

KEYNOTE INTERVIEW

The rich universe of sports



There are many complexities to the sports market that investors must become acquainted with before taking the plunge, say Joe Leccese, Justin Breen and Kelli Moll at Proskauer

Q What are the current drivers of demand for institutional capital in sports? How are those drivers impacting valuations?

Joe Leccese: To date, the primary driver of transactions has been the desire of controlling and non-controlling owners of professional sports teams to monetise portions of their investments. Some controlling owners, particularly in Europe, also have sought to bring in new capital. Institutional capital also has shown strong interest in ancillary and adjacent opportunities.

We are seeing an interesting bifurcation of the market regarding the type of

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instrument that private equity is offering. In Europe, we see more aggressive instruments being used by institutional investors, including hybrids and structured preferreds, because governance rules allow for that. In the US, most transactions have featured common equity.

Valuations are also strong thanks to the influx of private equity dollars into sport over the past five years. There is more competition for deals, which helps sustain valuations, and there are

more funds being attracted into the space. That includes both dedicated sports, media and entertainment players, as well as large, generalist asset management firms and sovereign wealth funds.

Justin Breen: Sports investments are attractive and offer consistent and reliable returns.

These assets have proved to be extraordinarily non-cyclical and do well even in downturns. There has not been a financial restructuring of a US sports team for many years. These are also scarce assets that come with a level of emotional resonance.

Q What are the unique dynamics of fundraising for sports, and what should GPs be thinking about when seeking capital?

Kelli Moll: It is an education process for most institutional investors. They need to understand why fund terms are different and why they cannot necessarily have the same investor protections as they might have elsewhere. All of this is driven by league rules and to allow the flexibility to meet the investment opportunities.

For example, in private equity more broadly, a lot of institutional LPs will negotiate the right for a no-fault dissolution of a fund. That does not work in sports funds, because the leagues are looking for these funds to be long-term investors and to not disappear.

Leagues are really looking for 10-year hold periods, so if a fund is five years into its investment period when it invests, that is creating a 15-year fund life. Investors have to understand the need to meet that mandate, and funds deal with it in different ways. Generally, there is an ability to extend the term on a year-by-year basis. Sometimes, liquidity rights are baked into fund documents at certain periods of time.

The ability to structure alternative investment vehicles to comply with sports league rules and build in flexibility to exercise excusal rights is an important element of fund formation. Ultimately, it all comes down to educating the investors on what the leagues are looking for, why they are looking for it, and how we can meet those requirements.



Very few investments can be viewed live on TV to see how they are doing, which creates a 'cool' factor for asset managers and their LPs.

Kelli Moll: The non-cyclical, non-correlated nature of this asset class is also driving interest. There is a belief that these investments will deliver strong returns from a multiples perspective and, as a result, we see a lot of firms out there working to source opportunities.

Q Where do you currently see the most compelling investment opportunities for funds?

JB: The most obvious opportunities tend to be with the major sports, both at the league and the team levels, in the US in particular. But there are so many other growing opportunities beyond that.

There is a much broader ecosystem at play. We have done deals recently in multiple different European football

leagues, in rugby, cricket, tennis, volleyball, lacrosse, golf, professional surfing – you name it. We have been involved on the team side, the league side and the investor side.

Our asset management clients see a wide array of additional investment opportunities in the space, including stadiums and infrastructure, media rights, content production, betting and fan engagement initiatives, sponsorship, ticketing and e-sports, just to name a few.

KM: From the fund manager perspective, there is a rich universe of opportunities: for example, the world of emerging-markets sport is one growth area, as is women's sport. While not everyone owns a TV, everyone has a phone, and with that comes the ability to watch their favourite teams through streaming services. That is driving further worldwide growth.

JL: One of the attractive attributes of this asset class is that investors can both maximise upside opportunities and also enjoy inherent mitigants to downside risk. If you are investing in a club with a global following and a legacy that goes back decades, particularly in a sport without relegation, there is a floor on your risk exposure.

Q What additional complexities do funds have to navigate when moving into sports investing?

KM: The complexities are really interdisciplinary. On the fund formation side, it is about navigating the league rules and optimising the tax structuring of these investments. On the tax side, there is a lot of structuring involved in bringing in sovereigns and other non-US investors.

Most private equity firms are not used to asking LPs about their affiliations in sport, such as whether they or their beneficial owners hold existing investments in leagues. If you have investors interested in your sports fund

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JOE LECCESSE

who have other outside sports exposures, structuring around a potential league restriction becomes a key deal mechanic.

JB: The complexities of the rules and restrictions require a team effort. Those restrictions differ between leagues and countries and, with respect to certain sports, can implicate governance regimes that span across multiple countries at once. All of this creates an interesting backdrop that needs to be factored into transactions. Asset managers have expectations about exit rights, governance rights and restrictive covenants, for example, and many of those do not fit easily with the restrictions imposed by the leagues or teams they are investing in. With a deep understanding of the rules, you can navigate the art of the possible.

This has led to a lot of hybrid investment products in this space, where permitted. Some investments look like regular debt, some look like regular common equity, but the vast majority are hybrid, layering in debt-like features with equity-like features. We are always trying to be creative and navigate the various rules and restrictions.

It's also extremely important to understand the broader sports, media and entertainment landscape, particularly with respect to the ways in which an investment in one asset may implicate an investment in a seemingly unrelated asset. We always tell our clients that each deal is not necessarily about that particular deal, but about making sure you do not create issues for the fund more broadly. There is a lot to take into consideration.

JL: There is also a political and public relations perspective to sports investing. We all saw what happened in Europe when enormous pressure exerted by fans ended plans for the formation of a European super league. Funds and investors have to be strategic in how they are investing and when they are taking control, putting respect for fan bases at the heart of their investment thesis.

Q **Looking forward, how is the global sports opportunity evolving, and what does that mean for investors?**

JL: Sports follow the human experience, so it is highly likely that continued economic growth will keep expanding the global middle class. As more people have more disposable income, their consumption of sports will grow.

There are eight billion people in the world, but only a few thousand that play elite soccer, NFL football, NBA basketball, etc. With advances in training and increased competition on the playing surface, those games are going to become even more entertaining, and what is already a trillion-dollar-plus asset class will continue to expand.

Emerging markets present a real growth opportunity for leagues and teams across Africa, South America and Asia. We will continue to see globalisation centred around the big, traditional brands, as well as the growth of emerging sports and a significant opportunity in women's sports.

"[Sports assets] come with a level of emotional resonance. Very few investments can be viewed live on TV... which creates a 'cool' factor"

JUSTIN BREEN

JB: From an investor perspective, you are going to see more dedicated sports, media and entertainment platforms being raised, because these asset classes are so nuanced and require a specialist approach.

This is currently a very bespoke market where every deal feels different from the next, but over time we are likely to see more coalescence around some key market terms. That will create efficiencies and drive investor understanding, all of which will further support growth of the asset class.

KM: There is a lot of appetite among institutional investors, and as more investment firms enter into this asset class, there is going to be more market acceptance of the nuances associated with sports investing.

Maybe the deals get less bespoke over time as investors get more comfortable, but right now, flexibility is the mindset required in fund structuring to meet the complexities of this market. ■

Joe Leccese is chairman emeritus and co-chair of the sports group, Justin Breen is co-head of the global finance practice, and Kelli Moll is a partner and private funds leader at Proskauer