teams are controlled by corporations, but evidence shows that there is far less use of this ownership structure as compared to what one may expect, while this model is far more widespread in European countries.

---

[66] M. T. Brown, D. A. Rascher, M. S. Nagel, C. D. McEvoy, *Financial Management in the Sport Industry,* 2016, p. 37.
[67] G. Foster, S.A. Greyser, B. Walsh, *The business of sports,* New York: South-Western College Publishers, 2005.
[68] M. T. Brown, D. A. Rascher, M. S. Nagel, C. D. McEvoy, *Financial Management in the Sport Industry,* 2016, pp. 37-38.
[69] J. A. Winfree, M. S. Rosentraub, *Sports Finance and Management. Real Estate, Entertainment and the Remaking of the Business*, 2012, p. 55.

After having analyzed ownership models adopted at team level, it is interesting to further investigate what are the different options at league level, as the structure of a league also affect the financial management of the teams belonging to it. Decisions made at league level impacting teams' financial management include admission criteria, competition structure, revenue sharing mechanisms and player relations. In principle, a league may be structured according to two different models: the single-entity ownership model and the distributed club ownership model[70].

With a single-entity structure, a single group or an individual owns the league and all of the teams that compete within that league. This structure is frequently used with new or start-up leagues: for example, the Women's National Basketball Association (WNBA) was owned by the NBA. An advantage of the single-entity structure is that antitrust law does not apply, as it does to leagues that use the distributed club ownership model. Collusion, agreements that eliminate competition, and other violations of antitrust law are not possible when one entity owns a league and all of its teams. Therefore, single-entity leagues can place franchises in preferred cities and assign players to specific teams in specific cities. The assignment of players to teams also allows a league to promote competitive balance within the league so that no one team dominates competition[71]. A financial advantage for single-entity leagues is that player salary costs are constrained. Players sign contracts with the league, so there is no bidding for players on an open market. In 2014, the average MLS salary was $226,000. Kaká was the league's top earner at $7.17 million, and 25 players earned the league minimum for players under the age of 25, that was $36,500. The league's salary philosophy is to pay for impact players while constraining costs on defenders and goalkeepers[72]. A drawback to single-entity status is that it provides little economic incentive at the club level[73]. For the franchises, there is no benefit to operating well, as the benefits are completely shared with the other franchises in the league, although the losses are also equally shared. This is one of the reasons why the WNBA and NBA Development League began to move away from the single- entity structure and toward the distributed club ownership model[74].

On the other hand, the distributed club ownership model results to be more widespread, in particular adopted by Major League Baseball, the NBA, the NHL and the NFL. According

---

[70] G. Foster, S.A. Greyser, B. Walsh, *The business of sports,* New York: South-Western College Publishers, 2005.
[71] M. T. Brown, D. A. Rascher, M. S. Nagel, C. D. McEvoy, *Financial Management in the Sport Industry,* 2016, pp. 40-41.
[72] A. Keh, *Many in MLS playing largely for love of the* game, The New York Times, October 26th 2014.
[73] G. Foster, S.A. Greyser, B. Walsh, *The business of sports,* New York: South-Western College Publishers, 2005.
[74] J. Lombardo, *A new play for the AFL?*, SportsBusiness Journal, February 25th 2008.

to this structure, each individual franchise has its ownership group, and revenues at league level (such as those from national TV contracts) are centrally collected and then distributed to each team participating in the league. The main drawback of this ownership model is that conflicts related to the financial management of the league can arise: for example, large and small-market franchises tend to have different opinions about the revenue sharing mechanism.

3.2.2 Ownership Structures in the EU Sports Industry: a closer look at Football teams.

The European Sports Industry presents different ownership structures as compared to the US one, especially when it comes to Football, that will be the focus of next pages. In particular, given its relevance in the global Sports Industry, the English Premier League will be analyzed and then key peculiarities of the other top-four European Football leagues (i.e., Italian Serie A, Spanish La Liga, German Bundesliga and French Ligue One) will be further assessed.

Since its inception in 1992, the English Premier League has been mainly characterized by three different ownership models: the stock market ownership model, the supporter trust ownership model and the foreign investor model of ownership. In all three cases the Football team is incorporated as a limited liability company and is controlled by a holding company owning the shares, but according to the adopted model different implications derive.

3.2.2.1 English Premier League: Stock Market Model of Ownership.

Although the first Football club to go public on a stock exchange has been Tottenham Hotspur in 1983, the stock market ownership model became popular in the mid-1990s. In particular, the rapid commercialization of the Football Industry following the Premier League foundation in 1992 resulted in the perception that a significant increase in broadcasting rights would have enabled Football clubs to become profitable businesses. As a consequence, during a four-year period, from January 1993 to January 1997, shares in the Football Industry rose seven-hundred seventy-four percent and outperformed the overall stock market by a factor of ten. By 2000, there was a total of 22 Football clubs listed on the London Stock Exchange, the Alternative Investment Market and the OFEX: altogether, a total of £167 million had been raised through these IPOs[75], then invested to restructure stadiums, develop commercial

[75] Initial Public Offering.

operations, reduce borrowing, provide additional working capital and improve liquidity to existing shareholders[76].

Then, after booming, the stock market ownership model started to decline with many Football teams delisting from their respective stock exchanges. There are three main reasons why the Football clubs have chosen to delist. First, although stock market flotation enabled football clubs to generate initial outside investment, investor returns in the form of dividends and capital gains through share price increases were poor. Manchester United was the only club on the stock market to generate annual profits and shareholder returns. Second, the objective of a Football club is to promote Football as a sporting activity and as a business. In European sport, and Football in particular, the sporting objective has long been established and understood. Therefore, the fundamental principles of profit maximization and providing a return for investors that govern the stock market model do not dovetail neatly in the context of a Football club. Third, there have been recent changes in ownership at many of the listed clubs as foreign investors have become more prominent in English Football. A change in ownership is usually accompanied by the Football club reverting back to private company status and leaving the stock market as the club is no longer owned by a range of shareholders and it reduces the administrative obligation required to maintain a stock market listing[77].

3.2.2.2 English Premier League: Supporters Trust Model of Ownership.

A supporter's trust is an independent, not-for-profit, democratic, cooperatively owned organization that seeks to influence the governance of a Football club through improved supporter representation and also to develop stronger links among a club, a community, and a supporter base. The first trust was established in 1992 at Northampton Town, being part of a consortium that saved the club from financial collapse. Since then, the supporter trust ownership structure has increasingly grown in 2000, when the Labor government backed the establishment of an organization called Supporters Direct. The greatest part of trusts are incorporated as an Industrial and Provident Society, a mutual, not-for-profit organization without share capital, usually exercising their influence on the clubs through ownership of shares and board representation[78].

---

[76] S. Morrow, *The New Business of Football: Accountability and Finance in Football*, MacMillan Business, 1999, p. 67-91.
[77] S. Chadwick, S. Hamil, *Managing Football. An International Perspective*, 2010, pp. 21-22.
[78] *Idem*, p. 23.

However, if it is true that the trust model can be successful in the lower reaches of the Football League (English second division), it has been questioned whether this model can be successfully applied in the Premier League[79].

3.2.2.3 English Premier League: Foreign Investor Model of Ownership.

The foreign investor ownership model has been the most vivid trend in the last years within the English Premier League, where fourteen out of twenty clubs are controlled by foreign entities, either wealthy people and institutional investors.

There are three clear reasons to explain the rise in foreign investments. First, as the football industry has become more commercialized, the costs required to operate a club in the Premier League, taking into account the significant rise in player wages, have increased substantially. Many owners have been unable to provide the required levels of investment in order to compete and have sold their majority stake in the club to wealthy foreign investors. (This was the case at Liverpool, where David Moores sold his 51.6 percent stake in the club, as he was unable to provide the finance needed to relocate from Anfield to a new stadium). Secondly, the ownership of a club in the Premier League can be an attractive proposition for foreign investors, notably as a ‘‘trophy’’ asset, conferring global notoriety and fame on owners simply by virtue of owning a participant in the Premier League competition. The Premier League is the most popular league in the world, and there is an element of prestige in owning one of the member clubs. Third, the high value of the most recent domestic, overseas, and highlights broadcasting rights of approximately £5.1 billion between up until 2025 and the opportunities for global expansion to maximize the brand potential in emerging markets such as Asia are attractive to foreign investors[80].

The main issue linked to the foreign investor model of ownership is the apparent financial mismanagement following the acquisitions. In fact, foreign investors usually run their clubs as “trophy assets”, a model according to which ongoing investments in losses are required and results are delivered only in the form of capital growth, as competitive pressure to win outweighs any intent to limit costs[81].

---

[79] A. Brown, *‘Not for Sale’? The Destruction and Reformation of Football Communities in the Glazer Takeover of Manchester United*, Soccer and Society, 2007, p. 617.
[80] S. Chadwick, S. Hamil, *Managing Football. An International Perspective*, 2010, pp. 25-26.
[81] *Annual Review of Football Finance 2011: Pressure to Change*, Deloitte Sport Business Group, 2011.

3.2.2.4 English Premier League: Ownership Structure Influence on Clubs' Financial and Sporting Performance[82].

In conventional businesses it is easy to expect that primary investors' goal is to make a profit out of the company owned, however, this rarely occurs in Football and so does in the English Premier League[83]. Considering that the Premier League is currently the most appealing European Football League and the most profitable in the world, it is clear that there is a huge mismatch between revenues and costs in the Football industry: in particular, the biggest costs a club faces are players purchases and paying for their salaries, and as we already saw the general trend is increasing (see 2.3.3.1). The paradox between revenues and costs in the English Premier League can be explained according to how the ownership structures in the leagues have evolved. In the last years there as been a general trend of clubs moving away from stock exchanges in favor to private investors, in particular foreign ones. While clubs' revenues continuously increased during the years, their profitability has become poor and poorer, characterized by an increase in debt level and losses. This can be explained by the shift from being listed to being taken private: generally speaking, the guiding principle in the stock market is the profit maximization, and this could not apply when clubs are owned by wealthy, private investors.

The Sheffield Hallam University conducted an interesting study analyzing the relationship between ownership structures and club performance in the English Premier League, investigating the effect of different ownership model on clubs' financial and sporting performance. In particular, five key financial indicators have been investigated: growth, profitability, return on capital employed, liquidity and defensive positioning. The first three allowed to understand a club's ability to generate profits and a potential return for its shareholders, while the latter examined the ability to meet its obligations with creditors and its capital structure. Seven further financial ratios have been analyzed: turnover increase, profit increase, profit, return on capital employed (net assets), current ratio, debt and gearing.

---

[82] From R. Wilson, D. Plumley, G. Ramchandani, *The Relationship between Ownership Structure and Club Performance in the English Premier League*, Sheffield Hallam University, Sport Business and Management: An International Journal, 2013.
[83] J. Beech, "Finance in the football industry", in S. Hamil and S. Chadwick, *Managing Football: An International Perspective*,2010 Oxford, pp. 119-151.

Indicator	Calculation	Interpretation
Turnover increase (%)	This year's turnover – last year's turnover)/last year's turnover	Higher score is more desirable
Profit increase (%)	(This year's profit (loss) after taxation – last year's profit (loss) after taxation)/last year's profit (loss) after taxation	Higher score is more desirable
Profit (%)	After tax return on sales as a % of turnover	Higher score is more desirable
ROCE (%)	Profit after taxation as a % of net assets	Higher score is more desirable
Current ratio	Current assets/current liabilities	Higher score is more desirable
Debt (%)	The absolute amount of debt divided by total	Lower score is more desirable
Gearing (%)	Total amount of borrowings both short and long term. Calculated as gearing percentage of shareholders' funds	Lower score is more desirable

Table 3.1 – Financial ratios and their interpretation[84].

Clubs have been then ranked against each other relative to each financial ratio for each season under analysis (2001-2010), receiving seven individual ranks for any given season, then summed up to compute an overall financial score incorporating all sides of financial performance. On the other hand, to account for sporting performance, a club's final positioning in the League in any season under review has been taken as the basis for measuring the on-the-pitch success. Then, financial and sporting performance data were analyzed using two different statistical tests: a correlation analysis was conducted to examine the relationship between clubs' financial performance and final positioning in the League; one-way analysis of variance (in short, ANOVA) tests were then used to assess the effect of ownership model on clubs' overall performance, both financial and sporting. The analysis has been conducted in two steps: first

[84] Table from R. Wilson, D. Plumley, G. Ramchandani, *The Relationship between Ownership Structure and Club Performance in the English Premier League*, Sheffield Hallam University, Sport Business and Management: An International Journal, 2013.

the relationship between financial and sporting performance has been assessed, then the focused shifted on the effects of ownership models on both financial and sporting performance.

First, by using correlation analysis, the relationship between the financial performance of English Premier League clubs in a given season and their corresponding final league positioning has been assessed. Figure 3.1summarizes the correlation coefficients (r-values) for league positioning and financial performance of clubs in the period between 2001 and 2010. For growth, profitability and liquidity indicators, a negative value of the correlation coefficient indicates that, as a club's league position improves (or worsens), so does its financial performance and vice versa. A positive correlation coefficient indicates that the analyzed financial indicators are inversely correlated with league positioning. On the other hand, for the defensive positioning indicators and overall finance score, the opposite is true: a negative correlation coefficient shows an inverse relationship, and a positive one inficates a direct association with league positioning. For all indicators, a score of +/- 1 would indicate perfect correlation with league position, and a zero coefficient indicates absence of any systematic trend between the relevant variables.

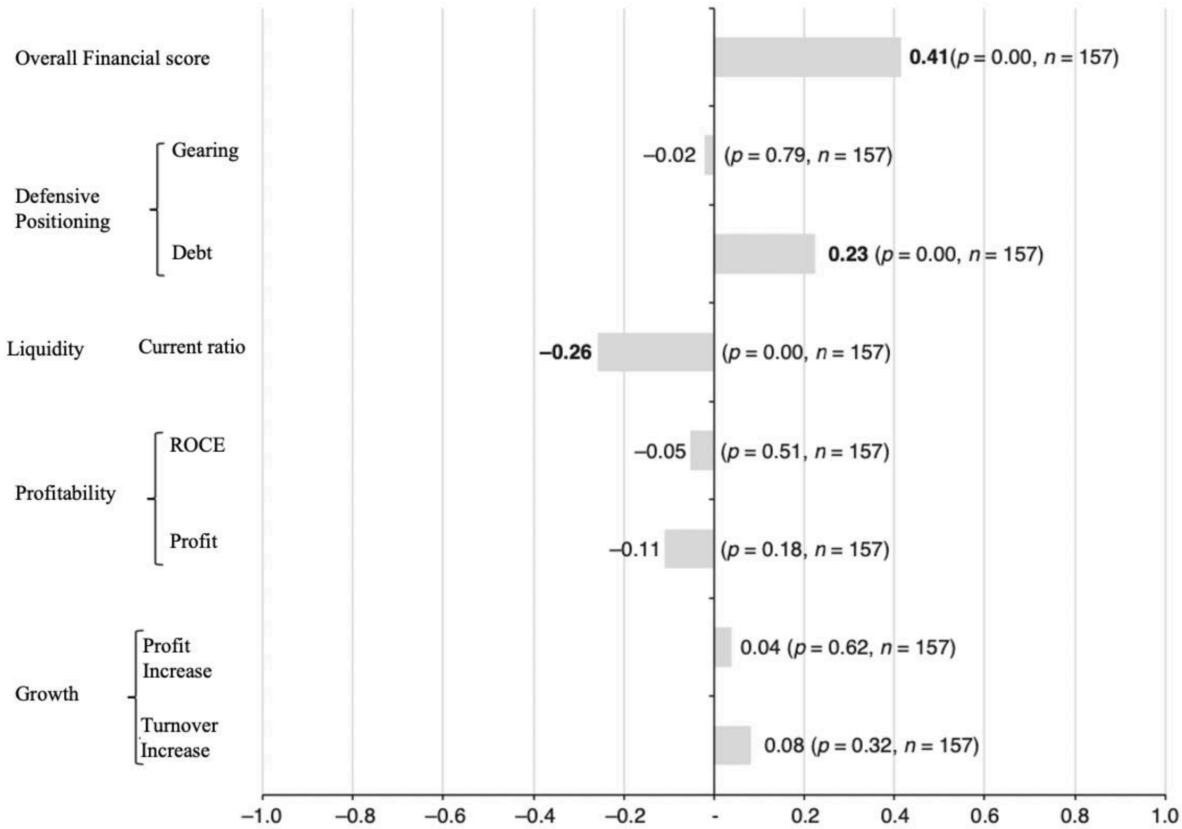

Figure 3.1 – Correlation coefficients for finance and league performance[85].

[85] *Idem.*

As the figure above shows, the correlation between the key financial indicators examined and league performance has been found to be weak and not statistically significant. However, two exceptions exist: correlation coefficient for the current and debt ratios are statistically significant (bold numbers in Figure 3.1), meaning there is some evidence indicating that clubs with good liquidity tend to perform better from a sporting point of view, and the same applies to those clubs having lower debt levels. In addition, also the overall financial score shows statistical significance, meaning that better financial management is associated with better sporting performance for English Premier League teams.

This correlation analysis has been then expended to investigate any effect coming from the ownership structure of clubs. Consistently with the overall trend, there was no statistical significance between the two growth indicators (i.e., profit and turnover increase) and league ranking when data was analyzed by ownership type. However, liquidity and defensive positioning indicators, as well as the overall financial score, show a stronger relationship between financial and sporting performance when it comes to the stock market ownership model: this suggest that if the stock market model is seen to outperform other models in financial terms, then this might also be reflected in the club's final positioning in the league.

This hypothesis has been further tested to check for any effect from ownership model in the club's financial and sporting performance. Below the main findings of this study:

- Domestic ownership and stock market models showed higher net profit as a proportion of turnover, as compared to clubs owned by foreign investors.
- Clubs whose shares are traded on the stock exchange showed a better liquidity positioning and lower debt levels than privately owned clubs, either controlled by domestic or foreign investors.
- Private and domestic-owned clubs outperformed foreign-owned ones in terms of debt performance, with the latter exhibiting higher debt levels than the other two ownership structures.
- Overall, analyzing ownership structures correlation with the aggregated financial score it turns out that the stock market model is the most financially efficient structure. It was already established that a correlation had been found between a club's financial performance and final league positioning; moreover, this relationship showed more strength for the stock market model, thus it can be argued that this ownership structure performs better in terms of league positioning too.

- In terms of league positioning, domestically owned clubs showed a poorer performance as compared to both foreign and stock market ownerships, while the comparison between the last two was not statistically significant.

Overall, the main findings of the study carried out by the Sheffield Hallam University suggest that the stock market ownership structure performs better from a financial perspective as compared to the private ownership model, both domestic and foreign, and from a sporting perspective only relative to domestically owned Football clubs. The fact that clubs floating on the market outperforms the others from a financial perspective might be explained by the financial discipline imposed by the stock exchange on listed companies (as well as clubs). However, the authors of the study specify that these finding cannot be directly extended to other Football leagues different from the English Premier League, and that further investigation would be required.

3.2.2.5 Ownership Structures in other top-four European Football Leagues.

While clubs participating in the English Premier League are mostly incorporated as limited companies, in the other top-four European Football leagues (Italian Serie A, French Ligue One, German Bundesliga and Spanish La Liga) there are other legal structures that are peculiar to their legal frameworks.

Starting from Italy, professional Italian Football clubs are controlled either by wealthy individuals and families, or (indirectly) through corporate groups. Therefore, family management predominates in the Italian landscape: its main implication is a lack of separation between ownership and control, translating into less external pressure and discipline which, in turn, can have consequences on the clubs' financial behavior[86]. Three clubs, namely Juventus, Lazio and Roma, are listed on the Italian stock exchange, although only a minority percentage of shares are listed, enabling the family or corporations to maintain control and thus demonstrating little separation between ownership and control[87]. The greatest part of Italian football clubs are not profitable businesses, so they can be framed as "trophy" assets in the hands of their owners.

[86] S. Hamil, S. Morrow, C. Idle, G. Rossi, S. Faccendini, T*he governance and regulation of Italian football*, Soccer & Society, 2010, pp. 373-413.
[87] S. Morrow, *The People's Game?: Football, Finance and Society*, 2003.

Continuing with the French case, strict legislations forbidding the clubs' control in the hands of foreign investors limited teams' financial capabilities[88], and as a consequence French Football experienced year of crisis in the 1970s and 1980s, leading to constitutional changes allowing for private investments. Ultimately, in 1999 the introduction of the *Société anonyme sportive professionelle* permitted Football clubs to convert to limited companies[89].

German football clubs were traditionally constituted as non-for-profit member associations. Since 1998, German clubs have been permitted to incorporate the professional football club as a subsidiary of the member association. This subsidiary company is constituted as a limited company or even a public limited company[90]. Although German football clubs can list on the stock market, the ultimate ownership and decision-making power remains under the control of the member association. The German Football Association rules state that the member association retains 50 per cent plus one vote of the incorporated football club, ensuring that the majority ownership of German football clubs cannot be granted to any one individual[91]. What supports the member ownership model of governance is the belief that by involving fans clubs will act in the benefit of their communities looking at long-term objectives. Moreover, this ownership structure should guarantee the participation of football fans into the clubs' management activities, avoiding conflicts of interest between the investors and fans-members[92].

Lastly, the majority of the professional clubs in Spain are constituted as *Sociedades Anonimas Deportiva*. This model was introduced to the Spanish football industry in 1990 following a period of financial crisis brought on by the lack of central regulation, increasing commercial pressures, rising costs, poor financial performance and high levels of debt[93]. Anyway, the introduction of the SAD model did not have the expected effects on the clubs' financial statements. On the one hand, the conversion into SADs involved an intense process of concentration of capital in the hands of a small number of shareholders, often just one person; and at the same time, the debt situation of a fair number of Spanish clubs became critical. This situation led the *Liga de Fútbol Profesional* to approve control regulations in January 2013 to contribute to the economic and financial sustainability of professional football[94]. Moreover, the

---

[88] A. King, *The European Ritual: Football in the New Europe*, 2003.
[89] F. Bolotny, *Football in France*, In W. Andreff, S. Szymanski, *Handbook on the Economics of Sport*, 2006.
[90] S. Chadwick, S. Hamil, *Managing Football. An International Perspective*, 2010, p. 30.
[91] H. Dietl, E. Franck, *Governance Failure and Financial Crisis in German Football*, Journal of Sports Economics, 2007), p. 665.
[92] L. Ferkins, D. Shilbury, *Board strategic balance: an emerging sport governance theory*, Sport Management Review, 2015, pp. 489-500.
[93] G. Ascari, P. Gagnepain, *Spanish Football*, Journal of Sports Economics, 2006, pp. 76–89.
[94] I. Acero, R. Serrano, P. Dimitropoulos, *Ownership structure and financial performance in European football*, Coporate Governance: The International Journal of Business in Society, 2017.

introduction of the SAD model brought an end to the membership model of ownership at all Spanish clubs except for FC Barcelona, Real Madrid, Athletic Bilbao, and Osasuna, who were allowed to retain the membership model of ownership as they had recorded a positive balance in their accounts during the 1985–1986 season. These clubs are governed democratically on the one member, one vote basis. At Barcelona, over 160,000 mebers pay an annual membership fee that entitles them to vote for the club president every four years and to elect members to the board to oversee the administration of the club. They are also eligible for election to the assembly of delegates, a 3,000- member body that has responsibility to vote on issues of club governance[95].

3.2.2.6 Ownership Structures and Financial Performance in other Top-Four European Football Leagues[96].

As already done for the English Premier League case (see 2.4.2.2.4), we now deep dive into the relationship between ownership structures and financial performance in other top-four European Football leagues.

In particular, correlation analysis suggests a non-linear relationship (inverted U-shaped curve) between ownership concentration and financial performance, mainly driven by monitoring (positive) and expropriation (negative) effects. The starting point to demonstrate this hypothesis is a database containing information on ninety-four top-European Football clubs from the 2007/2008 – 2012/2013 seasons. The model used to analyze the relationship between ownership concentration and financial performance uses Return on Assets (ROA) to measure the financial performance. Then, in the specification of the model the following control variables have been included:

- Football club size: measured by the natural logarithm of each club's total assets at the end of each fiscal year. In particular, firm size is positively correlated to financial performance, leading to economies of scale in operations, a greater control over external stakeholders, and higher appeal *vis-à-vis* top players increasing the possibility of better financial performances[97].

[95] S. Chadwick, S. Hamil, *Managing Football. An International Perspective*, 2010, p. 30.
[96] From I. Acero, R. Serrano, P. Dimitropoulos, *Ownership structure and financial performance in European football*, Coporate Governance: The International Journal of Business in Society, 2017, pp. 511-523.
[97] M. Orlitzky, *Does firm size confound the relationship between corporate social performance and firm financial performance?*, Journal of Business Ethics, 2001, pp. 167-180.

- Debt: high indebtedness negatively affects a club's future investment opportunities, impacting also the long-term operating performance and solvency[98]. On the other hand, other studies suggest that a firm's leverage can also act as control mechanism over managers by reducing the quantity of free cash flow, thus increasing the financial discipline of the club and guaranteeing the optimization of financial resources[99].
- Growth Sales: a variable capturing growth opportunity, estimated as the annual mean growth rate of operating income from the previous three seasons.

Correlation analysis demonstrates a significant positive effect of ownership concentration on ROA, confirming the initial hypothesis. In particular, main outcomes confirm a non-linear relationship (inverted U-shaped curve) between ownership concentration and performance, a consequence of both the monitoring and expropriation effects. In clubs with disperse ownership, an increase in the level of ownership concentration has a positive effect on performance (monitoring effect). However, when the level of ownership concentration is high, the effect becomes negative as a result of the possible risk of the expropriation of minority shareholders (expropriation effect). Thus, the results suggest that high level of ownership concentration have a negative effect on financial performance. A solution could come from regulators introducing regulations enabling control mechanisms in clubs where the level of ownership concentration is very high. The German Bundesliga, whose clubs show the best financial results, coupled with very good sporting results, can be taken as an example: the "50+1" rule imposed can be taken as good ownership model, giving stakeholders not only a voice but also power and control, increasing clubs' financial discipline too.

3.3 How to Finance a Sport Organization.

The increasing complexity that came with the transformation of Sports from being a playful practice into a structured industry has led many professional teams across various regions and leagues to face capital raising needs to be successful in their operations. Any club or sports organization that want to raise capital has five main options at its disposal. The first three options belong to the "traditional" finance and are accessible to any company: debt financing, equity financing and retained earnings. The latter are more peculiar of the Sports

[98] M. Singh, S. Faircloth, *The impact of corporate debt on long term investment and firm performance*, Applied Economics, 2005, pp. 875-883.
[99] I. Acero, N. Alcalde, *Ownership structure and board composition in a high ownership concentration context*, European Management Journal, 2014, pp. 646-657.

Industry and are government funding and gifts. In the following pages all the five financing options will be analyzed, with a deep dive into debt and equity financing solutions accessible to sports organizations.

3.3.1 Debt Financing: Loans, Project Financing and Bonds.

Debt financing is the most widespread and preferred capital raising solution in the Sports Industry, also considering both pros and cons. Sports organizations willing to issue new debt to raise capital can chose among various options belonging to the "traditional" finance: corporate loans, project financing, forward funding future revenue streams, corporate bonds, mini bonds and private placements.

Through corporate loans, banks lend an amount of money either to be destined to a general or specific purpose, charging an interest rate accounting for the borrower's risk positioning. Lenders likely require a securitization of the corporate loan exploiting the firm's assets, sometimes also requiring the owners to put its personal assets as a further guarantee.

On the other hand, through project financing sports organizations borrow financial resources to purchase or develop real estate assets such as stadiums, training grounds or other facilities. Generally, the funds come as the costs are incurred, with the lender monitoring the progress of the work through their project supervisor.

To raise funds, sports organizations can also leverage on expected revenues streams coming from naming rights, transfer fees, sponsorship and merchandising revenues, or any other revenue stream locked by a contractual agreement between the borrower itself and a third party. In particular, those expected cash inflows can be used as collateral for an upfront loan. This is a very common practice in Football: for example, Leicester City from English Premier League last took out bank loans to finance the new training ground and stadium expansion by revolving around Riyad Mahrez's transfer to Manchester City and TV rights form Premier League[100].

The abovementioned financing solutions are not always available to all the sports organizations, as the amounts that can be raised are often limited by the fact that many of the clubs are loss-making businesses, giving lenders cause for concern. When those financing solutions are not available, clubs and Sports organization can raise funds by accessing the bond market. The first option available is raising funds through corporate bonds: investors lend the

[100] J. Blackwell, *Leicester City take out bank loans to help finance new £100m training ground and King Power Stadium expansion*, LeicestershireLive, May 11th 2020.

borrower an amount of money for a fixed time period, either receiving regular coupons (coupon bond) or not (zero coupon bond, in this case receiving a lump sum at maturity), plus interests on the capital lent. Corporate bonds are listed on the stock exchange, so they can be bought and sold by investors provided that there is an active debt market. A special type of corporate bonds is the mini bonds: they are unregulated, unlisted and not tradeable, cheaper to be issued and more flexible, but still less attractive for investors. Moreover, those organizations who want to maintain a degree of confidentiality can issue bonds through private placements directly to a small group, typically institutional, group of investors, such as insurance companies and pension funds. Issuing bonds to raise cash is quite common in Football. For example, to finance the transfer of Cristiano Ronaldo from the Real Madrid CF (see 2.3.3.1.1), the Italian Football club Juventus FC issued a five-year €175 million bond in 2019 reserved to institutional investors only. Given its purpose, the bond has been named by investors the "CR7 bond" (from the Football player's acronym) and got a lot of success among investors: initially it should have amounted to €150 million, but considering the extra demand from the market Juventus FC board of directors decided to issue an additional €25 million. The first Italian Football club to issue a bond has been S.S. Lazio in 1997, cashing in approximately €25 million (50 million Italian lirae)[101].

3.3.2 Equity financing: Tapping the Stock Market is still a Rarity in the Sports Industry.

Sports organizations that want to raise new capital, beyond doing it through debt financing, can decide to access the equity market. In this framework, equity capital is raised through the issuance of new shares, either in the form of common stock or preferred equity, representing a portion of the club's ownership. In particular, companies that are privately owned (i.e., whose shares are not listed on a stock exchange) have access to the equity financing through the Initial Public Offering (IPO). The IPO is the process through which the share capital of a privately owned firm gets listed on a public stock exchange, starting to float in the market. In particular, to meet capital needs of a company the primary IPO is conducted: in a primary IPO the company issues new shares to the public, thus diluting the ownership of the initial shareholders, and the capital raised is then used to finance the firm's operations.

Although tapping equity markets is a very common practice for firm, this does not hold for Sports companies. Starting from the US case, the Green Bay Packers (an NFL team) are the

[101] G. Dragoni, *Juventus, sul mercato un CR7 bond a 5 anni*, Il Sole 24 Ore, February 13th 2019.

only single team whose ownership structure resemble the stock market ownership model: in fact, its shares do not confer any of the advantage given by "traditional" stocks (i.e., are not tradeable on a public exchange, do not provide voting rights, do not pay dividends, etc…), representing more a sort of "collectible item"[102]. While there are some teams that are indirectly exposed to financial markets through being controlled by listed parent companies, it can be concluded that the NFL, MLB, NBA and NHL all have no teams that is listed on a public stock exchange. The same rarity of professional listed sports team seems to apply in Europe too, with the exception of few Football clubs. As previously seen (see 2.4.2.2.1), Football club listings boomed in the early 2000s, to then start a wave of delisting.

3.3.2.1 Pros and Cons of Going Public from a Sports Organization's point of view.

An Initial Public Offering is a good solution for those sports organization that want to raise large amounts of capital. Anyway, an IPO comes with both pros (financing real estate developments, financing top-players transfers, liquidation and increasing brand loyalty) and cons (costs and disclosure commitments).

Starting from the advantages from which a sports organization can benefit by going public, the amount of cash raised during an IPO can be invested with different purposes. For example, it has become quite common for professional sports organization to own the most up to date and renewed facilities as possible: stadiums and training grounds can be very expensive, and private owners often cannot afford such investments, so offering the club's stock to public investors could be a solution to raise the capital needed to invest in real estate developments. While in the past Sports facilities were generally financed by public institutions to keep teams in town, recently there has been a sharp decline in such subsidies, as taxpayers are no more willing to see their tax bills increasing to help wealthy owners in building their clubs' facilities[103]. The amount of cash raised through an IPO could also be invested in players' transfers: this had been a common practice in the English Premier League in the early 2000s[104]. Especially in recent times, players' transfer prices have skyrocketed, so issuing stocks to raise cash can be a good way to finance their acquisitions.

Professional sports teams' value has increased throughout the years, in some cases arriving at hundreds of millions of euros, then making changes of ownership very limited, as it

[102] L. Saunders, *Are the Green Bay Packers the worst stock in America?*, Wall Street Journal, 2012.
[103] M. Kane, *Stadium Financing Increasingly Using Private Fund Sources*, New York Journal, 1999.
[104] B. Smith, *How different types of ownership structures could save major league baseball teams from contraction*, Journal of International Business and Law, 2003, pp. 92-93.

is limited too the pool of potential buyers that can afford millionaires investments. Hence, an owner looking for potential buyers willing to purchase a stake in his/her club can decide to do it through an IPO: in this way, the owner can liquidate part of his/her shareholding, without giving up the team's control[105].

Last but not least, the sale of stock to the general public presents the opportunity for a sport franchise to increase its loyal fan base, in this way increasing brand loyalty. This brand loyalty can be beneficial to the owner in the form of increased merchandise purchases, website visits, season ticket sales, and revenue in general[106].

Although pursuing an IPO can bring the above-mentioned benefits to a Sports organization, going public implies many challenges and costs as well. Beyond the fact that different leagues apply different policies and restrictions to their clubs' ownership structure, one of the biggest IPO criticism is the costs associated to making a Sports club going public. The costs associated to an IPO have been debated for a long time in literature, with research showing that the costs of carrying out an IPO corresponds to around 15% or more of the raised capital[107], a very large sum if considering the amount of capital usually raised during IPOs. Aside from the many monetary costs, there will also be many opportunity costs incurred throughout the process. An example of this is the time commitment that key personnel of the organization will have to attribute to the sale of stock. Executives will need to spend much time meeting with lawyers, accountants, and financial advisors throughout the process, taking them away from their normal day-to-day responsibilities. The management of the organization prior to an IPO often has to go on "road shows" in order to promote the sale and gain awareness: this, again, occupies key personnel and can have negative effects of short-term operations and efficiency[108]. Moreover, the costs associated to an IPO do not end after the offering is completed, as recurring costs will be incurred to draft the documentation required by stock exchange regulators, set up shareholders meetings and other activities.

Another disadvantage linked to an IPO corresponds to disclosure commitments. In fact, going listed requires the periodic publication of financial statements and other key information, with a consequent loss of confidentiality and exposure to the general public. The exposure to

[105] R. Schaffer, *A piece of the rock (or the rockets): the viability of widespread public offerings of a professional sport franchises*, Virginia Sports and Entertainment Law Journal, 2006.
[106] J. Hubman, *A Financial Analysis of Publicly Traded Professional Sports Teams*, The College at Brockport: State University of New York, 2011, p. 3.
[107] G. Kratofil, Direct public offerings can fill business' capital needs, Kansas City Business Journal, 1999.
[108] J. Hubman, *A Financial Analysis of Publicly Traded Professional Sports Teams*, The College at Brockport: State University of New York, 2011, pp. 5-6.

the general public can be an issue for Sports organization, as newspapers and journalist often put a lot of attention over Sports topic, thus causing further cause for concern.

3.3.2.2 Three reasons why IPOs are uncommon in Sports Industry.

As previously mentioned, IPOs are not a common way to raise capital in the Sports Industry. In fact, Sports organizations prefer raising cash through other sources, such as debt markets. The unpopularity of the IPOs within the Sports Industry suggests that professional sports team do not benefit from listing their shares (as it happens on average in other industries), and this can be verified through three lenses: managerial, operational and financial disincentives[109].

Managerial disincentives can be defined as any impediment in the management of a business impeding the achievement of defined objectives. Sports team owners' objectives can be grouped into two clusters: win-maximization, i.e., managing the team to maximize the chances of success; profit-maximization, i.e., managing the team to maximize the Return on Investments (ROI). The existing literature and empirical analyses suggest that there are various managerial disincentives that can outweigh the advantages of an IPO. For example, one of the main consequences of listing stocks is an increase in the club's financial discipline, imposed by financial markets and their regulators. The increased financial discipline can negatively impact managers' freedom about investments decisions, such as buying a new player, and owners' objective of win-maximization versus profit-maximization[110]. This imposed constrains on the freedom to invest in talents poses a tough challenge on professional sports teams as existing research suggest that overinvestments pay off in sports. In particular, given the strong correlation between talent investment and winnings, sports clubs usually have a genuine incentive to overinvest[111]. Hence, unlisted sports team experience a competitive advantage over listed ones, as the former are not subject to financial scrutiny limiting their freedom to invest in talents. This limits the appeal of IPOs in the eyes of sports managers.

On the other hand, operational disincentives correspond to any impediment negatively affecting the sportive performance of a sports organization. Research shows contradicting results about IPOs impact on clubs' sporting performance. Some studies found that most clubs

[109] C. K. Oh, *Why Are Sports Team IPOs Uncommon?,* Joseph Wharton Scholars, 2019, p. 6.
[110] D. Russell, *Football And The English: A Social History Of Association Football In England, 1863-1995*, 1997.
[111] H. M. Dietl, E. Franck, L. Markus, *Overinvestment in team sports leagues: a contest theory model*, Scottish Journal of Political Economy, 2008, pp. 353-368.

perform worse after going public[112], while others conclude that there is a statistically significant positive relationship between pre- and post-IPO average point won per game played. In particular, the latter show that European listed Football clubs increased their average points per game by 0.078, that for an average season of thirty-eight games, implies 2.964 additional point on the final standings, although the correlation coefficient is quite small, thus suggesting a marginal practical magnitude of an IPO impact over listed clubs' sporting performance[113].

Lastly, financial disincentives refer to IPO's negative impact on sports team's financial performance, spotted by analyzing pre- and post-IPO financial statements and financial metrics, such as total and current assets, total and current liabilities, revenues and net income. Key ratios to understand IPO's impact on a listed club's financial performance are debt ratio, current ratio, player registration rights/assets, player registration rights/revenue, return on assets and net margin. Existing literature suggests that IPOs in the Sports Industries are linked with three main effects. First of all, proceeds raised through the IPO are generally used for balance sheet consolidation and not for players acquisition, primarily regarding debt reduction as money raised are likely to be used for deleveraging purposes[114]. Second, stock prices of listed sports team are strictly linked to their sporting performance[115], providing investors with opportunities of realizing capital gains, but at a high cost given high volatility, still benefiting from diversification opportunities thanks to a very low correlation with the market[116]. Last but not least, a stock market listing seems to have had no, if not detrimental, impact on the sports team's profitability, which is further in line with the prediction that the raised capital was used mainly for balance sheet consolidation. Lastly, the proceeds not having had much material impact on talent acquisition could perhaps explain why the coefficient for the average points won per game variable was marginal; an unchanged level of players would correspond with an unchanged performance result[117]. Thus, financially wise, the only beneficial effects of IPOs seem to be deleveraging, although having no significant impact on other key financial ratios.

Considering the above, private sports organizations owners do not find listing their clubs an attractive capital raising option over debt financing. Strong managerial disincentives,

---

112 D. G. Baur, C. McKeating, *Do Football Clubs Benefit From Initial Public Offerings?*, International Journal of Sport Finance, 2011, pp. 40-59.
113 C. K. Oh, *Why Are Sports Team IPOs Uncommon?,* Joseph Wharton Scholars, 2019, pp. 8-23.
114 *Idem.*
115 D. G. Baur, C. McKeating, *Do Football Clubs Benefit From Initial Public Offerings?*, International Journal of Sport Finance, 2011, pp. 40-59.
116 J. Hubman, *A Financial Analysis of Publicly Traded Professional Sports Teams*, The College at Brockport: State University of New York, 2011
117 C. K. Oh, *Why Are Sports Team IPOs Uncommon?,* Joseph Wharton Scholars, 2019, p. 25.

coupled with the lack of evidence of operational and financial benefits, drive IPOs attractiveness down from the clubs' owners' point of view.

3.3.3 Other Financing Options in the Sports Industry: Government Funding and Gifts.

We have seen that sports organizations mostly rely on debt markets to meet their financing need, rather than being exposed to public equity markets. In addition to these two "traditional" financing options, the Sports Industry benefits from other two additional capital raising solution: government funding and gifts.

In the Sports Industry, professional and amateur sports teams can rely upon receiving financing from governmental sources, justified by the high social impact coming from sports initiatives. In the US, for example, this is a common practice for high schools and universities too, receiving public funds in order to promote and support sport programs for students. In particular, for all sport organizations, government financing may be provided by federal, state, or municipal sources and may include land use, tax abatements, direct stadium financing, state and municipal appropriations, and infrastructure improvements[118]. Table 3.2 reports example from the US of direct stadium financing from government sources.

Stadium	Issuer	Security
AT&T Stadium	City of Arlington, Texas	Sales tax, hotel tax, rental car tax
Camden Yards	Maryland Sports Authority	State appropriation
US Cellular Field	Illinois Sports Authority	Hotel tax, state appropriation
Great American Ballpark	Hamilton County, Ohio	Sales tax
Marlins Park	Miami Dade Country	Hotel tax, tourism tax

Table 3.2 – US examples of publicly funded sports facilities[119].

On the other hand, sports organizations can rely also on gifts financing. Gifts financing corresponds to charitable donations, either cash or in-kind, destined to an organization. Major collegiate sports programs, as well as non-profit sports organizations, deeply rely on gift financing, representing their main source of operating and investing income. For what concerns

118 M. T. Brown, D. A. Rascher, M. S. Nagel, C. D. McEvoy, *Financial Management in the Sport Industry,* 2016, p. 30.
119 UBS Wealth Management Research, 2012.

the US case, research shows that in 2014 colleges received $1.26 billion in athletic department donations[120].

3.4 Capital Budgeting and Investments Decisions in Sports Organizations.

Every business must face limited financial resources, thus making it necessary to decide where to invest in order to reach specific goals. Capital budgeting, in particular, is the process through which sports organizations assess, evaluate and select investment opportunities that are consistent with their values, vision, mission and overall corporate strategy. As already mentioned, the Sports Industry has become more and more dependent on revenue streams coming from non-core activities, such as real estate investments, media and entertainment. Hence, when analyzing the financial returns of a sports team, in addition to core investments in players' transfers, these other non-core investments must be analyzed too. The sporting activity of any sports team is usually at the center of a conglomerate, but parallel activities developed around the sporting activity itself could actually account for most of the revenues.

In order to choose among different investment opportunities, a proper analysis must be carried out to extract some key metrics that can be used to carry out a comparison between them. For example, investments can be compared by referring to their expected rate of return and risk profile. Moreover, a correlation analysis can be performed to assess how the new investment performance would be affected by the already existing investments, and vice versa. In fact, the value of investments relative to marginal profits can vary a lot depending on what a team has already invested in. So, like any other company, sports companies and their managers have to properly assess expected profits and the level of risk assumed when making any investment decision and long-term commitments. The rate of return on an asset investment is one of the most used metrics to choose among different investment options. The rate of return across a given year can be calculated using the following formula, where r_t is the rate of return, C_t is the sum of any cash flow generated by the asset during the period t, V_t is the asset value in period t, and V_{t-1} is the value of the asset in the previous period:

$$r_t = \frac{C_t + V_t - V_{t-1}}{V_{t-1}}$$

[120] B. Wolverton, S. Kambhampati, *Colleges raised a record $1.26 billion for sports in 2014*, The Chronicle of Higher Education, January 30th 2015.

In the context of the Sports Industry where, for example, the investment asset could be either a facility or a player, the rate of return coincides with any profits generated by that asset and received by the owner, plus any increase in the asset value, all divided by the asset initial value. Many variables can affect the expected rate of return, so an in-depth analysis is required. For example, if the league where the team plays is going to sign a big media contract, then it would be expected that profits for the team will increase too; if the economy is forecasted to undergo a recession, then future profit will most likely not be as flourishing as in the previous case. In order to incorporate all these factors impacting the rate of return on a given asset, the expected rate of return can be used: one way to assess it is based on averages of past results, using the following formula where r_E is the expected rate of return, r_j is the return in year j, across a time period of n years:

$$r_E = \frac{\sum_{j=1}^{n} r_j}{n}$$

The expected rate of return taken as it is, is not the best estimates of future returns, but financial analysts having a deep understanding of the company's financial statements usually offer projections integrated with further information used to structure different scenarios, to then get a range of possible outcomes. In fact, for example, in the Sports Industry we can take the example of a F1 team winning a championship: it is not given for granted that the same team will win the championship the year after too, hence the following year's rate of return will be most likely lower. But financial analysts can overcome these limits by means of more sophisticated tools.

3.4.1 Risk, diversification and correlation.

Once the expected return over a future time period has been estimated, next step is integrating this metrics with some risk indicators. Usually, risk related to the expected return is linked to the variability of future performance (hence, the variability of the return itself). Then, if the expected return is based on almost certain factors, then there is little risk associated with that. On the other hand, if the expected return is linked to some very unpredictable factors, then there will be a higher level of risk linked to that return.

When coming to the Sports Industry, there is not a straight definition of risk, so it is not very clear what constitutes a risky investment. Maybe a team in a new startup league would be considered risky; one can imagine situations where future returns on sports teams were somewhat easy to calculate and situations where future returns were difficult to project. Risk can come from a variety of sources. Because the biggest investments for sports teams are players and the facilities used, that is where assessments must be initially made. Probably the most common type of risk for sports teams is the risk of player performance. Often player or team performance is highly variable across time. Furthermore, team revenue changes drastically depending on how players perform. There is also some risk associated with the team's facility. If a facility is not popular or does not work in terms of enhancing the fan experience, money is lost[121]. Apart from risk sources peculiar to the Sports Industry, a team also faces other sources of risk shared in common with other industries, such as the market risk. Market risk is a broad term, involving social and political events that can impact the demand side of the economy, thus impacting the companies' financials.

Although there could be better sources of information, and to keep consistent with the calculation of the expected returns, the past information included in previous returns can be a way to estimate the investment risk. One measure of risk is the standard deviation, assessed by the following formula:

$$\sigma_r = \sqrt{\frac{\sum_{j=1}^{n}(r_j - r_E)^2}{n-1}}$$

The standard deviation represents a measure of dispersion, hence risk: on average, expected returns will be one standard deviation far from the average return. Usually, given investors' risk aversion, between two investments with the same expected return but one having a lower standard deviation, then the latter is preferred. Here the choice seems to be quite straightforward, but then a more challenging case would be the one where one investment opportunity has a higher expected return coupled with a higher standard deviation. So, given the tradeoff between risk and returns, a financial analyst needs a metric to compare different investment opportunities offering different level of returns and risks: one way to do so is by using the coefficient of variation. The coefficient of variation corresponds to the standard deviation divided by the average return: because a good investment has both low risk and high reward, the lower the coefficient the better it is.

[121] J. A. Winfree, M. S. Rosentraub, *Sports Finance and Management. Real Estate, Entertainment and the Remaking of the Business*, 2012, p. 380.

Other important aspects to be considered when analyzing investment opportunities are diversification and correlation effects. Diversified investments, i.e., unrelated, are usually preferred because a well-diversified portfolio has a lower level of risk as compared to one having correlated assets, because unrelated investments are subject to different factors and event impacting their performance. In the Sports Industry, for example, a diversified portfolio can be represented by an investor owning both a baseball team and a F1 team. But the full story is not as straightforward as this: even in the case of baseball and F1, there can be variables affecting both the sports in the same way, for example the national economy. In this case, one strategy to better diversify investments could be by investing internationally: this, for example, was the case of James Pallotta, who controlled both the Boston Celtics (NBA) and AS Roma (Italian Football league Serie A). On the other hand, having correlated investments is not always a synonymous of financial mismanagement. In fact, correlated investments can be managed to decrease the overall level of portfolio risk: having holdings composed by two risky investments that are negatively correlated can be a way to do so. For example, investing in teams in the same region could be a way to decrease risk by means of inversely correlated assets: for example, suppose that a fixed number of fans will attend Football matches in Milan, so they either go to AC Milan or FC Inter games (without considering all the minor leagues teams); in this case, there will be some uncertainty about which team to own to maximize ticketing revenues, but if the teams are jointly owned, then all the risk is canceled out. Hence, good investors should at first decide their risk tolerance level, and then opt for investment strategies accounting for both diversification and correlation effects.

3.4.2 Real Estate Investments: Ranking Investment Options through NPV and IRR.

When investing in facilities, sports managers have to carefully assess the financial feasibility of different options, and this is usually done by using two different metrics: the Net Present Value (NPV) and the Internal Rate of Return (IRR). In doing this, they have to account for any cash inflow and outflow linked to the investment, as well as for any opportunity cost and alternative to the assessed investment, i.e., what would happen if the new facility were not built.

The starting point to assess the NPV of an investment is identifying the cashflow linked to it. Then, identified cash inflows must be discounted at a proper discount rate in order to find their present value, net of any discounted cash inflow:

$$NPV = CF_0 + \sum_{t=1}^{n} \frac{CF_t}{(1+r)^t}$$

The main issue of assessing an investment NPV is finding the right discount rate, as in doing this the amount of risk involved in the discounted cashflows should also be accounted for (i.e., cashflows uncertainty). One way to assess the right discount rate is by using the Capital Asset Pricing Model (CAPM), whose theory is behind the scope of this study. A further challenge that analysts encounter when assessing an investment NPV is forecasting future cashflows, as for example the number of additional fans a new facility will attract is not easy to forecast, given that many variables can affect this outcome.

To rank different investment options, an alternative to the NPV is the IRR. The Internal Rate of Return is the discount rate that gives the investment a NPV equal to zero, and the rule suggests opting for those investment opportunities whose IRR is higher than the cost of capital, so that through the investment value is created.

3.4.3 Investing in Players' Transfers.

Sports organizations core business take place in stadiums, arenas and circuits, so the most important investments for teams are their players and athletes. As previously analyzed (see 2.3.3.1), player salaries are the main component of the cost side on a sports organization P&L, and players' value on the balance sheet are high as well. While for most people outside of the business there is no reason to pay such high salaries to players, there are economic principles backing player contracts: their wages are strictly dependent on how much value they bring to the team.

To assess investments in players the rationale of expected returns and risk still applies, but there are some other basic financial concepts that can help in choosing which player to invest in.

3.4.3.1 How to assess an athlete's value.

The concept of Marginal Revenue Product (MRP) is at the basis of estimating an athlete's value. To understand what the MRP represents, two more basic concepts must be introduced: the marginal product and marginal revenue. The marginal product is the additional units of output a worker produces, while marginal revenue corresponds to the revenue generated by one additional unit of output[122].

Starting from the marginal product, players and teams' objective is to win games (or races, in the case of Motorsports). Therefore, the marginal product of an athlete corresponds to the number of additional wins he contributed to. In collective sports where a player performance is strictly linked to other players, and given the high uncertainty surrounding the sporting performance of athletes and teams, it is very challenging to assess marginal products. Thinking about Football, if AC Milan wins thirty games per season, but would have won only twenty without Zlatan Ibrahimović, then his marginal product is ten wins.

On the other hand, the marginal revenue is linked to the economic contribution arising from one additional unit of output, that in the case of sports organizations is a win. When assessing marginal revenues, not only ticketing sales, but any revenue stream (media, licensing, merchandising, etc…) must be included in the analysis. For example, continuing with the example above, if AC Milan earns €4 million for any win, then Zlatan Ibrahimović marginal revenue product would be €40 million.

Sports legends might also bring in more value than their simple marginal product. For example, the Italian Football player Francesco Totti who played with As Roma (Italian Serie A), brought many fans to the stadium during the final phase of his career, when his sporting contribution to the team was limited as compared to before.

3.4.3.2 Player Contracts and Incentive Schemes.

Player contracts take different characteristics depending on the sports, but some basic and common aspects are shared among them. What is critical when evaluating contracts is their present value, keeping in mind that usually contracts signed between athletes and clubs are multiyear. Thus, to find a contract's present value, future payments have to be discounted at a

[122] G. W. Scully, *Pay and performance in Major League Baseball,* American Economic Review, 1974, pp. 915–930.

proper discount rate. The following formula, where N is the number of years corresponding to the contract duration, can be used at this purpose:

$$Contract_{PV} = \sum_{t=1}^{N} \frac{Salary}{(1+r)^t}$$

In assessing the contract value it is important to keep in mind the time value of money, as players and team owners have contrasting interest in structuring contracts: on the one hand, players prefer "front loading" their contracts, as it is more convenient to receive higher amounts in the initial years rather than in the future, given that this will increase the contract's present value; on the other hand, team owners usually try to "back load", meaning that they prefer paying players more at the end of their contracts to reduce their present value. Moreover, front loading and back loading can be part of a club's capital budgeting strategy. For example, in those leagues where there is a salary cap like NFL or NHL, teams might face constraints impeding them from paying players more than a given amount in certain years, and as a consequence contracts are adjusted in the years to meet salary cap requirements.

Another basis of contracts shared among different sports and geographies are incentives clauses. This is not something characteristic to the Sports Industry only, but is a general tool used to solve the principal-agent problem, i.e., principals and agents having different interests and incentives. To fix this conflict, workers (i.e., players) typically have clauses in their contracts to make their goal aligned to those of the company, like for example receiving a a percentage of the company profit. Anyway, the Sports Industry presents some additional challenges to solve this problem, due to the collegiate nature of sports. In fact, for example, if a Football player is paid based on how many goals he scores, then he will be more likely to be selfish when playing, then going against the team's interests. On the other hand, in those sports like Baseball where the performances are more individual, then it is easier to solve the principal-agent problem. In team sports the key to overcome this challenge is by providing players with incentive schemes that fully align with the teams' goals, that is, winning games: teams typically give provide bonuses based on fixed teams' goals, such as winning the championship or a certain number of matches.

Something that is strictly linked with incentives is the contract length, as long-term commitments bring in both advantages and disadvantages: on the one hand, long-term agreements provide stability to the player and team; on the other hand, teams run the risk that the performance of players will change as he/she ages. Moreover, some studies demonstrate that, on average, players usually perform better in the last year of their contract, in particular when they do not have signed yet an agreement for the next season, and future wages will strictly depend on current performance.

3.4.3.3 Correlation between Players: Increasing Value through Complementarity.

As any other investment, player can be seen either as complements or substitutes, thus the performance of players can be correlated. Of course, this is true in collective sports, where for example if one position player performs well, then it will be likely that other players will benefit from his performance, thus increasing their own performance too.

When making investment decisions about players, sports managers should think about how one particular player relates to others, just like with any other investment one should think how it relates to other investments in the portfolio. This is not an easy assessment to be performed as many factors can play a significant role in determining the final outcome but, for example, a player's past performances could be assessed also in relation to similar players he had played with. This is more an art than a science, but still it is a critical factor to be determined in order to make the right investment decisions in the framework of capital budgeting.

3.4.3.4 Option Value for Players: the Benefits of Flexibility.

In the traditional finance, an option is something that provide an investment with flexibility. There are two main types of options: call options, the option to buy an asset at a pre-specified price at a given date in the future; put options, the option to sell an asset at a pre-specified price at a given date in the future. Options do not force their possessors to either buy or sell the underlying asset, rather they provide them with the opportunity to sell or buy only if it becomes convenient doing so.

Many players have a type of option. In fact, nearly all players give teams some options. Because of the uncertain nature of sports, teams always like to have options. For example, suppose that a hockey team has an injury-prone starting goalie with a 30 percent chance of getting hurt during the season. Suppose that the same team has a defenseman who can play goalie if necessary. The uncertainty of the starting goalie's health can create an option value for the defenseman. Now, consider three possible outcomes. The first outcome is that the starting goalie remains healthy and gives up an average of one goal per game. The second outcome is that the starting goalie gets hurt and the defenseman must play goalie. With this outcome, the team gives up an average of two goals per game. That results from the loss of the starting goalie and the requirement to replace the defenseman. The third outcome is that the goalie gets hurt and nobody else on the team can play goalie very well. If the team is not able to find a reasonable replacement, this will hurt the team drastically and they will give up three goals per game. Table 3.3 shows the possible outcomes If the hockey team can use the defenseman as the backup goalie, then on average the team will yield 1.3 goals per game. If they have no reasonable replacement for goalie, they will yield 1.6 goals per game[123]. Therefore, the option value of a defenseman's ability to play goalie is the difference of the two averages or 0.3 goals per game. If this is the case, it should be part of a player's marginal product. If we assume that the defenseman is worth 0.5 goals per game when he is playing as a defenseman, then his total benefit also should include the 0.3 goal option value, for a total value of 0.8 goals. That value is worth a certain number of wins. If 0.8 goals produce 10 additional wins across the season, then the player's marginal product is 10 games. Certain "utility" players often are valuable just in case they are needed. Having options is always a benefit; if a team is hiring a player, it is helpful to be able to quantify these options[124].

Goals Given Up per Game		Backup Goalie	
		Defenseman	None
Goalie's health	No injury (70% chance)	1	1
	Injury (30% chance)	2	3
Expected value of goals yielded per game		1.3	1.6

Table 3.3 – Option value of a player[125]

[123] With the defenseman replacement, the expected value is equal to 0.7(1) + 0.3(2) = 1.3. Without the defenseman, the expected value is equal to 0.7(1) + 0.3(3) = 1.6.
[124] J. A. Winfree, M. S. Rosentraub, *Sports Finance and Management. Real Estate, Entertainment and the Remaking of the Business*, 2012, pp. 394-395.
[125] Table from J. A. Winfree, M. S. Rosentraub, *Sports Finance and Management. Real Estate, Entertainment and the Remaking of the Business*, 2012.

3.4.3.5 Players' Sporting Performance: Why Clubs Enjoy Taking Risk?

When choosing among different investment options, risk is one of the drivers. In the traditional finance, due to the risk-aversion nature of the average investors, they are usually not willing to buy a high-risk investment, thus lowering its price. If there are two investment options providing the same expected return but one having a higher risk profile, then the latter has to be cheaper in order to attract investors.

Conversely, some studies suggest that sports team, given the same expected return among investment options, often prefer to sign riskier players. Examples of risky players can be the ones who are injury prone, or whose performance varies a lot. So, if two players have the same expected on-the-pitch performance but different degrees of variance, then teams would seek to sign the one whose performance has shown higher variance[126]. A possible explanation of why sports team usually prefer signing risky players is that if their performance is poor, then they can bench them[127].

There is another possible explanation for teams hiring risky players. It is possible that sports teams face a unique revenue structure. Typically, when a firm produces more goods, the additional revenue from producing the goods decreases, and there are diminishing marginal returns. If teams are producing wins, then this might not be the case. A traditional business would rather produce a certain amount of goods every year than produce a high amount one year and a small amount the next year. Again, sports teams might be different. Let's think of these alternatives for sports teams. Would a team rather have a medium record every year, or finish in last place half of the time and win a championship half of the time. Given how fans respond to team quality, their revenues might be higher if their win/loss record varied from year to year. Obviously, teams want to win every year, but given their constraints, they might be better with a 50% chance of winning and a 50% chance of losing, than a 100% chance of winning just half their games. To say it another way, there is a big difference between a first-place team and an average team compared to the difference between an average team and a bad team[128]. If that is true, a direct consequence would be sports team having an increasing marginal revenue curve. While economists typically do not support the idea of an increasing marginal revenue curve, there are reasons to think why this could be the case. Supposing teams have an

---

[126] C. Bollinger, J. Hotchkiss, *The upside potential of hiring risky workers: evidence from the baseball industry*, Journal of Labor Economics, 2003, pp. 923–944.
[127] E. P. Lazear, *Hiring risky workers*, in Internal Labour Market, Incentives, and Employment, 1998.
[128] J. A. Winfree, M. S. Rosentraub, *Sports Finance and Management. Real Estate, Entertainment and the Remaking of the Business*, 2012, pp. 395-396.

increasing marginal revenue curve, this might be the reason why they prefer hiring risky players, and this might hold even stronger for small-market teams: by taking chances on players who might or might not pan out, small-market teams with small payrolls can increase the likelihood of winning[129].

3.5 Emerging Revenue Sources: Four Ways to boost a Sports Organization's P&L.

Professional sports league, together with participating teams, are constantly looking for emerging revenue sources to address specific financial needs. We have so far seen how in the past years the importance of real estate and facility investments has grown: most of the sports facilities built in the early 20th century have been replaced, at first by larger sports venue designed to offer large seating capacities, then by smaller facilities offering their attendees a full set of amenities. Throughout this process involving real estate developments, the focus has been on revenue maximization for team and stadium owners. Among the others, recent trends suggest that team owners can leverage on four emerging revenue sources: ticket reselling, luxury seating, seat licenses and variable ticket pricing.

Evidence suggests that seasons ticket and one-game tickets are increasingly being sold on secondary markets. The perception of ticket reselling has changed a lot in recent years: from being an unfair practice, it has evolved into a structured and regulated business, with lots of teams and leagues having already recognized its importance, most of them trying to be involved in. For example, in 2007 StubHub signed a contract to be MLB's exclusive secondary ticket reseller[130].

Regarding revenue streams linked to facilities, the objective of stadium owners has always been to maximize the sales of season tickets: they provide upfront revenues, facilitate game management as the number of attendants is quite steady, and are an indirect source of financing, as fans usually pay for season tickets before the sports season starts. Luxury tickets share all these benefits with season tickets; thus, they have become an important revenue driver for teams. In addition to "traditional" luxury suites and club seats, some facilities are offering luxury suites that do not have a direct view of the field of play. These luxury suites are part of a growing trend to attract higher-end customers, who can afford to pay for exclusive access to certain areas of the facility. Whereas most teams 25 years ago worried primarily about the total

[129] R. Fort, J. Winfree, *Sports really are different: The contest success function and the supply of talent*, Review of Industrial Organization, 2009, pp. 69–80.
[130] A. Branch, *StubHub! and MLB strike precedent-setting secondary ticketing deal*, TicketNews, August 2nd 2007.

number of attendees, now many teams pay significant attention to attracting a small number of affluent customers, whether they are individuals or businesses[131].

Another recent trend linked to stadium attendance and to the move towards high-priced seating is the use of personal seat license: it is the right, bought after paying a one-time fee, to purchase tickets for a specific seat, either for a limited or permanent time frame. Like season tickets, they can provide teams with huge upfront cash inflows.

For many years, teams set ticket prices without carrying out thorough market research to find optimal prices maximizing revenues, doing no to little adjustments from one season to the other based on team's performance. As research and technology in sports have improved, more franchises are employing variable ticket pricing (VTP) to capture added revenues by increasing initial ticket prices for highly demanded games and decreasing ticket prices for lower-demanded games, in an effort to attract customers who would not attend at the "typical" price. VTP has proved profitable for many sport franchises, who are now replacing it in some cases with dynamic ticket pricing, in which the ticket price is altered instantly (like a stock on a stock exchange) as demand increases or decreases. The complexity and prevalence of dynamic pricing are likely to increase as teams continue to study their ticket prices and as more advanced software becomes available[132].

[131] M. T. Brown, D. A. Rascher, M. S. Nagel, C. D. McEvoy, *Financial Management in the Sport Industry*, 2016, p. 519.
[132] *Idem*, p. 520.

CHAPTER FOUR – PRIVATE EQUITY & THE SPORTS INDUSTRY. THE FORMULA 1 CASE.

4.1 Introduction

The huge amount of funds gathered by PE funds in recent years has been looking for alternative asset classes that are able to generate potentially high returns. Among the different options, the Sports Industry is being more and more successful in attracting PE investments. Investors have looked at sports organization for years, but in many cases league bylaws prevented their investments, especially in the US. As previously analyzed (see 3.2), regulatory frameworks have recently changed allowing for PE investment in sports organizations. Sports is an appealing landscape for investors as owners of sports franchises have benefitted from huge returns in the past years. For example, NBA, MLB and NFL in the US have all seen their valuations skyrocketed, outpacing the S&P 500 over the past 20+ years.

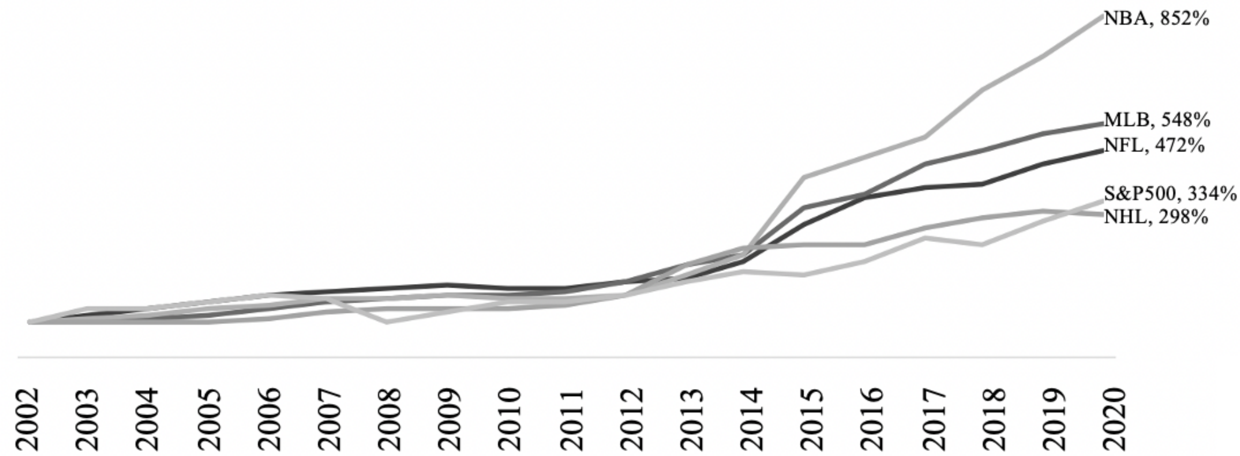

Figure 4.1 – NBA, MLB, NFL and NHL total returns vs S&P 500[133].

Among PE interests in the Sport Industry, minority investments seem to be one of the most active trends, as there are many cases of PE firms partnering with owners and leagues. In the US, this was not possible until 2019, when regulations changed in the MLB, MLS and NBA, allowing minority investments from PE investors, and providing clubs and leagues with the opportunity to raise new capital to finance growth opportunities or to liquidate other investors. In fact, one of the main benefits of PE entering the Sports Industry is that by doing so, the

[133] Data from Sportico.

liquidity of the industry is increasing, also allowing owners of multi-billion franchises to liquidate their investments, something that was not easily feasible years ago.

4.2 Investment Thesis & Main Risks behind PE Investments in the Sports Industry.

PE investors are attracted by investment opportunities within the Sports Industry for several reasons. First and foremost, what makes sports organizations financially attractive is their ability to lock-in huge media rights revenues. In fact, Sports is one of the biggest content-creator machines, especially when it comes to live events, and with the entertainment industry shifting from traditional broadcast to on-demand and streaming services, this gives Sports a competitive advantage over other emerging industries.

In general, the return prospects are compelling, with minority stakes investors targeting 15% to 20% gross annual returns. However, owners expect much of this to be derived from capital appreciation rather than income. Most owners (majority or minority) buy in at low-single-digit cash flow yields and see double-digit appreciation. Additionally, returns may vary significantly depending on the time horizon, deal structuring, discounts captured, and more. Despite an overlap with the technology, media, and telecom (TMT) sector, sports investments have a much different return profile. These minority investments have a return profile more akin to value-add in real estate: long-term media rights with built-in escalations are similar to long- term leases; certain new projects, from online sports betting to NFTs, act like options and could substantially add to the overall total return. Among all, the investment thesis is supported by five key drivers[134]:

- *Portfolio diversification*: as previously mentioned (see chapter 3), sports team are usually not correlated with other assets. The uncorrelation is mainly driven by two key revenue sources: locked in long-term media rights and seasonal tickets sales, hedging sports organizations against downturns during recessionary periods. Anyway, some sort of cyclicality is still present, as when the economy shifts towards recession periods, people's spending capacity decreases, and as a consequence fans are less willing to spend their money to buy stadium tickets, thus decreasing ticketing revenues. Anyway, from a risk management point of view, sports teams usually help in lowering a portfolio overall risk, as they are usually exposed to different sources of risk as compared to "traditional" portfolio

[134] *PitchBook Analyst Note: Sports Teams and Private Equity Pair Up*, PitchBook Data, May 13th 2021, p. 5.

assets, such as the risk of a player lockout. Thus, the uncorrelation from a risk point of view helps in decreasing the overall level of risk of a portfolio.

- *Discounts*: as we said, PE investors usually buy minority stakes in sports teams, and when investors go for minority investments, they usually do it only if heavy discounts apply. In fact, a minority investment means the lack of control over the club, and this must be discounted in the final price. On top of that, the significant illiquidity of the Sports Industry often leads to additional discounts. Hence, PE investors usually benefit from two sources of discount: minority discounts and illiquidity discount, estimated to account for in the range of 20% to 30% of the market value[135]. Buying minority stakes at a discount not only limits the initial cash outflow for investors but comes with other benefits too: buying at a lower price will boost cash-on-cash returns and lift the upside potential of the investment.
- *Scarcity*: the limited number of sports teams make them scarce, thus more attractive from an investor point of view. In fact, only 151 teams take part either in the NFL, NBA, MLB, MLS and NHL, while only 98 teams participate in the top-five European Football leagues (English Premier League, Italian Serie A, German Bundesliga, French Ligue 1, and Spanish La Liga). In addition to the restricted number of sports team, also their highly infrequent trading nature (sports team can easily go for decades without changing ownership) makes the buyer bid higher prices to acquire them. Moreover, as we already discussed (see 2.3.2), the Sports Industry is a "safe" one when it comes to the potential threat of new entrants, as strict rules on new club's acceptance means that current teams' owners do not have to worry about the possibility of new entrants increasing teams supply, and thus reducing their prices. If supply increases, the owners of the incumbent clubs in the league often receive rewards in the form of huge expansion fees.
- *Media rights*: sports leagues can negotiate huge media rights agreements leveraging on the sports content creator capacity and riding the wave of on-demand streaming. A series of streaming platforms are trying to enter the industry and they are willing to bid higher prices to secure media rights against traditional TV broadcasting companies. For example, Amazon recently won the bid to secure exclusive rights to stream the Thursday Night Football event (NFL) up until 2033 for $1 billion/season, being the first time a streaming platform winning an exclusive package[136]. Overall, streamers and broadcasters invest 26%

[135] *Idem*, p. 6.
[136] A. Sherman, J. Young, *NFL Finalizes New 11-year Media Rights Deal, Amazon Gets Exclusive Thursday Night Rights*, NBC Sports, March 18th 2021.

of their resources into sports contents[137], and the sports rights market is expected to jump from $48.6 billion in 2019 to $85 billion by 2024.

- *Sports betting*: the rise of sports betting in the US market represents a huge opportunity for sports organizations for two reasons. First, sports leagues and teams can monetize this opportunity by collecting data and reselling it to sports betters: not only the value of data will rise as sports betting becomes popular, but also thanks to technological developments making the data collection process more accurate. Second, sports betting may boost team valuations as it gets more and more people and betters more interested in watching games; this can especially help in attracting younger generations, as gambling gamifies sports making it more attractive for younger communities used to play video games.
- *NFTs*: Nonfungible tokens (NFTs) represent one of the most recent trends born from new developments in the blockchain industry and present league and clubs with the opportunity to monetize further revenue sources, from virtual playing cards to ownership of images, videos and other digital contents. Overall, the NFT market amounted to $338 million in 2020[138], with experts predicting a huge expansion in the coming years. For what concerns the Sports Industry, NBA already entered the NFTs market under Top Shot selling officially licensed digital collectibles with more than 800,000 registered users and around $500 million revenues in around half a year[139]. As it could happen with the sports betting market, the increasing interest of young generations for NFTs may drive them towards sports contents, thus increasing the overall sports "consumers".

Although sports assets can help in managing risk across investment portfolios, PE funds investing in sports organizations are exposed to a series of risks, among the others: lower leagues relegation, leagues shutdowns, and generational changes. For what concerns European Football, being relegated to a lower league can be a serious threat for the team's brand image, and that is why PE funds often try to invest in leagues media right companies instead of directly investing into teams, but when they do so they usually target top clubs in each league. A notable source of risk is also the possibility of leagues shutdowns: as we already observed, the restrictions imposed by governments to limit the effects of the pandemic posed a serious threat for sports organizations. Lastly, for what concerns generational changes, many of the younger

---

[137] S. Roxborough, *Sports Rights Now Make Up 26 Percent of Global Content Spend*, Hollywood Reporter, October 16th 2019.
[138] *NFT Yearly Report 2020*, NonFungible, February 16th 2021.
[139] M. Long, *NBA Top Shot Maker Dapper Labs Secures US$305m in Fresh Capital*, Sports Pro Media, March 31st 2021.

generations under twenty-five prefer watching eSports rather than traditional ones[140], and for this reason PE funds investing in sports organizations must be able to drive their corporate strategies to seize this huge opportunity.

4.3 Different Investment Opportunities: NBA, NFL, MLB, MLS, NHL, European Football and Motorsports.

Private Equity investors willing to invest money in the Sports Industry can chose among different investment options, ranging from franchises in the NBA, NFL, MLB, MLS and NHL, if they seek opportunities in the US, to European Football teams, most likely the ones taking part in the top-five leagues, if they look for investment opportunities in Europe. On top of that, PE investors can also decide to buy stakes in Motorsports franchises. In this paragraph we are going to briefly analyze the different peculiarities of the abovementioned leagues from a PE fund point of view, starting from the US case and then continuing with European Football.

Starting from investment options in the US, the NBA represents a sizeable opportunity for PE investors. First, it has the most attractive demographics as compared to other leagues, with fans being mostly international and, according to some research, under the age of forty-five[141]. NBA also has a very effective strategy to attract younger fans, doing so through its 2k video game franchise, being one of the most streamed game on Twitch. Moreover, NBA teams can count on their social media reach to attract new fans and retain old ones, also thanks to the league's stars, in many cases being real influencers. Lastly, NBA teams can also count on sizeable media rights deals, with the last negotiating contract expected to go from a $24 billion deal to a $75 billion one[142]. Huge media deals are one of the key drivers of the PE investors' attention for franchises in the NBA. The combination of these factors makes NBA franchises a desirable asset for PE investors. As a consequence, all these benefits come with a price being incorporated in higher trading multiples: the median NBA franchise is worth around 7.4x its revenues (see figure 4.2), compared with 6.1x and 5.7x for median NFL and MLB teams, respectively[143].

NFL has been the leading sports league in the US when it came to monetization strategies through media and IP, leveraging on fan passion on way no other league was able to replicate. The salary cap imposed to the franchise and the draft structure of the league kept NFL

[140] *The State of Online Video 2017*, Limelight Networks.
[141] J. Lombardo, D. Broughton, *Going Gray: Sports TV Viewers Skew Older*, *Sports Business Journal*, June 5th 2021.
[142] J. Young, *NBA is Next Up for a Big Rights Increase, and $75 Billion is the Price*, CNBC, March 22, 2021.
[143] Data from PitchBook analysis.

competitive, making it an enjoyable league for fans. All these factors lead average NFL team value at around $3 billion, despite being the US league with fewest games in the season[144]. Still today NFL is a cash generating machine, especially when it comes to media rights: the league signed a new deal that will run starting from 2023 season and will cover eleven seasons, expected to lock-in $113 billion revenues[145]. The league can count on the largest audience in North America, and the $10.3 billion per season under the new deal is a huge improvement from the $5.9 billion per season under the current media contract. Anyway, investors looking for opportunities in the NFL should consider some risks too. First, the league streaming capabilities are limited if compared to other leagues such as the NBA; however, this area can represent a growth opportunity if the needed measures will be undertaken. Second, very high team valuation suggests no or little room for further appreciation, then often leading investors to look for opportunities in quickly growing, cheaper leagues.

Continuing with the analysis of the US case, the MLB represents one of the most popular sports leagues, still lacking an appropriate level of competition making evident the difference between top teams and smaller ones. Anyway, this gap can represent an appealing investment opportunity for PE firms looking for smaller, maybe undervalued teams. Differently from NBA and NFL, growth across the league does not look vivid: the age of the fan base seems to be one of the main areas of concern, with the average fan being aged 57 years[146] and the league loosing 6.3 million fans in the last eight years[147]. Despite these concerns, MLB is still set to receive attention from broadcasters: the league recently signed a new deal with Fox and Turner, bringing in +50% revenues as compared with the current contract, starting from 2022[148]. Contrary to the NFL, MLB stands out when it comes to technology (especially through BAMTech investment) making the league known across the globe for example through streaming services. Moreover, the league is at the forefront of tracking data and statistics, giving it a competitive advantage to ride the rising wave of the betting market. When it comes to risks, the main area of concerns seems to be the lack of a salary cap as it happens for other leagues, with top-three teams spending being way far more than other teams, meaning that only a handful

[144] P. J. Schwartz, R. Williams, *2020 NFL Valuations: National Football League Interactive Franchise Valuations*, Sportico, August 25th 2020.
[145] O. Poindexter, *NFL Locks in $113 Billion for 11-Season Media Right Deals*, Front Office Sports, , March 18th 2021.
[146] J. Lombardo, D. Broughton, *Going Gray: Sports TV Viewers Skew Older*, Sports Business Journal, June 5th 2021.
[147] D. Johnson, *Overall Health for Professional Baseball in Trouble*, Wtop News, June 10th 2020.
[148] *Turner Sports Expands Rights Deal with MLB Through 2028*, USA Today, September 24th 2020.

of clubs compete for the title every year, decreasing the competition across the league, thus its appeal towards fans (and, as a consequence, towards investors too).

While it is true that Soccer is the most popular sport in the world, engaging every generation from children to older people, when it comes to the US and Canada its viewership lags many other leagues. If on the one hand this could be an area of concern, on the other it could represent an opportunity not yet exploited, and as a consequence many investors see vast growth potential for the MLS and competing teams. As it usually happens, this growth opportunity is reflected into teams' valuation, which for an average MLS team comes at nearly 10x its revenues (see figure 4.2), by far the highest compared to major leagues in the US. The first and most important growth catalyst is represented by the next media rights deal starting from the 2023 season, according to many bringing in tons of cash into the teams' pockets. A direct consequence of this expected media rights deal could be lifting the salary cap, in this way attracting more and more top players to meet fans' expectations. Moreover, another driver suggests an opportunity to grow MLS teams: compared to the 98 Football teams from the top five European leagues, there are far fewer MLS teams per person in the US and Canada, thus there are potentially more fans per MLS team to monetize. Lastly, investors interested in MLS teams do not have to worry about relegation risk, making investments prospects more appealing. Private Equity funds already finalized some investing in the MLS space: in 2012, Providence Equity Partners paid between $125 million and $150 million for a 25% stake in Soccer Marketing United, the marketing and media arm of the MLS; in 2017, MLS bought this stake back and reports suggest Providence made approximately 3x their capital on the purchase. With the robust growth opportunities in the space and relatively low club values, PE may be particularly interested in MLS franchises[149].

To conclude the analysis of the US investment opportunities in the Sports arena, Hockey has always been appealing for American fans. Thanks to its fan base, the NHL is appealing toward advertisers as well: Hockey fans are the highest income audience of any major sport in North America, and this may allow teams and the league itself to monetize a higher advertising spending per fan than other leagues[150]. On the other side, several impediments limit the growth potential of the league: the sport is more expensive to play than others, thus limiting the talent pool; moreover, geographical constraints make the talent pool limited too, as although there may be ice rinks in Florida, the majority of players in the NHL still come from Canada[151].

[149] *PitchBook Analyst Note: Sports Teams and Private Equity Pair Up*, PitchBook Data, May 13th 2021, p. 13.
[150] M. Egan, *Puck Crazy: Is the NHL Recession Proof?*, Fox Business, January 25th 2016.
[151] R. Szporer, *NHLers by Country: On Top of Their Game and the World*, The Hockey Writers, January 21st 2021.

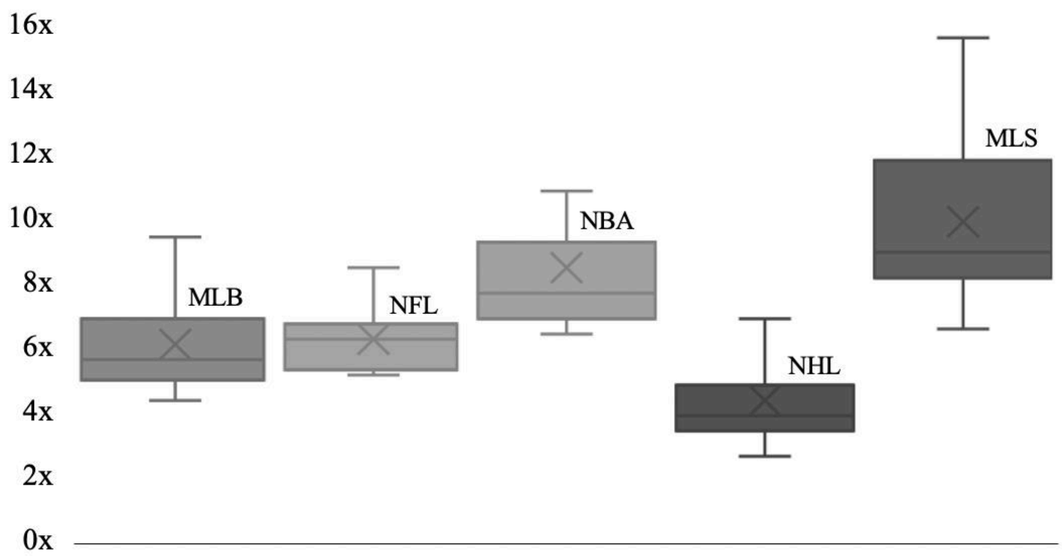

Figure 4.2 – Quartile ranges for valuation to revenue multiples in specific US leagues[152]

Passing from the US to the European case, in the old continent the most attractive investment opportunities come from the top-five European Football leagues, namely the English Premier League, the Italian Serie A, the German Bundesliga, the Spanish La Liga and the French Ligue One. The reason why owning one of the team belonging to these leagues is appealing from an investor point of view is clear: you can own a piece of the most popular teams globally. Of course, the appeal is also translated into numbers. For example, when it comes to sports media rights, Football viewership rights in total are expected to jump from \$12.8 billion to \$31.9 billion in the next five years[153]. Of this huge pie, the bigger slice will flow into the top five European Football league pockets. On the other side, differently from the MLS, PE firms investing into European Football leagues face the risk of relegation, negatively affecting the brand value of less skilled teams. This is way PE investors usually decide to invest in top teams, as they rarely are in danger of relegation. If on the one hand this practice represents a safe bet, on the other it may cap values for mid-tier teams.

Lastly, Private Equity investors can opt for opportunities coming from the Motorsports. Main championship, such as Formula 1, Moto GP or the newest Formula E gathered a lot of interest from private investors. In fact, they usually are able to lock in huge media rights deal for the long-term, allowing for revenues stabilization and high visibility. Moreover, they are

---

[152] Chart from *PitchBook Analyst Note: Sports Teams and Private Equity Pair Up*, PitchBook Data, May 13th 2021, p. 9.
[153] *Will 'OTT' Shake Up the Football Broadcasting Industry?*, KPMG Football Benchmark, April 15th 2020.

usually global championship developed in all continents, thus relying upon a global fan base with all the benefits that come along, as for example in terms of sponsorship. As we will later analyze (see 4.4), one of the most successful PE investment in the Sports Industry has actually taken place within Motorsports: CVC's acquisition of Formula 1 in 2006 and the subsequent sale, ten years later in 2016, to Liberty Media Group. Moreover, in the last chapter we are going to deep dive into a brand-new Motorsports championship, E1 Series, to assess how their founders can attract the interests of Private Equity funds in the medium term to complete a successful exit.

In conclusion, we analyzed different investment opportunities available to Private Equity funds willing to invest in the Sports Industry. There is one common factor that any sports organization, league, team and championship must leverage on in order to increase their growth opportunities and to attract PE firms' interest: eSports. Much of the value in eSports has accrued to game developers and semi- related apps, such as Twitch and Discord. Teams are still far less valuable than in traditional sports leagues because they reap a slim share of profits. Additionally, investors in the space face the threat of new games disrupting viewership. While some sports, such as soccer, may take viewership share from football in the US over the next 20 years, the development cycle in gaming evolves much quicker. New games such as Fortnite can disrupt the ecosystem in a short timeframe, diminishing viewership in other leagues but also presenting an opportunity[154].

4.4 The Formula 1 Case Study: CVC and Liberty Media Group Deal.

When it comes to past Private Equity investments in the Sports Industry, most of the time it also comes to CVC, one of the biggest players in the PE industry and one of the most active in the field of Sports. Among the others, CVC completed a remarkable investment when it first bough (in 2006) and then sold (in 2016) a stake in the most famous Motorsport championship, Formula 1 (thereinafter also F1). In the following pages we will briefly dive deep into what F1 is and what are its main revenue drivers, then we will focus on the CVC sale to Liberty Media to understand the investment thesis behind this remarkable deal.

[154] *PitchBook Analyst Note: Sports Teams and Private Equity Pair Up*, PitchBook Data, May 13th 2021, p. 15.

4.4.1 How it Works: Who Does What in Formula 1.

Formula 1 is the highest category of single-seater open-wheel racing cars on a circuit defined by the International Automobile Federation (FIA). The championship was born in 1948 (replacing Formula A, which in turn arose only two years earlier, in 1946), then becoming world-class in the 1950 season. The term "Formula" refers to a set of rules to which all participants, cars and drivers, must adapt to; they introduce a number of restrictions and specifications in cars, in order to avoid excessive technical disparities between cars, to place limits on their development and to reduce the risk of accidents, and throughout the years the Formula has undergone many changes. The championship is structured around three main players: Formula 1, the teams and FIA.

Formula 1 is the exclusive commercial rights holder of the FIA Formula 1 World Championship, and it will be so until 2110. Being the rights holder, its responsibilities and main tasks involve:

- Identifying racing venues and negotiating fees from promoters to host, stage and promote the F1 event.
- Negotiating deals regarding broadcasting rights, as well as producing international TV feeds through state-of-the-art production facilities.
- Sourcing, negotiating and establishing relationships with sponsors and advertisers, as well as providing premium hospitality services.
- Handling logistics for participating teams, for example to move cars, equipment and personnel.

Besides Formula 1, racing teams represent the core of the championship and they are responsible for the design and racing of F1 cars. To do so, it was estimated that at the time of the Liberty Media acquisition (2015) an average team would have spent around $220 million annually[155]. The main funding sources for teams include payments from Formula 1, as well as sponsorships and advertising both on cars and team's uniform, technology licensing and contribution from shareholders, usually represented by a corporate parent.

Lastly, FIA (*Fédération Internationale de l'Automobile*) is the governing body that regulates a series of Motorsport championship, with F1 being the most important one. Since 1950, it administers and regulates all sporting and technical aspects related to the FIA Formula

[155] D. Rencken, *Revealed: How much F1 teams spend*, Autosport, November 26th 2015.

1 World Championship, such as how races are run, specification of engines, design of cars and tires types.

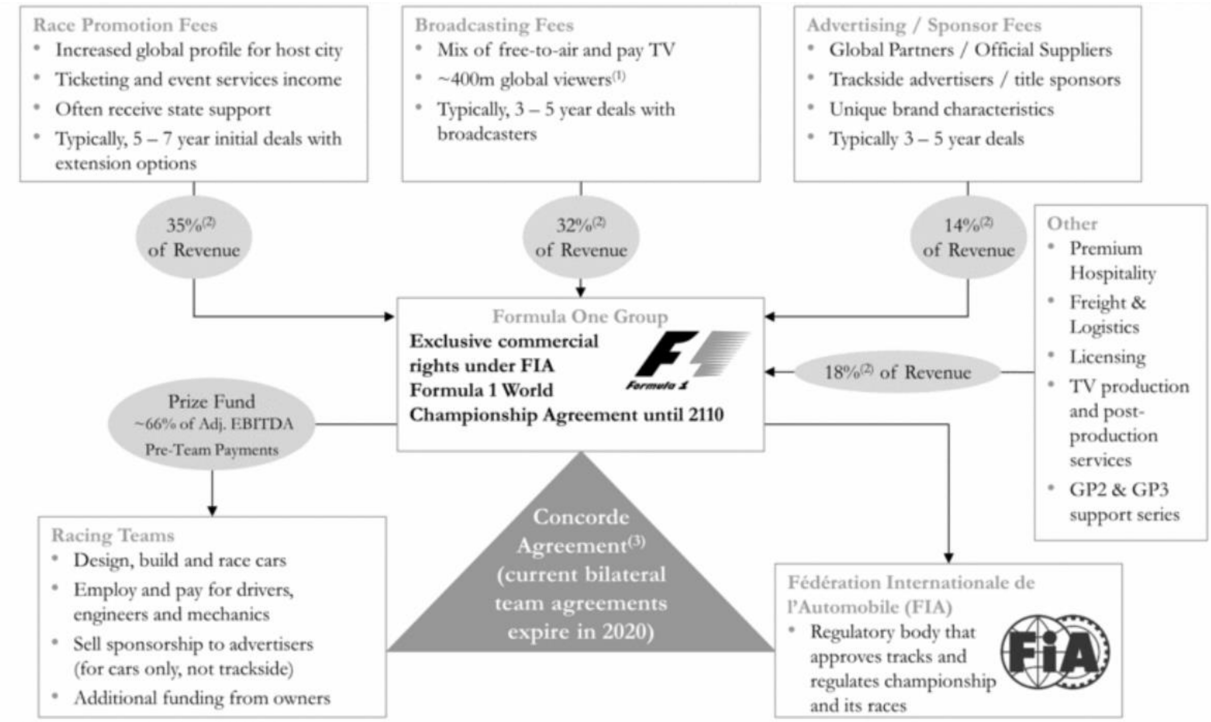

Figure 4.3 – How F1 Works. Revenues percentages referred to season 2015.[156]

4.4.2 Formula 1 Key Revenues Generation Drivers.

As figure 4.3 shows, Formula 1 relies on three main revenue sources: race promotion fees, broadcasting fees and advertising/sponsorship fees. We now dive deep into each of three to analyze key drivers.

Race promotion was F1's largest source of income in 2015, accounting for $653 million, or 36%, of revenue. This is more than double the $300 million recorded at the time of CVC's acquisition in 2006. Promotion income is driven by fees paid to host, stage and promote F1 events, which, in turn, generates tourism for the hosting country. Contracts for race typically last five to seven years and feature annual escalators[157]. Typically, F1 retains broadcasting rights and obtain trackside advertising, race title sponsorship, hospitality and other race-related rights from promoters. The incentives for hosting cities are very high as F1 attracts thousands of fans on a racing weekend, and usually demand to host races has exceeded supply.

[156] Figure taken from Liberty Media Corporation Presentation of Formula 1, November 2016, p. 15.
[157] The new playbook: How private equity fell in love with sport, Private Equity International, November 3rd 2020.

2015 Race	Race Day Attendance
Britain	140,000
Mexico	134,850
USA	101,667
Melbourne	101,500
Comparison	Average Attendance
NASCAR	99,853
NFL	70,000
2014 FIFA World Cup	52,918

Table 4.1 – F1 attendance vs other sports events[158].

In 2015, Formula 1 contents were distributed in more than 200 countries, generating broadcasting fees contributing for 32% of its annual revenues, equal to $587 million. In particular, at that time F1 signed agreements with around 100 broadcasters lasting from 3 to 5 years. In 2015, F1 races has been enjoyed by 400 million unique TV viewers globally, with viewership being significantly influenced by driver and team nationality, as well as by their performance. Moreover, the shift to Pay-TV had two competing effects: on the one hand, it affected aggregate reach, but on the other hand it deepened the coverage and enhanced viewing for interested fans.

As mentioned, the third most important revenue driver is advertising and sponsorship, responsible for $262 million, or 15%, of F1's 2015 revenues, compared with $190 million in 2006. These contracts, which can include race-title sponsorship and track-side advertising, typically span three to five years. F1's key partnerships included Pirelli, which has been its exclusive official tire partner since 2011, and shipping business DHL, its longest-serving partner at 15 years[159]. Sponsors are willing to invest their money into Formula 1 as fans usually associate the brand with luxury, speed and technology, offering a differentiated proposition relative to most of the other major sports.

[158] Data from Liberty Media Corporation Presentation of Formula 1, November 2016, p. 16.
[159] The new playbook: How private equity fell in love with sport, Private Equity International, November 3rd 2020.

Besides race promotion, broadcasting and advertising/sponsorship fees, Formula 1 can count on additional revenue sources, such as hospitality, freight and logistics, TV production and post-production, overall accounting for 18% of 2015 revenues.

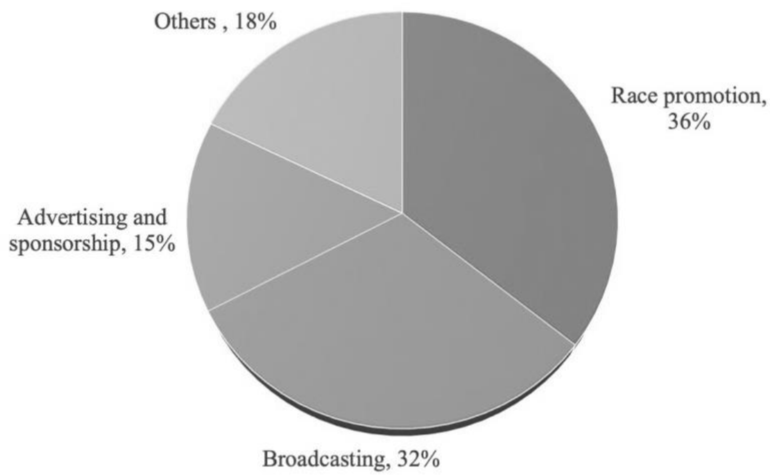

Figure 4.4 – Formula 1 2015 revenues split.

	Season		
($ million)	**2013A**	**2014A**	**2015A**
Number of races	19	19	19
Race Fees	34.5%	33.5%	35.3%
Broadcast	30.7%	32.0%	32.3%
Advertising & Sponsorship	15.8%	14.9%	14.4%
New Media	-	-	-
Other	19.0%	19.6%	18.0%
Revenue	**$1,639**	**$1,702**	**$1,697**
Growth		*3.9%*	*(0.3%)*
Team Payments	($777)	($843)	($883)
Other COGS	(301)	(289)	(256)
Gross Profit	$560	$571	$558
Gross Margin	*34.2%*	*33.5%*	*32.9%*
SG&A	($82)	($89)	($94)
EBITDA	**$478**	**$481**	**$464**
EBITDA Margin	*29.2%*	*28.3%*	*27.3%*
Tax	($16)	($14)	($6)
Capex	(3)	(2)	(1)
Unlevered FCF	**$459**	**$466**	**$456**
FCF Margin	*96.1%*	*96.8%*	*98.4%*

Table 4.2 – Formula 1 Financial profile overview[160].

4.4.3 CVC's Acquisition of Formula 1: Everything Started in 2006.

CVC, one of the most important Private Equity funds and among the most active in the Sports arena bought Formula 1 in 2006. At that time, the deal was structured under a leveraged buyout, funding the acquisition with $965.6 million from CVC's investment Fund IV and a $1.1 billion loan from the Royal Bank of Scotland. As the Delta Topco's (the F1 parent company) Articles of Association reported, CVC shares entitled it to appoint representatives,

[160] Table from *Liberty Media Corporation Presentation of Formula 1*, November 2016, p. 21.

known as I Directors, who can “exercise one vote more than the total number of votes exercised by the other directors.” The Articles add that the purpose of this is “to ensure that the I Directors will always have sufficient votes to pass a resolution of the board”, thus putting a huge premium on CVC’s stake.

Although CVC managers have been able to create and extract a huge value from Formula 1, increasing the appeal of the championship, during the ten-year investment period major changes took place, and some of them resulted in some (usually smaller) teams’ dissatisfaction. Soon after CVC’s acquisition, the first change was implemented: the share of the F1 profits being paid to the racing teams increased, passing from 47% to 50% of television rights and race promoter fees[161]. Anyway, Formula 1 approach towards TV rights under the CVC tenure has been sometimes controversial from the teams’ perspective, as it has been selling media rights at the highest possible price, regardless of what the consequences for fans could have been. For example, F1 disappeared from the free-to-air TV in many countries, shifting to the pay-per-view model. Another disruptive change that took place during the CVC tenure regarded the internationalization of the championship: in a ten-year period, the calendar expanded from nineteen to twenty-one races, with the non-European rounds having increased by 50% in the same period. This change had both positive and negative effects from a team point of view: on the one hand, it increased the visibility of the championship, thus making F1 more appealing towards sponsors globally; on the other hand, more races taking place far from the teams’ European bases meant higher costs to travel across the globe every weekend, thus putting financial pressure on them. Lastly, if on the one hand the $1.1 billion loan from the Royal Bank of Scotland helped CVC in boosting its ROI (through the leverage effect, by decreasing the Equity contribution from the fund), on the other hand it also had a side effect for Formula 1: every year $230 million must be paid out as interests on the loan, thus putting pressure on CVC’s managers that were forced to aggressively exploit any opportunity for profit.

4.4.4 CVC 2016 sale of Formula 1 to Liberty Media Group: an All-Time Record Exit.

Ten years after the acquisition, in 2016, CVC sold its stake in Formula 1 to the entertainment company Liberty Media, completing one of the most successful investment in the fund’s history, embodied in a 351.8% ROI[162]. In the following pages we are going to dive

[161] K. Collantine, *How the CVC era changed F1 – and what Liberty might mean*, RaceFans, September 8th 2016.
[162] C. Sylt, *CVC Becomes Formula One's Most Successful Owner With $4.4 Billion Haul*, Forbes.

deep into the transaction details, as well as into the investment thesis that brought Liberty Media to acquire the most famous Motorsports championship in the world.

Starting from the key terms of the transaction, Liberty Media's offer resulted in a $8.0 billion Enterprise Value for Delta Topco, the parent company of Formula 1. Considering the $3.4 billion net debt and $0.2 billion deal-related adjustments, the Equity value amounted to $4.4 billion, an extremely huge increase the price paid by CVC to acquire F1 ten years earlier. The selling shareholders of Delta Topco, guided by CVC, were entitled to receive a mix of cash, subordinated exchangeable note and Liberty Media's shares:

- Cash contribution equal to $1.1 billion, directly sourced from Liberty Media Group.
- Subordinated exchangeable note value equal to $0.4 billion.
- Newly issued 138 million Liberty Media shares, equal to $2.9 billion as of the transaction announcement date[163].

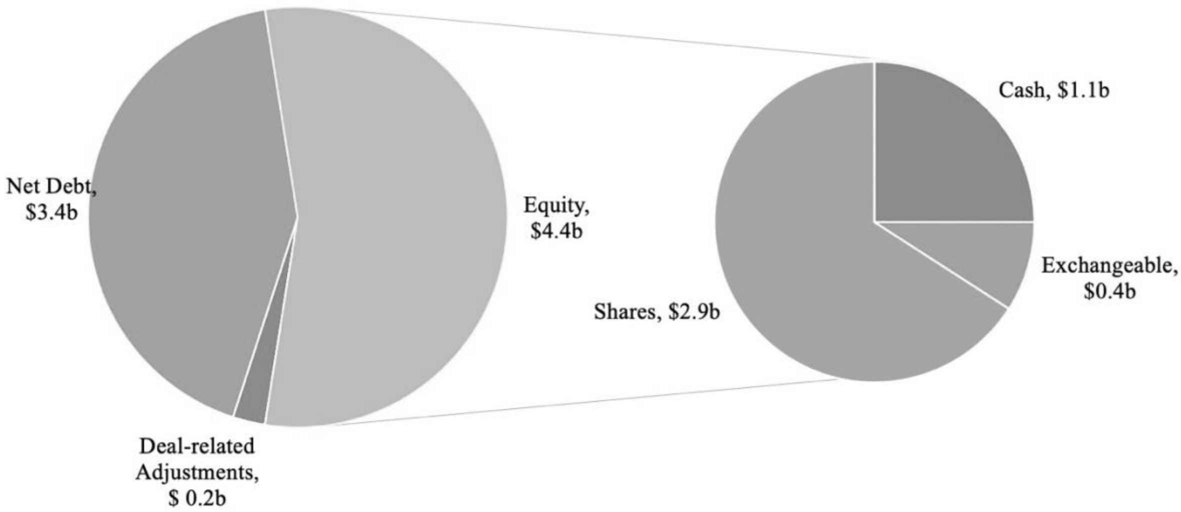

Figure 4.5 – Transaction value and structuring.

Thus, considering the deal structure, CVC and other Delta Topco shareholders will still own a stake in Formula 1 but through Liberty Media shares. In particular, according to the pro forma Formula 1 ownership structure, F1 seller shareholders will retain, all together, a 64.7% stake, with Liberty Media existing shareholder retaining the other 35.3%. for what concerns CVC, its ownership passed from a 38.1% stake to a 24.7%[164].

[163] *Liberty Media Corporation Agrees To Acquire Formula One*, CVC Press Release, September 7th 2016.
[164] *Liberty Media Corporation Presentation of Formula 1*, November 2016, p. 4.

	% F1 Ownership	
	Pre-Transaction	*Post-Transaction*
Liberty Media Group	**-**	**35.3%**
CVC	38.1%	24.7%
Waddell & Reed	20.5%	13.3%
LBI	12.1%	7.8%
Bambino Holdings	8.4%	5.4%
Management	6.1%	3.9%
Delta Topco Shareholders	**100%**	**64.7%**
Total	100%	100%

Table 4.3 – Ownership structure pre- and post-transaction.

Liberty Media Group had a very strong investment thesis, supported by five key pillars: F1 being a unique global sport entertainment business, a rising market for premium sports rights, clear revenue growth trends coupled with significant profitability and cash-flow conversion, multiple areas for future upside potential and, lastly, a low-risk business model with high revenue visibility.

Starting from the first pillar, Formula 1 was a very attracting asset for everyone that was looking for investments in the Sports Industry, and it was even more for Liberty Media, a global company owning interests in a broad range of media, communication and entertainment businesses. From Liberty's point of view, F1 represented a unique global sports competition with a massive reach, developed around 21 different countries and 5 continents, attracting over 400 million unique TV viewers in 2016. Moreover, Formula 1 was recognized for having a rich heritage founded on 67 years long history, and for being an iconic brand associated with speed, luxury, and high-tech innovation.

The second pillar upon which Liberty Media built its investment thesis was a rising market for premium sports rights, and in that arena Formula 1 was a key player, driven by an increase in demand from broadcasters, advertisers and sponsors in order to gain access to massive audiences, that as previously mentioned became widely international during the CVC tenure. From the chart below it can be seen how the average annual value for broadcasting contracts in other major sports increased during the Liberty Media acquisition as compared to previous contracts.

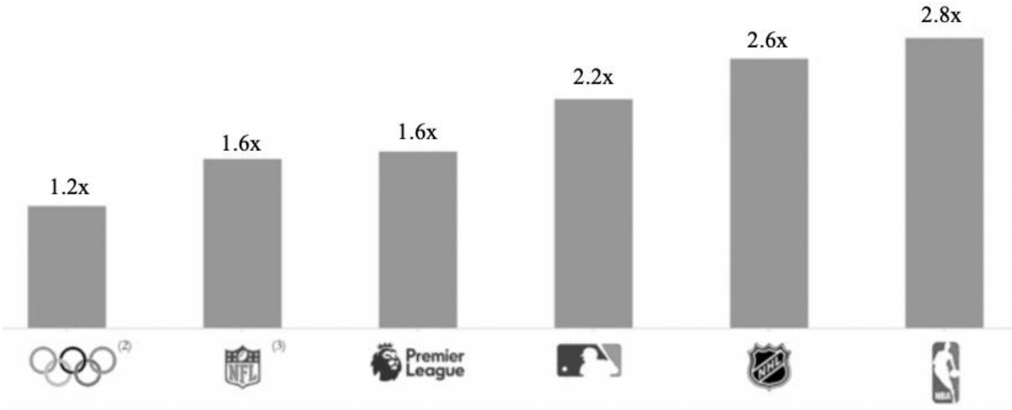

Figure 4.6 – Media rights contracts average annual value increase vs. prior contract[165].

The third pillar of the investment thesis was represented by revenue growth trends coupled with significant profitability and high cash-flow conversion. In particular, two main trends were supporting the revenues growth: annual escalators in contractual agreements and race calendar optimization. These two drivers had also a positive side effect, resulting in an increase for the value of live sports media rights, and a minimal growth in advertising and sponsorship. Overall, in a three-year period during which the total number of races passed from 19 to 21, revenues grew from $1,639 million in 2013 to $1,829 in 2016 million, a +12% increase[166]. From a financial point of view, Formula 1 showed a very interesting profile: attractive margins and very low capital needs generated an outstanding profitability, coupled with a high cash flow conversion rate (EBITDA margin at 26%, Unlevered FCF margin at around 26%, resulting in an unlevered cash flow conversion of 98%). Moreover, Formula 1 had a very interesting cost profile, with the biggest slice being representer by variable costs, namely team payments that were calculated as a percentage of the Prize Fund adjusted EBITDA. Lastly, the vast majority of revenue were generated in USD, thus having almost a zero-currency risk.

[165] Chart from Liberty Media Corporation Presentation of Formula 1, November 2016, p. 7.
[166] *Liberty Media Corporation Agrees To Acquire Formula One*, CVC Press Release, September 7th 2016.

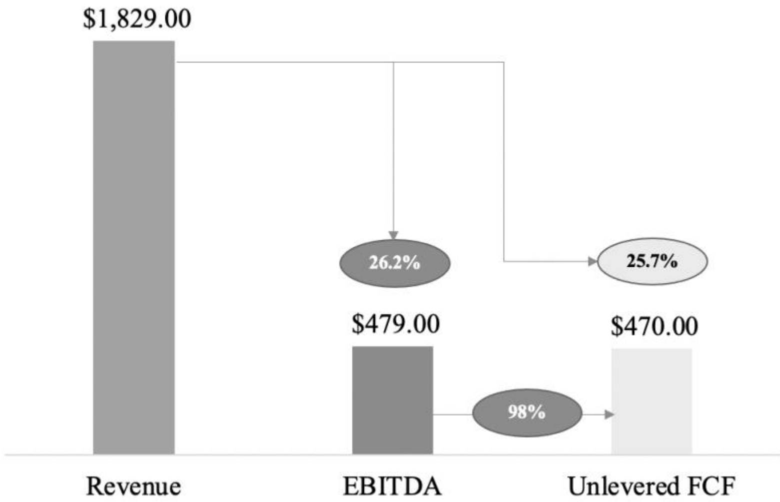

Figure 4.7 – Formula 1 2015 key financials.

To support Liberty Media Group investment thesis were also five key drivers of future upside potential, namely[167]:

- Race promotion: investors saw the opportunity to increase the number of races, optimizing their mix and entering new strategic markets, keeping the focus on Europe as the foundation of the F1 championship, but still capturing growth opportunities in America and Asia.
- Broadcasting: the broadcasting agreements renewal with Sky happening in March 2016 and running for the period 2019-2024 suggested potential for upside across Formula 1 rigthts portfolio, increasing the monetization of TV rights in conjunction with increased promotion of sport.
- Advertising and sponsorship: supporting and coordinating advertising and sponsorship deals alongside teams was seen as an opportunity to ensure the maximization of the championship potential.
- Digital: at the time of the acquisition, Formula 1 derived only a 1% of its total revenues from digital services, hence building targeted digital platforms directed to the most engaged fan base was considered an opportunity to build an additional revenue stream.
- Expanding franchise: leveraging on F1 brand reputation across the globe, Liberty Media saw the opportunity to increase revenues from merchandising and side activities to be added to the race event itself, in order to attract more and more fans at the racing venues.

Last but not least, Liberty Media considered Formula 1 to be a valuable asset to be added to their portfolio because of its low-risk business model with a high revenue visibility. In

[167] Liberty Media Corporation Presentation of Formula 1, November 2016, p. 9.

particular, F1 was recognized to be a global brand appealing for very attractive demographics, similarly to the English Premier League or the UEFA Champions League, but with the advantage of being a global competition. The majority of the revenue streams were locked under long-term contracts, thus making Formula 1 hedged against economic downturns and providing management with high visibility on future, expected financial performance.

If Liberty Media Group relied upon five strong pillars to support their investment thesis, on the other hand they also highlighted some specific risks. First of all, under the most current Concorde Agreement (see 2.3.1) running at the time of the transaction, teams would have had the right to higher payment from F1, as well as numerous governance rights. Second, the expansion of the management team and the loss of Formula 1 key personnel would have required time and expenses to adapt to the new *status quo*, thus posing a risk for the organization. Lastly, rival Motorsports events could be established (as it actually happened with the birth of Formula E championship), mining the *quasi*-monopoly of F1 in the Motorsports arena.

CHAPTER FIVE – E1 SERIES: HOW TO MAXIMIZE VALUE AND ATTRACT PRIVATE EQUITY FUNDS' INTEREST[168].

5.1 Introduction.

In this chapter, the last one of this study, we are going to deep dive into one of the most prominent championship in the Motorsports arena: E1 Series. In the following pages we will understand what this championship is about, who its promoters are, its timeline and how it will be structured. Lastly, based on the main findings of the previous pages, the objective of this chapter is to suggest some key value drivers to be activated in order to attract Private Equity funds' interest, in order to allow E1 Series founders to complete a successful exit in a medium-term horizon.

5.2 E1 Series: Water, Electrified. What this Championship is about and How does it Work?

E1 Series will be the first sustainable powerboat championship, born with the objective of increasing the awareness and positively impacting the conservation of the seas and oceans, the most important ecosystem we can rely on for the survival of the planet. E1 Series, set to kick-off its first season in March 2023, will be composed by ten to twelve teams, each one having one pilot racing at a time on a 100% electric powerboat, everyone committed to the sustainability across the full value chain, from R&D to logistics, and until the final races. At the center of this project there is RaceBird, a 150 kW powerboat produced by SeaBird Technologies in collaboration with industry-leading partners, such as Victory Marine, Caponnetto Hueber and Sail GP.

The first aim of the flight shipments two founders, Alejandro Agag and Rodi Basso, is to build a sports platform to fill the gap in the maritime mobility. In fact, maritime transport is heading towards de-carbonization, but the progress is very low and the process being at its initial phases. A research from Enel Foundation suggests that the demand for electric boats is set to increase in the next five years (see figure 5.1). Hence, E1 Series will have a key role in developing a platform to accelerate technological developments, as well as to increase the desirability of electric boats towards the public.

[168] All relevant information and key data about E1 Series from investors presentation decks, kindly provided by E1 Series CEO Mr Rodi Basso and CFO Mr Richard Draisey.

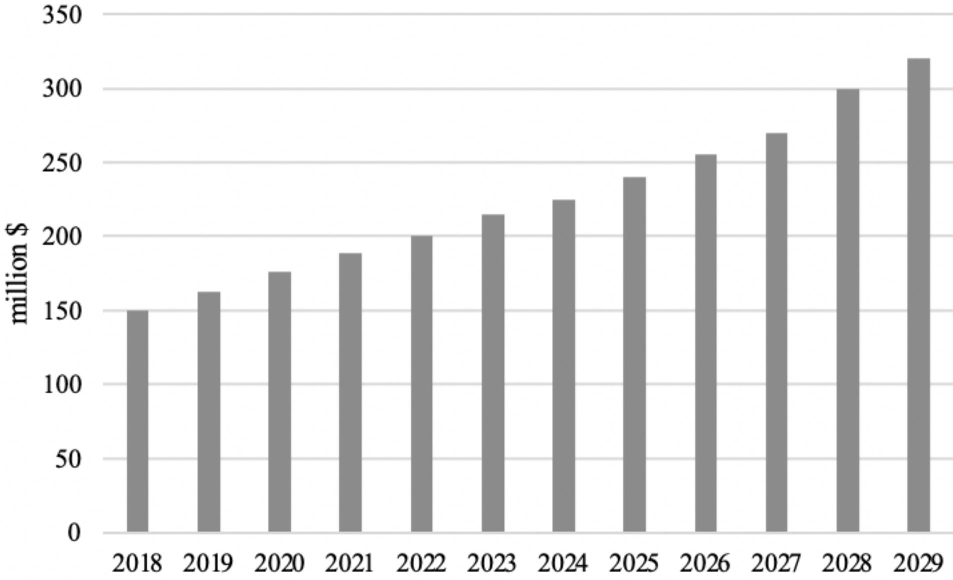

Figure 5.1 – Electric recreational boats market size[169].

In this growing market, E1 will be the only global championship that will promote innovation through the electrification of the marine mobility, providing the acceleration platforms for boat manufacturers, teams and hosting cities to step away from fossil fuels in favor for cleaner and more sustainable energy sources. Moreover, E1 secured itself an exclusive, worldwide license to organize and promote an all-electric powerboat championship from the *Union Internationael Motonautique* (UIM, the international powerboat governing federation), lasting for a minimum of twenty-five years, extendable up until 50 years.

E1 Series is an ambitious project, initially launched in September 2020 at the *Yacht Club de Monaco*, and is grounded on a strong base of four key pillars:

- Racing: competing teams will engage the most competitive pilots to create an attractive event that will be able to gather both Motorsports passionate and newer fans.
- Legacy: E1 will leave its footprint wherever its races will be run, providing hosting cities and ports with infrastructure for future use, in this way facilitating the shifts toward electric mobility in the marine industry, leaving a long-lasting legacy.
- Innovation: as already mentioned, E1 aims at filling the gap in the marine mobility by providing a platform for technological developments to accelerate the innovation processes.

[169] Data from Enel Foundation.

- Sustainability: last but not least, E1 aims also at preserving seas and oceans and in order to be successful, it will provide the needed tools for scientific research useful to come up with new ideas about the marine ecosystem preservation. Moreover, the focus on sustainability will be evident across the entire value chain, avoiding air shipments for the boats and needed equipment, making use of electrified transportation vehicles.

E1 Series sample calendar is developed around ten events per season, with races being run across the globe between five European hosting cities (London, Geneva/Zurich, Naples, Monaco and Barcelona) and five remote races (Greenland, New York, Miami, Amazon and Middle East). As we will later analyze, the geographical spread of E1 will give the championship a competitive advantage, giving the opportunity to leverage on a global reach as it already happens, for example, in Formula 1 (see 4.4). Each race will have the same format, structured according some key pillars: 10-12 teams, with one RaceBird and pilot for each team; short and exciting races, creating an enjoyable event to excite fans and provide broadcasters with enough content. Races will be unpredictable, given that at least for the first seasons every team will be provided with the same powerboat model, and energy management will be the key for success: no recharging options will be provided to the teams, thus efficiency and team strategy will be the key variables to win the championship.

Lastly, a key strength point of E1 Series is represented by the people involved in the project, making up a team that can leverage on high expertise in the Motorsports arena. Among the others:

- Alejandro Agag, Founder and Chairman: born in Madrid in 1970, he decided to leave the world of politics in 1991 and move into Motorsports where, together with his business partner Flavio Briatore, purchased the F1 TV rights in Spain. A few years later Agag bought the Campos Racing GP2 Team, revamping it into the highly successful Barwa Addax Team. After investing in English football club QPR, Agag, together with his business partner Enrique Bañuelos, founded Formula E Holdings, winning the tender to promote the new FIA Formula E Championship. Few years later, Alejandro founded another Motorsports championship, known as ExtremE[170].
- Rodi Basso, Co-Founder and Chief Operating Officer: graduated in Aerospace Engineering, Rodi started his career working for NASA, and after this experience he joined Motorsports joining successful Formula 1 teams such as Ferrari, Red Bull Racing and McLaren Racing.

[170] Biography of Alejandro Agag from the *Fédération Internationale de l'Automobile* (FIA) website.

- Richard Draisey, Chief Financial Officer: after graduating in Business, Richard joined McLaren Racing for seven years covering the role of Financial Strategy and Transformation Director.
- Yanni Andreopulos, Chief Marketing and Commercial Officier: graduated in Law at the University of Cambridge, Yanni gained almost fifteen years of experience working in the Sports Industry for prominent institutions like NBA, Hammarabu Football and Formula E.

Last but not least, E1 Series can count on a strong financial partner: the Saudi Arabia Public Investment Fund (PIF). In fact, on June 2021 the PIF's investment has been announced, supported by a strong investment thesis: E1 Series is in line with the funds' 2021-2025 strategy, focusing on thirteen key strategic sectors including Sports & Entertainment and Renewable Energy. To get the backing the ninth wealthiest sovereign wealth fund at a so early stage of the project highlights the potential of E1 Series, suggesting a roadmap full of success for the team[171].

5.3 Key Revenue Drivers: Media Rights, Sponsorships, Participation and Hosting Fees.

From a financial point of view, E1 Series is strongly supported by four key revenue drivers, with the opportunity to further expand them through "lateral" streams, as it will be analyzed later on. In particular, the four P&L pillars are the followings: media rights, sponsorship, participation fees and hosting fees.

Starting from media rights, E1 Series will be leveraging on a wide fan base, targeted into five key groups:

- Sports enthusiasts: people passioned about sports that enjoy following different leagues and championships, such as Football, Motorsports or Boat Racing. They represent a huge fan base, accounting 1.1 billion individuals spread all over the globe, with 56% of them being male and aged 44 on average.
- Tech enthusiasts: this group is represented by people interested in newest technological developments, always trying to keep themselves up to date. For them, besides technology, sustainability is a key issue and are usually willing to recognize a premium (i.e., a higher price) for those products and services promoting the respect for the environment. They are estimated to be 109 million in total, 56% of which being male and aged 35 on average.

[171] *E1 Series and PIF announce partnership to create world's first electric powerboat championship*, PIF Press Release, June 6th 2021.

- Racing enthusiasts: they are represented by people that love Motorsports, enjoying championships such as Formula 1, MotoGP or WSBK, and as such enjoy also looking at drivers pushing themselves at the limit of their capabilities. The racing enthusiasts bucket gather around 145 million fans, 65% of which are male, on average 38 years old.
- Ocean conservationists: this bucket of potential fans is not linked with the Motorsports arena, but still can represent a huge opportunity for E1 Series as they are really keen on climate change related issues, and usually supports those initiatives that try to find remedies to pollution, climate change and seas/oceans conservation. This bucket gathers 259 million people, with the majority of them being female (51%) and aged 36 on average.
- Gen Z: the last bucket of addressable fans is represented by Gen Z, defined as those people born in between 1995 and 2010[172], accounting for as much as 2.4 billion individuals, showing a 50/50 gender split. Gen Z are digital natives who respect brands telling a true story, and their consumption habits express their identity, being a matter of ethical concern; being digital natives, by definition they are used to virtual experiences as well as to offline ones. Gen Z represents a huge, maybe the biggest, opportunity for E1 Series.

When it comes to the broadcasters, E1 Series can leverage on existing relationships through Formula E and Extreme E, two already settled Motorsports championships whose founder is Alejandro Agag. Broadcasters will be attracted by a strong content production strategy: live sports actions and highlights will be broadcasted thank to the use of 360° cameras, as well as through drone coverage and onboard cameras covering multiple angles, making fans excited and engaged by the fights between ReceBirds. The content production strategy will be flexible developed around the following key points, with the objective to engage with the widest possible fan base, from those who only wants to enjoy the races to those that will become enthusiasts of E1: each race will have 1 hour of live programming, dedicated to those fans who only want to watch live races; if fans want to enjoy most of the part of the racing day, live events throughout the day will be streamed; in order to engage with those fans who wants to know more about the championship and the drivers, year-round digital contents will be provided, in this way also engaging with younger demographics; lastly, to build a competitive narrative around E1 Series, regular documentary-styled contents focused on sustainability and post-race will be broadcasted. A global broadcast coverage developed around twenty live races programms, ten magazine show episodes, and eight to twelve documentary episodes, will allow

[172] T. Francis, F. Hoefel, *True Gen': Generation Z and its implications for companies*, McKinsey & Co., November 12th 2018.

E1 Series to potentially achieve a cumulative TV audience of more than 170 million viewers, divided as shown in the table 4.4.

Region	**Race programming**	**Magazine**	**Docuseries**	**Total audience**
Africa & Middle East	11,644,010	4,892,681	80,854	16,617,545
Asia Pacific	38,861,295	6,714,522	8,897,905	54,473,722
Central & South America	25,500,086	2,816,575	321,729	28,638,390
Europe	52,008,983	12,408,799	496,590	64,994,363
North America	4,901,147	773,441	414,277	6,088,815
Grand Total	132,995,521	27,606,018	10,211,285	170,812,824

Table 5.1 – Global TV cumulative audience including repeats[173].

Thus, numbers show that E1 Series has a great potential in terms of media rights and from previous analyses (see 4.4) we know that in global Motorsports championship deals can lock in high revenues streams.

The second key revenue driver is represented by sponsorship contracts. When it comes to sponsorships and advertising, to sign good deals E1 Series can leverage on a key strength point: sustainability. It is already known that consumers are more and more rewarding those companies that commit themselves to sustainability related topics. Hence, corporation will have a huge incentive in partnering with E1. In general, sponsors will be able to enjoy both general and "at race" rights: on the one hand, sponsors will benefit from association rights, gaining access to E1 IP and logos; second, they will have access to a (likely) huge fanbase, and also to the data generated collected from them, enjoying direct marketing opportunities too; on the other hand, sponsors will benefit from race-day advertising and brand integration, as well as from premium hospitality. So, E1 Series has all the conditions needed to sign sponsorship agreements, that will bring in new financial resources to be invested to foster the championship growth, while building a network of companies committed to sustainability-linked initiatives.

The third revenue stream is represented by participation fees paid by the teams. E1 will be structured according to a franchise model, around a maximum of twelve teams, each one

[173] Data from SMG YouGov.

racing on two powerboats. Any team that wants to join E1 Series will be asked to pay an entry fee equal to €2 million. Tin this way, teams will own a 25-year long license, that could even be sold to other teams willing to enter the championship, but the transaction will require E1's board approval. On top of the entry fee, each team will be required to pay a yearly running fee equal to €1 million. Overall, as shown in table 5.2, each team will sustain an average participation cost of 1.5 million per season, among the others covering the following:

- 2x RaceBird;
- 3x standard powertrain;
- High voltage batteries;
- Logistics management to each race location;
- Full charging infrastructure and services;
- Paddock infrastructures, including garages;
- TV production and compound.

Besides owning the license and getting the right to take part in the championship, competing teams will also be entitled to 80% of the RaceBird TV-visible space for sponsorship purposes.

	Cost (€)
Annual fee	1,000,000
Spare parts	200,000
Salaries	150,000
Travel expenses	100,000
Other	50,000
Total costs	**1,500,000**

Table 5.2 – Forecasted yearly team participation cost.

Last but not least, the fourth key revenue driver is represented by the hosting city fee. Cities across the globe will have huge incentives in hosting the E1 races, as they will be broadcasted all over the continents, giving cities the opportunity to join a worldwide reach. What makes E1 a huge of opportunity is the surrounding of the races: E1 will be more than just a race, bringing to hosting cities an "Electric and Mobility Festival", taking place during the week leading up to the E1 event, providing the right platform to showcase the commitment to sustainable urban mobility. Cities that are willing to host E1 races will need to undertake a proper assessment and evaluation process that will be based on some pre-established criteria (financial, environmental, commercial, etc.). Besides attracting a huge fan base towards their locations, hosting cities will benefit from a set of commercial rights, such as: waterside advertising for local brands, with TV-visible positioning on racing infrastructures; trade shows, expos and conferences, and a full set of ancillary events that will take place during the week preceding the race.

5.4 Suggested Key Actions to Pursue Value Maximization.

The objective of this last section is to provide E1 Series management team with a dashboard of suggested actions to be undertaken in order to pursue value maximization and attract the interests of Private Equity funds in a medium-term horizon, ranging from five to six years. In particular, we will now go briefly through the “standard” must-haves for a project in order to fit with a PE portfolio, but then the focus will shift towards other suggested strategies.

Private Equity firms usually look for target companies and projects respecting a series of standard requirements in order to complete a successful leveraged buyout. A good LBO candidate is a company or a project showing the following characteristics:

- Steady and predictable cash flows: the target’s cash flows need to be steady in order to meet the interest payments on debt needs, as they come due at predetermined date and the company must always be solvent to not undergo a financial crisis. Moreover, predictable cash flows help in carrying over financial planning and forecasts, as well as in reducing the cost of debt given reduced uncertainty. As we already saw for the Formula 1 case study (see 4.4), Motorsports project can rely in stable and pre locked-in cash flows thanks to the predominance in their P&Ls of media rights deals, bringing in more and more financial resources. This seems to be the case for E1 Series too, that as we already mentioned has a great potential when it comes to media rights, having the possibility to leverage on a global reach, as well as on a global fan base.
- Clean balance sheet with little debt: significant pre-existing obligations to other debt holders will make new layers of debt from the buyout fund riskier to pay off. Thus, a cleaner balance sheet allows excess cash flows to go towards the new debt of a LBO. From a financial point of view, E1 Series does not need to invest heavily on Capital Expenditures (CAPEX), given the absence of fixed assets needs. Moreover, as mentioned before, E1 can count on a strong financial partner as PIF.

- Defensible and strong market positioning: the LBO target needs to be in a position where it can generate large profits. A market position that is guarded by high barriers to entry makes a LBO candidate more attractive because it lowers the risks linked to the cash flows. Linked to that, we mentioned E1 Series being the first and only full electric powerboat championship, with a strong footprint based on sustainability. On top of that, as we already discussed E1 Series can count on an exclusive, worldwide license to organize and promote an all-electric powerboat championship from the UIM lasting for 25 years, and that can be extended up until 50 years. Thus, E1 Series can rely upon very high barriers to entry, making it almost impossible for any potential competitor to threaten its competitive advantage.
- Strong management team: most private equity firms rely on the management of the company to actually execute the company improvements, and a significant part of the due diligence is spent interviewing the management team. As we analyzed, E1 Series is promoted by one of the most experienced management team in the Motorsports industry, especially from professionals that have been already involved in top-tier Motorsports projects such as Formula E, Ferrari and Redbull Racing F1 team, McLaren Racing and Extreme E. E1 Series management team represent a key strength point for the credibility of the projects, giving a sense of trustworthiness to any third party.
- Limited CAPEX and Net Working Capital requirements: considering that any increase in CAPEX and NWC (Net Working Capital) accordingly reduces the cash flow, PE firms prefer to invest in those companies/projects having limited NWC and CAPEX need, so that any available cash flow can be used either to finance growth or to pay down debt obligations. We already mentioned that E1 Series can count on very limited CAPEX needs, as fixed assets are not required for the running of the project.
- Synergies and potential for expense reduction: PE firms usually work closely with the managers to find ways to increase profits as quickly as possible, and reducing costs is one of the first strategy to be implemented. E1 Series can count on a series of synergies coming from Extreme E. In fact, Alejandro Agag is also the founder of Extreme E, and the ambition is to create synergies between the two all-electric championships: for example, part of the calendar will be shared between E1 Series and Extreme E so that all the needed equipment can be shipped in one transport ship, thus saving costs.
- Large amount of tangible assets for loan collateral, coupled with divestible assets: more collateral enables lower-interest financing, thus reducing interest payments and the amount of cash needed to pay back debt. Potential loan collateral includes current assets such as

cash and inventory, as well as long-term assets like property, plant, and equipment. As we mentioned, E1 Series has the benefit of having very low CAPEX need, meaning that it will have a light asset base. Thus, a potential buyer could not count on collateral assets to lower interest payment, raising the need for alternative strategies, such as using as collateral the future cash flows from already locked-in media right deals.

- Viable exit strategy: a PE fund only realizes returns when exiting an investment, implementing one of the options that we thoroughly analyzed at the beginning of this research (see 1.4.4). When it comes to E1 Series, the best option is the sale to a strategic buyer, on the back of the Formula 1 case study.

Thus, we can confirm that E1 Series is an extremely good candidate for a Private Equity fund, respecting eight out of ten LBO candidate characteristics. We now deep dive into a dashboard composed by three suggested actions to implement in order to maximize E1 Series value and to attract PE funds' interest: strengthening the presence on social media, riding the wave of eSports and implementing data collection tools. All of them are based on recent trends in the Sports and Private Equity Industries, as analyzed in previous chapters.

5.4.1 Key Action #1: Strengthening the Presence on Social Media.

The first suggested action corresponds to strengthening the social media presence. As already discussed, the pandemic has had a huge effect on the relationship between sports teams and fans. Thus, sports organizations are now forced to reinvent the way through which they engage with fan, providing both online and offline solutions. So, those sports organizations already having in place the required tools to interact and engage with fans through online platforms can benefit from a competitive advantage as compared to those that rely exclusively or mostly on offline means. Of course, when it comes to business valuation, having a competitive advantage secure those sports organization a premium, as already discussed in 5.4. In particular, social medias are the preferred online platforms for fans that want engage with sports organizations (among the others). Thus, for E1 Series strengthening its presence on social medias is a key point in order to first gain a competitive advantage, and then secure a premium when it comes to valuation. Having a strong presence on social medias comes with several benefits, all of them representing key revenues growth drivers: enlarge the fan base, increase sponsorship and advertising revenues, and collecting data about fans.

Starting from the first positive effect, having a strong presence on social media has an extremely positive impact on the fan base. On the one hand, it helps tightening the engagement with respect to already existing fans, maybe helping in turning occasional fans into E1 Series enthusiasts, thus increasing the number of fans with a higher willingness to pay when it comes to products linked to E1. On the other hand, building a strong presence on social media has the positive effect of enlarging the fan base by attracting new fans: strangers to E1 Series may get in touch with the championship by simply watching a video on Instagram or Facebook, then becoming interested and with the time passioned about it. Social media represent a key instrument when it comes to engagement strategies for Gen Z: as we mentioned before, Gen Z is composed by 2.4 billion individuals who are very used to engage in everyday life through social medias. Thus, having a strong footprint on social media comes with higher probabilities to engage with those 2.4 billion people, increasing by far the growth potential of E1 Series. Moreover, when it comes to social media, there is a lot of literature suggesting a strong correlation between the presence on social media and firm equity value, thus showing that investors are ready to pay a premium for those companies having built a strong presence on online channels[174].

5.4.2 Key Action #2: Riding the Wave of eSports.

As previously analyzed in section 2.3.5.1, eSports represents a huge opportunity for any sports organization looking for additional revenue stream, as well as looking for strategies to keep its business up to date with the most recent trend. eSports has experienced an exponential growth from the beginning of 2000s, and as already mentioned the eSports Industry reached a global market size of $950 million in 2020. But when it comes to eSports, the best is yet to come, as its market size is expected to grow up to $1.1 billion in 2021, continuing with this extraordinary trend in the years to come. What makes eSports such a huge opportunity is the ease of access for a total addressable consumer base that reaches skyrocketing numbers in terms of individuals. Moreover, not only eSports benefits from gamers, but it also benefits from those individuals that do not play any game, but still are interested in video games and enjoy looking at other players playing on streaming platforms, such as Twitch. Of course, this increases the visibility of any content related to the video game itself, thus increasing the value of the overall platform. As we mentioned throughout the Porter's five forces analysis of the Sports Industry, eSports can be a threat of substitutes for those sports organizations that decide to not invest in

[174] For example, see L. Xueming, Z. Jie, D. Wenjing, *Social Media and Firm Equity Value*, College of Business, University of Texas at Arlington, 2013.

this growing market, but on the other hand it represents a huge opportunity for those who decide to ride its wave.

First, what makes eSports a key action to implement for E1 Series is the shared addressable consumers base. As mentioned in Chapter 2, eSports mainly involves young (26 years old on average), male (more than 70%), tech-savvy, and highly educated individuals. This is pretty much in line with E1 Series potential fan base, both in terms of Gen Z and tech enthusiasts, overall amounting at around 2.6 billion people. Thus, introducing eSports can have an exponential effect on E1 Series viewership: on the one hand, gamers that get in touch with E1 Series' eSports platform could enjoy the history behind the championship and start watching the races; on the other hand, E1 fans could be interested in eSports too, thus deciding to play on the "virtual" championship, resulting in an increased fan engagement.

Second, eSports represents a huge opportunity of diversification for E1 Series, both from an operational and a financial point of view. From an operational point of view, eSports enriches the E1 project and provides its fans with a broader array of challenges to enjoy. In particular, eSports can be implemented following two different strategies that are not mutually exclusive:

- Option 1: E1 management can introduce eSports by developing a video game to be sold on the market simulating the "offline" powerboats races. Within the Sports Industry, different sports organizations decided to invest in eSports by developing their own video games. For example, on the market there are two video games licensed by the NBA, NBA 2K (developed and distributed by Take Two Inc.) and NBA Live (developed and distributed by EA Sports). Talking about NBA 2K, its latest edition NBA 2K21 has sold in more than 10 million copies, boosting Take Two revenues in 2021 (together with Grand Theft Auto Online) up to $3.37 billion, registering 2.3 million daily players and 73% Y-o-Y growth when it comes to recurrent consumer spending[175]. Thus, evidence shows that eSports represents a key revenue driver, both directly from video game sales, and indirectly through increased fan engagement.
- Option 2: as an alternative or on top selling to the market its own video game, E1 Series can introduce a parallel championship based on virtual reality, structured around the following key points:
    - The "virtual E1 Series" can take place in conjunction with the "offline" E1 Series, thus moving weekend by weekend the physical location where gamers are based.

[175] *Take-Two hits $3.37bn revenue in record year*, gamesindustry.biz, May 18th 2021.

Ideally, the eSports arenas should be set up besides the ports where the "offline" races will take place. In this way, eSports will be a way to also increase fans attendance at the racing venues.

- eSports teams can be the same ones that will take part to the "offline" championship, building their own eSports branch, as well as third parties. As it happens for the "offline" championship, anyone who wants to join the eSports E1 Series have to pay a yearly subscription fee, and in exchange will benefit from shared media rights revenues, as well as money prizes.
- The same broadcasters that will distribute the "offline" E1 Series can be offered with the opportunity of streaming the eSports E1 Series. Thus, introducing eSports represents a huge opportunity to also increase media rights and broadcasting revenues.
- Sponsors that will invest in the "offline" championship will be offered with the opportunity to benefit from increased visibility through eSports, in exchange for higher sponsorships fees.

Continuing with the NBA case, the NBA2 K has also developed its own virtual league, known as NBA 2K eSports League. It experienced an extraordinary growth in terms of viewers and revenues in the recent past, and in particular during the pandemic, when the broadcasts on Twitch went up by 69% as compared to 2019 average unique viewers per stream. In a recent interview, NBA 2K managing director Brendan Donohue said that "The model that exists on the NBA side for the most part carries over to the 2K side", with the eSports league having signed partnerships with AT&T, Snickers, New Era Caps, Panera Bread and many more sponsors[176]. NBA 2K eSports League games are currently broadcasted by ESPNs, ESPN's digital platforms, Sportsnet in Canada and on eGG Network in Southeast Asia and Loco in India, marking the first-ever broadcasts of 2K League games on linear television[177].

Thus, creating an eSports championship represent a huge opportunity for two main reasons: on the one hand it increases the popularity of E1 Series as a whole, with all the monetary benefits that follow; on the other hand, it represents a strategy to diversify the business and to hedge against risks, as it happened during the lockdown in the NBA business case. All the benefits linked to the implementation of a eSports championship increase the value of the E1 Series project, thus making it more attractive from an investor's perspective. Moreover,

[176] R. Williams, *Nba's 2k Esports League Grows During Pandemic with Eyes on Expansion*, Sportico, January 19th 2021.
[177] P. Murray, *With The Growth Of Esports, NBA 2K League Is Taking Off*, Forbes, October 11th 2020.

owning a parallel virtual championship can represent a huge opportunity for future strategic decisions: if successful, the eSports E1 Series can be spun off from the "offline" championship and sold to private investors, being a way for the founders to monetize the initial investment, but still owning the control over the "core-business", i.e., the "offline" E1 Series championship.

5.4.3 Key Action #3: Implementing Data Collection Tools.

As investigated throughout this research, in particular in section 4.2, data collection is one of the key trends in the Sports Industry that is attracting investments from Private Equity firms. In particular, collecting data can be beneficial to E1 Series' P&L in multiple way. On the one hand, data can be collected and monetize by being sold to multiple stakeholders. On the other hand, data collection can be beneficial to improve the performance of the RaceBird powerboats, as well as to improve technological developments about the electrification of the marine industry.

Starting from the implementation of the right tools to build an additional monetization route, data collected can be useful for multiple purposes. First, we already mentioned an increasing market size for the betting industry in the US: the online sports betting market is expected to jump from the current $9.7 billion market size, to $37 billion in 2025[178]. This represents a huge opportunity for E1 Series in connection with data collection: if the needed tools are put in place, E1 can collect data and real time statistics about the RaceBirds powerboats and during the race to be sold to sports betters. The more E1 Series will get popular, the more the data collected will rise in value, as well as new technological developments will make the collection process easier and more efficient. Second, collecting data about both on-track and remote fans can allow E1 to support its revenue stream, by selling those data (in accordance with current data protection laws) to multiple stakeholders: hosting cities, sponsors and broadcasters.

On the other hand, collecting data about powerboats performance can be beneficial to the E1 project from two different points of view. First, collected data can be used to improve the RaceBirds powerboats performance, making the races more and more exciting to watch. The amount of conclusion that racing teams can draw from the data collected about vehicle performance is impressive. Relying on the rights tools, engineers can identify and implement any opportunity to increase the performance of the powerboats. Moreover, critical parameters

[178] D. Randall, *ARK Invest's Cathie Wood looks past rising consumer prices to focus on deflation*, Reuters, July 13th 2021.

can be measured thanks to data collection in order to increase the safety and the reliability of the powerboats, thus reducing the overall risk linked to the project (and to lower risks, all else being equal, correspond a higher value). Then, collected data about boats performance can be sold to boat manufacturers in order to improve technological developments in the electrification process of the marine industry.

Hence, we have seen that data collection can be useful for multiple purposes in the E1 framework. First, it represents a monetization strategy, both by selling data and statistics about powerboats performance to sports betters, and by selling data collected from fans to multiple stakeholders. Second, data collection is a useful toll to improve the performance of RaceBirds powerboats, and collected data can also be sold to boat manufacturers to improve the electrification process of the marine industry.

Conclusions.

Throughout this research we have gone through three macro topics. First, we have analyzed the main characteristics of Private Equity funds. In particular, we have assessed funds structure, both in the US and in Europe, to then deep dive into a PE fund life cycle. We have seen how each of the phase plays a key role in the generating abnormal returns, from the capital raising process to exit options. Regarding exit options, we came to the conclusion that PE funds can tap either private and public markets. On the private side, they can decide to liquidate their investments by selling their stakes to strategic buyers or to other PE investors. On the public side, PE investors can liquidate their stakes by undertaking an IPO process. Each of the available exit opportunity must be carefully analyzed in order to maximize the return on the investment.

Then, we have deep dived into the Sports Industry, assessing its main characteristics and key financial factors driving the industry. In particular, we have gone through the key forces shaping the industry thanks to the Porter's five forces analysis. Key findings suggest that sports organizations must watch out the bargaining power of suppliers, both athletes and broadcasting companies, and the threat of substitutes, in particular from eSports. Regarding eSports, we have highlighted how it can be a threat and an opportunity at the same time: sports organizations can turn it into a huge opportunity by investing in eSports, riding the wave of an ever-growing market. For what concerns key financial drivers, we have analyzed different ownership structures available to sports organizations to understand what the key implications from a sportive and financial point of view are. We concluded that, among the others, Football clubs do not benefit from listing their shares, as this imposes a higher financial discipline over their management team especially when it comes to talent acquisition, creating a competitive advantage for those clubs that are privately owned. For this reason, we concluded that the most common way to finance a sports organization is by recurring to the debt market.

Lastly, from the main findings of the first two macro topics we have analyzed Private Equity investments in the Sports Industry, understanding key drivers building their investment thesis. In particular, one of the reason why PE funds enjoy sports clubs is for diversification purposes: locked-in long-term media rights deals, coupled with season tickets sale, make sports organization uncorrelated with other assets on the markets. Moreover, we assessed that the scarcity of sports club drives up their valuation, making them more expensive to be acquired.

Then, to prepare for the analysis of E1 Series, we have gone through the most important business case when it comes to Private Equity investments in Motorsports: CVC and Liberty

Media Group deal for the transfer of Formula 1 ownership. In particular, we assessed Liberty Media investment thesis, that brough to recognize an Enterprise Value for Formula1 equal to $8.0 billion, resulting in a 351.8% ROI for CVC. Then, we analyzed one of the most promising projects in the Motorsports arena, E1 Series, the first-ever 100% electric powerboats championship, set to kick off its first season in 2023. In this context, we have gone through the key pillars of the E1 project, leveraging on the electrification of the marine industry, on a global footprint, as well as on sustainability propositions, making E1 Series business proposal to be followed carefully in coming years. We verified as E1 represents a good investment opportunity for Private Equity funds, respecting eight out of ten "standard criteria" that a target company needs to meet in order to be a good candidate for PE investments. Lastly, based on the key findings coming from the first four chapters, we suggested a dashboard of three key actions to implement in order to attract Private Equity funds' interest in a medium-term horizon: strengthening the presence on social media, riding the wave of eSports and implementing data collection tools.

References

A

Accordo con il Manchester United per la cessione definitiva del calciatore Cristiano Ronaldo, Juventus FC press release, August 31st 2021.

Accordo Con Il Real Madrid Per L'acquisizione Definitiva Del Calciatore Cristiano Ronaldo, Juventus FC press release, July 10th 2018.

I. Acero, R. Serrano, P. Dimitropoulos, *Ownership structure and financial performance in European football*, Coporate Governance: The International Journal of Business in Society, 2017.

U. Allenstein, O. Gediehn, S. Lehmann, D. Singer, *Esports as a Sponsorship Asset? What CMOs should know*, McKinsey & Company, June 2020.

An analysis of the working conditions of professional sports players, UNI Global Union, European Commission, 2011.

M. Anis, *Sense, Analyze, Engage: How to Successfully Monetize Your Fan Ecosystem*, Infosys, 2017.

Annual Review of Football Finance 2011: Pressure to Change, Deloitte Sport Business Group, 2011.

C. Arkenberg, D. Van Dyke, J.D. Tengberg, N. Baltuskinis, *eSports graduates to the big leagues. Can the industry help media and entertainment companies access a changing audience?*, Deloitte Sports Consulting, 2018.

Average MLB salary at $4.17 million, down 4.8% from 2019, ESPN, 16th April 2021.

B

D. G. Baur, C. McKeating, *Do Football Clubs Benefit From Initial Public Offerings?*, International Journal of Sport Finance, 2011.

J. Beech, "Finance in the football industry", in S. Hamil and S. Chadwick, *Managing Football: An International Perspective*,2010 Oxford.

J. Blackwell, *Leicester City take out bank loans to help finance new £100m training ground and King Power Stadium expansion*, LeicestershireLive, May 11th 2020.

C. Bollinger, J. Hotchkiss, *The upside potential of hiring risky workers: evidence from the baseball industry*, Journal of Labor Economics, 2003.

F. Bolotny, *Football in France*, In W. Andreff, S. Szymanski, *Handbook on the Economics of Sport*, 2006.

A. Branch, *StubHub! and MLB strike precedent-setting secondary ticketing deal*, TicketNews, August 2nd 2007.

A. Brown, *'Not for Sale'? The Destruction and Reformation of Football Communities in the Glazer Takeover of Manchester United*, Soccer and Society, 2007.

M. T. Brown, D. A. Rascher, M. S. Nagel, C. D. McEvoy, *Financial Management in the Sport Industry,* 2016.

Business Sustainability Risk and Performance Index 2020, EcoVadis, 2020.

C

G. Campanella, W. Ricciotti, *L'investimento in un fondo di private equity: guida al processo di selezione e due diligence*, AIFI, 2012.

S. Chadwick, S. Hamil, *Managing Football. An International Perspective*, 2010.

E. Coutinho da Silva, A. Luzzi Las Casas, *Sport Fans As Consumers: An Approach To Sport Marketing*, British Journal of Marketing Studies, 2017.

K. Collantine, *How the CVC era changed F1 – and what Liberty might mean*, RaceFans, September 8th 2016.

D

C. Demaria, *Introduction to Private Equity, Debt and Real Assets: From Venture Capital to LBO, Senior to Distressed Debt, Immaterial to Fixed Assets*, 3rd edition, 2020.

H. Dietl, E. Franck, *Governance Failure and Financial Crisis in German Football*, Journal of Sports Economics, 2007).

H. M. Dietl, E. Franck, L. Markus, *Overinvestment in team sports leagues: a contest theory model*, Scottish Journal of Political Economy, 2008.

P. Downward, A. Dawson, T. Dejonghe, *Sport Economics. Theory, evidence and policy*, 2009.

G. Dragoni, *Juventus, sul mercato un CR7 bond a 5 anni*, Il Sole 24 Ore, February 13th 2019.

E

E1 Series and PIF announce partnership to create world's first electric powerboat championship, PIF Press Release, June 6th 2021.

Edelman Trust Barometer Special Report: Institutional Investors, Edelman, November 2020.

M. Egan, *Puck Crazy: Is the NHL Recession Proof?*, Fox Business, January 25th 2016.

European PE Breakdown, Pitchbook, 19th January 2021.

F

L. Ferkins, D. Shilbury, *Board strategic balance: an emerging sport governance theory*, Sport Management Review, 2015.

R. Fort, J. Winfree, *Sports really are different: The contest success function and the supply of talent*, Review of Industrial Organization, 2009.

G. Foster, S.A. Greyser, B. Walsh, *The business of sports,* New York: South-Western College Publishers, 2005.

T. Francis, F. Hoefel, *True Gen': Generation Z and its implications for companies*, McKinsey & Co., November 12th 2018.

From Madrid to Turin: Ronaldo Economics, KPMG Football Benchmark, 2018.

G

P. Giorgio, *2021 Outlook for the US Sports Industry*, Deloitte Center for Technology, Media & Telecommunications, 2021.

Global eSports and Live Streaming Market Report, Newzoo, 2021.

Global Private Equity Report 2021, Bain & Company, 2021.

H

S. Hamil, S. Morrow, C. Idle, G. Rossi, S. Faccendini, T*he governance and regulation of Italian football*, Soccer & Society, 2010.

Hockey Central. The Original Six, 1942-43 to 1966-67, National Hockey League

How Sustainability is Fundamentally Changing Customer Preferences, Capgemini Research Institute, July 2020.

J. Hubman, *A Financial Analysis of Publicly Traded Professional Sports Teams*, The College at Brockport: State University of New York, 2011

I

R. Ippolito, L. L. Etro, *Private Capital. Principi e pratiche di private equity e private debt*, 2019.

J

D. Johnson, *Overall Health for Professional Baseball in Trouble*, Wtop News, June 10th 2020.

K

M. Kane, *Stadium Financing Increasingly Using Private Fund Sources*, New York Journal, 1999.

A. Keh, *Many in MLS playing largely for love of the* game, The New York Times, October 26th 2014.

A. King, *The European Ritual: Football in the New Europe*, 2003.

B. Klayman, *High gasoline prices pinch NASCAR fans*, USA today, June 30th 2008.

G. Kratofil, Direct public offerings can fill business' capital needs, Kansas City Business Journal, 1999.

M. Kreidler, *State of uncertainty for women's sports*, ESPN, July 24th 2009.

L

E. P. Lazear, *Hiring risky workers*, in Internal Labour Market, Incentives, and Employment, 1998.

J. Lee, B. Marquard, B. Sniderman, *Embedding trust into COVID-19 recovery*, Deloitte, 2020.

Liberty Media Corporation Agrees To Acquire Formula One, CVC Press Release, September 7th 2016.

Liberty Media Corporation Presentation of Formula 1, November 2016.

J. Lombardo, *A new play for the AFL?*, SportsBusiness Journal, February 25th 2008.

J. Lombardo, D. Broughton, *Going Gray: Sports TV Viewers Skew Older*, *Sports Business Journal*, June 5th 2021.

M. Long, *NBA Top Shot Maker Dapper Labs Secures US$305m in Fresh Capital*, Sports Pro Media, March 31st 2021.

M

V. Matheson, *Caught under a mountain of Olympic debt*, The Boston Globe, August 22nd 2008.

C. D. Merwin, M. Sugiyama, P. Mubayi, T. Hari, H. P. Terry, A. Duval, *Esports. From Wild West to Mainstream*, Goldman Sachs, 2018.

D. Mortlock, C. Kim, A. James, *What If Sport Fans Cut the Cord?*, Bain & Company, 13th October 2020.

S. Morrow, *The New Business of Football: Accountability and Finance in Football*, MacMillan Business, 1999.

S. Morrow, *The People's Game?: Football, Finance and Society*, 2003.

P. Murray, *With The Growth Of Esports, NBA 2K League Is Taking Off*, Forbes, October 11th 2020.

N

D. Newton, *With Ganassi pulling the plug on a team, question remains: Will it getworse?*, ESPN, July 1st 2008.

NFT Yearly Report 2020, NonFungible, February 16th 2021.

J. I. Norris, D. L. Wann, R. K. Zapalac, *Sport Fan Maximizing: Following the Best Team or Being the Best Fan?*, Journal of Consumer Marketing, 2014.

O

C. K. Oh, *Why Are Sports Team IPOs Uncommon?,* Joseph Wharton Scholars, 2019.

M. Orlitzky, *Does firm size confound the relationship between corporate social performance and firm financial performance?*, Journal of Business Ethics, 2001.

M. Ozanian, *The Stadium Revenue Each NFL Team Will Lose If Games Are Played Without Fans*, Forbes, May 18th 2020.

P

PitchBook Analyst Note: Sports Teams and Private Equity Pair Up, PitchBook Data, May 13th 2021.

O. Poindexter, *NFL Locks in $113 Billion for 11-Season Media Right Deals*, Front Office Sports, , March 18th 2021.

M. E. Porter, *How Competitive Forces Shape Strategy*, Harvard Business Review, 1979.

R

D. Rencken, *Revealed: How much F1 teams spend*, Autosport, November 26th 2015.

L. Rickwood, *Sports Scores, Stats and Big Data Analytics Bring Whole New Ballgame*, WhatsYourTech.ca, May 23rd 2018.

D. Russell, *Football And The English: A Social History Of Association Football In England, 1863-1995*, 1997.

S. Roxborough, *Sports Rights Now Make Up 26 Percent of Global Content Spend*, Hollywood Reporter, October 16th 2019.

S

L. Saunders, *Are the Green Bay Packers the worst stock in America?*, Wall Street Journal, 2012.

R. Schaffer, *A piece of the rock (or the rockets): the viability of widespread public offerings of a professional sport franchises*, Virginia Sports and Entertainment Law Journal, 2006.

P. J. Schwartz, R. Williams, *2020 NFL Valuations: National Football League Interactive Franchise Valuations*, Sportico, August 25th 2020.

G. W. Scully, *Pay and performance in Major League Baseball,* American Economic Review, 1974.

M. Scott, *English Premier League sells British TV rights for $7.8 billion*, The New York Times, February 10th 2015.

A. Sherman, J. Young, *NFL Finalizes New 11-year Media Rights Deal, Amazon Gets Exclusive Thursday Night Rights*, NBC Sports, March 18th 2021.

M. Singh, S. Faircloth, *The impact of corporate debt on long term investment and firm performance*, Applied Economics, 2005.

B. Smith, *How different types of ownership structures could save major league baseball teams from contraction*, Journal of International Business and Law, 2003.

A. R. Sorkin, *Henry Paulson Returns to Finance, to Run Climate-Focused Fund*, New York Times, 6th January 2021.

Sports Global Market Report 2021: COVID-19 Impact and Recovery to 2030, Research and Markets.

B. Stewart, A. C. T. Smith, M. Nicholson, *Sport Consumer Typologies: A Critical Review*, Sport Marketing Quaterly, 2003.

C. Sylt, *CVC Becomes Formula One's Most Successful Owner With $4.4 Billion Haul*, Forbes.

R. Szporer, *NHLers by Country: On Top of Their Game and the World*, The Hockey Writers, January 21st 2021.

T

Take-Two hits $3.37bn revenue in record year, gamesindustry.biz, May 18th 2021.

E. Talmor, F. Vasvari, *International private equity*, 2011.

The eSports Playbook, Nielsen, 2017.

The new playbook: How private equity fell in love with sport, Private Equity International, November 3rd 2020.

The Sports Market. Major trends and challenges in an industry full of passion, A.T. Kearney Paris, 2011.

The State of Online Video 2017, Limelight Networks.

Turner Sports Expands Rights Deal with MLB Through 2028, USA Today, September 24th 2020.

V

T. Van Riper, *Where real estate is whacking sports*, Forbes, July 14th 2009.

W

Will 'OTT' Shake Up the Football Broadcasting Industry?, KPMG Football Benchmark, April 15th 2020.

R. Williams, *Nba's 2k Esports League Grows During Pandemic with Eyes on Expansion*, Sportico, January 19th 2021.

R. Wilson, D. Plumley, G. Ramchandani, *The Relationship between Ownership Structure and Club Performance in the English Premier League*, Sheffield Hallam University, Sport Business and Management: An International Journal, 2013.

J. A. Winfree, M. S. Rosentraub, *Sports Finance and Management. Real Estate, Entertainment and the Remaking of the Business*, 2012.

B. Wolverton, S. Kambhampati, *Colleges raised a record $1.26 billion for sports in 2014*, The Chronicle of Higher Education, January 30th 2015.

X

L. Xueming, Z. Jie, D. Wenjing, *Social Media and Firm Equity Value*, College of Business, University of Texas at Arlington, 2013.

Y

J. Young, *NBA is Next Up for a Big Rights Increase, and $75 Billion is the Price*, CNBC, March 22, 2021.

Z

P. Zygband, H. Collignon, N. Sultan, C. Santander, U. Valensi, *The Sports Market. Major trends and challenges in an industry full of passion*, A.T. Kearney, 2011.

Other Sources

CEPRES Market Intelligence.

Enel Foundation.

Fédération Internationale de l'Automobile (FIA).

NACE 9312 – Activities of Sports Clubs, Eurostat.

NAICS 711211 – Sports Teams and Clubs, NAICS Association.

PitchBook analysis.

SMG YouGov.

Sportico.

Sustainable finance taxonomy - Regulation (EU) 2020/852.

UBS Wealth Management Research, 2012.

LUISS

Department of
Business and Management

Chair of Equity Markets & Alternative Investments

Private Equity Investments in the Sports Industry.
E1 Series: How the First-Ever Electric Powerboats Championship Can Attract Funds' Interest.

Prof.

Marco Morelli

SUPERVISOR

Prof.

Guido Traficante

CO-SUPERVISOR

ID: 722731

Lorenzo De Spirito

CANDIDATE

Academic Year 2020/2021

Page intentionally left blank

TABLE OF CONTENT

CHAPTER ONE – OVERVIEW OF PRIVATE EQUITY FUNDS

1.1 Introduction

The term Private Equity (PE) stems for the investment activity in the risk capital of unlisted companies. Historically, this type of investment has always been classified as opposed to liquid investments, typical of regulated financial markets. PE funds are not passive investors, in addition to providing companies with new capital they also take a sit in their boards in order to manage the corporate strategy to reach specific goals, generating the desired return on the investment.

1.2 What do Private Equity funds do?

The objective of the active PE investor is to invest in the risk capital of companies having great potential, and to enhance their assets aiming at divesting within a medium-long term horizon. From the companies' founders' point of view, opening up the risk capital to PE investors generally denotes the willingness to grow thanks to the guidance of professionals, sharing with them any realized capital gain. Other times, especially during the early stages of a company's life, this type of investment is the only way of raising new capital for young companies having no track records, which therefore would not obtain financing from standard financial institutions, such as banks. Within the PE macro-class, we can distinguish three different main sub-classes: Venture Capital, Growth Capital and Leveraged Buoyout (LBO)[1].

1.3 The life cycle of Private Equity funds.

The life cycle of a PE fund is divided into five phases: capital raising, company scouting and investment process, investment management, and exit. The capital raising can be undertaken in two ways: through the management team in the vest of promoter, looking for investors who are willing to commit their financial resources in the fund; or by hiring a placing agent, who has a broader market vision, with specific advisory skills and usually having a strong network of potential investors. The next step corresponds to the portfolio companies' selection process. Three key aspects should be taken into consideration: the amount that is deemed appropriate to be invested considering total capital subscribed by the investors; the temporal sustainability of the investment; and the expected risk-return profile[2]. The investment management phase starts with the fund providing the needed capital to the company and the

[1] R. Ippolito, L. L. Etro, *Private Capital. Principi e pratiche di private equity e private debt*, 2019, pp. 151-153.
[2] G. Campanella e W. Ricciotti, *L'investimento in un fondo di private equity: guida al processo di selezione e due diligence*, AIFI, Commissione rapporti con gli investitori istituzionali, 2012, p. 14.

managers implementing any operational activity to increase the company value: they have to implement strategies to increase revenues or cut costs, possibly both. Lastly, exit strategies are as important as the investment management process, as they both contribute to the PE fund value creation. PE funds that want to exit from an investment have different options. On the private market, a PE fund can sell its stake to a strategic buyer (usually a competitor) or to another financial sponsor (secondary buyout). On the other hand, a PE fund can tap the public financial markets and sell its stake through an Initial Public Offering.

1.4 Covid-19 impact on the Private Equity industry.

Different events taking place in 2020 have put the PE industry to the test. First of all, Covid-19 came in, first in China, then spreading all over the world, impacting the world economy. But many other events undermined global stability: the US presidential elections, tensions between Iran and the US and oil prices plummeting. Despite these, dealmakers did not stop their activity, continuing closing deals while, on the other hand, exits and fund-raising fell in line with five-year averages[3]. If, on the one hand, deal count remained depressed all over the year, on the other hand, deal and exit values reverted back vigorously in Q3 2020. In terms of resources invested, H2 ended up being as strong as any second half in recent PE history.

1.5 Recent trends: the ESG case for PE funds.

ESG (Environmental, Social and Governance) is a broad term that still miss a standard definition and time-tested methodologies to measure either factors' impact or their return on investments. This brings in some skepticism around the theme by Private Equity investors. Despite that, especially in Europe, ESG factors are being demanded by a growing number of funds: globally, 88% of funds are using ESG performance indexes to make investment decisions, while 87% of them said they are rewarding those company that are reducing their short-term return on capital to reallocate resources to ESG initiatives[4]. One of the reasons why European PE firms, instead of US ones, are plotting the route towards ESG investing is because of regulators. The European Commission recently established the EU Taxonomy, taking effect in December 2021, a classification system establishing the conditions an economic activity has to meet in order to be qualified as environmentally sustainable[5].

[3] *European PE Breakdown*, Pitchbook, 19th January 2021.
[4] *Edelman Trust Barometer Special Report: Institutional Investors*, Edelman, November 2020.
[5] Sustainable finance taxonomy - Regulation (EU) 2020/852.

CHAPTER TWO – OVERVIEW OF THE SPORTS INDUSTRY.

2.1 Sports Industry Overview.

Despite its relevance in today's world economy, there is not yet a standard definition of what the Sports Industry is. It is perceived as one of the most heterogeneous industry, both for its composition and for the business models of the key players shaping the market. From a broader point of view, the Sport Industry consists in selling sports services and related contents by teams, clubs and athletes offering the audience a show to be enjoyed. Talking about key financials, the global Sports market is expected to grow from $388 billion in 2020 to $441 billion in 2021 at a compound annual growth rate (CAGR) of 13.5%, while it is expected to reach $600 billion in 2025 at a CAGR of 8.0%[6].

2.2 Key Players and Forces Shaping the Sport industry.

In the next pages we are going to assess the attractiveness of the Sport industry according to the Porter's five forces model[7]:

- Competitive Rivalry: we can assess it from three different points of view: between clubs belonging to the same league, between leagues belonging to the same sport, and between different sports. It is in the nature of the leagues themselves to make clubs competing against each other. Clubs are in competition for different reasons, from increasing the heritage and track-record of the clubs, to increasing their financial performance. Regarding competition at leagues level, it is in the best interest of each league within the same sport to increase their prestige to attract an ever-growing share of interests and consequent investments. Lastly, regarding competition among different sports, Football is king with almost a 50% share of the global Sport Event market, followed by US football, Baseball, Formula 1, Basketball, Hockey, Tennis and Golf[8], and the competition is mainly driven by the media rights, ticketing and merchandising revenues stream.
- **Threat of New Entrants**: it strictly depends on the different regulation ruling each of the leagues. For example, the potential threat of new entrants in the Football industry is very limited: any league has a limited number of spots, so every year a limited number of clubs can participate and if a new club wants to enter the top league it would have to start from the lowest league.

[6] *Sports Global Market Report 2021: COVID-19 Impact and Recovery to 2030*, Research and Markets.
[7] M. E. Porter, *How Competitive Forces Shape Strategy*, Harvard Business Review, 1979.
[8] *The Sports Market. Major trends and challenges in an industry full of passion*, A.T. Kearney Paris, 2011.

- **Bargaining Power of Suppliers**: in the context of sports, two main suppliers are the athletes (they are at the core of the Sports Industry and can be regarded as "content provider"), and media companies. Clubs have faced over the years an increase in athletes' bargaining power, especially in the form of salary and benefits increase, both in the US and Europe. On the other end, broadcasters represent a double threat for clubs and leagues owners: on the one hand, the broadcasting of sport events may be seen as a substitute to the sale of stadium tickets; on the other hand, sports have become more and more dependent on the media revenue stream, shifting the bargaining power towards broadcasting companies[9].
- **Bargaining Power of Customers:** differently from other industries, here we can define a main, unique cluster of customers: fans. The primary aim of any sports club is to attract and retain the highest possible number of fans, as they usually are the ones contributing the most to ticketing, merchandising and media revenues. Anyway, given their high fragmentation, fans do not represent a serious threat for Sports organization.
- **Threat of Substitutes:** the threat of potential substitutes in the Sport Industry evolves from two different angles: first, within the Sport Industry itself; then, outside the Sport Industry. Inside the Sport Industry, and within the same sport practice, each league or championship represent a potential substitute for other leagues; moreover, each sport practice represents a potential threat for other sport practices. Outside of the Sports Industry, players have to deal with a main threat: eSports, grounded on a massive market size, globally reaching $950 million in 2020 and expected to hit the $1.1 billion figure in 2021, with over 75% of the revenues coming from media rights and sponsorship[10].

2.3 Recent Trends and Key Challenges Impacting the Sports Industry.

During 2020 the global pandemic hit the Sports Industry as no external force had never done before. Countermeasures taken by governments and restrictions on event attendance, such as current limits on stadium capacities, are still in place in 2021 and likely to be extended in 2022 seasons. Then, sports organizations' priority is to identify new revenue drivers that can help in stabilizing their cash flows and financial profiles. On the back of recent trends, the Sports Industry is presented with two key challenges: expanding revenue generating sources, offsetting the loss of "traditional" revenue streams; and redesigning the relationship with fans, in order to overcome current limits on stadium attendance and fans' gatherings.

[9] P. Downward, A. Dawson, T. Dejonghe, *Sport Economics. Theory, evidence and policy*, 2009, p. 292.
[10] *Global eSports and Live Streaming Market Report*, Newzoo, 2021.

CHAPTER THREE – FINANCIALS OF THE SPORTS INDUSTRY.

3.1 Economic and Financial Forces Impacting the Sports Industry.

Among the different factors influencing the economics of Sports, four of them must be watched out closely: the economic cycle, the television and broadcasting market, the real estate market, and sustainability issues. The economic cycle, made up of four different phases (growth, peak, recession and recovery) has a strong influence on the Sports Industry: as the economy flows through the different stages of growth and contraction, the Sports Industry experiences flourishing periods alternated with downturns. Another important factor in Sports finance is television and broadcasting revenue. It is a guaranteed form of revenue, with long-term contracts in place between leagues, conferences, teams and networks: television revenues somewhat insulate the industry from short-term slowdowns in the economy, such as during the recession of 2007–2009[11]. Continuing, the development of real estate surrounding stadiums and sport venues has become one of the way sports organizations generate additional revenues. A major part of the fans' experience is the game itself played on the field, but the full enjoyment of the match is more and more linked to the inclusion of numerous amenities in the stadium, letting fans to enjoy a three hundred- and sixty-degrees experience. Last but not least, sustainability is one of the most important themes driving todays' economic policies and interventions, and as such it influences strategies and decisions at Sports Industry level too.

3.2 Ownership Structures and Financial Performance.

When analyzing key financials behind a sports team or league it is very important to start by understanding its ownership structure, as it has major implications in tax, economics and legal obligations. Team owners can choose among several structures, including sole proprietorships, partnership, limited liability corporations, governmental and non-profit. At each ownership structure different pros and cons correspond. In the US professional sports, most teams are operated as for-profit businesses structured according to various ownership models[12]. The three most common are: private investor, multiple owners and corporations[13]. At leagues level, in principle, a league may be structured according to two different models: the single-entity ownership model and the distributed club ownership model[14]. On the other hand,

---

[11] M. T. Brown, D. A. Rascher, M. S. Nagel, C. D. McEvoy, *Financial Management in the Sport Industry,* 2016, p. 46.
[12] M. T. Brown, D. A. Rascher, M. S. Nagel, C. D. McEvoy, *Financial Management in the Sport Industry,* 2016, p. 37.
[13] G. Foster, S.A. Greyser, B. Walsh, *The business of sports,* New York: South-Western College Publishers, 2005.
[14] G. Foster, S.A. Greyser, B. Walsh, *The business of sports,* New York: South-Western College Publishers, 2005.

the European Sports Industry presents different ownership structures as compared to the US one, especially when it comes to Football. For example, since its inception in 1992, the English Premier League has been mainly characterized by three different ownership models: the stock market ownership model, the supporter trust ownership model and the foreign investor model of ownership. The Sheffield Hallam University conducted an interesting study analyzing the relationship between ownership structures and club performance in the English Premier League, investigating the effect of different ownership model on clubs' financial and sporting performance. The main findings suggest that the stock market ownership structure performs better from a financial perspective as compared to the private ownership model, both domestic and foreign, and from a sporting perspective only relative to domestically owned Football clubs. The fact that clubs floating on the market outperforms the others from a financial perspective might be explained by the financial discipline imposed by the stock exchange on listed companies (as well as clubs).

In the other top-four European Football leagues (Italian Serie A, French Ligue One, German Bundesliga and Spanish La Liga) there are other legal structures that are peculiar to their legal frameworks. In Italy, for example, professional Italian Football clubs are in general controlled either by wealthy individuals and families, or (indirectly) through corporate groups. In Germany, since 1998, Football clubs have been permitted to incorporate as a subsidiary of the member association. This subsidiary company is constituted as a limited company or even a public limited company[15]. Although German football clubs can list on the stock market, the ultimate ownership and decision-making power remains under the control of the member association, retaining 50 per cent plus one vote of the incorporated Football club[16].

3.3 How to Finance a Sport Organization.

Any club or sports organization that want to raise capital has five main options at its disposal. The first three options belong to the "traditional" finance and are accessible to any company: debt financing, equity financing and retained earnings. The latter are more peculiar of the Sports Industry and are government funding and gifts.

Debt financing is the most widespread and preferred capital raising solution in the Sports Industry, also considering both pros and cons. Sports organizations willing to issue new debt to raise capital can chose among various options belonging to the "traditional" finance:

---

[15] S. Chadwick, S. Hamil, *Managing Football. An International Perspective*, 2010, p. 30.

[16] H. Dietl, E. Franck, *Governance Failure and Financial Crisis in German Football*, Journal of Sports Economics, 2007), p. 665.

corporate loans, project financing, forward funding future revenue streams, corporate bonds, mini bonds and private placements.

Sports organizations that want to raise new capital, beyond doing it through debt financing, can decide to access the equity market. Equity capital is raised through the issuance of new shares, either in the form of common stock or preferred equity, representing a portion of the club's ownership. In particular, companies that are privately owned (i.e., whose shares are not listed on a stock exchange) have access to the equity financing through the Initial Public Offering (IPO). Anyway, IPOs are not a common way to raise capital in the Sports Industry, and its unpopularity suggests that professional sports team do not benefit from listing their shares (as it happens on average in other industries), and this can be verified through three lenses: managerial, operational and financial disincentives[17]. For example, some studies found that most clubs perform worse after going public[18], while others show that European listed Football clubs increased their average points per game by 0.078, that for an average season of thirty-eight games, implies 2.964 additional point on the final standings[19]. Considering the above, private sports organizations owners do not find listing their clubs an attractive capital raising option over debt financing.

In addition, leveraging in their social impact, sports organizations benefits from other two additional capital raising solution: government funding and gifts.

3.4 Capital Budgeting and Investments Decisions in Sports Organizations.

Capital budgeting, in particular, is the process through which sports organizations assess, evaluate and select investment opportunities that are consistent with their values, vision, mission and overall corporate strategy. Investments can be compared by referring to their risk profile and expected rate of return. One way to assess it is based on averages of past results, using the following formula (where r_E is the expected rate of return, r_j is the return in year j, across a time period of n years):

$$r_E = \frac{\sum_{j=1}^{n} r_j}{n}$$

Once the expected return over a future time period has been estimated, next step is integrating this metrics with some risk indicators. Usually, risk related to the expected return is linked to the variability of future performance (hence, the variability of the return itself). The

[17] C. K. Oh, *Why Are Sports Team IPOs Uncommon?,* Joseph Wharton Scholars, 2019, p. 6.
[18] D. G. Baur, C. McKeating, *Do Football Clubs Benefit From Initial Public Offerings?*, International Journal of Sport Finance, 2011, pp. 40-59.
[19] C. K. Oh, *Why Are Sports Team IPOs Uncommon?,* Joseph Wharton Scholars, 2019, pp. 8-23.

most common type of risk for sports teams is the risk of player performance, as team revenues change drastically depending on how players perform[20]. Apart from risk sources peculiar to the Sports Industry, a team also faces other sources of risk shared in common with other industries, such as the market risk. One measure of risk is the standard deviation, representing a measure of dispersion, hence risk. Usually, given investors' risk aversion, between two investments with the same expected return but one having a lower standard deviation, then the latter is preferred.

3.4.1 Real Estate Investments: Ranking Investment Options through NPV and IRR.

When investing in facilities, sports managers have to carefully assess the financial feasibility of different options, and this is usually done by using two different metrics: the Net Present Value (NPV) and the Internal Rate of Return (IRR). The starting point to assess the NPV of an investment is identifying the cashflow linked to it. Then, identified cash inflows must be discounted at a proper discount rate in order to find their present value, net of any discounted cash inflow:

$$NPV = CF_0 + \sum_{t=1}^{n} \frac{CF_t}{(1+r)^t}$$

The main issue of assessing an investment NPV is finding the right discount rate, as in doing this the amount of risk involved in the discounted cashflows should also be accounted for (i.e., cashflows uncertainty). One way to assess the right discount rate is by using the Capital Asset Pricing Model (CAPM), whose theory is behind the scope of this study. To rank different investment options, an alternative to the NPV is the IRR. The Internal Rate of Return is the discount rate that gives the investment a NPV equal to zero, and the rule suggests opting for those investment opportunities whose IRR is higher than the cost of capital, so that through the investment value is created.

3.4.2 Investing in Players' Transfers.

Sports organizations core business take place in stadiums, arenas and circuits, so the most important investments for teams are their players and athletes. To assess investments in players the rationale of expected returns and risk still applies, but there are some other basic financial concepts that can help in choosing which player to invest in. The concept of Marginal Revenue Product (MRP) is at the basis of estimating an athlete's value. To understand what the MRP represents, two more basic concepts must be introduced: the marginal product and

[20] J. A. Winfree, M. S. Rosentraub, *Sports Finance and Management. Real Estate, Entertainment and the Remaking of the Business*, 2012, p. 380.

marginal revenue. The marginal product is the additional units of output a worker produces, while marginal revenue corresponds to the revenue generated by one additional unit of output[21]. Starting from the marginal product, players and teams' objective is to win games (or races, in the case of Motorsports). Therefore, the marginal product of an athlete corresponds to the number of additional wins he contributed to.

3.4.2.1 Player Contracts.

Player contracts take different characteristics depending on the sports, but some basic and common aspects are shared among them. What is critical when evaluating contracts is their present value, keeping in mind that usually contracts signed between athletes and clubs are multiyear. In assessing the contract value it is important to keep in mind the time value of money, as players and team owners have contrasting interest in structuring contracts: on the one hand, players prefer "front loading" their contracts, as it is more convenient to receive higher amounts in the initial years rather than in the future, given that this will increase the contract's present value; on the other hand, team owners usually try to "back load", meaning that they prefer paying players more at the end of their contracts to reduce their present value.

3.4.2.2 Option Value for Players: the Benefits of Flexibility.

In the traditional finance, an option is something that provide an investment with flexibility. There are two main types of options: call options, the option to buy an asset at a pre-specified price at a given date in the future; put options, the option to sell an asset at a pre-specified price at a given date in the future. Many players have a type of option, in that many of them can cover different roles. Because of the uncertain nature of sports, teams always like to have options and if a team is hiring a player, it is helpful to be able to quantify these options[22].

3.4.2.3 Players' Sporting Performance: Why Clubs Enjoy Taking Risk?

Some studies suggest that sports team, given the same expected return among investment options, often prefer to sign riskier players (like injury prone, or whose performance varies a lot)[23]. A possible explanation of why sports team usually prefer signing risky players is that sports teams face a unique revenue structure. Typically, when a firm produces more

[21] G. W. Scully, *Pay and performance in Major League Baseball,* American Economic Review, 1974, pp. 915–930.
[22] J. A. Winfree, M. S. Rosentraub, *Sports Finance and Management. Real Estate, Entertainment and the Remaking of the Business*, 2012, pp. 394-395.
[23] C. Bollinger, J. Hotchkiss, *The upside potential of hiring risky workers: evidence from the baseball industry*, Journal of Labor Economics, 2003, pp. 923–944.

goods, the additional revenue from producing the goods decreases, and there are diminishing marginal returns. If teams are producing wins, then this might not be the case. Let's think of these alternatives for sports teams. Would a team rather have a medium record every year, or finish in last place half of the time and win a championship half of the time. Given how fans respond to team quality, their revenues might be higher if their win/loss record varied from year to year. Obviously, teams want to win every year, but given their constraints, they might be better with a 50% chance of winning and a 50% chance of losing, than a 100% chance of winning just half their games[24]. If that is true, a direct consequence would be sports team having an increasing marginal revenue curve, and this might be the reason why they prefer hiring risky players[25].

3.5 Emerging Revenue Sources: Four Ways to boost a Sports Organization's P&L.

Professional sports league, together with participating teams, are constantly looking for emerging revenue sources to address specific financial needs. Among the others, recent trends suggest that team owners can leverage on four emerging revenue sources: ticket reselling, luxury seating, seat licenses and variable ticket pricing. Evidence suggests that seasons ticket and one-game tickets are increasingly being sold on secondary markets. Ticket reselling has evolved into a structured and regulated business, with lots of teams and leagues having already recognized its importance, most of them trying to be involved in. For example, in 2007 StubHub signed a contract to be MLB's exclusive secondary ticket reseller[26]. Luxury tickets have become an important revenue driver for teams. Luxury suites and club seats are part of a growing trend to attract higher-end customers, who can afford to pay for exclusive access to certain areas of the facility[27]. Another recent trend linked to stadium attendance and to the move towards high-priced seating is the use of personal seat license: it is the right, bought after paying a one-time fee, to purchase tickets for a specific seat, either for a limited or permanent time frame. Like season tickets, they can provide teams with huge upfront cash inflows. Lastly, as market research and technology in sports have improved, more franchises are employing variable ticket pricing (VTP) to capture added revenues by increasing initial ticket prices for highly demanded games and decreasing ticket prices for lower-demanded games, in an effort to attract customers

---

[24] J. A. Winfree, M. S. Rosentraub, *Sports Finance and Management. Real Estate, Entertainment and the Remaking of the Business*, 2012, pp. 395-396.
[25] R. Fort, J. Winfree, *Sports really are different: The contest success function and the supply of talent*, Review of Industrial Organization, 2009, pp. 69–80.
[26] A. Branch, *StubHub! and MLB strike precedent-setting secondary ticketing deal*, TicketNews, August 2nd 2007.
[27] M. T. Brown, D. A. Rascher, M. S. Nagel, C. D. McEvoy, *Financial Management in the Sport Industry*, 2016, p. 519.

who would not attend at the "typical" price. VTP has proved profitable for many sport franchises, who are now replacing it in some cases with dynamic ticket pricing, in which the ticket price is altered instantly (like stocks on a stock exchange) as demand increases or decreases[28].

CHAPTER 4 – PRIVATE EQUITY & THE SPORTS INDUSTRY. THE FORMULA 1 CASE.

4.1 Introduction

The huge amount of funds gathered by PE funds in recent years has been looking for alternative asset classes that are able to generate potentially high returns. Among the different options, the Sports Industry is being more and more successful in attracting PE investments. Sports is an appealing landscape for investors as owners of sports franchises have benefitted from huge returns in the past years. For example, NBA, MLB and NFL in the US have all seen their valuations skyrocketed, outpacing the S&P 500 over the past 20+ years[29].

4.2 Investment Thesis & Main Risks behind PE Investments in the Sports Industry.

First and foremost, what makes sports organizations financially attractive is their ability to lock-in huge media rights revenues. In fact, Sports is one of the biggest content-creator machines, especially when it comes to live events, and with the entertainment industry shifting from traditional broadcast to on-demand and streaming services, this gives Sports a competitive advantage over other emerging industries. In general, the return prospects are compelling, with minority stakes investors targeting 15% to 20% gross annual returns. Most owners (majority or minority) buy in at low-single-digit cash flow yields and see double-digit appreciation. Among all, the investment thesis is supported by five key drivers[30]: portfolio diversification, minority and illiquidity discounts, scarcity of sports teams, flourishing media rights deals, sports betting and Nonfungible tokens (NFTs). On the other hand, PE funds investing in sports organizations are exposed to a series of risks, among the others: lower leagues relegation, leagues shutdowns, and generational changes. Private Equity investors willing to invest money in the Sports Industry can chose among different investment options, ranging from franchises in the NBA, NFL, MLB, MLS and NHL, if they seek opportunities in the US, to European Football teams, most likely the ones taking part in the top-five leagues, if they look for investment opportunities in Europe. On top of that, PE investors can also decide to buy stakes in Motorsports franchises.

---

[28] *Idem*, p. 520.
[29] Data from Sportico.
[30] *PitchBook Analyst Note: Sports Teams and Private Equity Pair Up*, PitchBook Data, May 13th 2021, p. 5.

4.3 The Formula 1 Case Study: CVC and Liberty Media Group Deal.

When it comes to past Private Equity investments in the Sports Industry, most of the time it also comes to CVC, one of the biggest players in the PE industry and one of the most active in the field of Sports. Among the others, CVC completed a remarkable investment when it first bough (in 2006) and then sold (in 2016) a stake in the most famous Motorsport championship, Formula 1 (thereinafter also F1).

CVC structured F1 acquisition under a leveraged buoyout, funding the acquisition with $965.6 million from CVC's investment Fund IV and a $1.1 billion loan. Ten years after the acquisition, in 2016, CVC sold its stake in Formula 1 to the entertainment company Liberty Media Group, completing one of the most successful investment in the fund's history, embodied in a 351.8% ROI[31]. Liberty Media's offer resulted in a $8.0 billion Enterprise Value for Delta Topco, the parent company of Formula 1. Considering the $3.4 billion net debt and $0.2 billion deal-related adjustments, the Equity value amounted to $4.4 billion, an extremely huge increase the price paid by CVC to acquire F1 ten years earlier. The selling shareholders, guided by CVC, were entitled to receive a mix of cash, subordinated exchangeable note and Liberty Media's shares. Liberty Media Group had a very strong investment thesis, supported by five key pillars: F1 being a unique global sport entertainment business, a rising market for premium sports rights, clear revenue growth trends coupled with significant profitability and cash-flow conversion, multiple areas for future upside potential and, lastly, a low-risk business model with high revenue visibility. Moreover, to support Liberty Media Group investment thesis were also five key drivers of future upside potential, namely[32]: race promotion, broadcasting revenues, advertising and sponsorship revenues, digitalization, and expanding the franchise.

CHAPTER 5 – E1 SERIES: HOW TO MAXIMIZE VALUE AND ATTRACT PRIVATE EQUITY FUNDS' INTEREST[33].

5.1 E1 Series: Water, Electrified. What this Championship is about and How does it Work?

In this chapter, the last one of this study, we are going to deep dive into one of the most prominent championship in the Motorsports arena: E1 Series, the first sustainable powerboat championship, born with the objective of increasing the awareness and positively impacting the

---

[31] C. Sylt, *CVC Becomes Formula One's Most Successful Owner With $4.4 Billion Haul*, Forbes.

[32] Liberty Media Corporation Presentation of Formula 1, November 2016, p. 9.

[33] All relevant information and key data about E1 Series from investors presentation decks, kindly provided by E1 Series CEO Mr Rodi Basso and CFO Mr Richard Draisey.

conservation of the seas and oceans. E1 Series is set to kick-off its first season in March 2023, and will be composed by ten to twelve teams, each one having one pilot racing at a time on a 100% electric powerboat. The first aim of the two founders, Alejandro Agag and Rodi Basso, is to build a sports platform to fill the gap in the maritime mobility. E1 Series sample calendar is developed around ten events per season, with races being run across the globe between five European hosting cities (London, Geneva/Zurich, Naples, Monaco and Barcelona) and five remote races (Greenland, New York, Miami, Amazon and Middle East). The geographical spread of E1 will give the championship a competitive advantage, giving the opportunity to leverage on a global reach as it already happens, for example, in Formula 1. Lastly, a key strength point of E1 Series is represented by the people involved in the project, making up a team that can leverage on high expertise in Motorsports. Among the others: Alejandro Agag (Founder and Chairman), already founded Formula E Holdings and the new FIA Formula E Championship[34]; Rodi Basso (Co-Founder and CEO, who joined Motorsports in successful Formula 1 teams like Ferrari, Red Bull Racing and McLaren Racing.

5.2 Key Revenue Drivers: Media Rights, Sponsorships, Participation and Hosting Fees.

From a financial point of view, E1 Series is strongly supported by four key revenue drivers, with the opportunity to further expand them through "lateral" streams, as it will be analyzed later on. In particular, the four P&L pillars are the followings: media rights, sponsorship, participation fees and hosting fees. Starting from media rights, E1 Series will be leveraging on a wide fan base, targeted into five key groups: sports enthusiasts, people passioned about sports that enjoy following different leagues and championships (1.1 billion individuals, 56% male and aged 44 on average); tech enthusiasts, people interested in newest technological developments, always trying to keep themselves up to date (109 million in total, 56% male and aged 35 on average); Racing enthusiasts, people that love Motorsports, enjoying championships such as Formula 1, MotoGP or WSBK (145 million fans, 65% male on average 38 years old); Ocean conservationists, people really keen on climate change-related issues (259 million people, 51% female and aged 36 on average); Gen Z, those people born in between 1995 and 2010[35], digital natives who respect brands telling a true story, and their consumption habits express their identity (2.4 billion individuals, with a 50/50 gender split). The second key revenue driver is represented by sponsorship contracts. When it comes to sponsorships and

[34] Biography of Alejandro Agag from the *Fédération Internationale de l'Automobile* (FIA) website.
[35] T. Francis, F. Hoefel, *True Gen': Generation Z and its implications for companies*, McKinsey & Co., November 12th 2018.

advertising, to sign good deals E1 Series can leverage on a key strength point: sustainability. It is already known that consumers are more and more rewarding those companies that commit themselves to sustainability related topics. Hence, corporation will have a huge incentive in partnering with E1. The third revenue stream is represented by participation fees paid by the teams. E1 will be structured according to a franchise model where any team will pay an entry fee equal to €2 million (owning a 25-year long license) and a yearly running fee equal to €1 million. Last but not least, the fourth key revenue driver is represented by the hosting city fee. Cities across the globe will have huge incentives in hosting the E1 races, as it will be more than just a race, bringing to hosting cities an "Electric and Mobility Festival", taking place during the week leading up to the E1 event, providing the right platform to showcase the commitment to sustainable urban mobility.

5.3 Suggested Key Actions to Pursue Value Maximization and attract PE funds.

The aim of this research, after having gone through the PE and Sports Industry, the aim of this research is to suggest possible way to increase E1 Series value and attract PE funds' interest, besides the "standard" requirements for a target company to be appealing from a PE fund point of view. Hence, we now deep dive into a dashboard composed by three suggested actions: strengthening the presence on social media, riding the wave of eSports and implementing data collection tools. All of them are based on recent trends in the Sports and Private Equity Industries, as analyzed in previous chapters.

- Key Action #1: Strengthening the Presence on Social Media**.** The first suggested action corresponds to strengthening the social media presence. As already discussed, the pandemic has had a huge effect on the relationship between sports teams and fans. Thus, sports organizations are now forced to reinvent the way through which they engage with fan, providing both online and offline solutions. In particular, social medias are the preferred online platforms for fans that want engage with sports organizations (among the others). Thus, for E1 Series strengthening its presence on social medias is a key point in order to first gain a competitive advantage, and then secure a premium when it comes to valuation. Literature suggests a strong correlation between the presence on social media and firm equity value, thus showing that investors are ready to pay a premium for those companies having built a strong presence on online channels[36].

[36] For example, see L. Xueming, Z. Jie, D. Wenjing, *Social Media and Firm Equity Value*, College of Business, University of Texas at Arlington, 2013.

- Key Action #2: Riding the Wave of eSports. As previously analyzed, eSports represents a huge opportunity for any sports organization looking for additional revenue stream. eSports represents a huge opportunity of diversification for E1 Series, both from an operational and a financial point of view. From an operational point of view, eSports enriches the E1 project and provides its fans with a broader array of challenges to enjoy. In particular, eSports can be implemented following two different strategies: by developing a video game to be sold on the market, simulating the "offline" powerboats races, or in an alternative (or on top of selling its own video game) E1 Series can introduce a parallel championship based on virtual reality, structured around the following key points. Moreover, owning a parallel virtual championship can represent a huge opportunity for future strategic decisions: if successful, the eSports E1 Series can be spun off from the "offline" championship and sold to private investors, being a way for the founders to monetize the initial investment, but still owning the control over the "core-business", i.e., the "offline" E1 Series championship.
- Key Action #3: Implementing Data Collection Tools. As investigated throughout this research, data collection is one of the key trends in the Sports Industry that is attracting investments from Private Equity firms. In particular, collecting data can be beneficial to E1 Series' P&L in multiple way. On the one hand, data can be collected and monetized by being sold to multiple stakeholders. On the other hand, data collection can be beneficial to improve the performance of the RaceBird powerboats, as well as to improve technological developments about the electrification of the marine industry.

References

B

D. G. Baur, C. McKeating, *Do Football Clubs Benefit From Initial Public Offerings?*, International Journal of Sport Finance, 2011, pp. 40-59.

A. Branch, *StubHub! and MLB strike precedent-setting secondary ticketing deal*, TicketNews, August 2nd 2007.

M. T. Brown, D. A. Rascher, M. S. Nagel, C. D. McEvoy, *Financial Management in the Sport Industry*, 2016, p. 46.

C

G. Campanella e W. Ricciotti, *L'investimento in un fondo di private equity: guida al processo di selezione e due diligence*, AIFI, Commissione rapporti con gli investitori istituzionali, 2012, p. 14.

S. Chadwick, S. Hamil, *Managing Football. An International Perspective*, 2010, p. 30.

D

P. Downward, A. Dawson, T. Dejonghe, *Sport Economics. Theory, evidence and policy*, 2009, p. 292.

H. Dietl, E. Franck, *Governance Failure and Financial Crisis in German Football*, Journal of Sports Economics, 2007, p. 665.

E

European PE Breakdown, Pitchbook, 19th January 2021.

Edelman Trust Barometer Special Report: Institutional Investors, Edelman, November 2020.

F

R. Fort, J. Winfree, *Sports really are different: The contest success function and the supply of talent*, Review of Industrial Organization, 2009, pp. 69–80.

G. Foster, S.A. Greyser, B. Walsh, *The business of sports*, New York: South-Western College Publishers, 2005.

T. Francis, F. Hoefel, *True Gen': Generation Z and its implications for companies*, McKinsey & Co., November 12th 2018.

G

Global eSports and Live Streaming Market Report, Newzoo, 2021.

I

R. Ippolito, L. Etro, *Private Capital. Principi e pratiche di private equity e private debt*, 2019, pp. 151-153.

L

Liberty Media Corporation Presentation of Formula 1, November 2016, p. 9.

O

C. K. Oh, *Why Are Sports Team IPOs Uncommon?*, Joseph Wharton Scholars, 2019, p. 6.

P

PitchBook Analyst Note: Sports Teams and Private Equity Pair Up, PitchBook Data, May 13th 2021, p. 5.

M. E. Porter, *How Competitive Forces Shape Strategy*, Harvard Business Review, 1979.

S

G. W. Scully, *Pay and performance in Major League Baseball*, American Economic Review, 1974, pp. 915–930.

Sports Global Market Report 2021: COVID-19 Impact and Recovery to 2030, Research and Markets.

C. Sylt, *CVC Becomes Formula One's Most Successful Owner With $4.4 Billion Haul*, Forbes.

T

The Sports Market. Major trends and challenges in an industry full of passion, A.T. Kearney Paris, 2011.

W

J. A. Winfree, M. S. Rosentraub, *Sports Finance and Management. Real Estate, Entertainment and the Remaking of the Business*, 2012, p. 380.

X

L. Xueming, Z. Jie, D. Wenjing, *Social Media and Firm Equity Value*, College of Business, University of Texas at Arlington, 2013.

Other sources

Sustainable finance taxonomy - Regulation (EU) 2020/852.

Data from Sportico.

Fédération Internationale de l’Automobile (FIA).