

Borussia Dortmund

Reappraisal

It's not over till it's over!

Travel & leisure

17 June 2019

Price €8.42

Market cap €775m

Net cash (€m) at 31 March 2019 including finance leases 12.7

Shares in issue 92.0m

Free float 60.1%

Code BVB

Primary exchange FRA

Secondary exchange N/A

Pushing champions Bayern Munich to the wire can only have enhanced Borussia Dortmund's (BVB) famed 'Echte Liebe' brand. Three prominent player signings immediately post-season mark its resolve to improve even on a campaign that clearly exceeded expectations with a new head coach and a developing squad. That player spend (estimated at c €75m) is almost covered by the proceeds from January's bumper transfer of Pulisic, while a new independent squad valuation, highlighting Jadon Sancho (19) as the most valuable Bundesliga player (€100m), confirms BVB's substantial hidden reserves (broadly, c €300m, according to www.transfermarkt.de). We are broadly maintaining forecasts for this year and next with renewed confidence.

Year end	Revenue* (€m)	EBITDA (€m)	PBT** (€m)	EPS** (€)	DPS (€)	EV/EBITDA (x)
06/17	328.4	74.1	61.1	0.56	0.06	10.1
06/18	313.3	126.6	111.2	1.03	0.06	5.7
06/19e	370.0	105.0	93.0	0.86	0.06	7.1
06/20e	383.0	110.0	98.0	0.91	0.06	6.9

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

What a difference a year makes

Last-day competition for the Bundesliga title rather than Champions League qualification, Dortmund's minimum target, exemplifies the club's performance gain in 2018/19. This is all the more creditable after prior season upheavals, notably three changes of head coach in quick order and the loss of exceptional talent such as Aubameyang and Dembélé. Sporting expectations are now inevitably higher, so we welcome significant investment in established, if still developing players (current internationals Brandt, Hazard and Schulz) rather than youth, in line with planned squad optimisation during coach Favre's second summer transfer window.

Forecasts maintained on increasing resilience

While two bumper transfers make FY18 a hard act to follow, we look for a clear rise this year in operational profit thanks to c 20% higher pre-transfer revenue, driven by broadcasting income from the Champions League. This period's own bumper deal (Pulisic to Chelsea for €64m) should further secure our maintained EBITDA forecast for the full year as we expect only break-even in Q4 (negative €1.9m in Q418). For FY20, the absence of changes in media contracts and competitions suggests profit consolidation, assuming Champions League qualification. Transfer dealings are the joker in the pack; it is invidious to single out Sancho, but disposal at current valuation might alone yield the bulk of our EBITDA forecast.

Valuation: Long-term play

www.transfermarkt.de's new Bundesliga player valuation (c €480m, adjusted for loans/disposal) provides a respected pointer to BVB's hidden reserves (c €300m surplus of market value to net player assets). While notional and at sporting cost, this underpins our forecasts in view of increased reliance on transfers. The share price is at a c 20% discount to a simple sum-of-the-parts valuation of €10.75.

Share price performance



%	1m	3m	12m
Abs	(4.9)	7.7	39.7
Rel (local)	(5.7)	3.2	51.4
52-week high/low		€10.09	€5.40

Business description

The group operates Borussia Dortmund, a leading German football club, Bundesliga runners-up in 2018/19, DFB Cup winners in 2016/17 and competing in next season's UEFA Champions League (round of 16 participants in 2018/19).

Next events

Edison roadshow, London	18 June 2019
DFL-Supercup vs Bayern Munich	3 August 2019
Preliminary results	Late August 2019

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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: narrow runners-up in the Bundesliga and group stage winners in the Champions League. The club's fabled stadium (the Westfalenstadion, now formally Signal Iduna Park) has long enjoyed the highest average football attendance (over 80,000) in the world. 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: Long-term play

Borussia Dortmund has the lowest rating among listed peers, based on prospective EV/EBITDA and EV/Pre-transfer revenue. An EV/EBITDA rating of 7x 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 barely 2x prospective. The company's transfer policy continues to generate significant hidden reserves in player values. Despite a positive balance of transfers since 2013/14, the surplus of market value, estimated by www.transfermarkt.de, to net player assets is c €300m.

Sensitivities

- Reliance on sporting fortunes, especially on participation in lucrative UEFA competitions.
- Serious player injuries cannot be foreseen, but are 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.

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 fund-raising in 2014, backed by key sponsors and new partnerships, was a strong endorsement of strategy.

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, four DFB Cups and six DFL-Supercups, as well as the Champions League in 1997 and the European Cup Winners' Cup in 1966.

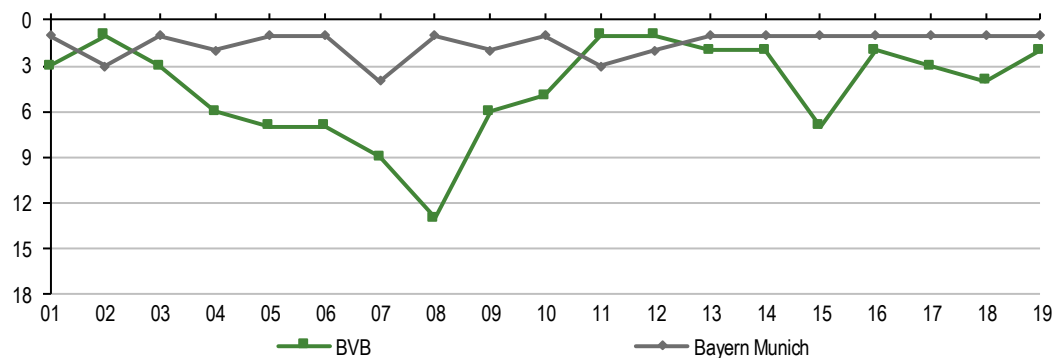
Exhibit 1: Club honours

German championship*	1956, 1957, 1963, 1995, 1996, 2002, 2011 and 2012
DFB Cup	1965, 1989, 2012 and 2017
DFL-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 56 seasons of the Bundesliga, the club has achieved top six status (the benchmark for UEFA competition qualification) on 25 occasions (including the recent season when it was second) in addition to its five titles. Indeed, 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 2001



Source: Bundesliga

Head coach: Lucien Favre joined Dortmund in May 2018 after two years as head coach at Nice. He took Nice to their highest league position for 40 years (third, with Champions League qualification) in his first season with the club but European competition was narrowly missed in the following season (8th in Ligue 1). Over the previous decade he gained valuable Bundesliga experience as coach both at Hertha Berlin (fourth in 2008/09) and then at Borussia Mönchengladbach (third in 2014/15). This followed a long and successful association with Swiss football, both as a player (regular international with 24 caps and a Swiss league title with Servette) and as a manager (two league titles with FC Zürich). He is 61 and his contract at Dortmund runs until June 2020.

Sporting director: Michael Zorc 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. Aged 56, he is under contract until 2021.

Participation in the recent season by matches started is shown in Exhibit 3, which also highlights key changes for 2018/19 (acquisitions shown in bold).

Exhibit 3: BVB squad participation in 2018/19 season							
(45 matches: 34 Bundesliga + eight Champions League + three DFB Cup)							
	Nationality	Age**	At BVB since	From	Contract expiry	Matches started	Goals§
Goalkeeper***							
Roman Bürki	Sui*	27	2015	Freiburg	2021	40	-
Defenders							
Abdou Diallo	Fr	22	2018	Mainz	2023	37	1
Manuel Akanji	Sw*	23	2018	Basel	2022	31	1
Lukasz Piszczek	Pol*	33	2010	Hertha Berlin	2020	26	1
Achraf Hakimi	Mor*	19	2018	Real Madrid (on loan)	2020	25	3
Raphaël Guerreiro	Por*	23	2016	Lorient	2020	21	6
Dan-Axel Zagadou	Fr	19	2017	PSG B	2022	20	2
Marcel Schmelzer	Ger*	30	2005	BVB II	2021	9	-
Ömer Toprak	Tur*	29	2017	Bayer Leverkusen	2021	6	-
Midfield							
Axel Witsel	Bel*	29	2018	T J Quanjian	2022	40	6
Thomas Delaney	Den*	26	2018	Werder Bremen	2022	33	3
Jadon Sancho	Eng	18	2017	Manchester City U18	2022	31	13
Mario Götze	er*	26	2016	Bayern Munich	2020	26	7
Julian Weigl	Ger*	22	2015	1860 München	2021	21	1
Christian Pulisic	US*	19	2014	Chelsea (on loan)	2019****	17	7
Mahmoud Dahoud	Ger	22	2017	Borussia M'gladbach	2022	12	1
Forwards							
Marco Reus	Ger*	29	2012	Borussia M'gladbach	2023	35	21
Jacob Bruun Larsen	Den	19	2017	BVB U19	2021	17	3
Paco Alcácer	Sp*	24	2018	Barcelona	2023	15	19
Marius Wolf	Ger	23	2018	Eintracht Frankfurt	2023	15	1
Maximilian Philipp	Ger	24	2017	Freiburg	2022	11	2

Source: Bundesliga, BVB. Note: *Full international. **Age at start of season. ***Also four starts by Hitz and one start by Oelschlägel. ****Sold to Chelsea 1.19. §Excludes goals in DFB Cup penalty shootout and one own goal. **Bold** = acquisitions this season.

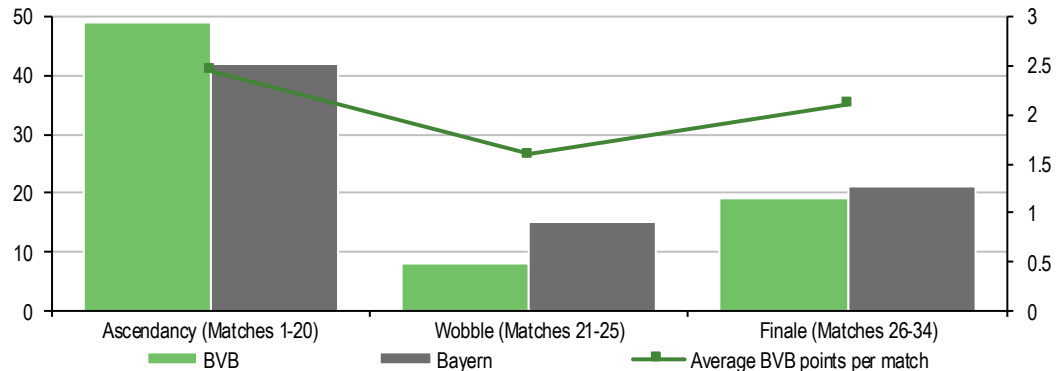
In terms of attack, the loss of exceptional goal scorer Aubameyang to Arsenal in January 2018 (21 goals in all competitions in the first half of 2017/18) was mitigated by remarkably effective finishing by Barcelona signing Alcácer. His Bundesliga goal tally (18) was second only to that of Bayern's Lewandowski and achieved mainly as a substitute (his record goals-per-minute ratio was, for example, double that of 2018/19 Premier League's three joint top scorers). This was complemented by a resurgent Reus, whose most prolific Bundesliga season for five years (17 goals) reflected renewed fitness (27 starts against only 11 in 2017/18). Sancho came of age with a dozen goals (the youngest Dortmund player to reach double figures in a season) and the second-highest number of assists in Europe's five major leagues. Impressively, he started all but two of Dortmund's last 28 games. There was also a significant contribution from Götze, especially in the second half of the season; his seven goals marked his most successful campaign since returning to the club in 2016.

As for midfield, summer arrivals, Witsel and Delaney, proved immediately a robust, creative and stable partnership, with a pass completion rate of over 90% and seven goals. In particular, Witsel started all but five of BVB's 45 competitive matches. In defence, the absence of veterans Sokratis (now at Arsenal), and Schmelzer and Toprak (largely through injury) was made good by the rapid integration of Diallo and Hakimi (on loan from Real Madrid) alongside Akanji.

At the start of the season, the 2018/19 squad of 25 had an average age of 24, compared with 26 for Bayern and 23 for Leipzig and 25 for Leverkusen, its closest Bundesliga rivals. Key contributors such as Sancho, Hakimi, Diallo and Akanji were well below this average, while seasoned Götze and Reus were only 26 and 29 respectively.

The race for the 2018/19 Bundesliga title

Exhibit 4: Bundesliga 2018/19



Source: Bundesliga

In what was expected to be a transitional season with a target simply of a top-four finish, Dortmund markedly outperformed. After a troubled 2017/18 (29 points behind champions Bayern and Champions League qualification only on goal difference), taking the title race to the very last day with the club's third-highest points total (up 21 y-o-y and 10 ahead of third-placed Leipzig) was no mean feat. Indeed, for five months and 18 games (more than half the season) BVB topped the table, at one point (Matchday 15) by a striking nine points. There was then a sudden dip in form in February (see Exhibit 4) as successive draws, including the late concession of a three-goal lead vs Hoffenheim, and only the second defeat of the season, coincided with exits from the Champions League and DFB Cup. This allowed Bayern to close the gap by Matchday 25, but to Dortmund's credit for the rest of the season a clear pick-up (average of 2.1 points per game) saw the champions being all but matched and Champions League qualification achieved as early as Matchday 30.

Results in European competition were also positive, if ultimately disappointing. A Champions League group win with 13 points was in stark contrast to just two points in 2017/18. The highlight was an impressive 4-0 win over Atlético Madrid, the heaviest defeat in seven years under coach Simeone. By mid-February, Dortmund's form had dipped (see above), reflected in disappointing losses (0-4 on aggregate) to Tottenham in the round of 16.

Well-defined strategy

After its financial troubles (see page 2) 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 recent development record with Dembélé, Aubameyang and Pulisic, excitement centres on Sancho (highlighted), whose market value was newly upgraded by €20m to €100m by www.transfermarkt.de. However, Exhibit 5 confirms an array of hidden reserves in the form of first-team regulars, prominent new signings or teenage newcomers such as Balerdi and Gómez (Sancho valued at €5m only a year ago). 2018/19 saw BVB win the German U19 championship for the eighth time. On disposals, management has achieved a balance with considered sales, be it 'too good an offer to refuse' (Dembélé) or 'an extremely lucrative bid, given the low contract maturity' (Pulisic).

Exhibit 5: Significant player transactions

Disposals since 2016 (€25m+)						
	Date	Age at disposal	Cost (€m)	Transfer fee (€m)	Buyer	
Henrikh Mkhitaryan	2016	27	27	42	Manchester United	
Mats Hummels	2016	27	4	35	Bayern Munich	
Ilkay Gündogan	2016	25	5	27	Manchester City	
Ousmane Dembélé	2017	20	15	105	Barcelona	
Pierre-Emerick Aubameyang	2018	28	13	64	Arsenal	
Christian Pulisic	2019	20	Free	64	Chelsea	
Current squad development (players with estimated market value of €25m+)						
	Date	Age at signing	Cost (€m)	Current value (est) (€m)	Contract expiry	
Jadon Sancho	2017	17	9	100	2022	
Marco Reus	2012	23	17	50	2023	
Manuel Akanji	2018	22	21	40	2022	
Abdou Diallo	2018	22	28	35	2023	
Axel Witsel	2018	29	20	32	2022	
Dan-Axel Zagadou	2017	18	Free	28	2022	
Thomas Delaney	2018	26	20	27	2022	
Julian Weigl	2015	19	3	25	2021	
Raphaël Guerreiro	2016	22	12	25	2020	
Mario Götze	2016	24	22	25	2020	
New signings (from 7.19)						
Julian Brandt	2019	23	25	50	2024	
Thorgan Hazard	2019	26	26	38	2024	
Paco Alcácer	2019*	25	21	37	2023	
Nico Schulz	2019	26	26	25	2024	
Youth development:						
Leonardo Balerdi	2019	19	15	14	2024	
Sergio Gómez	2018	17	3	3	2021	

Source: www.transfermarkt.de. Note: *On loan from Barcelona for 2018/19 season.

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 last five seasons. The comparison with Bayern is telling as Bundesliga performance is also noted. While Dortmund has ensured European football with a net positive balance and easily outpaced other domestic rivals (over the last five years 16% more Bundesliga points than the nearest, Bayer Leverkusen), there is a glaring 22% points inferiority to Bayern.

Exhibit 6: Net transfer balances since 2014/15 of selected Champions League regulars

€m	2014/15	2015/16	2016/17	2017/18	2018/19	Cumulative since 2014/15	
						Net balance	Bundesliga rank (points)
Borussia Dortmund	-60 (7)	+23 (2)	-10 (3)	+146 (3)	+23 (2)	+122	2 (319)
Bayern Munich	-5 (1)	-56 (1)	-18 (1)	-84 (1)	+74 (1)	-88	1 (411)
Manchester City	-58	-141	-178	-226	-23	-626	
Manchester United	-146	-54	-138	-153	-47	-538	
PSG	-47	-93	-75	-140	-105	-459	
Barcelona	-85	-13	-91	-127	+5	-310	-
Juventus	-26	-71	-21	-15	-152	-285	
Chelsea	+7	-3	-24	-60	-155	-236	
Liverpool	-52	-35	+5	+16	-144	-209	
Inter Milan	+7	+13	-139	-61	+1	-180	
Atlético Madrid	-30	+18	-37	-19	-61	-128	
Real Madrid	-21	-69	+8	+88	-45	-40	-
Tottenham	-4	+17	-31	-18	+5	-31	

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 newly rated by Brand Finance as the 12th most valuable football brand, as in 2018. Apart from a global fan base (see below), average Bundesliga home match attendance of over 80,000 is consistently the highest in the world, followed by Barcelona, Manchester United and Bayern Munich at c 75,000, according to www.transfermarkt.de. 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 (over 55,000 season tickets), which is a powerful platform for advertising.

Management aims to monetise this, as follows:

- **Advertising (26% of FY19e non-transfer revenue and +8% in FY18):** 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, until 2025), Signal Iduna (stadium, until 2021) and Puma (kit, until 2020). There are now 10 'BVB Champion Partners' and about 50 lower-tier sponsors. This activity is outsourced to Lagardère, which receives commission on revenue generated. BVB is pioneering virtual advertising to international audiences at Bundesliga home games.
- **Merchandising (8% of FY19e pre-transfer revenue and -25% in FY18):** 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.
- **New media:** In promoting brand awareness, BVB continues to be active on social media, attracting 36m users on Instagram, Facebook, Twitter, YouTube and Sina Weibo at end 2018. While Facebook remains the mainstay (now 15m 'likes'), the strongest growth has been on Instagram (since June 2018 followers up 30% at 7.5m). However, both are small compared with Chelsea and Arsenal which have respectively 48m and 38m Facebook 'likes' and 17m and 14m Instagram followers. New channels include short video platform TikTok and English-language Twitter. Asia is proving receptive, with the company's Sina Weibo account among the fastest-growing profiles of European clubs in China. BVB's own app still enjoys strong demand (1.3m users in 2017/18), as does its website, whose home page was recently judged by NetFed to be the second-best in the Bundesliga.
- **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-TV, shows club videos, Bundesliga matches and all other competitive matches in full length. Current subscription costs are €1.99 a month.
- **Matchday operations (12% of FY19e pre-transfer revenue and -4% in FY18):** Management regards Signal Iduna Park, Germany's largest football stadium with capacity for 81,360, as its most valuable asset other than 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 pricing as a community club, the scope for ticketing revenue growth seems limited. Apparent underachievement with the likes of Manchester United, where ticketing was 19% of FY18 revenue, is thus unfair; Bayern Munich's 16% revenue share (FY18) is a better comparative. Two-thirds of capacity is pre-sold as season tickets, which brings revenue visibility, and an annual footfall of 1.4 million spectators at Bundesliga games brings ancillary income from merchandising and catering. The stadium is not multi-functional.
- **Broadcasting (46% of FY19e pre-transfer revenue and -3% in FY18):** 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 from 2018/19. Predictably, media rights have driven the 55% increase in league income over the last four years. Indeed, the rise in 2017/18 alone was a third, thanks to the new Bundesliga contracts (still predominantly with Sky Deutschland but no longer exclusively). From 2018/19 there should also be material benefit from UEFA distribution for the new Champions League cycle since the competition's revised format, eg more 'big name' clubs and staggered viewing times, is aimed at boosting the appeal to broadcasters. The

share for clubs competing in the group stage onwards is forecast by UEFA to increase by 50% to €1.95bn pa.

Management

The company's senior management (see below) is backed by highly experienced members 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 runs 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 RölsPartner, one of the leading business consultancies in Germany. He was awarded 'CFO of the year 2013' by the German Finance Magazin.
- **Sales & marketing and digitalisation: Carsten Cramer** became a further managing director in 2018, having served as sales & 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 VP 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.
- 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, accounting for c 55% of its revenue excluding transfers, which is similar to key peers.
- There is a potential conflict between sporting objectives and financial requirements, highlighted by an increased reliance on transfers.

Valuation

Asset-rich

The share price is at c 20% discount to a simple sum-of-the-parts valuation of €10.75/share (€9.5 before), based on estimated market value of players c €480m, per www.transfermarkt.de, adjusted to exclude Pulisic (sold) and Hakimi and Alcácer (on loan), brand value €481m (at May 2018 per Brand Finance) and financial position (€28m net cash at end FY19e).

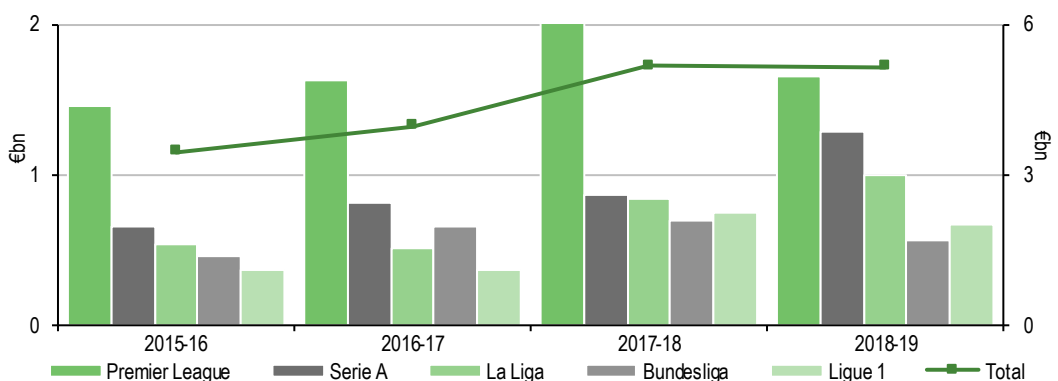
This squad valuation necessarily does not allow for step changes in the value of emerging talent, which Dortmund is so adept at identifying and which is attracting the attention of major clubs at ever younger ages. Potential prodigies such as Balerdi and Gómez (Exhibit 5) may emulate the uplift (admittedly unrealised) of estimated €91m attributable to similarly youthful Sancho or the bumper realised returns on Dembélé and Pulisic. There may also be appreciation by established talent, eg last month's triple signing of internationals (Brandt, Hazard and Schulz), which has already elicited clear upgrades on approval of their Dortmund prospects.

Dortmund's success at value creation is evident in the 13% rise in value per share from €9.5 in our SOTP exercise in April 2018. At that point, the share price discount was twice the current level, reflecting major sporting uncertainties and a troubled season.

Indeed, the company's transfer policy consistently generates substantial hidden reserves in player values. The past three years saw average capital gains of c €88m (our estimate), including the 'exceptional' Dembélé transaction, and the scope for further gains is high. The surplus of market value to net player assets is c €300m if the reported March 2019 carrying value of €180m is set against www.transfermarkt.de's adjusted valuation of c €480m.

Beyond this is sustained transfer market buoyancy, shown by a doubling in spend to over €5bn in 2018/19 by the five major European leagues over the last four years (Exhibit 7). Consolidation in the season just ended is understandable after such a heady rise (30% in 2017/18 alone). This comes at a price in terms of player replacement, but Dortmund is a net seller.

Exhibit 7: Player transfer market spend by five major European leagues over last four years



Source: www.transfermarkt.de

Disposals do of course carry the threat of undue sporting detriment. With management's objective to declare an annual net profit, the scale of intangible amortisation (over €60m pa) and operating cost pressures (we estimate pre-transfer negative EBITDA in Q319 despite 18% higher operating income) risk 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.

Low rated

Among listed peers, there is limited comparability with Dortmund in terms of valuation indicators. By far the largest by market cap, Manchester United offers very limited free float, while Juventus has a majority shareholder and sizeable net debt. Olympique Lyonnais's renewed Champions League participation may allow a higher outturn this year (H1 EBITDA up 30%), although H218 included substantial transfer profit. Against available peer numbers BVB is rated the lowest in terms of EV/EBITDA and EV/Pre-transfer revenue.

Exhibit 8: Valuation comparison with major listed peers (EBITDA includes transfer activity)					
	EV	EBITDA	EV/EBITDA (x)	Pre-transfer revenue	EV/Pre-transfer revenue (x)
Prospective (Y/E June 2019)					
Borussia Dortmund	€747m	€105.0m	7.1	€370m	2.0
Manchester United	£2717m	£210m*	12.9	£622m*	4.4
Historic (Y/E June 2018)					
Borussia Dortmund	€724m	€126.6m	5.7	€313m	2.3
Manchester United	£2683m	£195.2m	13.7	£590m	4.5
Juventus	€1910m	€121.5m	15.7	€402m	4.8
Olympique Lyonnais	€400m	€73.9m	7.2	€164m	2.4

Source: Company accounts. Note: *Midpoint of May guidance. Includes estimated €27m transfer gain.

Financials

FY19e: H1 was again a tale of two quarters (Exhibit 9). While Q1 lacked a bumper transfer, hence c 70% lower EBITDA y-o-y, the following period was unaffected by transfers and saw a rise in EBITDA (from €2m in Q218 to €31m), which was striking in the face of persistent wage pressure (+11%). Admittedly against a weak comparative, the three months to December saw an impressive 41% increase in pre-transfer revenue, driven by sporting success, ie 10 Bundesliga wins against two and top of the Champions League group table compared with just two points last time, and a favourable y-o-y fixture pattern. This led to a near doubling in TV marketing income from European competition. On-field buoyancy also permeated advertising, up 6% thanks to Champions League knockout bonuses, in addition to the benefit of newly enhanced virtual advertising to international audiences, and merchandising, up 8%. In Q3 the transfer of Pulisic broadly matched that of Aubameyang in the prior period, while Champions rather than Europa League involvement drove 18% higher pre-transfer income. Despite such quarterly volatility, we broadly retain our assumptions for this year (just €5m pre-transfer revenue upgrade) with no allowance for significant end of season dealings.

FY20e: Our forecasts for this period are also broadly maintained (€5m income upgrade is flow-through from this year). Transfer activity is expected to be on a par with the current year, as are operational factors, ie competition and broadcasting.

Exhibit 9: Revenue and profit analysis									
Year end June (€m)	H118	Q318	Q418	FY18	H119	Q319	Q419e	FY19e	FY20e
Home matches									▲
Bundesliga	8	6	3	17	9	5	3	17	17
Champions League	3	-	-	3	3	1	-	4	4
Europa League	-	2	-	2	-	-	-	-	-
Domestic cups	1	-	-	1	1	1	-	2	3
Revenue									
Match operations:									
Bundesliga	13.1e	9.2e	5.1e	27.4	14.8e	7.9e	5.2	27.9	28.5
Champions League	5.8e	-	-	5.8	6.0e	2.1e	-	8.1	8.2
Europa League	-	3.3e	-	3.3	-	-	-	-	-
Domestic cups	2.2e	-	-	2.2	0.7e	1.5e	-	2.2	5.0
Other	2.6e	0.3e	0.6e	3.5	5.9e	0.4e	0.5	6.8	6.3
Total	23.8	12.8	5.7	42.3	27.4	11.9	5.7	45.0	48.0
Broadcasting:									
Bundesliga	43.4	21.6	23.0	88.0	48.4	24.1	25.5	98.0	103.0
Champions League	28.1	-	-	28.1	56.7	11.3	1.8	69.8	70.0
Europa League	-	2.9	0.7	3.6	-	-	-	-	-
Domestic cups	2.6	-	-	2.6	0.5	0.7	-	1.2	4.0
Total	74.1	24.5	23.7	122.3	105.6	36.0	27.3	169.0	177.0
Advertising	45.2	22.3	26.5	94.0	46.5	22.9	27.6	97.0	99.0
Merchandising	19.4	5.5	4.6	29.5	18.2	6.2	5.1	29.5	29.5
Catering/other	13.0	5.7	6.5	25.2	16.0	6.6	6.9	29.5	29.5
Revenue before transfers	175.6	70.9	67.0	313.3	213.6	83.7	72.6	370.0	383.0
Transfers	136.2**	72.6***	13.9	222.7	42.4	69.5	18.1	130.0	130.0
Total revenue	311.8	143.5	80.7	536.0	256.0	153.2	90.8	500.0	513.0
Other operating income	2.8	0.2	0.9	3.9	4.2	0.8	0.5	5.5	5.0
Labour costs	(94.3)	(45.0)	(47.4)	(186.7)	(101.3)	(52.1)	(50.6)	(204.0)	(214.0)
Material costs	(12.3)	(4.2)	(3.6)	(20.1)	(11.6)	(5.5)	(3.9)	(21.0)	(21.0)
Other operating costs	(124.2)	(49.9)	(32.4)	(206.5)	(93.3)	(45.3)	(36.9)	(175.5)	(173.0)
EBITDA	83.9	44.6	(1.9)	126.6	54.1	51.1	(0.2)	105.0	110.0

Source: Edison Investment Research. Note: ▲ Assuming Champions League round of 16 and DFB Cup semi-final. *Including disposal of Dembélé. **Including disposal of Aubameyang. ***Including disposals of Sokratis and Yarmolenko. ****Including disposal of Pulisic.

Exhibit 10: Financial summary

	€'000s	2016	2017	2018	2019e	2020e
June		IFRS	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS						
Revenue		376,300	405,700	536,000	500,000	513,000
EBITDA		86,700	74,100	126,600	105,000	110,000
Operating Profit (before amort. and except.)		75,900	62,600	115,500	94,000	99,000
Intangible Amortisation		(32,000)	(51,900)	(59,000)	(64,000)	(66,000)
Exceptionals		(7,500)	0	(20,400)	0	0
Other		0	0	0	0	0
Operating Profit		36,400	10,700	36,100	30,000	33,000
Net Interest		(2,100)	(1,500)	(4,300)	(1,000)	(1,000)
Other financial items		0	0	0	0	0
Profit Before Tax (norm)		73,800	61,100	111,200	93,000	98,000
Profit Before Tax (FRS 3)		34,300	9,200	31,800	29,000	32,000
Tax		(4,900)	(900)	(3,300)	(3,000)	(4,000)
Profit After Tax (norm)		62,700	51,900	94,500	79,100	83,300
Profit After Tax (FRS 3)		29,400	8,300	28,500	26,000	28,000
Minority interests		0	0	0	0	0
Net income (normalised)		62,700	51,900	94,500	79,100	83,300
Profit after tax (FRS3)		29,400	8,300	28,500	26,000	28,000
Average Number of Shares Outstanding (m)		92.0	92.0	92.0	92.0	92.0
EPS - normalised (c)		68.2	56.4	102.7	86.0	90.5
EPS - (IFRS) (c)		32.0	9.0	31.0	28.3	30.4
Dividend per share (c)		6.0	6.0	6.0	6.0	6.0
EBITDA Margin (%)		23.0	18.3	23.6	21.0	21.4
Operating Margin (before GW and except.) (%)		20.2	15.4	21.5	18.8	19.3
BALANCE SHEET						
Fixed Assets		302,800	354,900	341,900	392,000	418,000
Intangible Assets		65,300	141,500	109,700	165,000	190,000
Tangible Assets		188,400	184,700	180,700	180,000	178,000
Investments		49,100	28,700	51,500	47,000	50,000
Current Assets		121,800	123,700	136,400	99,000	95,000
Stocks		10,200	9,000	5,600	6,000	6,000
Debtors		51,100	48,800	23,000	28,000	28,000
Cash		51,700	49,300	59,500	35,000	26,000
Other		8,800	16,600	48,300	30,000	35,000
Current Liabilities		(78,800)	(140,900)	(119,000)	(112,000)	(112,000)
Creditors		(76,200)	(130,600)	(117,000)	(112,000)	(112,000)
Short term borrowings		0	0	0	0	0
Finance leases		(2,600)	(10,300)	(2,000)	0	0
Long Term Liabilities		(36,200)	(25,400)	(23,000)	(22,000)	(22,000)
Long term borrowings		0	0	0	0	0
Finance leases		(19,000)	(8,700)	(6,700)	(7,000)	(7,000)
Other long term liabilities		(17,200)	(16,700)	(16,300)	(15,000)	(15,000)
Net Assets		309,600	312,300	336,300	357,000	379,000
CASH FLOW						
Operating Cash Flow		44,400	117,900	163,500	115,000	130,000
Net Interest		(1,400)	(2,100)	(3,700)	(1,000)	(1,000)
Tax		(300)	(5,500)	(1,700)	(3,000)	(4,000)
Capex		(9,400)	(8,100)	(7,200)	(8,300)	(8,500)
Acquisitions/disposals		(20,500)	(96,500)	(123,600)	(120,000)	(120,000)
Financing		(7,700)	0	(1,300)	0	0
Dividends		(4,600)	(5,500)	(5,500)	(5,500)	(5,500)
Net Cash Flow		500	200	20,500	(22,800)	(9,000)
Opening net debt/(cash)		(29,600)	(30,100)	(30,300)	(50,800)	(28,000)
Finance leases initiated		0	0	0	0	0
Other		0	0	0	0	0
Closing net debt/(cash)		(30,100)	(30,300)	(50,800)	(28,000)	(19,000)

Source: Borussia Dortmund, Edison Investment Research

Contact details 11 Rheinlanddamm 207-209 D-44137 Dortmund Germany +49 (0) 231 90 20 745 www.bvb.de/aktie	Revenue by geography N/A												
Management team													
Chief Executive: Hans-Joachim Watzke Before his appointment in 2005, Mr Watzke had been treasurer of the football club for four years. His contract as CEO runs to the end of 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 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 RölfsPartner, one of the leading business consultancies in Germany. He was awarded 'CFO of the year 2013' by the German Finance Magazin.												
Sales & Marketing and Digitalisation: Carsten Cramer Carsten Cramer recently joined the board in 2018, having served as sales & 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 VP with nationwide duties.													
<table border="1"> <thead> <tr> <th data-bbox="146 757 1129 790">Principal shareholders</th> <th data-bbox="1129 757 1442 790"> (%)</th> </tr> </thead> <tbody> <tr> <td data-bbox="146 790 1129 824">Evonik Industries</td> <td data-bbox="1129 790 1442 824">14.8</td> </tr> <tr> <td data-bbox="146 824 1129 857">Bernd Geske</td> <td data-bbox="1129 824 1442 857">9.3</td> </tr> <tr> <td data-bbox="146 857 1129 891">Borussia Dortmund</td> <td data-bbox="1129 857 1442 891">5.5</td> </tr> <tr> <td data-bbox="146 891 1129 925">Signal Iduna</td> <td data-bbox="1129 891 1442 925">5.4</td> </tr> <tr> <td data-bbox="146 925 1129 954">Puma</td> <td data-bbox="1129 925 1442 954">5.0</td> </tr> </tbody> </table>		Principal shareholders	(%)	Evonik Industries	14.8	Bernd Geske	9.3	Borussia Dortmund	5.5	Signal Iduna	5.4	Puma	5.0
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Companies named in this report Bayern Munich, Real Madrid, Manchester United, Juventus, Atlético Madrid, Barcelona, PSG, Chelsea, Puma, Evonik, Signal Iduna													

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