The "Business" of Sport

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When we discuss business, we most often use revenue streams to exemplify it. Where does the organization derive its revenue from? Who are the consumers and what sources of revenue exist? Understanding those questions allows those interested in sport business and management to better understand the business and decision-making process in sport.

	Fiscal Year Ended June 30,		
	2021	2020	2019
Revenue:			
Connected Fitness Products	$ 3,149.7	$ 1,462.2	$ 733.9
Subscription	872.2	363.7	181.1
Total revenue	4,021.8	1,825.9	915.0
Cost of revenue:			
Connected Fitness Products	2,239.3	833.5	427.8
Subscription	330.5	155.7	103.7
Total cost of revenue	2,569.8	989.1	531.4
Gross profit	1,452.0	836.7	383.6
Operating expenses:			
Sales and marketing	729.7	477.0	324.0
General and administrative	662.4	351.6	207.0
Research and development	247.8	89.0	54.8
Total operating expenses	1,639.8	917.6	585.8
Loss from operations	(187.8)	(80.8)	(202.3)

We can see from the annual report that for 2021, they generated over $4 billion in total revenue with the majority coming from their connected fitness products (signature bike and treadmill). However, the cost of producing that revenue was about 64% ($2.5 B) leaving a 36% gross profit margin. Then, operating costs amounted to $1.6B, which resulted in an operating loss of close to $200 million.

Net cash (used in) provided by operating activities	(239.7)	376.4	(108.6)

Cash Flows from Financing Activities:			
Proceeds from issuance of common stock upon initial public offering, net of offering costs	–	1,195.7	–
Proceeds from issuance of convertible notes, net of issuance costs	977.2	–	–

Unfortunately, this operating loss also resulted in a decrease in cash flow, despite an increase in revenue of over 100% from 2020. Furthermore, we see that they are financed, not by operating activities, but by the proceeds from their IPO and borrowing money. This helps to explain hiring McKinsey, their current managerial decisions and the marked loss of share price and market value.

During the COVID-19 pandemic and lock down order to try and prevent the spread of the disease, fitness centers and gyms had to completely shut down. This resulted in their revenue streams freezing and helps explain some of Peloton's large increase in revenue as members shifted to at-home workouts. However, the real trouble for some operators was the large debt load they carried. Town Sports International was an owner/operator of 186 fitness clubs primarily in the U.S. Their stated business strategy was to maximize members and membership revenue through acquisitions and membership retention strategies. As seen, membership revenue comprises 77% of total revenue from operations, with additional member focused revenue comprising the other 23%.

	For the Years Ended December 31,					
	2019	%	2018	%	2017	%
Total revenue	$ 466,760	100.0%	$ 443,094	100.0%	$ 403,042	100.0%
Non-Membership Revenue:						
Personal training revenue	76,763	16.4%	73,458	16.5%	69,735	17.3%
Other ancillary club revenue[1]	24,393	5.2%	23,293	5.3%	17,197	4.3%
Fees and Other revenue[2]	6,426	1.4%	5,737	1.3%	5,876	1.4%
Total non-membership revenue	$ 107,582	23.0%	$ 102,488	23.1%	$ 92,808	23.0%

Part of their acquisition strategy was to borrow money in order to finance growth. But, as the major risk of debt is the repayment, they noted: "Our debt under the 2013 Term Loan Facility, of which $177.8 million was outstanding as of December 31, 2019, is due on November 15, 2020. Our cash balance as of December 31, 2019 was $18.8 million and thus we do not have adequate sources of cash to repay our debt". They subsequently defaulted and declared bankruptcy highlighting the risk inherent in borrowing and the challenges with a non-diversified revenue streams.

When we contrast the operations of fitness organizations that are dominated by a single stream of revenue with a professional sport franchise, the value of diversification is apparent. Being grandfathered into the NFL as a publicly owned team, the Green Bay Packers issue an annual report that provides a glimpse into the operations of professional sport franchises. The NFL has a robust revenue sharing program amongst the franchises based on league wide revenues dominated by broadcasting rights, then corporate partnerships and merchandising. Then, teams add local revenues that are comprised of ticket sales, concessions, team sponsorship agreements and local broadcasting agreements. NFL franchises show a 60-40 split between league and local revenues, which helps their financial stability.

Statement of Income	2020	2019
Revenue	*$ thousands*	
National	$295,971	$274,293
Local	210,914	203,650
Total revenue	$506,885	$477,943
Expenses		
Player costs	226,548	243,082
Team	46,510	63,595
Sales, marketing & fan engagement	66,994	66,927
Facilities, net*	33,429	30,466
General & administrative	63,101	73,149
Total expenses	436,582	477,219
Profit from operations	$70,303	$ 724
Net income	$34,862	$ 8,368

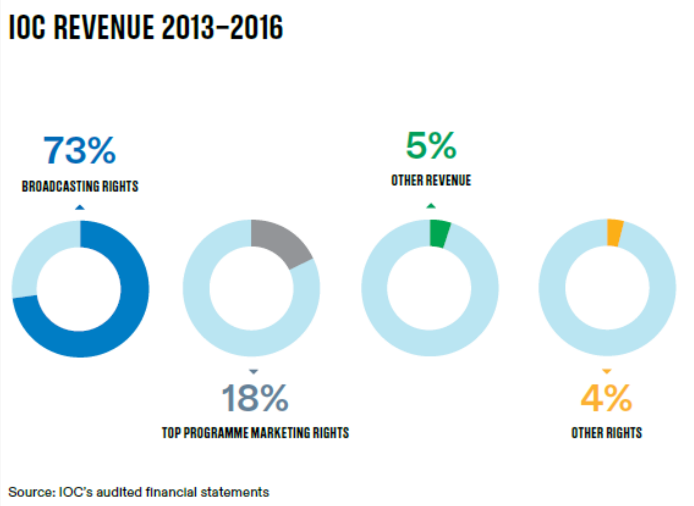
From an international sport perspective, FIFA has been looking into hosting the quadrennial World Cup every two years. Using their annual report from 2019, we can see why:

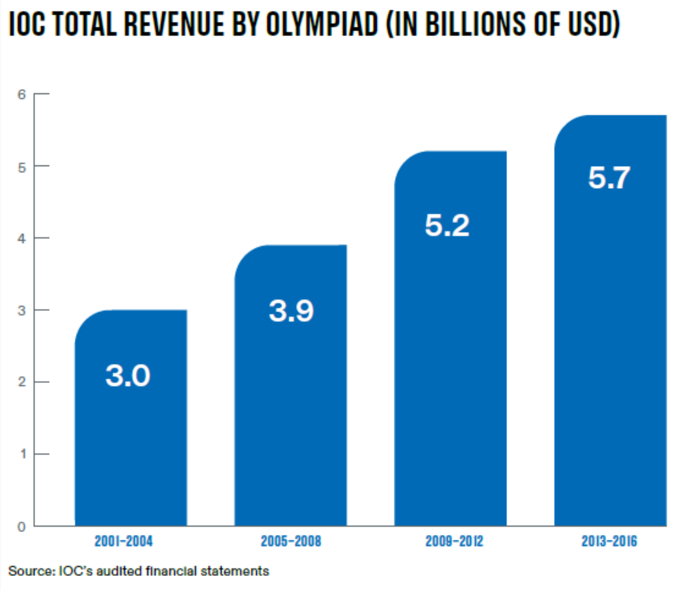
Consolidated statement of comprehensive income

in TUSD	Note	2019	2018
REVENUE			
Revenue from television broadcasting rights	1	342,602	2,543,968
Revenue from marketing rights	2	164,848	1,143,312
Revenue from licensing rights	3	159,527	184,573
Revenue from hospitality/accommodation rights and ticket sales	4	7,931	689,143
Other revenue	5	90,766	79,958
Total revenue		**765,674**	**4,640,954**
EXPENSES			
Competitions & Events	6	–239,203	–1,974,317
Development & Education	7	–512,700	–578,469
Football Governance	8	–32,765	–31,479
Total expenses from football activities		**–784,668**	**–2,584,265**
FIFA Governance & Administration	9	–217,943	–190,586
Marketing & TV Broadcasting	10	–43,643	–116,303
Total expenses from administrative activities		**–261,586**	**–306,889**
Result before taxes and financial result		**–280,580**	**1,749,800**
Taxes and duties	13	–623	–28,965
Financial costs	11	–93,954	–189,808
Financial income	12	189,870	282,970
Net result for the year		**–185,287**	**1,813,997**

When the World Cup was held in 2018, FIFA generated $4.6 billion in total revenue, almost 80% of which came from broadcasting and marketing (corporate partnership) revenue. When the World Cup is held, FIFA generates substantial revenue, underscoring their decision to have that event played more frequently.

The IOC is an interesting organization as they function on a four-year cycle for events, corporate partnership (TOP program) and broadcasting. The majority of their income is generated by broadcasting (73%) and sponsorship (18%), which signifies that in order to receive broadcasting revenues, the Winter and Summer Games need to be held and broadcast.





What we learn about the business of sport is the importance of broadcasting and the impact this has on the operations of the organizations. If games are played, and broadcast, then this is the largest source of revenue to a rights holder. When looking to grow and expand a sport, it is vital to have a fan base that can be reached with broadcasting interest in order to generate the most revenue. We also see that organizations that are cavalier with borrowing money or are dominated by a single revenue stream are at greater financial risk. Sport managers need to understand the importance of diversification of revenue and the importance of cultivating an audience to achieve greater financial independence.