

Beware Of The Boom

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The new head of our Sports Ventures Unit looks at some of the unique issues which must be tackled by sports businesses in an improving market if they are to succeed.

Sport is not just an activity in which people participate for personal enjoyment, it is a global business turning over several billion pounds a year. And business is picking up. Advertising drives the business of sport and, after enduring a “bath shaped” recession in recent years, all forecasts for the advertising sector predict significant growth in 2005. Tax breaks for investors, the increasing attraction of fast growing markets such as AIM together with the general excitement always created by sport are also contributing to increased financing, acquisition and investment activity in the sector.

However, whilst this increased activity will mean increased opportunities for some sports businesses, it could also mean increased risk, with the echoes of the bust which followed the last boom in sport still resounding through the industry. Building a business in any sector is a challenging exercise, but the unique characteristics of the sports sector present an additional set of challenges to those working within it, even when things are looking up. As every novice sailor is taught, a boom can knock the unwary overboard.

Having said that sports businesses face unique challenges, they do share their fundamental objectives with businesses in other sectors. Maximising the success of the business and the rewards to its stakeholders is the universal goal. In the short term, that means seeking to maximise profits. The longer term life-cycle of the business could involve expansion, either organically or by the acquisition of other businesses. Borrowing or new equity investment could be required to fund such expansion. At all of these stages risks will have to be taken but should be carefully considered and managed. Ultimately, the business might be disposed of to a private buyer or to the public.

However, additional issues faced by many businesses in sport can complicate matters. For example, if the business is essentially a sports team its customers are unlikely to simply switch brands if they no longer enjoy the product (e.g. if the team falters). Such customer loyalty might be the envy of businesses in other sectors but can also mean that the customers feel that they have at least as much of a stake in the business as its actual owners. Even if the “product” is a good one (i.e. if the team is successful), customers may still feel entitled to object to the way the business is run, how it is structured or by whom it is owned (as Malcolm Glazer is presently learning). Therefore, such sports

businesses may have to take into account the views of its customers, not only in terms of the “product”, but also when taking decisions on issues of structure, ownership and internal governance.

Further, as well as the law of the land businesses in the sports sector will often have to comply with a raft of secondary regulation issued by an industry regulator (e.g. a sports governing body). Whilst such regulation is designed to safeguard the industry as a whole, it may hinder the ability of particular businesses to succeed or even survive (for example, recently proposed UEFA rules on “homegrown” players or English football’s points penalties for clubs entering administration). As the financial or other penalties that could be imposed upon a business which contravenes such regulations could turn success into failure, a detailed knowledge of them is essential.

The vast majority of businesses in the sports sector do not participate directly in sport though, but instead exploit a product derived from broadcast/media coverage or other means of exploitation or association with particular sports or participants. These businesses face other issues. The available properties (or at least those from which significant revenues can be generated) are relatively limited and, with the exception of an even more limited number of elite properties, are susceptible to fluctuations in popularity which can be much more rapid and pronounced than products in other sectors. Therefore, access to a diverse range of lucrative sports properties is highly desirable. However, relatively few businesses within the sector can boast such a portfolio themselves. In reality, most businesses in the sector are small to medium sized, owner-managed businesses, and those which focus on a single sport are highly exposed to the vagaries of the market. Consolidation of businesses by acquisition or “merger” therefore becomes increasingly attractive and this trend is likely to become more prevalent in 2005.

With increased public ownership of sports businesses and other “stakeholders” taking an increasingly active interest in them as described above, accountability has become an increasingly important issue. Therefore, many sports businesses (especially those in the media spotlight or connected with “quasi-public” governing bodies) are under growing pressure to improve their internal governance. However, whilst many sports businesses are high-profile, even the largest of them are relatively small when compared with other sectors - the annual turnover of Manchester United plc, “the world’s richest football club”, is not much greater than a large branch of Tesco. Therefore, although such businesses are under pressure to adopt cumbersome and expensive operating and corporate governance practices and engage high-priced advisers more suitable for a blue chip plc, this is often simply uneconomical. However, the adoption of sensible practices and obtaining appropriate professional advice is essential, as losses caused by bad management or excessive risk-taking which may be sustainable in other sectors may be fatal to businesses in sport.

Therefore, whilst businesses in the sector face the same basic issues as those in other sectors, the peculiar environment in which they operate must constantly be taken into account. The accepted wisdom and methodology applicable to the development of businesses in other industry sectors cannot simply be replicated wholesale in the sports sector (as football’s experience with flotations and securitisations in recent years has demonstrated). Consequently, whether they are executives or advisers, people working in the sports marketplace need to be not only well-versed in general

principles of finance, commerce and law, but also alive to the issues peculiar to sport that can be crucial to the success or failure of a sports venture.

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