Follow the money: Unpacking sports media from the coronavirus shutdown

By Ed Desser and John Kosner

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Everyone is talking about how and when sports will return. Few are addressing the pain to come: the great adjustment and renegotiation chain. For now, force majeure language in nearly all agreements forestalls this process. These provisions prevent either party from being in breach of the agreement for failure to perform due to "Act of God" reasons beyond their control. Usually applied when weather, technology or a labor stoppage causes a single rescheduling, we now face the unique situation of everything stopping. Almost every programming and distribution agreement is implicated. Thinking this process through end to end ... it's best to follow the money.

Without the ability to play games or stage events, many pro athletes don't get paid. Typically, they get a per-game fee over a season as part of a multiyear contract, governed by their sports' collective-bargaining agreements. The CBAs for NFL, NHL, and NBA (but not MLB) require a percentage of leaguewide annual

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revenue to be paid to players collectively. No games, and no telecasts, means very little revenue. While there are timing issues, and one must think about baseball where the CBA does not have a salary cap, reduced revenue essentially means reductions in player pay (a huge issue for unfortunate free agents next offseason.) Same for stadium rent, game-day operations and team travel. This also means that teams owe fans ticket refunds and media, advertisers and sponsors make-goods.

From a TV network perspective, no games means a savings on game production, but also no premium live event ad revenue. In many cases, the network will still receive affiliate fees, but these are based on providing a certain amount of tent-pole programming. Each network and each distributor will need to take a look at its agreements and contemplate adjustments. Can games be rescheduled or added in a future season? Are the networks already over-delivering on their programming covenants or will they need to return some affiliate payments? ESPN commands a multiple of ESPN Classic's rate, which is essentially what the mothership has become. When the games finally resume, will viewing audience be higher or lower? Will ad sales benefit from less competition and pent-up demand or suffer from budget cuts due to the economy or lack of time to sell and plan promotional activations? Ultimately, networks will, for the most part, be entitled to some relief from rights fees when some portion of the events can't be delivered or effectively replaced. This means some costs will go down (though new replacement programming costs something), and ad revenue is likely to be much lower. Net net, the value the sports networks deliver to affiliates during the COVID-19 pandemic will be lower.

The collision of pro sports on television this fall will provide a tsunami of viewing options — with or without fans in the stands.

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From the distribution affiliates perspective, they get less quality programming from the networks, but the same number of hours, so expect them to still have to pay some or all of the networks' license fees. Fans will still pay bundled package prices for overall programming, but are getting less value for their money, and they may be entitled to rebates due to the lost sports product. The attorney general of New York has already asked for such rebates for state cable customers.

At every stage of this process there are existing agreements, and various mitigating factors going in different directions. For example, distributors losing subscribers due to the economic downturn will have less available revenue to pay to networks. In turn, those networks will have less to pay to leagues/teams. The teams will have less to pay to players. Teams playing games without fans (or just fewer of them) will have less income than before (and some new expenses like testing, security, and hotel nights for "home games.") But their media rights will actually become more valuable in a world now avoiding sports bars, without fans in arenas, and where even watching together is unlikely unless it's the family under your own roof. Plus, for a while, there won't be any new entertainment programming produced to compete with sports.

Then consider the ecosystem changes already in play before the crisis. Cord cutting and cord shaving may have accelerated these past months. Deals coming up for renewal/extension will face a new business environment. Fewer subscribers lowers the amount available to pay for programming. However, tech titans will see an opportunity to use their fortress balance sheets and "Niagara Falls" cash flows to leap into the last remaining programming category they have previously eschewed.

Huge league deals upcoming in the NFL, NHL, and NBA could all be affected, not to mention the dozens of regional club deals coming up to bat. But ESPN+, Amazon Prime and other digital sports platforms provide new ground for the leagues to occupy. Packages may morph, but nothing has materialized that fundamentally changes the sports fan demand equation.

If anything, as ratings for ESPN's "The Last Dance" and NFL draft attest, months without live sports is only driving up interest. We expect when games return, there will be much unsatisfied demand. While that may not exhaust the sports programming supply the same as supermarket toilet paper shelves, we can expect a tsunami of viewing to the summer/fall collision of NBA, NHL, NFL, and MLB, plus delayed Masters, Kentucky Derby, PGA Tour, Grand Slams and championship fights, especially with a reduced fall TV season.

Following the money further provides a path forward. In a new post-COVID world there will be less money available at least for a while. Thus, it will be incumbent on everyone in the sports industrial complex to find ways to create the new pie and be able to divide it equitably. Betting will become more important, as will advanced data. A variety of customized highlights products can be automatically created. Team and athlete channels can provide unprecedented access and enhanced production values from current Zoom videos. We would suggest that the North Star is actually the fans. Making them more than whole is both a good story and good business.

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