

# Borussia Dortmund

Initiation of coverage

## Das Wunder von Dortmund

While Borussia Dortmund's recent on-field heroics may be hard to match underlying profit progression marks this management's turnaround of the business, and positive development of its powerful brand, on a platform of sustained playing success. A material long-term boost to domestic TV rights reduces concerns about player wage pressures and consumer spend, while disciplined finances hold the company in good stead in a market subject to growing regulation. This year's likely step change in pre-transfer EBITDA should be a catalyst for the underrated share price.

Year end	Revenue* (€m)	EBITDA* (€m)	PBT** (€m)	EPS** (€)	DPS (€)	EV/EBITDA* (x)
06/11	138.5	21.7	18.1	0.23	0.00	12.4
06/12	189.1	36.8	45.1	0.59	0.06	7.1
06/13e	239.0	53.0	42.0	0.61	0.06	4.5
06/14e	233.0	49.0	36.0	0.53	0.06	4.3

Note: \*Before player transfer income \*\*PBT and EPS are normalised, excluding intangible amortisation, exceptional items and share-based payments.

## Coherent strategy

This management has transformed the company's fortunes since near-bankruptcy in 2005. It is successfully pursuing a well-defined strategy centred on developing core revenue sources such as broadcasting, advertising, match operations and merchandising. It is maximising success on the field without taking on new debt, while achieving a balance between financial and sporting interests.

## Major uplift in profit before transfers

The current year could see a near 50% increase in underlying EBITDA even before lucrative rewards for success in its imminent Champions League semi-final against Real Madrid. Such progress is impressive in view of substantially higher costs associated with the club's new star signing, Marco Reus, key contract renewals, merchandise expansion and stadium refurbishment. Although a €4m transfer gain on completed transactions is included in our forecasts, the boost could well be material, given the newly-announced end of season sale of Mario Götze. FY14 may also surprise as we have not allowed for Champions League participation beyond the group stage (qualification is now confirmed). Reaching the semi-finals, as this year, could earn additional €12m UEFA participation revenue alone. Company finances are strong (net cash is in prospect for FY14e even before transfers).

## Valuation: Underrated

The company's success in creating a sustainable business is not being recognised by current valuations. Despite a lack of comparable peers, an EV/EBITDA (pre-transfer) of just 4.5x FY13e ignores the long-term potential of strong brand development, valuable media rights and sustainable cash flow, backed by freehold property and substantial subscription revenue, and hidden reserves from player development. More reasonable would be 5x (share price €3.70), as would a P/E of 7x (€4.30). Free cash flow yield of 7% would be justified by the sustainability of cash flow (€4.60). EV against resilient and growing revenue is only 1.0x prospective.

Leisure

23 April 2013

**Price** €3.25

**Market cap** €200m

Net debt including finance leases at end December (€m) 57.7

Shares in issue 61.4m

Free float 81%

Code BVB

Primary exchange Frankfurt

Secondary exchange N/A

## Share price performance



%	1m	3m	12m
Abs	0.3	9.1	29.6
Rel (local)	6.1	12.3	17.0

52-week high/low €3.33 €2.13

## Business description

The group operates Borussia Dortmund, a leading German football club, recent back-to-back champions of the Bundesliga and semi-finalist in this season's UEFA Champions League.

## Next events

Deutsche Börse Spring Conference	6 May 2013
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Q3 results	15 May 2013
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Edison roadshow	22 May 2013
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## Investment summary: Das Wunder von Dortmund

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### Company description: A leading German football club

Borussia Dortmund has been a major force in German football for decades. Second only to Bayern Munich in terms of Bundesliga titles over the last 20 years, it was the first German club to win a European competition (the European Cup Winners' Cup in 1966) and the Champions League in 1997. This season it is a Champions League semi-finalist and second in the Bundesliga. The club's fabled stadium (the Westfalenstadion, now formally the Signal Iduna Park) is the largest in Germany and has long enjoyed the highest average attendance (c 80,000) in the country (indeed in Europe last year). Borussia Dortmund was formed as the Ballspielverein Borussia 09 e.V. Dortmund in 1909 (hence the BVB 09 logo) and has been listed on the Frankfurt Stock Exchange since 2000.

### Valuation: Low even in a fickle industry

Despite a lack of comparability with peers, Borussia Dortmund is rated among the lowest. However, we prefer to focus on the company's success in creating value in a sustainable business. Its EV/EBITDA (before transfers) rating of just 4.5x FY13e does not, in our view, reflect the long-term potential of powerful brand development, valuable media rights and sustainable positive cash flow, backed by freehold property, substantial subscription revenue, and hidden reserves from player investment. More reasonable would be 5x (share price €3.70), as would a P/E of 7x (price €4.30). Free cash flow yield of 7% (currently 10%) would be justified by the evident sustainability of cash flow (price €4.60). EV as a share of resilient and growing revenue is only 1.0x prospective. The company's transfer policy continues to generate significant hidden reserves in player values. Despite a neutral balance of transfers since 2009 the surplus of market value, as estimated by [www.transfermarkt.de](http://www.transfermarkt.de), to net player assets at December 2012 is c €216m.

### Sensitivities

The company's business operations are dependent on the success of the football club. Participation in lucrative UEFA competitions cannot be relied upon although the club has qualified for next season's Champions League. While serious player injuries cannot be foreseen, the club has a strong squad and minimises the risk of poor investment by intensive scouting and medical examinations. The company competes for a share of disposable consumer income, which may be eroded by economic downturn, but home attendance remains buoyant. Borussia Dortmund is reliant on the strength of its brand. The club is subject to external governing bodies, which may change the structure of German and European football; in terms of finances the company is in tune with a market subject to growing regulation. Negotiation of key media contracts is outside the company's control and those contracts may change, as recently with regard to Bundesliga TV rights. The club is obliged to pay players and coaching staff in line with competitors; its wages/revenue ratio is relatively low. Aware of potentially conflicting sporting and financial aims, management seeks to ensure that cash flows stabilise at a positive level on a lasting basis.

### Financials

After financial troubles under previous management Borussia Dortmund has successfully implemented a clear strategy focused on developing core revenue sources such as advertising, merchandising, match operations and broadcasting. Management is maximising success on the field without taking on new debt, while achieving a balance between financial and sporting interests.

The current year is headed for record profitability, even before the lure of further Champions League progress. The company reports quarterly; Q3 results to March are due on 15 May.

## Company description: A leading German football club

### Rich pedigree

Since its formation in 1909 Borussia Dortmund has become one of Germany's most successful football clubs, having won eight national championships, three German Cups and four German Supercups as well as the Champions League in 1997 and the European Cup Winners' Cup in 1966.

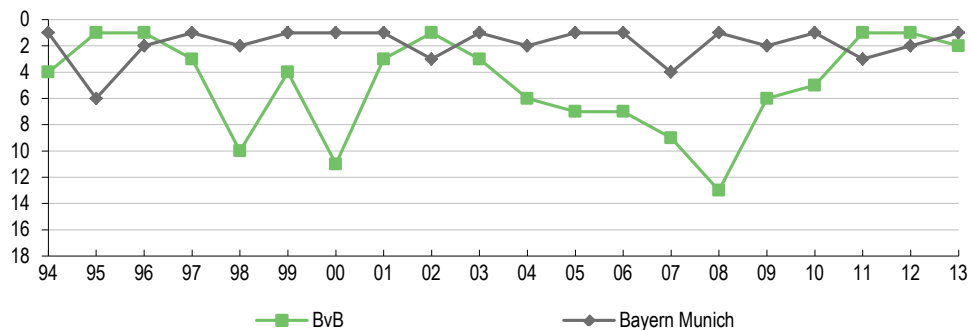
#### Exhibit 1: Club honours

German championship*	1956, 1957, 1963, 1995, 1996, 2002, 2011 and 2012
DFB Cup	1965, 1989 and 2012
German Super Cup	1989, 1995, 1996 and 2008**
UEFA Champions League	1997 (defeated Juventus 3-1 in final)
European Cup Winners' Cup	1966 (defeated Liverpool 2-1 in final)
Intercontinental Cup	1997 (defeated Cruzeiro 2-0 in final)

Source: Bundesliga; Note: \*Bundesliga from 1964. \*\* Unofficial.

During the 50 years of the Bundesliga the club has achieved top six status (the current benchmark for UEFA competition qualification) on 20 occasions (including this season where it is now second) in addition to its five titles. Indeed, more recently, as shown in Exhibit 2, Dortmund's performance in the Bundesliga has been second only to dominant Bayern Munich as the only other club to have won multiple titles in the last 20 years. The prolonged decline between 2003 and 2008 reflects financial troubles under the club's previous management.

#### Exhibit 2: Bundesliga performance over the last 20 seasons



Source: Bundesliga

### Continuing riches

**Head coach: Jürgen Klopp.** Before his appointment in 2008, Jürgen Klopp was coach of Mainz for seven years, guiding the club to promotion from the second division in 2004 and 11th place in the Bundesliga the following year. As a player for Mainz, he holds the club appearance record and is the second-highest goalscorer. He is 45 and his contract at Dortmund runs until 2016.

**Sporting director: Michael Zorc** has spent his entire career at Borussia Dortmund, first as player for 17 years (Bundesliga club appearance record), culminating in the Bundesliga and Champions League success of the mid 90s, and then as sporting director since 1998.

### Exhibit 3: Squad participation in Bundesliga this season

	Nationality	Age	At BVB since	From	Contract expiry**	Matches started***	Goals
<b>Goalkeepers</b>							
Roman Weidenfeller	Ger	32	2002	Kaiserslautern	2014	28	-
Mitchell Langerak	Australian	24	2010	Melbourne Victory	2016	2	-
<b>Defenders</b>							
Oliver Kirch	Ger	30	2012	Kaiserslautern	2014	1	-
Felipe Santana	Braz	27	2008	Figueirense	2014	12	2
Neven Subotic	Serb*	24	2008	Mainz	2016	23	2
Mats Hummels	Ger*	24	2008	Bayern München	2017	25	1
Lukasz Piszczek	Pol*	27	2010	Hertha Berlin	2017	26	2
Marcel Schmelzer	Ger*	25	2005	Magdeburg	2017	26	-
<b>Midfield</b>							
Sebastian Kehl	Ger	33	2002	Freiburg	2014	17	-
Moritz Leitner	Ger	20	2011	TSV 1860 Munich	2015	7	-
Ilkay Gündogan	Ger*	22	2011	Nuremberg	2015	23	3
Jonas Hofmann	Ger	20	2011	TSG Hoffenheim	2015	1	-
Mario Götze	Ger*	20	2001	-	2016	23	10
Jakub Blaszczykowski	Pol	27	2007	Wisla Krakau	2016	21	10
Kevin Großkreutz	Ger	24	2009	Rot Weiss Ahlen	2016	15	1
Leonardo Bittencourt	Ger	19	2012	Energie Cottbus	2016	1	-
Sven Bender	Ger*	23	2009	TSV 1860 Munich	2017	13	-
Nuri Sahin	Tur*	24	2013	Real Madrid	2013****	6	2
<b>Forwards</b>							
Robert Lewandowski	Pol*	24	2010	Lech Poznan	2014	26	23
Julian Schieber	Ger	24	2012	VfB Stuttgart	2016	4	3
Marco Reus	Ger*	23	2012	Borussia M'gladbach	2017	25	12

Source: Bundesliga, BVB. Note: \* Current full international; \*\* End of season; \*\*\* After 30 matches played to 20 April 2013 \*\*\*\* On loan

The first-team squad is one of the youngest in the Bundesliga, yet includes 10 current full internationals. While Kehl and Weidenfeller provide valuable experience, the likes of Götze, Großkreutz and Schmelzer have been successfully developed into the first-team squad. Dortmund is praised for its vibrant attacking style in keeping with the well-known enthusiasm and passion of its head coach. It has failed to score in only three of 45 games this season; it has scored at least two goals in each of its last seven home games, including Champions League, and 10 goals in its last two away Bundesliga fixtures. Most key players and coach Klopp are contracted until 2016 or beyond.

### Proven strategy

Following its financial troubles (see page 8) management has successfully pursued a well-defined business strategy centred on developing core revenue sources such as broadcasting, advertising, match operations and merchandising. It has focused vigorously on maximising success on the field without taking on new debt, while achieving a balance between financial and sporting interests.

- Squad development:** Exhibit 3 shows that the company is adhering effectively to its aim of assembling a competitive team with a focus on promising young players on a “cost-optimised budget.” Under coach Klopp transfer activity (Exhibit 4) has been admirably restrained with the only “trophy” signing being that of Marco Reus, which is rather “the return of the lost son to his spiritual home” (BVB website) as he played youth football for BVB. Robert Lewandowski has proved a bargain at under €5m as this season’s leading Bundesliga scorer and as a sharply appreciating asset ([www.transfermarkt.de](http://www.transfermarkt.de) market valuation: €28m). Otherwise identification of up-and-coming players at minimal cost (even free) and their development at the new “BVB Academy” are much to the fore, underpinning a healthy potential surplus to book value, as estimated by [www.transfermarkt.de](http://www.transfermarkt.de) and detailed in our table. On disposals, management is encouragingly aware of the potential conflict between financial and sporting interests and has achieved a good balance with considered sales, for example, of Sahin (meanwhile returned on loan from Real Madrid) and Kagawa.

**Exhibit 4: Significant player transactions by coach Jürgen Klopp since 2009**

IN	Date	Age at signing	Transfer fee (€m)	Current value (est) (€m)	Contract expiry
Mats Hummels	2009	20	4.2	24	2017
Kevin Großkreutz	2009	20	Free	6	2016
Sven Bender	2009	20	Free	14	2017
Lukasz Piszczek	2010	25	Free	12	2017
Robert Lewandowski	2010	21	4.7	28	2014
Moritz Leitner	2011	18	0.8	5	2015
Ilkay Gündogan	2011	20	5.5	20	2015
Marco Reus	2012	23	17.1	30	2017
Julian Schieber	2012	23	5.5	4	2016
Leonardo Bittencourt	2012	18	2.7	2	2016

Total estimated current value surplus to cost c €105m

OUT	Date	Age at signing	Transfer fee (€m)	Cost (€m)	Buyer
Alexander Frei	2009	29	4.2	4.1 (2006)	Basel
Nelson Valdez	2010	26	3.5	4.7 (2006)	Hércules
Nuri Sahin	2011	22	10.0	- (BvB)	Real Madrid
Shinji Kagawa	2012	23	16.0	0.3 (2010)	Man Utd
Lucas Barrios	2012	27	8.5	4.2 (2009)	Guangzhou
Ivan Perisic	2013	23	7.5	5.5 (2011)	Wolfsburg

Total estimated realised surplus to cost c €30m

Source: [www.transfermarkt.de](http://www.transfermarkt.de)

Dortmund's positive reconciliation of conflicting interests is further highlighted by the striking disparity in its recent net transfer balance (amount received less paid) with those of its fellow Champions League semi-finalists, as shown below. We have taken as illustration the last four seasons when coach Klopp was fully into his stride. The comparison with Bayern is particularly telling as Bundesliga performance is also taken into account (Dortmund's points tally is barely adrift, yet at a fraction of the latter's spend and importantly on a sustainable basis):

**Exhibit 5: Net transfer balances since 2009/10 of current Champions League semi-finalists**

€m	2009/10	2010/11	2011/12	2012/13*	Cumulative since 2009/10	
					Net balance	Bundesliga rank (pts)
Borussia Dortmund	-5 (5)	-2 (1)	+1 (1)	+7 (2)	+1	2 (274)
Bayern Munich	-52 (1)	-7 (3)	-39 (2)	-70 (1)	-168	1 (289)
Barcelona	-88	-20	-13	-32	-153	-
Real Madrid	-170	-83	-47	⇒	-300	-

Source: [www.transfermarkt.de](http://www.transfermarkt.de). Note: \*At 20 April. Bundesliga rank in brackets.

- Brand development:** The "Borussia Dortmund" brand is one of the company's prime assets. According to Sportfive, Germany's leading sports media rights agency, it has one of the largest fan bases with more than 25m German supporters and 3.6m fans and over 550 fan clubs worldwide. Average attendance of c 80,000 is the highest in Europe, and well ahead of its Champions League semi-final rivals. The ranking by Brand Finance last year as the 11th most valuable football brand may be expected to increase, given its current Champions League exposure. Reflecting the longstanding devotion of the club's Westphalia heartland and epitomised by the intense atmosphere of the "Gelbe Wand" ("Yellow Wall") at the "Südtribüne", the largest stadium standing area in the world, BVB's brand image is one of loyalty and enthusiasm, which is a strong platform for advertising.

Management aims to monetise this, as follows:

- Advertising (28% of FY13e revenue and +16% in FY12):** Typically long-term contracts with leading regional and international companies with a proven ability to renew at higher prices or market new opportunities. Principal sponsors are EVONIK (shirt, extended to 2016), SIGNAL IDUNA (stadium, extended to 2021) and PUMA (kit, until 2020). There are nine "BVBChampionPartners," including Opel and Brinkhoff's. This activity is outsourced to Sportfive, which receives commission on revenue generated.
- Merchandising (13% of FY13e revenue and +59% in FY12):** The award of licences and revenue from sale of merchandise, eg 230,000 shirts sold last year, about half of which via

the company's merchandising business. In addition to partners' wholesale distribution channels, sales are made via branded FanShops, e-commerce platform [www.shop.bvb.de](http://www.shop.bvb.de) and a truck that attends away matches. No overseas sales offices are envisaged.

- **New media:** New fans are being attracted via Facebook (2.1m on the official fan page, up 60% in the last six months) and Twitter (trebling of followers in the same period to over 200,000, still small against Chelsea and Arsenal [each over 2m], which indicates potential). Mobile phone apps and games are enjoying strong growth as is the web portal "meinBVB.de."
- **Pay TV:** In 2011 the company was the first Bundesliga club to offer its own TV package in co-operation with Deutsche Telekom. "BVB Total" shows all club Bundesliga matches "live" and matches in other competitions via delayed streaming. A sponsored talk show and an English-language "round-up" programme for international markets have also been devised.
- **Matchday operations (17% of FY13e revenue and +13% in FY12):** Management regards SIGNAL IDUNA Park, Germany's largest stadium, as its most valuable asset apart from the team. With home matches all but sold out and a strict policy of inflation pricing as a community club, the scope for ticketing revenue growth is limited. Apparent underachievement compared with the likes of Arsenal and Chelsea, where ticketing was 40% and 30% respectively of FY12 revenue, is thus unfair; Bayern Munich's 24% revenue share (FY12) is a better comparative and target. Two-thirds of capacity is pre-sold as season tickets, which brings significant revenue visibility, and an annual footfall of 1.4m spectators at Bundesliga games alone gives the potential for useful ancillary income. The stadium is not multi-functional.
- **Broadcasting (34% of FY13e revenue and +88% in FY12):** Marketing of media rights is conducted centrally by the Bundesliga and UEFA, hence outside company control. However, the system of revenue distribution to clubs is defined in advance, with UEFA announcing the allocation before the start of the season and the Bundesliga agreeing last year the sale of rights until 2016/17. UEFA raised distribution by 20% for this season after a minimal rise over the previous two years, while the new Bundesliga deal is worth an extra 45%, ie c €628m income pa. In terms of attendance, the Bundesliga is comfortably higher than the Premier League, La Liga and Serie A and the only one of these to have grown in recent years (+13% since 2008).

## Management

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The company's senior management is backed by highly experienced management of the non-sports businesses and coaching staff.

- **Chief Executive: Hans-Joachim Watzke.** Before his appointment in 2005 Mr Watzke was treasurer of the football club. His contract as CEO runs to 2016. He is the owner-founder of Watex, a leading manufacturer of protective clothing for industrial workers and firefighters.
- **Chief Financial Officer: Thomas Treß** was appointed second managing director in 2005 and has been responsible for finance since 2006. His contract as CFO runs to mid-2014. He was previously a partner at RölfsPartner, one of the leading business consultancies in Germany.

## Sensitivities

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- The company's business operations are dependent on footballing success. Weak performance on the field could cause revenue to fall and affect the ability to attract and retain players and coaches. Participation in lucrative UEFA competitions cannot be relied upon, although the club has qualified for the Champions League next season.



- While serious player injuries cannot be foreseen, the club maintains a strong team squad (22 players taking part in Bundesliga matches this season) and minimises the risk of poor investment in new players by intensive scouting and medical examinations.
- The company is competing for a share of disposable consumer income, which may be eroded by economic downturn. However, attendance at home matches is resilient (much the highest in the Bundesliga) and ticket prices are lower than those of leading competitors. The increasing popularity of the Bundesliga is evident in a sharp rise in the value of future broadcast rights.
- Borussia Dortmund is reliant on the perception of its brand. While damage may impair ability to attract sponsors and commercial partners, it invests heavily to deliver consistent quality.
- Long-term contracts with major sponsors give security independent of sporting performance.
- Borussia Dortmund is subject to external governing bodies, notably the Bundesliga, DFB, UEFA and FIFA, which may change the structure of German and European football. In terms of finances, the company is in tune with a market subject to growing regulation, notably the new break-even requirement for participation in UEFA competitions.
- Negotiation and pricing of key media contracts are outside the company's control and those contracts may change, as recently with regard to Bundesliga TV rights from next season.
- The company's digital media strategy is unproven. Piracy and illegal live streaming may adversely impact its broadcasting and new media and mobile revenue.
- The club is obliged to pay players and coaching staff in line with competitors. Labour costs in FY12 accounted for 42% of revenue excluding transfers, which is lower than key peers.
- Interest rate risk is minimised by the significant fixed element of borrowings and by interest-rate swap transactions. The company's principal loan (€20m) matures in June.
- Aware of a potential conflict between sporting objectives and financial requirements, management aims to ensure that cash flows stabilise at a positive level on a lasting basis.

## Valuation

Among major listed peers, there is limited comparability with Borussia Dortmund in terms of valuation indicators. By far the largest by market capitalisation, Manchester United and Arsenal offer very limited free float, while Juventus, although with similar market value to Dortmund, has a majority shareholder and has been heavily loss-making. Olympique Lyonnais is finding the going tough during its restructuring: H1 EBITDA before transfers saw a sharp move to loss on exclusion from the Champions League. Against available peer numbers (forecasts are not available for most) Borussia Dortmund is rated among the lowest:

**Exhibit 6: Valuation comparison with major listed peers**

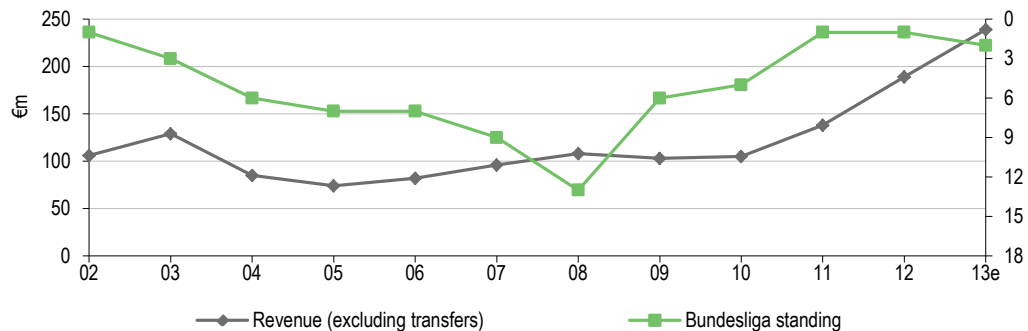
	EV	EBITDA	Revenue	EV/EBITDA	EV/Revenue
<b>Prospective</b>					
Borussia Dortmund	€239m	€53m	€239m	4.5	1
Manchester United	\$3.33bn	\$165m*	\$540m*	20.2	6.2
<b>Historic</b>					
Borussia Dortmund	€263m	€36.8m	€188m	7.1	1.4
Juventus	€365m	€3.1m	€214m	117.7	1.7
Arsenal	£1.09bn	£34.5m	£243m	31.7	4.5
Olympique Lyonnais	€48m	(€4.7m)	€132m	-	0.4

Source: Company accounts. Note: \*Mid-point of management guidance at February 2013, (\$1.52/£). Year-end June for all except Arsenal (May).

More broadly, we believe that the sustainability of the business model and scope for value creation are unrecognised in market valuations. In terms of pre-transfer EV/EBITDA (net debt including finance leases), the low rating of 4.5x FY13e (S&P Europe BMI:12.3x) clearly disregards the long-term potential of strong brand development, valuable media rights and positive cash flow, backed by substantial season ticket sales and hidden reserves from player investment. EV/EBITDA of 5x (share price €3.70) would be reasonable, as would a P/E of 7x (€4.30) vs S&P Europe BMI: 7.8x.

Borussia Dortmund is also being undervalued in respect of the strength of its non-transfer revenue. Exhibit 7 shows impressive resilience during a dip in playing fortunes, reflecting the longer-term nature of most of its income. The EV/non-transfer revenue FY13e multiple is just 1.0x.

**Exhibit 7: Revenue (excluding transfers) and Bundesliga performance since 2002**



Source: BVB accounts, Bundesliga

Value creation is further emphasised by the company's transfer policy, which continues to generate significant hidden reserves in player values. The past four years under coach Klopp have seen average capital gains of €8.7m and the potential for further gains remains high, viz the proposed end of season sale of Mario Götze. Despite a neutral balance of transfer income and expenditure since 2009 the surplus of market value, as estimated by [www.transfermarkt.de](http://www.transfermarkt.de), to net player assets at December 2012 is c €216m. That surplus is reassuring, even though it is to be treated with caution, as it is notional, and because company policy is for disposal only in special cases.

Free cash flow (see Exhibit 10) is running at €20m before acquisitions and disposals (with upside), implying a free cash flow yield of 10%. Given its evident sustainability, a more reasonable free cash flow yield would in our view be 7%, implying a share price of €4.60.

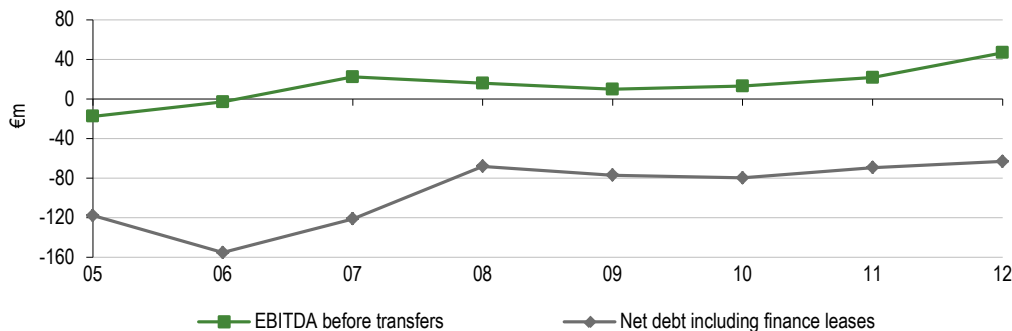
The company should be rewarded for its disciplined model at a time of increasing regulation. Unsustainable spend on wages and transfers will be penalised by new UEFA Financial Fair Play requirements (six clubs, including Champions League quarter-finalist Malaga, recently received one-year suspensions for unpaid bills). There is security in the freehold value of the stadium – as at December 2012 €127.6m or €2.04 NAV.

Although we regard it as peripheral to the valuation case, the significant sports media element of Dortmund's business may be viewed in the context of EV/EBITDA FY13e ratings of 19x and 7x for the two main listed sports rights owners, Perform Group and Chime Communications.

## Financials

Borussia Dortmund's financial turnaround has been remarkable, as evident in Exhibit 8. The company was at risk of bankruptcy in 2005, broadly attributed to extravagance, notably on foreign players, after Bundesliga success in 2002. New management (the current chief executive and CFO) implemented a reorganisation programme, which included the restructuring of liabilities through a long-term fixed-interest loan from Morgan Stanley, cost-cutting and a strategy of revenue development and sustainable investment in players, as detailed above. Key initiatives included the repurchase of the stadium, thereby eliminating high rental costs, and early repayment of the loan via a long-term agreement with marketing partner Sportfive, while early extension of flagship contracts endorsed the advertising strategy. Jürgen Klopp's appointment as coach was in tune with management's approach to player investment. Financial recovery was not flattered by European participation until 2011 and was in the teeth of economic downturn.



**Exhibit 8: Financial performance since 2005**


Source: BVB accounts

## FY13

The current year has shown further strong progress with first-half EBITDA before transfers up 12%, which is impressive in view of substantially higher costs associated with the club's new star signing, Marco Reus, certain key contract renewals, merchandise expansion and stadium refurbishment. The quarter to December more than maintained the heady pace of Q1 with double-digit top-line increases by all key activities. Advertising and merchandising were again to the fore (+29% and +45% respectively), thanks particularly to a change of kit supplier to PUMA and new Champions League partners, while a successful campaign boosted UEFA broadcasting income by c 30% (our estimate). There was also a useful contribution from lucrative release fees for national players. H1 PBT (negligible impact from transfer activity) was up 9% at €16.7m.

**Full-year:** Ahead of a semi-final against Real Madrid on 24 and 30 April, our forecasts do not assume qualification for the Champions League final in late May. There is thus material scope to surprise, given the final's participation fee of €6.5m (a further €4m for the winners) and associated advertising and merchandising potential in particular.

Unlike H212, the second half is characterised by Champions League activity, which drives our expectation of a more than doubling of EBITDA before transfers to €36.8m. Our revenue estimate of €16m UEFA revenue comprises €12m from taking part in the knock-out matches and €4m from the market pool. By contrast, there will be lower year-on-year benefit from the DFB Cup after the club's early elimination (cup winner last season). H2 labour costs are likely to be similar to the first half, which is encouraging in view of a rise of more than a half over the last two years (+31% in H1).

Although some transfer profit is included in forecasts (c €4m on January transactions), the boost could well be material after the newly-announced end of season sale of Mario Götze to Bayern Munich. No financial details have been formally disclosed but the release clause in his contract is reportedly set at €37m (source: <http://sportbild.bild.de>) and his market value according to [www.transfermarkt.de](http://www.transfermarkt.de) is €42m. Robert Lewandowski, top goalscorer in this season's Bundesliga, has also especially been the subject of transfer rumours; his contract expiry is at the end of next season and his market value according to [www.transfermarkt.de](http://www.transfermarkt.de) is €28m (the company paid €4.7m for his registration in 2010).

## FY14

Our forecasts assume continued participation in the Champions League (now confirmed), but not beyond the group stages, hence a marked reduction in revenue from both UEFA broadcasting and match operations, based on an unchanged distribution system (to be announced by UEFA in the summer). Apart from half the number of FY13 Champions League matches, there would be fewer performance bonuses in line with elimination at that stage of the competition. As an indicator of

potential upside, reaching the semi-finals, as this year, would earn additional €12m UEFA participation revenue alone, as per the current distribution system. Such incremental income (c 25% of our forecast EBITDA before transfers) is highly profitable and would be supplemented by similarly high-margin revenue from the UEFA market pool as well as from advertising and merchandising.

The step change in Bundesliga broadcasting revenue (typically cautious management is happy with our 38% forecast increase) reflects the new contract, while operating costs, including labour, are expected to be relatively stable after the investment of recent years. We assume no transfer activity.

<b>Exhibit 9: Revenue and profit analysis</b>								
Year end June (€m)	2011	H112	H212	FY12	H113	H213e	FY13e	2014e
<b>Home Matches:</b>							§	▲
Bundesliga	17	8	9	17	8	9	17	17
UEFA*	4	3	-	3	3	3	6	3
DFB Cup	-	1	-	1	1	-	1	2
<b>Away Matches:</b>								
UEFA*	4	3	-	3	3	3	6	3
DFB Cup	2	2	2+Final	4+Final	2	1	3	2
<b>Revenue</b>								
<b>Match operations:</b>								
Bundesliga	23.4	11.5e	13.0e	24.5	12.0e	13.5	25.5	26.3
Change	+7%	+5%	+5%	+5%	+4%	+4%	+4%	+3%
UEFA	3.3	4.4	-	4.4	5.5e	6.0	11.5	6.0
Change	n/m			+30%	+25%	n/m	+161%	-48%
DFB Cup	0.2	1.3e	0.6e	1.9	1.3e	0.4	1.7	1.7
Other (friendlies etc)	0.8	0.3e	0.4e	0.6	0.3e	0.5	0.8	1.0
<b>Total</b>	<b>27.7</b>	<b>17.5</b>	<b>13.9</b>	<b>31.4</b>	<b>19.1</b>	<b>20.4</b>	<b>39.5</b>	<b>35.0</b>
<b>Change</b>	<b>+18%</b>	<b>+20%</b>	<b>+6%</b>	<b>+13%</b>	<b>+9%</b>	<b>+47%</b>	<b>+26%</b>	<b>-11%</b>
<b>Broadcasting:</b>								
Bundesliga	26.8	10.9e	17.0e	27.9	11.3e	17.7	29.0	40.0
Change	+32%	+4%	+4%	+4%	+4%	+4%	+3%	+38%
UEFA	4.9	25.6	-	25.6	33.0e	16.0	49.0	31.0
Change	n/m			x5	+29%	n/m	+91%	-28%
DFB Cup	0.4	2.5e	4.4e	6.9	2.6e	1.4	4.0	4.0
<b>Total</b>	<b>32.1</b>	<b>39.0</b>	<b>21.4</b>	<b>60.4</b>	<b>46.9</b>	<b>35.1</b>	<b>82.0</b>	<b>73.0</b>
<b>Change</b>	<b>+52%</b>	<b>+124%</b>	<b>+45%</b>	<b>+88%</b>	<b>+20%</b>	<b>+64%</b>	<b>+36%</b>	<b>-11%</b>
<b>Advertising</b>	50.0	25.2	32.6	57.8	31.7	35.8	67.5	71.0
Change	+28%	+12%	+19%	+16%	+26%	+10%	+17%	+5%
<b>Merchandising</b>	14.5	11.8	11.2	23.0	17.8	14.2	32.0	35.0
Change	+61%	+76%	+43%	+59%	+51%	+27%	+39%	+10%
<b>Catering / other (rent etc)</b>	14.2	7.9	8.6	16.5	8.2	9.8	18.0	19.0
Change	+8%	+36%	+2%	+16%	+4%	+14%	+9%	+5%
<b>Total</b>	<b>138.5</b>	<b>101.4</b>	<b>87.7</b>	<b>189.1</b>	<b>123.7</b>	<b>115.3</b>	<b>239.0</b>	<b>233.0</b>
<b>Change</b>	<b>+32%</b>	<b>+51%</b>	<b>+23%</b>	<b>+37%</b>	<b>+22%</b>	<b>+31%</b>	<b>+26%</b>	<b>-2%</b>
Other operating income	4.3	2.4	5.2	7.6	3.5	4.5	8.0	8.5
Labour costs	(61.5)	(34.0)	(45.9)	(79.9)	(44.5)	(44.5)	(89.0)	(92.5)
Change	+28%	+18%	+40%	+30%	+31%	-3%	+11%	+4%
Share of revenue	44%	33%	52%	42%	36%	46%	40%	40%
Other operating costs	(59.6)	(42.6)	(37.4)	(80.0)	(52.3)	(46.7)	(99.0)	(100.0)
Change	+29%	+41%	+28%	+34%	+23%	+25%	+24%	+1%
<b>EBITDA before transfers</b>	<b>21.7</b>	<b>27.2</b>	<b>9.6</b>	<b>36.8</b>	<b>30.4</b>	<b>22.6</b>	<b>53.0</b>	<b>49.0</b>
<b>Margin</b>	<b>15.7%</b>	<b>26.8%</b>	<b>10.9%</b>	<b>19.5%</b>	<b>24.6%</b>	<b>19.6%</b>	<b>22.2%</b>	<b>21.0%</b>
Depreciation	(8.9)	(4.9)**	(5.2)**	(10.1)	(5.4)**	(5.6)**	(11.0)	(12.0)
<b>Operating Profit before transfers</b>	<b>12.8</b>	<b>22.3</b>	<b>4.4</b>	<b>26.7</b>	<b>25.0</b>	<b>17.0</b>	<b>42.0</b>	<b>37.0</b>
<b>Margin</b>	<b>3.0%</b>	<b>22.0%</b>	<b>5.0%</b>	<b>14.1%</b>	<b>20.2%</b>	<b>14.7%</b>	<b>17.6%</b>	<b>15.9%</b>
Profit on disposal of player registrations	10.7	-	23.2	23.2	Neg.	4.0¥	4.0	-
Transfer income	13.0	-	26.1	26.1	0.4	8.0	8.4	-
Less: Carrying value	2.3	-	2.9	2.9	0.4	4.0	4.4	-
<b>Operating Profit</b>	<b>23.514.9</b>	<b>22.3</b>	<b>27.6</b>	<b>49.9</b>	<b>25.0</b>	<b>21.0</b>	<b>46.0</b>	<b>37.0</b>

Source: Edison Investment Research. Note: \* Europa League in 2011, thereafter Champions League; § Assuming semi-finals of Champions League; ▲ Assuming group stage of Champions League; ¥ Assumed gain on disposals of Perisic and Löwe in January 2013 \*\* Edison estimate as not disclosed separately at half-year

## Cash flow

The company has achieved c €20m positive trading cash flow before transfers both last year and the year before. We expect a similar outturn in FY13 as higher trading profit and depreciation and amortisation of player registrations are offset by an increase in tax payments and capex. Likely €5m net inflow from already completed transfers and an inaugural dividend payment of €4m suggest a reduction of c €23m in net bank debt in the period, ie to €19m at June 2013. We assume no further transfers and a similar level of season ticket sales (deferred income) to last year. The unpredictability and potential size of both items makes forecasting of year-end net bank debt hazardous. There is also c €20m liability from finance leases.

### Exhibit 10: Financial summary

	€'000s	2011	2012	2013e	2014e
June		IFRS	IFRS	IFRS	IFRS
<b>PROFIT &amp; LOSS</b>					
Revenue		138,500	189,100	239,000	233,000
Cost of Sales		0	0	0	0
Gross Profit		138,500	189,100	239,000	233,000
EBITDA (before player transfers)		21,700	36,800	53,000	49,000
Player transfers		10,700	23,200	4,000	0
Operating Profit (before amort. and except.)		23,500	49,900	46,000	37,000
Intangible Amortisation		(8,600)	(8,500)	(12,000)	(14,000)
Exceptionals		0	0	0	0
Other		0	0	0	0
Operating Profit		14,900	41,400	34,000	23,000
Net Interest		(5,400)	(4,800)	(4,000)	(1,000)
Profit Before Tax (norm)		18,100	45,100	42,000	36,000
Profit Before Tax (FRS 3)		9,500	36,600	30,000	22,000
Tax		(4,100)	(9,100)	(4,500)	(3,300)
Profit After Tax (norm)		14,000	36,000	37,500	32,700
Profit After Tax (FRS 3)		5,400	27,500	25,500	18,700
Average Number of Shares Outstanding (m)		61.4	61.4	61.4	61.4
EPS - normalised (c)		22.8	58.6	61.1	53.3
EPS - normalised and fully diluted (c)		22.8	58.6	61.1	53.3
EPS - (IFRS) (c)		8.8	44.8	41.5	30.5
Dividend per share (c)		0.0	6.0	6.0	6.0
Gross Margin (%)		100.0	100.0	100.0	100.0
EBITDA Margin (%)		15.7	19.5	22.2	21.0
Operating Margin (before GW and except.) (%)		17.0	26.4	19.2	15.9
<b>BALANCE SHEET</b>					
Fixed Assets		196,600	210,400	220,000	213,100
Intangible Assets		18,400	25,700	34,000	31,000
Tangible Assets		170,700	182,600	183,900	180,000
Investments		7,500	2,100	2,100	2,100
Current Assets		25,100	38,300	48,000	59,500
Stocks		2,300	5,800	10,000	12,000
Debtors		19,600	24,500	28,000	32,000
Cash		1,100	5,300	7,000	12,000
Other		2,100	2,700	3,000	3,500
Current Liabilities		(63,400)	(61,900)	(69,000)	(74,500)
Creditors		(50,200)	(55,900)	(65,000)	(71,500)
Short term borrowings		(13,200)	(6,000)	(4,000)	(3,000)
Long Term Liabilities		(90,700)	(93,300)	(82,000)	(65,000)
Long term borrowings		(47,900)	(41,300)	(22,000)	0
Finance leases		(9,400)	(21,100)	0	0
Other long term liabilities		(33,400)	(30,900)	(60,000)	(65,000)
Net Assets		67,600	93,500	117,000	133,100
<b>CASH FLOW</b>					
Operating Cash Flow		27,600	32,700	44,000	44,000
Net Interest		(5,500)	(4,900)	(4,000)	(1,000)
Tax		(1,000)	(1,100)	(8,700)	(4,400)
Capex		(2,000)	(7,300)	(10,000)	(7,000)
Acquisitions/disposals		(5,900)	(1,500)	5,300	0
Financing		0	0	0	0
Dividends		100	100	(3,600)	(3,600)
Net Cash Flow		13,300	18,000	23,000	28,000
Opening net debt/(cash)		73,300	60,000	42,000	19,000
HP finance leases initiated		0	0	0	0
Other		0	0	0	0
Closing net debt/(cash)		60,000	42,000	19,000	(9,000)

Source: Edison Investment Research, company accounts

Contact details	Revenue by geography
Rheinlanddamm 207-209 D-44137 Dortmund Germany +49 (0) 231 90 20 745 <a href="http://www.bvb.de/aktie">www.bvb.de/aktie</a>	N/A

CAGR metrics	Profitability metrics	Balance sheet metrics	Sensitivities evaluation
EPS 2010-14e	N/A ROCE 13e	30.2% Gearing 13e	16.8% Litigation/regulatory
EPS 2012-14e	N/A Avg ROCE 2010-14e	N/A Interest cover 13e	11.5x Pensions
EBITDA 2010-14e	N/A ROE 13e	32.0% CA/CL 13e	0.7 Currency
EBITDA 2012-14e	15.4% Gross margin 13e	100% Stock days 13e	15.3 Stock overhang
Sales 2010-14e	N/A Operating margin 13e	19.2% Debtor days 13e	42.8 Interest rates
Sales 2012-14e	11.0% Gr mgn / Op mgn 13e	5.2x Creditor days 13e	85.5 Oil/commodity prices

Management team
<b>Chief Executive: Hans-Joachim Watzke</b> Before his appointment in 2005, Mr Watzke had been treasurer of the football club for four years. His contract as CEO has been extended to the end of 2016. He is also the owner-founder of Watex, a leading manufacturer of protective clothing for industrial workers and firefighters.
<b>Chief Financial Officer: Thomas Treß</b> Thomas Treß was appointed second managing director in 2005 and has been responsible for finance since the start of 2006. His contract has been extended to mid-2014. He was previously a manager and partner at Röf'sPartner, the leading independent German auditing and consulting firm.

Principal shareholders	(%)
Bernd Geske	11.7%
Borussia Dortmund	7.2%

Companies named in this report
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