

## Insight

### SPORTS BRANDS AND BRAND EQUITY

Now that the dust has settled on a controversial but successful FIFA 2018 World Cup and the French team enjoys the celebrations we can reflect on the event and what aspects are relevant to our investment world.

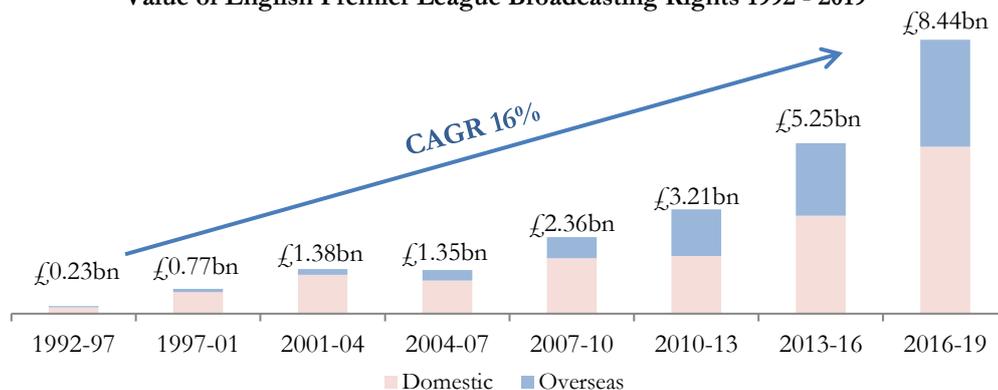
Not only is the FIFA World Cup one of the world's largest sporting events, it is also one of the biggest commercial occasions. Brands are everywhere with several historic sponsors of the event like Coca Cola, Visa and Adidas. New names like Hyundai, Qatar Airways and Wanda are a potent reminder of the impact of globalisation and the changes afoot in the balance of economic power alongside Gazprom representing the hosts.

J. Stern & Co. has a long track record in investing in strong brands. Brand equity is one of the key elements of the quality and value we look for in our investments. One of the most recognisable characteristics exhibited by these brands is the premium pricing they warrant, which leads to higher profitability, earnings growth and cash flow generation for the corporates that own them and the investors who hold the corresponding shares. We discussed this in insight a while ago (the "Cipriani principle", published in February 2017) and while we were discussing spaghetti with tomato sauce not global brands or sports, our conclusion is just as valid: "Once the basic quality of a product or service is established and maintained its competitive advantage can be more enduring than the most innovative and complex of competitors".

Most brands that sponsor events like the FIFA World Cup are not sports brands, but they want to benefit from the huge audiences attracted to those exciting events. Nonetheless, sports brands, whether they be equipment providers, celebrity athletes or simply sport clubs – participating or not – also benefit from structural trends that make them some of the highest value creators around.

First and foremost, the sports industry has enjoyed considerable growth thanks to consumers' reallocation of their spending power and time towards entertainment and in particular sport. More and more consumers globally either watch events (live or TV broadcasting) or participate directly (lifestyle). Globally TV channel spending on acquiring TV broadcasting rights for different sports has increased substantially over the past 20 years. Spending on sports equipment and exercise classes has witnessed the same trends.

Value of English Premier League Broadcasting Rights 1992 - 2019



Source: Deloitte, BBC Sport & J. Stern & Co. analysis

Sports brands, like luxury brands, have the ability to influence consumers' perceptions and behaviours, making them dream or feel that they are part of a community. The association of those brands with the sporting achievements of athletes, who are among the most influential and highest paid celebrities in the world, can make for a potent marketing cocktail, so much so that the growth trends and profitability of some of these brands are not dissimilar to luxury goods companies.

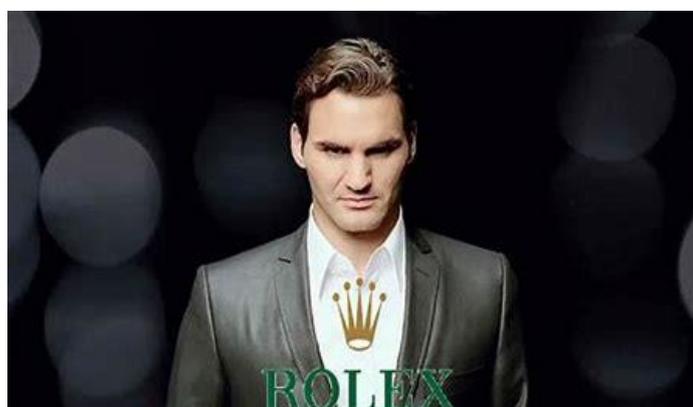


The theoretical value of brands is built around tangible features such as the quality of the product/service, but also around names and symbols. For sports brands in particular, intangible attributes embedded in consumers' minds are often further enhanced by the values carried by their sporting heroes. The goods or services have to deliver the tangible expectations, but those purchases by association will also deliver "dreams" via the images attached to the brand, or the feelings of success embedded within them.

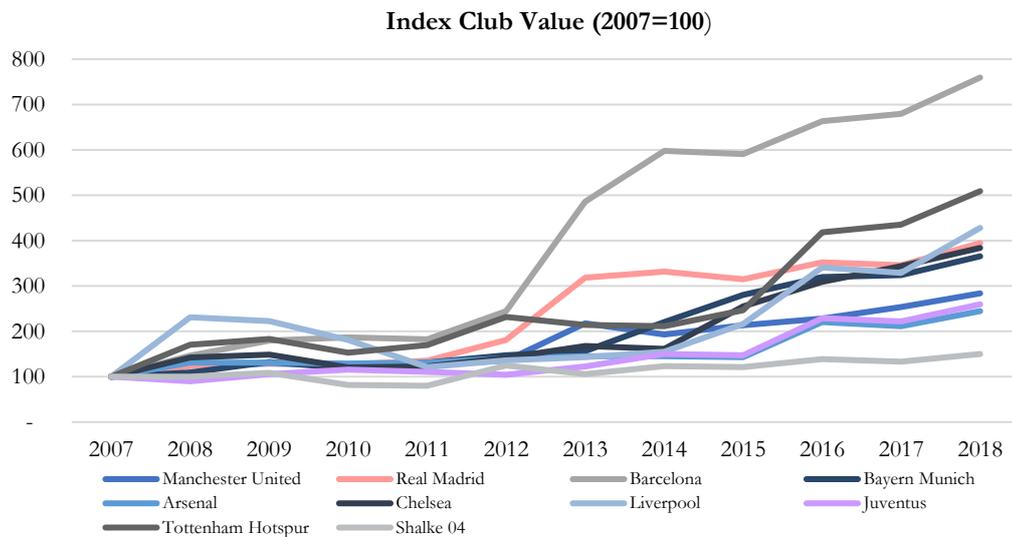
In essence, these "brands" have become integrated "lifestyle" propositions, moving their power from the local to the global stage. Tennis superstar Roger Federer is a prime example of this. His association with Rolex is as much about his person being synonymous with success, elegance and refinement as it is with being Swiss.

Among the fast-growing global sports industry, football has shown the fastest growth, attracting huge audiences at stadiums, through global TV broadcasting or increasingly social media.

Commercial revenues have become by far the most important component of financial growth and profitability for the world's biggest clubs, helped by their increasing global reach. As a result, football clubs have seen their value increase steadily over the past ten years. Their underlying marketing potential is so great that European football clubs in particular have attracted a continuous flow of potential from various parts of the world.



## Value of top ten European Football Clubs



Source: Forbes

However, there substantial differences between the clubs when it comes to the extent to which they have benefitted.

The top ten European clubs have seen their combined value compound at a rate of 13% per annum over the last 11 years (according to a Forbes' estimate of the most valuable football clubs), with Manchester United leading the group as the top franchise. It was valued at \$4.1 billion in 2018 and has held the number one ranking in eight of the last 11 years.

By contrast, FC Barcelona has seen its value increase at a rate of 20% per annum. The two clubs are interesting as they are both top clubs with remarkable sporting achievements in relatively comparable leagues. Both have grown revenues at roughly the same pace over that period of time (7% per annum for Barcelona and 8% respectively for Manchester United). By and large their financial performances have been fairly similar, and according to Forbes both clubs now have roughly the same valuation

However, a key differentiating attribute between the two has been their comparative success at marketing themselves through social media. Whereas both clubs benefit from the same global appeal and sell merchandise in most parts of the world, Barcelona has been much more successful at getting large crowds to follow the club through social media and interact with its communications.

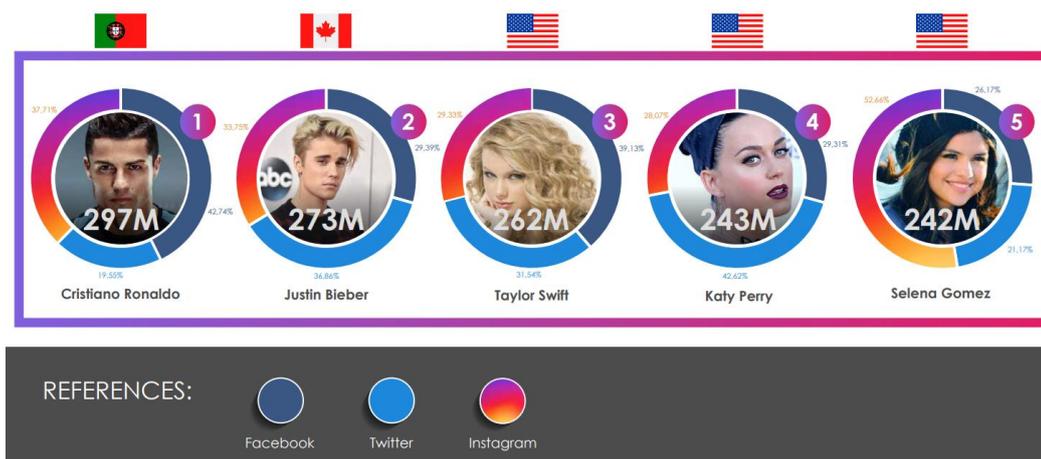
This success has stemmed from the intangible characteristics of the brand which allows consumers, in this case the club's fans, to feel closer to it and be part of a community despite being located at the other end of the world. This reinforces the brand loyalty and opens up new audiences and new opportunities for the business via the ability to target consumers in a more focused and precise way.



Source: FC Barcelona corporate communication

This is now further reinforced by social media's focus on athletes. Primary research among younger members of our team yielded interesting results. According to their latest numbers, the single most followed person in the world on social media is Cristiano Ronaldo with 297 million followers (across Facebook, Twitter and Instagram). He is then followed by a crowd of young musicians, with the next famous athlete Neymar at 177 million and Lionel Messi close behind at 171 million.

The numbers prove what we know: Beyond their prowess on the field, the brand equity carried by the best known individuals is enormous and is only going on to increase. The brand values of these individuals and of the clubs themselves illustrate how much sporting brands have developed beyond the tangible, results-driven performance of the actual team but also how much further they can go.

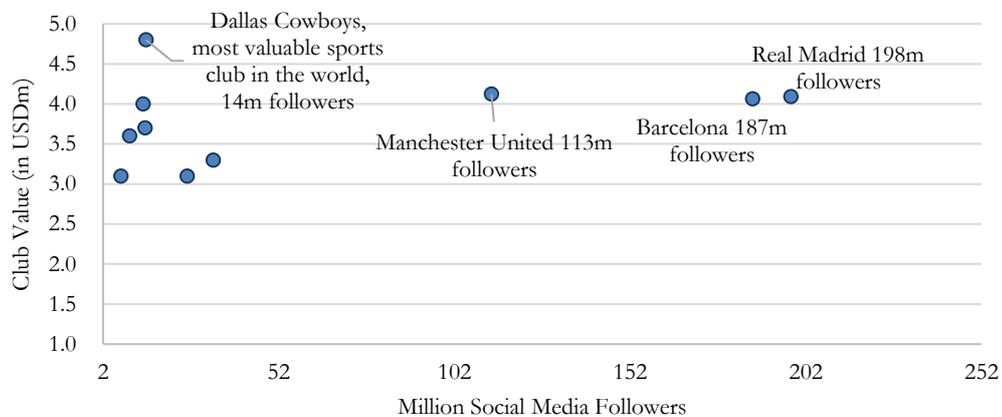


Source: Apple Tree Communication

Our views on valuation do not extend to the opportunistic purchase of Cristiano Ronaldo by Juventus for €100 million despite him having a limited number of years to perform at his peak. However, there are already signs that the number of followers of the club on social media has gone up and that sales of personalised merchandise sales have increased dramatically since his move. €100 million is a lot of money but what better and surer way for Juventus and its owners with their global business interests to enter the world of global mega-clubs?

Despite such deals, Forbes' ranking of the most valuable sports teams for 2018 shows that only three football clubs make the top ten, and although they are ranked 2nd, 3rd and 4th, all the other teams are US based franchises belonging to the NFL, NBA or MLB. More interestingly, the US franchises have low social media followings, and therefore despite their estimated relatively high valuations, it seems that football clubs have the potential to be much more highly valued, with their global appeal yet to be fully priced in.

**World's Most Valuable Sports Club vs Social Media Followers**



Source: Forbes and own research

Building brand equity is a long-term process, not dissimilar to building the winning team for the World Cup. Some football teams, like luxury brands, have refined the art of creating more value out of the intangible assets that are their brands, predominantly through the use of social media, to further enhance their commercial prospects.

How to invest in this value creation is another issue. Many of our investments touch on sports and brands, which play an important part in their businesses and prospects for value generation. We always look for opportunities to invest directly but have been selective in our investments. Our strongest views are currently on e-sports, with an exciting new industry developing. In line with our investment philosophy, we believe that the winning recipe comes from combining the long-term potential of high quality investment opportunities with the understanding of possible disruptive forces.

*Jean-Yves Chereau*  
*July 2018*

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