

Borussia Dortmund

Reappraisal

Bumps in the road

While longstanding brand and financial strengths hold true, Borussia Dortmund (BVB) is currently bedevilled by uncertainties. Some, such as the absence of a permanent coach and Champions League qualification, may be temporary. Potentially more challenging is the conflict between sporting and financial aims, given an apparent increased reliance on transfer gains (investor concern at the sale of exceptional goal-scorer Aubameyang is telling). However, there is undeniable reassurance in the scale of the surplus of market value to net player assets (broadly, c €240m per www.transfermarkt.de), further lively transfer inflation and BVB's prized development record. Moreover, finances remain resolutely robust.

Year end	Revenue* (€m)	EBITDA (€m)	PBT** (€m)	EPS** (€)	DPS (€)	EV/EBITDA (x)
06/16	281.3	86.7	73.8	0.68	0.06	5.1
06/17	328.4	74.1	61.1	0.56	0.06	6.0
06/18e	331.0	135.0	120.0	1.11	0.06	3.1
06/19e	375.0	85.0	71.0	0.66	0.06	5.0

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

Renowned player investment continues to pay off

The remarkable sale of Dembélé to Barcelona, followed by that of Aubameyang, all but comfortably guarantees a record EBITDA this year. This is welcome, given relative sporting disappointment, epitomised by premature exit from the Champions League and a likely near-halving in contribution to broadcasting revenue. Indeed we see creditable growth (maybe double-digit) in other pre-transfer income thanks to advertising and a new deal on domestic TV marketing, only for this to be offset by persistent high costs, notably labour. While this year is a hard act to follow owing to bumper transfers, we look for a clear rise in FY19 operational profit, assuming qualification for Champions League (BVB in the mix but minimal room for error) and more generous distribution from its new format. The markedly lower expected transfer gain for FY19 reflects the average of recent years excluding exceptionals.

Proven strategy and track record

Current management has transformed the company's fortunes since near-bankruptcy in 2005. It is 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 thanks to judicious player development.

Valuation: Unduly cautious

In a febrile atmosphere an EV/EBITDA of 5x more normal FY19e earnings ignores the long-term potential of strong brand development, valuable media rights and sustainable cash flow (estimated net cash €48m), backed by freehold property and substantial subscription revenue, and hidden reserves from player development. EV against resilient, growing pre-transfer revenue is barely 1x FY19e.

Travel & leisure

10 April 2018

Price €5.20

Market cap €478m

Net cash (€m) at December 2017 including finance leases 14.2

Shares in issue 92.0m

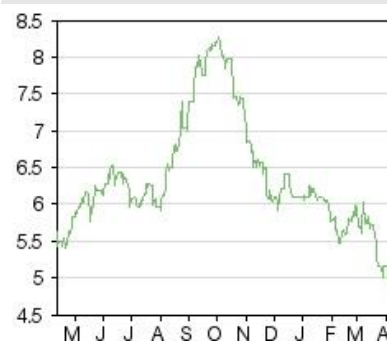
Free float 60.1%

Code BVB

Primary exchange Frankfurt

Secondary exchange N/A

Share price performance



% 1m 3m 12m

Abs (9.0) (15.8) (7.4)

Rel (local) (8.3) (8.1) (7.7)

52-week high/low €8.3 €4.9

Business description

The group operates Borussia Dortmund, a leading German football club, who were DFB Cup winners in 2016/17 and competed in this season's UEFA Champions and Europa Leagues (Champions League quarter-finalists in 2016/17).

Next events

Bundesliga season end 12 May 2018

Q318 results 15 May 2018

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Borussia Dortmund is a client of Edison Investment Research Limited

Investment summary

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 25 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. Last season was typically successful: victory in the German Cup, quarter-finalists in the Champions League and third place in the Bundesliga. The club's fabled stadium (the Westfalenstadion, now formally SIGNAL IDUNA PARK) has long enjoyed the highest average attendance (over 80,000) in the country and indeed in Europe. Borussia Dortmund was formed as Ballspielverein Borussia 09 e.V. Dortmund in 1909 (hence the BVB 09 logo) and was listed on the Frankfurt Stock Exchange in 2000.

Valuation: Unduly cautious

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. Despite current uncertainties, an EV/EBITDA rating of 5x FY19e 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. EV as a share of resilient and growing revenue is only 1x prospective. The company's transfer policy continues to generate significant hidden reserves in player values. Despite a positive balance of transfers since 2014, the surplus of market value, estimated by www.transfermarkt.de, to net player assets is c €240m.

Sensitivities

- Reliance on sporting fortunes, especially on participation in lucrative UEFA competitions.
- Serious player injuries cannot be foreseen but mitigated by a strong squad.
- Competes for a share of disposable consumer income but home attendance resilient and substantially pre-sold.
- Dependence on brand perception tempered by long-term contracts with major sponsors.
- Subject to external governing bodies, which may change the structure of German and European football.
- Negotiation of key media contracts is outside the company's control. Obligated to pay players and coaching staff in line with competitors.
- Potential conflict between sporting and financial aims. Increased reliance on transfer profit.

Financials

After its financial troubles under previous management Dortmund has successfully implemented a clear strategy focused on developing core revenue sources such as advertising, merchandising, match operations and broadcasting. Management is similarly intent on 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 EBITDA despite a disappointing season, notably in Europe and a consequent change of coach. The record outturn is driven by sales of star players, Dembélé and Aubameyang.

The company reports quarterly, with preliminary results for the full year due in late August.

Company description: A leading German football club

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

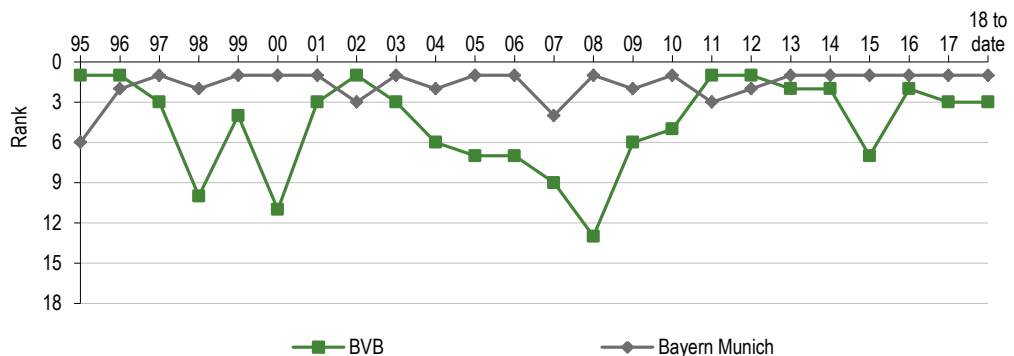
Exhibit 1: Club honours

German championship*	1956, 1957, 1963, 1995, 1996, 2002, 2011 and 2012
DFB Cup	1965, 1989, 2012 and 2017
German Supercup	1989, 1995, 1996, 2008,** 2013 and 2014
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 54 years of the Bundesliga the club has achieved top six status (the benchmark for UEFA competition qualification) on 24 occasions (also in the current season to date) in addition to its five titles. Indeed more recently, as shown in Exhibit 2, Dortmund's performance in the Bundesliga has been second just to dominant Bayern Munich as the only other club to have won multiple titles in the last 20 years or so. The prolonged decline between 2003 and 2008 reflects financial troubles under previous management, while the 2015 dip proved short-lived (change of coach) and still allowed successful international participation as Europa League quarter-finalists.

Exhibit 2: Bundesliga performance since 1995



Source: Bundesliga

Head coach: Peter Stöger joined Dortmund in December 2017, almost immediately after leaving Köln which he had managed since 2013. He took Köln to promotion to the Bundesliga in his first season with the club and back into European competition in 2017/18 for the first time for 25 years. Previously he enjoyed a long and successful association with Austria Wien, both as a player and then as coach and sporting director. He also won an Austrian league title with Rapid Wien which he represented in a European Cup Winners' Cup final. He was a regular Austrian international (65 caps, including the 1998 World Cup). He is 51 and his contract at Dortmund runs until June.

Sporting director: Michael Zorc (55) has spent his whole career at Dortmund, first as player for 17 years (Bundesliga appearance record), culminating in the Bundesliga and Champions League success of the mid 1990s and then as sports director since 1998. His contract has just been extended to 2021.

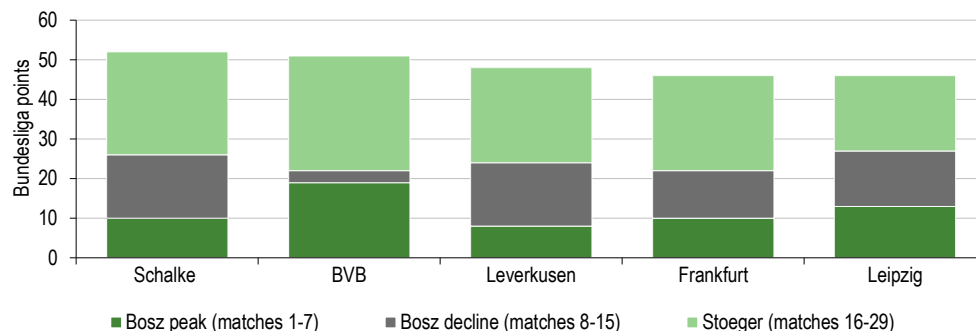
Exhibit 3: BVB squad participation in 2017-18 season (43 matches: 29 Bundesliga, six Champions League, four Europa League, three German Cup and one Supercup)

	Nationality	Age**	At BVB since	From	Contract expiry	Matches started	Goals§
Goalkeeper							
Roman Bürki	Sui*	26	2015	Freiburg	2021	42	-
Roman Weidenfeller	Ger*	37	2002	Kaiserslautern	2018	1	-
Defenders							
Sokratis Papastathopoulos	Gre*	29	2013	Werder Bremen	2019	37	3
Ömer Toprak	Tur*	28	2017	Bayer Leverkusen	2021	26	-
Lukasz Piszczek	Pol*	32	2010	Hertha Berlin	2020	26	-
Marcel Schmelzer	Ger*	29	2005	BVB U19	2021	22	1
Jeremy Toljan	Ger	23	2017	Hoffenheim	2022	19	1
Marc Bartra	Sp*	26	2016	Barcelona	2020****	17	4
Dan-Axel Zagadou	Fr	18	2017	PSG	2022	10	1
Raphaël Guerreiro	Por*	22	2016	Lorient	2020	9	2
Manuel Akanji	Sw*	22	2018	Basel	2022	6	-
Jan-Niklas Beste	Ger	18	2016	BVB U19	2018	1	-
Midfield***							
Christian Pulisic	US*	18	2014	BVB U19	2020	30	5
Mario Götze	Ger*	25	2016	Bayern Munich	2020	23	2
Julian Weigl	Ger*	21	2015	1860 München	2021	22	1
Gonzalo Castro	Ger*	30	2015	Bayer Leverkusen	2020	22	1
Shinji Kagawa	Jap*	28	2014	Manchester United	2020	19	6
Nuri Sahin	Tur*	28	2013	Real Madrid	2019	19	2
Mahmoud Dahoud	Ger	21	2017	Borussia M'gladbach	2022	18	-
Jadon Sancho	Eng	17	2017	Manchester City U18	2020	3	-
Forwards							
Pierre-Emerick Aubameyang	Gab*	28	2013	St Etienne	2021*****	24	21
Andrey Yarmolenko	Ukr*	27	2017	Dynamo Kiev	2021	19	6
Maximilian Philipp	Ger	23	2017	Freiburg	2022	15	7
André Schürrle	Ger*	25	2016	Wolfsburg	2021	15	3
Michy Batshuayi	Bel*	24	2018	Chelsea (on loan)	2018	12	9
Marco Reus	Ger*	28	2012	Borussia M'gladbach	2023	9	3
Alexander Isak	Swe	17	2017	AIK Solna	2022	2	1

Source: Bundesliga, BVB. Note: *Full international; **age at start of season; ***also one start by Dembélé, sold to Barcelona August 2017 and four starts by Subotic, sold to St Etienne January 2018; ****sold to Real Betis January 2018; *****sold to Arsenal January 2018; § excludes four goals in Supercup penalty shootout and two own goals; **bold**: acquisitions this season.

The current squad of 28 has an average age of 25, which is similar to that of closest Bundesliga rivals, and includes a dozen current full internationals. Participation this season by matches started is shown in Exhibit 3, which also highlights key changes for 2017/18, notably Yarmolenko and Philipp replacing Dembélé in attack and Toprak and Dahoud coming in for Ginter and Bender. However, arguably even more significant is the change that did not happen in August, ie retention of Aubameyang despite intense speculation. His goal-scoring (21 in all competitions) remained exceptional until his exit in January, which prompted the arrival of Batshuayi on loan from Chelsea.

Exhibit 4: The race for 2018/19 Champions League



Source: Bundesliga

The performance this season has been remarkably mixed, seen in Exhibit 4. Top of Bundesliga after seven games (record start for coach Peter Bosz), then eight matches without a win, leading to

Bosz's departure in December, and a more impressive start (13 league games undefeated apart from a recent dismal 6-0 loss to Bayern) under Peter Stöger. With just five matches to go, Dortmund is now third in the Bundesliga, so well placed for the Champions League next season (top four qualify directly under the new format). However, a tougher schedule (Bundesliga points total of outstanding opponents) than immediate rivals Schalke and Leipzig (Exhibit 4) and only a narrow advantage ensure "a race to the end," per coach Stöger. By contrast, this season's results in European competition were uniformly poor, ie only two points from Champions League in stark contrast to a group win last season, followed by a bumpy run in Europa League, when the team rode its luck against Atalanta only to disappoint against Salzburg in the round of 16.

Well-defined strategy

After its financial troubles (see page 9), Dortmund has successfully concentrated on developing core revenue sources such as broadcasting, advertising, match operations and merchandising. Management is similarly intent on maximising success on the field without taking on new debt, while achieving a balance between financial and sporting interests.

- **Squad development:** Exhibit 5 shows that BVB continues to adhere to its aim of putting together a competitive team with a focus on promising young players and on a tight budget. Identification of up-and-coming players at minimal cost (even free) and their development at the BVB Academy are to the fore, underpinning a healthy potential surplus to book value, as estimated by www.transfermarkt.de. Given an enviable development record with Lewandowski, Aubameyang, Reus and Dembélé, there is excitement both about Pulisic and Weigl (highlighted) as established first-team regulars despite their youth and the potential of teenage newcomers Isak and Sancho after impressive debuts. On disposals, management has achieved a balance with considered sales, be it "too good an offer to refuse" (Dembélé) or rationalisation of an oversupplied midfield or defence. Despite wariness at his loss, this may also apply to Aubameyang, given a good price and a strained relationship with the club.

Exhibit 5: Significant player transactions

Recent €10m+ disposals	Date	Age at signing	Cost (€m)	Transfer fee (€m)	Buyer
Mats Hummels	2016	27	4	35	Bayern Munich
Ilkay Gündogan	2016	25	5	27	Manchester City
Henrikh Mkhitaryan	2016	27	27	42	Manchester United
Ciro Immobile	2016	25	18	11	Sevilla
Ousmane Dembélé	2017	20	15	105	Barcelona
Sven Bender	2017	28	Free	12	Bayer Leverkusen
Matthias Ginter	2017	23	10	17	Bor. M'Gladbach
Emre Mor	2017	20	10	13	Celta Vigo
Adrián Ramos	2017	31	10	12	Chongqing
Marc Bartra	2018	27	10	15	Real Betis
Pierre-Emerick Aubameyang	2018	28	13	64	Arsenal

Total estimated realised surplus to cost before depreciation c €230m

Current squad development						
Under 26 at signing*	Date	Age at signing	Transfer fee (€m)	Current value (est) (€m)	Contract expiry	
Marcel Schmelzer	2008	20	Free	7	2021	
Marco Reus	2012	23	17	35	2023	
Sokratis Papastathopoulos	2013	25	10	22	2019	
Christian Pulisic	2014	16	Free	45	2020	
Shinji Kagawa	2014	25	8	13	2020	
Julian Weigl	2015	19	3	30	2021	
Mario Götze	2016	24	22	20	2020	
Raphaël Guerreiro	2016	22	12	20	2020	
André Schürrle	2016	25	30	18	2021	
Maximilian Philipp	2017	23	20	20	2022	
Mahmoud Dahoud	2017	21	12	18	2022	
Manuel Akanji	2018	22	21	20	2022	
Youth development:						
Alexander Isak	2017	17	9	6	2022	
Jadon Sancho	2017	17	9	8	2020	
Dan-Axel Zagadou	2017	18	Free	5	2022	
Sergio Gómez	2018	17	3	2	2021	

Source: www.transfermarkt.de. Note: *excludes transfer fees under €10m without likely major value uplift.

Dortmund's positive reconciliation of conflicting interests is further highlighted by the disparity in its net transfer balance (amount received less paid) with those of certain fellow Champions League regulars. Exhibit 6 shows the last five seasons. The comparison with Bayern is telling as Bundesliga performance is also noted. While Dortmund has ensured European football at a fraction of Bayern's net spend and easily outpaced other domestic rivals (over the last five years 14% more Bundesliga points than nearest, Bayer Leverkusen), there is a glaring 25% points inferiority to Bayern, with the recent 6-0 "thrashing" (www.bundesliga.com) by the new Bundesliga champions an unwelcome reminder.

Exhibit 6: Net transfer balances since 2013/14 of selected Champions League regulars

€m	2013/14	2014/15	2015/16	2016/17	2017/18	Cumulative since 2013/14	
						Net balance	Bundesliga rank (points)
Borussia Dortmund	-6 (2)	-61 (7)	+18 (2)	-11 (3)	+129 (3)	69	2 (310)
Bayern Munich	-23 (1)	-5 (1)	-47 (1)	-21 (1)	-86 (1)	-182	1 (411)
Manchester City	-107	-59	-154	-180	-223	-723	
Manchester United	-77	-143	-54	-138	-156	-568	
Paris St. Germain	-109	-47	-96	-79	-145	-476	
Barcelona	-73	-88	-14	-89	-93	-357	-
Chelsea	-60	-3	-3	-34	-65	-159	
Juventus	12	-20	-77	-17	-5	-107	
Real Madrid	-62	-11	-63	4	63	-69	-

Source: www.transfermarkt.de. Note: Bundesliga rank in brackets.

- **Brand development:** The Borussia Dortmund brand is one of the company's prime assets. It has been rated for 2017 by Brand Finance as the 11th most valuable football brand, unchanged in rank on 2016 but markedly higher in terms of value owing to renewed Champions League exposure. In addition to a global fan base (see below) average Bundesliga home match attendance of c 80,000 is consistently the highest in Europe. Reflecting the longstanding devotion of the club's Westphalia heartland and epitomised by the fervent 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 intensity and loyalty, which is a powerful platform for advertising. Management aims to monetise this as follows:
 - **Advertising (27% of FY18e non-transfer revenue and +3% in FY17):** 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 2025), SIGNAL IDUNA (stadium, extended to 2021) and PUMA (kit, until 2020). There are 12 BVB ChampionPartners (Opel, bwin, Eurowings, Brinkhoff's, SIGNAL IDUNA, Sprehe, Sparda-Bank, unitymedia, Wilo, Hankook, THORN and ROWE) as well as about 50 lower-tier sponsors. This activity is outsourced to Lagardère, which receives commission on revenue generated.
 - **Merchandising (11% of FY18e pre-transfer revenue and -1% in FY17):** the award of licences and revenue from the sale of team merchandise. In addition to partners' wholesale distribution channels, sales are made via a major FanWelt centre near the stadium, branded stores (FanShops) in Dortmund, sales kiosks at the stadium and e-commerce, www.bvbonlineshop.com (33% of FY17 sales).
 - **New media:** in promoting brand awareness, BVB continues to be very active on social media, attracting 1.2m new followers across all its platforms in H118 alone. While Facebook remains the mainstay (currently 15.4m 'likes' on the official fan page), the strongest growth has been on Instagram (since June 2017 followers up 20% at 5m) and on Twitter (3.2m followers). However, both are small compared with Chelsea and Arsenal, which have respectively 48m and 38m Facebook 'likes' and 11m Instagram followers, which confirms encouraging scope for Dortmund. Asia is proving especially receptive, highlighted by a live stream to around half a million people during the 2016 tour of China and a 25% rise in followers on Sina Weibo in H118, boosted by the successful 2017 return visit and the launch of the company's Chinese language website. BVB's own app still enjoys strong demand (usage up 6% in H118), as does the dedicated 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. The subscription channel BVB Total shows club videos, Bundesliga matches and all other competitive matches in full length. Current subscription costs are €4.95 for a month or €39.09 for a year.
 - **Match day operations (13% of FY18e pre-transfer revenue and -6% in FY17):** management regards SIGNAL IDUNA PARK, Germany's largest football stadium with capacity for 81,360, as its most valuable asset apart from the team. Known as the Westfalenstadion until 2005, the facility was built for the 1974 World Cup but has since been extensively enlarged and modernised. With home matches sold out and a policy of inflation based pricing as a community club (indeed FY17 saw a price freeze), the scope for ticketing revenue growth seems limited. Apparent underachievement with the likes of Arsenal and Manchester United, where ticketing was 24% and 19% respectively of FY17 revenue, is thus unfair; Bayern Munich's 17% revenue share (FY16) is a better comparative. Two-thirds of capacity is pre-sold as season tickets, which brings revenue visibility, and an annual footfall of 1.4m spectators at Bundesliga games alone brings ancillary income from merchandising and catering. The stadium is not multi-functional.

- **Broadcasting (37% of FY18e pre-transfer revenue and +52% in FY17):** 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 well in advance, with the Bundesliga agreeing in 2016 the sale of rights for four seasons from 2017/18 and UEFA selling rights on a three-year basis, effective 2018/19. The new Bundesliga deal (still predominantly with Sky Deutschland but no longer exclusively) is worth an extra 85%, ie c €1.15bn income pa. As for average attendance, the Bundesliga (41,000) is much higher than the Premier League (36,000), La Liga (28,000) and Serie A (22,000). UEFA has yet to announce distribution to clubs for the next Champions League cycle but promised on announcement of the competition's reform that it will be 'increased significantly' (our FY19e forecast assumes a rise of about a third in BVB Champions League revenues). The new format, notably more 'big name' clubs and staggered viewing times, is aimed at boosting the appeal to broadcasters.

Management

The company's senior management (see below) 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 was recently extended to 2022. He is also 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 has also been extended to 2022. He was previously a partner at Rölf'sPartner, one of the leading business consultancies in Germany. He was awarded "CFO of the year 2013" by the German "FINANCE-Magazine."
- **Sales and marketing and digitalisation: Carsten Cramer** recently became a further managing director, having served as sales and marketing director since 2010. He joined from leading sports marketing agency Sportfive (now Lagardère Sports) where he served latterly as a team leader at BVB and then as senior vice-president with nationwide duties.

Sensitivities

- The company's business operations are dependent on sporting success. Weak performance could cause revenue to fall and affect the ability to attract and retain players and coaches. Participation in lucrative UEFA competitions cannot be relied on, although the club has qualified regularly and will benefit from broader Champions League access for Bundesliga teams.
- There is substantial reliance on player transfer earnings which are volatile and hard to predict.
- While serious injuries cannot be foreseen, the club maintains a strong squad and minimises the risk of poor investment in new players by intensive scouting and medical examinations.
- The company competes 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.
- Dortmund is dependent on the strength and perception of its brand. While damage may impair its ability to attract sponsors, the company invests heavily to ensure consistent quality.
- Long-term contracts with major sponsors give security independent of sporting performance.
- Dortmund is subject to external governing bodies, eg 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 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.
- The company's digital media strategy is still developing. Piracy and illegal live streaming may adversely affect its broadcasting and new media and mobile revenue.
- The club is obliged to pay players and coaching staff in line with competitors. Labour costs have risen sharply in recent years, accounting in FY17 for over 50% of its revenue excluding transfers, which is similar to key peers.
- 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

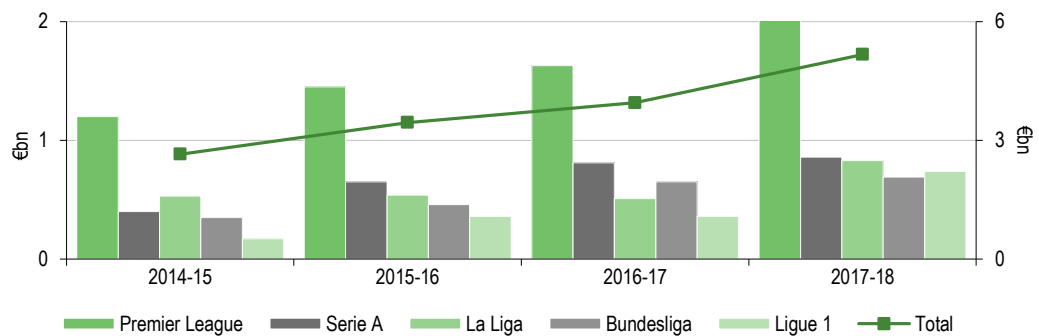
Among major listed peers, there is limited comparability with BVB in terms of valuation indicators. By far the largest by market cap, Manchester United and Arsenal offer very limited free float, while Juventus has a majority shareholder and sizable net debt. The failures of Arsenal and Olympique Lyonnais to qualify for current Champions League suggest a lower outturn this year but both have booked much higher year-on-year transfer profit. Against available peer numbers (consensus forecasts are not available for most) BVB is rated the lowest, even using normal FY19e.

Exhibit 7: Valuation comparison with major listed peers (EBITDA includes transfer activity)						
	Mkt cap	EV	EBITDA	EV/EBITDA	Pre-transfer revenue	EV/pre-transfer revenue (x)
				(x)		
Prospective						
Borussia Dortmund	€471m	€423m	€85.0m	5.0	€375m	1.1
Manchester United	£2250m	£2550m*	£180.0m**	14.2	£580m**	4.4
Historic						
Borussia Dortmund	€471m	€441m	€74.1m	6.0	€328m	1.3
Manchester United	£2250m	£2460m*	£210.7m	11.7	£581m	4.2
Arsenal	£2150m	£2200m	£144.3m	15.2	£423m	5.2
Juventus	€620m	€780m	€159.9m	4.9	€412m	1.9
Olympique Lyonnais	€168m	€367m	€51.0m	7.2	€198m	1.9

Source: Company accounts. Note: *\$1.41/£. ** Mid-point of guidance at February 2018.

Value creation is emphasised by the company's transfer policy, which is generating substantial hidden reserves in player values. The past two years saw average capital gains of c €63m (our estimate), even before the "exceptional" Dembélé transaction, and the scope for further gains is high. The surplus of market value to net player assets is c €240m if the reported December 2017 carrying value of €184m, which included Aubameyang, is set against sports website www.transfermarkt.de's current valuation of €405m. Moreover, it necessarily does not allow for step-changes in the value of emerging talent, which Dortmund is so adept at identifying and which are attracting the attention of major clubs at ever younger ages. Potential prodigies such as Sancho, Isak and Gómez (Exhibit 5) may emulate the uplift (admittedly unrealised) of estimated €45m attributable to similarly youthful Pulisic, let alone the bumper return on Dembélé. Beyond this is the benefit of sustained transfer market buoyancy, highlighted by a doubling in spend by the five major European leagues over the last four years and by almost a third in 2017/18 alone (Exhibit 8)

Exhibit 8: Player transfer market spend by five major European leagues over last four years



Source: www.transfermarkt.de

This comes at a price in terms of player replacement but Dortmund is a net seller. More concerning is the threat of undue sporting detriment by disposals. With management's objective to declare an annual net profit, the scale of intangible amortisation (over €60m pa) and operating cost pressures (marginal EBITDA in Q218 without the buttress of transfers) risks a disruptive volume of transactions. While we are satisfied, as above, that the company has the resources to meet such financial needs, it is reasonable to be wary about the sporting impact.

More immediately, our FY19 forecasts are subject to Champions League involvement next season (Europa seems almost assured as BVB now nine points clear of seventh place) as well as satisfactory appointment of a permanent coach and key striker. A strong end to the season could see both current interims (Stöger and Batshuayi) retained on a long-term basis.

The share price is at almost 50% discount to a simple sum-of-the-parts valuation of €9.50, based on estimated market value of players (€405m per www.transfermarkt.de), brand value (€420m at June 2017 per Brand Finance) and financial position (€48m net cash FY18e). Speculation about a change in ownership rules to allow investors to take majority stakes may have been calmed by the clubs' recent vote to retain the so-called 50+1 rule, under which fee-paying club members must own more than 50% of voting rights. However, this may only be temporary as German clubs' requirement to be competitive financially in Europe will not abate.

Financials

Borussia Dortmund's turnaround has been remarkable. The company was at risk of bankruptcy in 2005, broadly attributed to extravagance, notably on foreign players, after Bundesliga success. New management (the current CEO 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. Key initiatives included the repurchase of the stadium, 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. A c €140m fundraising in 2014, backed by key sponsors and new partnerships, was a strong endorsement of strategy.

FY18e: H1 was a tale of two quarters (Exhibit 9). While Q118 was notable for the Dembélé transfer, which drove a doubling of EBITDA vs Q117, the following period was unaffected by transfers and saw a reduction in EBITDA (c €7m, relatively minor in full-year context) on flat revenue owing mainly to wage pressure, compounded by one-off severance costs related to the previous coach's set-up. Other operating costs more than doubled largely owing to transfer-related expenses. In Q2 Champions League setbacks led to much lower (c 40%) international broadcasting income, albeit

fortuitously redeemed by the initial benefit of the new deal on domestic TV marketing. While advertising remained encouraging (up 7%), marked by new Champion Partners Opel and bwin, there was a further decline in merchandising (down 24%), which is common across the league.

Despite such quarterly volatility, we retain our operational assumptions for this year. Our recent €37m EBITDA upgrade for H2 reflects January transfers (principally Aubameyang and Bartra) with no allowance for end of season dealings.

FY19e: we are now a little more cautious about transfer gains, given Aubameyang's exit so soon after Dembélé. We assume FY19 transfers to be on a par with the average of the last three years, largely excluding the impact from exceptional Dembélé. However, management recently stated a need to adjust the squad, even if subject to the decisions of the new coach. Operationally, there should be a sizeable boost in broadcasting income (tba by UEFA – we assume up over a third on FY17) from the revamped Champions League; however, this is dependent on qualification over the remaining five Bundesliga games.

Exhibit 9: Revenue and profit analysis									
Year end June (€m)	Q117	Q217	H217	FY17	Q118	Q218	H218e	FY18e	FY19e
Home matches:									▲
Bundesliga	3	5	12	17	3	5	9	17	17
Champions League	1	2	2	5	1	2	-	3	4
Europa League	-	-	-	-	-	-	2	2	-
Domestic cups	1	1	1	3	1	-	-	1	2
Away matches:									
Champions League	1	2	2	5	1	2	-	3	4
Europa League	-	-	-	-	-	-	2	2	-
Domestic cups	1	-	2+final	3+final	1	2	-	3	3
Revenue									
Match operations:									
Bundesliga	4.7e	8.2e	14.1e	27.0	4.8e	8.3e	13.9e	27.0	27.5
Champions League	1.9e	3.8e	3.8e	9.5	2.0e	3.9e	-	5.9	8.0
Europa League	-	-	-	-	-	-	4.0e	4.0	-
Domestic cups	1.1e	1.0e	3.2e	5.3	1.2e	0.5e	0.1e	1.8	3.5
Other	0.8e	0.8e	0.6e	2.2	2.6e	0.5e	1.2e	4.3	2.5
Total	8.5	13.8	21.6	43.9	10.6	13.2	19.2	43.0	41.5
Broadcasting:									
Bundesliga	16.2	16.3	33.6	66.1	21.6	21.8	44.6	88.0	92.0
Champions League	19.6	14.0	16.5	50.1	18.9	8.5	-	27.4	68.0
Europa League	0.9	-	-	0.9	-	-	4.0	4.0	-
Domestic cups	1.6	(0.3)	7.3	8.6	1.8	1.5	0.3	3.6	4.5
Total	38.3	30.0	57.5	125.8	42.3	31.8	48.9	123.0	164.5
Advertising	17.8	22.3	47.3	87.4	21.3	23.9	50.8	96.0	99.0
Merchandising	9.2	14.0	16.3	39.5	8.7	10.7	17.6	37.0	37.0
Catering / other	7.8	7.4	16.7	31.9	5.8	7.2	19.0	32.0	33.0
Revenue before transfers	81.6	87.4	159.4	328.4	88.7	87.0	155.3	331.0	375.0
Transfers	45.2*	-	32.1	77.3	136.2**	-	73.8**	210.0**	75.0***
Total revenue	126.8	87.4	191.5	405.7	224.8	87.0	229.1	541.0	450.0
Other operating income	1.0	0.7	2.5	4.2	0.5	2.3	2.2	5.0	5.0
Labour costs	(38.4)	(43.8)	(95.7)	(177.9)	(43.9)	(50.4)	(100.7)	(195.0)	(205.0)
Share of revenue before transfers	47%	50%	60%	54%	49%	58%	65%	59%	55%
Material costs	(5.8)	(8.6)	(11.5)	(25.9)	(5.6)	(6.7)	(11.7)	(24.0)	(24.0)
Other operating costs	(43.4)	(25.9)	(62.7)	(132.0)	(94.4)	(29.8)	(67.8)	(192.0)	(141.0)
EBITDA	40.1	9.8	24.2	74.1	81.4	2.5	51.1	135.0	85.0

Source: Edison Investment Research. Note: ▲ Assuming Champions League round of 16 and DFB Cup semi-final. *Including disposal of Mkhitarjan. **Including disposals of Dembélé, Bender, Mor, Bartra and Aubameyang. ***Notional (assumed average of transfer revenue of three previous years excluding "exceptional" Dembélé and Aubameyang transactions).

Exhibit 10: Financial summary

	€'000s	2016	2017	2018e	2019e
June		IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS					
Revenue		376,300	405,700	541,000	450,000
EBITDA		86,700	74,100	135,000	85,000
Operating Profit (before amort. and except.)		75,900	62,600	123,000	73,000
Intangible Amortisation		(32,000)	(51,900)	(64,000)	(60,000)
Exceptionals		(7,500)	(100)	(1,100)	0
Other		0	0	0	0
Operating Profit		36,400	10,600	57,900	13,000
Net Interest		(2,100)	(1,500)	(3,000)	(2,000)
Other financial items		0	0	0	0
Profit Before Tax (norm)		73,800	61,100	120,000	71,000
Profit Before Tax (FRS 3)		34,300	9,100	54,900	11,000
Tax		(4,900)	(900)	(7,000)	(1,000)
Profit After Tax (norm)		62,700	51,900	102,000	60,400
Profit After Tax (FRS 3)		29,400	8,200	47,900	10,000
Average Number of Shares Outstanding (m)		92.0	92.0	92.0	92.0
EPS - normalised (c)		68.2	56.4	110.9	65.7
EPS - (IFRS) (c)		32.0	8.9	52.1	10.9
Dividend per share (c)		6.0	6.0	6.0	6.0
EBITDA Margin (%)		23.0	18.3	25.0	18.9
Operating Margin (before GW and except.) (%)		20.2	15.4	22.7	16.2
BALANCE SHEET					
Fixed Assets		302,800	354,900	364,000	348,000
Intangible Assets		65,300	141,500	147,000	140,000
Tangible Assets		188,400	184,700	182,000	180,000
Investments		49,100	28,700	35,000	28,000
Current Assets		121,800	123,700	149,000	166,000
Stocks		10,200	9,000	10,000	10,000
Debtors		51,100	48,800	50,000	50,000
Cash		51,700	49,300	59,000	76,000
Other		8,800	16,600	30,000	30,000
Current Liabilities		(78,800)	(140,900)	(140,000)	(138,000)
Creditors		(76,200)	(130,600)	(137,000)	(135,000)
Short term borrowings		0	0	0	0
Finance leases		(2,600)	(10,300)	(3,000)	(3,000)
Long Term Liabilities		(36,200)	(25,400)	(18,000)	(18,000)
Long term borrowings		0	0	0	0
Finance leases		(19,000)	(8,700)	(8,000)	(8,000)
Other long term liabilities		(17,200)	(16,700)	(10,000)	(10,000)
Net Assets		309,600	312,300	355,000	358,000
CASH FLOW					
Operating Cash Flow		44,400	12,200	1,000	30,000
Net Interest		(1,400)	(2,000)	(2,800)	(2,200)
Tax		(300)	(5,500)	(6,000)	(6,000)
Capex		(9,400)	(8,100)	(9,000)	(9,300)
Acquisitions/disposals		(20,500)	9,100	40,000	10,000
Financing		(7,700)	0	0	0
Dividends		(4,600)	(5,500)	(5,500)	(5,500)
Net Cash Flow		500	200	17,700	17,000
Opening net debt/(cash)		(29,600)	(30,100)	(30,300)	(48,000)
Finance leases initiated		0	0	0	0
Other		0	0	0	0
Closing net debt/(cash)		(30,100)	(30,300)	(48,000)	(65,000)

Source: Company data, Edison Investment Research

Contact details	Revenue by geography
1 Rheinlanddamm 207-209 D-44137 Dortmund Germany +49 (0) 231 90 20 745 www.bvb.de/aktie	N/A
Management team	
Chief executive: Hans-Joachim Watzke	Chief financial officer: Thomas Treß
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 2022. He is also the owner-founder of Watex, a leading manufacturer of protective clothing for industrial workers and firefighters.	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 June 2022. He was previously a partner at RöfIsPartner, one of the leading business consultancies in Germany. He was awarded CFO of the year 2013 by the German FINANCE-Magazine.
Sales and marketing and digitalisation: Carsten Cramer	
Carsten Cramer recently joined the board, having served as sales and marketing director since 2010. He was previously at leading sports marketing agency Sportfive (now Lagardère Sports) where he served latterly as a team leader at BVB and then as senior vice-president with nationwide duties.	
Principal shareholders	(%)
Evonik Industries	14.8
Bernd Geske	9.2
Borussia Dortmund	5.5
SIGNAL IDUNA	5.4
PUMA SE	5.0
Companies named in this report	
Bayern Munich, Real Madrid, Arsenal, Manchester United, Juventus, Atlético Madrid, Barcelona, PSG, Chelsea, PUMA, EVONIK, SIGNAL IDUNA	

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