

LA LIGA DEALS SET TO KICK-OFF - LATHAM & WATKINS

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Increased profitability and stability in the Spanish football league is creating ideal conditions for overseas investment.

Spanish football's top division (La Liga) has been home to some of the world's best players, including Ronaldo and Messi. Its highly skilled football is enjoyed by fans across the globe, and the league — given its high sporting profile and performance in international competitions (such as the Champions League) — has been more successful than any other European domestic league in recent years. Yet,

for overseas investment and takeover deals, La Liga remains a second-tier player on the European stage.

A large number of Spanish clubs are controlled by historical owners — including some clubs that are family owned — and no Spanish club is publicly listed. As such, many Spanish clubs are need further investment.

This investment is needed for a variety of reasons: to compete for promotion to La Liga; avoid relegation; reach European competitions, or, in some cases, compete with Real Madrid, Barcelona, or Atletico Madrid on the pitch.

In February 2018, the Chinese investment group Dalian Wanda sold a 17 per cent stake in Atletico Madrid to Israeli investment vehicle Quantum Pacific Group — the most recent example of foreign investment in La Liga. Teams including Malaga, Español, and Valencia have each received backing from foreign equity investors in recent years with mixed results — both in terms of profitability and on-pitch performance. However, the vast majority of clubs in La Liga have yet to attract as much interest from investors as clubs in the English Premier League. American, Russian, Middle Eastern and Asian investors have taken over numerous English Premier League clubs, including those that historically finish towards the bottom of the table, or even those that are not in England's top division.

Historically, the uneven distribution of broadcasting rights between clubs, high debt levels, and various tax-related issues have deterred many overseas investors from investing in clubs in La Liga. However, in recent years, clubs in La Liga have become more profitable and financially stable (possibly as a knock on effect of domestic financial fair play regulations). We believe this will lead to increased global investment in Spanish football clubs.

Moreover, we believe that change may be on the way as La Liga clubs are becoming a more attractive investment proposition in light of recent developments with respect to the allocation of revenues from broadcasting rights. Until 2015, Barcelona and Real Madrid negotiated their own broadcasting deals, taking a disproportionate share of broadcasting revenues for themselves and creating severe financial inequality among Spanish clubs, which were left with little room to negotiate favourable deals. However, La Liga took over the negotiation of broadcasting rights three years ago, resulting in a more equal distribution of broadcasting revenues that are heavily determined by on-pitch team performance.

As a result, La Liga's lower-ranked clubs now enjoy a predictable, and higher, stream of revenue from broadcasting rights. Revenues received from broadcasting rights are centrally distributed by La Liga according to a fixed schedule. Broadcasting revenues increased by €270.7m between 2014/15, and by 31% between 2015/16. In the 2016/17 season, La Liga overtook Germany's Bundesliga to become the second-highest revenue generating league in the world behind the English Premier League, according to Deloitte. La Liga clubs will receive at least €3.4 billion in revenue from La Liga broadcasting rights for the 2019-2022 cycle. We believe this predictable, increasing, and stable cash flow will enhance investors' ability to secure acquisition financing or to refinance existing debt on more favourable terms. This is due to the ability of clubs and investors to use income and receivables generated from broadcasting rights to secure bonds issued, or bank debt incurred, with respect to the acquisition of clubs.

La Liga's financial fair play regulations, established in 2013, have also served to improve Spanish clubs' finances. La Liga was one of the first major European domestic leagues to enforce strict financial regulations on member clubs, mirroring UEFA Financial Fair Play Regulations. Subsequently, according to the La Liga Financial Report 2016, debt ratios have fallen as clubs in La Liga have reduced their net debt by €835m between 2011/12 and 2015/16 and decreased debt-to-income ratios from 1.8 to 0.9 during the period.

In addition to the increased levels of broadcasting revenues, we also believe that there is significant upside potential for investors to benefit from increasing revenues from image rights, sponsorship deals, and merchandising (as La Liga continues to extend its global reach), as well as from increasing match day revenues. With respect to match day revenue, La Liga's lower attendance levels leave plenty of opportunity to generate additional ticket sales and other revenue as the average attendance at La Liga matches fell to 27,000 per match last year, compared to 38,500 per match in the Premier League and 44,000 per match in the Bundesliga.

Like other complex industries, investing in football is not without risk. Valuing a football club is not an easy task and requires evaluating multiple criteria. In addition to conducting extensive financial, legal, and tax due diligence, purchasers must conduct extensive due diligence on the sporting side of the transaction and consider the threat of relegation in their investment decision. Inexperienced investors in the sector are more likely to overlook the sporting side of an investment in a football club. Some purchasers can lack internal resources to evaluate and manage a football club on the sporting side, and focus solely on financial performance of the target. Choosing the right executives and advisers — aside from financial and legal advisers — to assess and manage the squad, is critical.

Despite the risks associated with buying a football club, the fundamentals in Spain are strong, and we believe that the conditions are right for La Liga deal-making to kick off.

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