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A-Rod's dollars make sense for Yankees

By Vince Gennaro, Special to Yahoo! Sports
November 27, 2007

Despite the posturing, bruised egos and serpentine route of the courtship, Alex Rodriguez and the New York Yankees are a money-making marriage unparalleled in professional sports.

We know the details of Rodriguez's contract: $275 million for

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Combining Rodriguez's value over the life of the contract and considering the economic effect of the new Yankee Stadium set to open in 2009, he is likely to generate approximately $450 million of "value" for the Yankees, according to my analysis of his impact. Assuming the Yankees exceed the luxury-tax threshold in each of the 10 years and trigger the 40 percent luxury tax, the total cost for Rodriguez will come to $427 million.

The true economic value of A-Rod is based on the Yankees' revenue growth and asset appreciation that we can attribute to him. Economists call this a player's marginal revenue product, but I've expanded it beyond revenue to include the marginal value of the Yankees' assets — their ownership stake in the YES Network and the value of the franchise.

Rodriguez has two sources of value: performance and marquee. Performance value is determined by the impact of his playing performance on the Yankees' win total and the resulting financial gains from the team being more successful because of his contribution. We derive marquee value from A-Rod's persona, image and even the more tangible value of drawing fans to watch him chase future personal milestones.

By adding his performance and marquee values for each year, we can assess the full 10-year value of A-Rod to the Yankees and prove why the $275 million salary with the potential for $30 million more in incentives negotiated by Rodriguez made a lot more sense than the $350 million his agent, Scott Boras, originally postulated.

PERFORMANCE VALUE

When the Yankees make the playoffs, which they've done 12 consecutive seasons, it's worth nearly $40 million. A World Series victory is worth $70 million, calculations that I explained in my previous story for Yahoo! Sports, World Series financial scoreboard. Winning in New York draws more money than anywhere else, so it's no surprise the Yankees have carried baseball's biggest payroll eight consecutive seasons and 11 out of 12.

Revenues respond to winning, and by combining statistical tools, including regression analysis, with attendance, ticket pricing and a host of other financial data, we can estimate the change in revenues that corresponds to each level of regular-season wins. I detail this concept, the win-curve, for each MLB team in my book, "Diamond Dollars: The Economics of Winning in Baseball."

Each team's win-curve is as unique as a fingerprint, incorporating the size of the market, loyalty and expectations of the local fan base, plus the depth and breadth of a team's revenue streams. Teams that own a stake in a regional sports network (RSN), such as the Yankees, Red Sox and Mets, have a leg up on their competition when it comes to generating value from winning. Through their ownership stake, they directly benefit from increased ad revenues and the appreciation in the value of the network that can result from being the flagship broadcast partner of a winning sports franchise.

And nothing defines winning like postseason success. Teams often see dramatic jumps in season tickets, merchandise sales and broadcast ratings in the year following a playoff run. As a result, the player (or group of players) that boosts teams into the playoffs, or at least keeps them there — the last piece of the puzzle — can create significant financial value.

The perfect storm of player value comes when a player in a large market joins a team with highly developed revenue streams and makes the difference between reaching the postseason or spending October at home. A-Rod and the Yankees potentially fit this description as well as any player-team combination in baseball today.

In order to fairly assess A-Rod's value, there are some quirks to account for in the Yankees' win-curve. The normally demanding Yankee fans may soon take a temporary break from their fixation on winning. With the last season at historic Yankee Stadium and the opening of an amenity-filled new version in '09, the Yankees should have near capacity crowds regardless of their wins and losses in 2008 and 2009.

The stadium trance has serious implications on A-Rod's value. One key component of the Yankees' revenue equation — attendance — will only be modestly affected by players' on-field contributions, at least in the short term.

Eventually, though, the financial stakes of winning will spike. The highest ticket prices in baseball. An abundance of only-in-New York-expensive luxury suites. Expensive concessions and even more expensive merchandise. The Yankees' win-curve will become a steep, slippery slope.

Win and rake in the cash.

Lose and beg for a tourniquet to stop the financial hemorrhaging.

Figure 1 shows two versions of the Yankees win-curve — the 2007 version in the current Yankee Stadium and the eventual post-grand opening version in the new Yankee Stadium. Additional revenue from winning doesn't typically begin until a team exceeds 70 victories.

Judging the fair value of a long-term contract can
often hinge on the assumptions made about the player's performance, his rate of decline with age and his injury risk. Using conservative but realistic assumptions, over the next several years we can expect A-Rod to perform closer to his level of play in 2004, his first year as a Yankee, when he hit .290 with 35 home runs and 120 RBIs. Excellent year, no question, but nothing like his two MVP seasons in pinstripes. We’ll then assume a gradual and steady decline during the back half of his 10-year deal, ultimately finishing his career as a .270-batting, 20-homer-hitting aging superstar.

The net result is a modest dollar valuation for his on-field performance in the beginning and end of his new contract, with a dramatic, lucrative spike in the middle years, while he’s still in his prime and the new stadium effect is passé.

Figure 2 shows estimates of A-Rod’s performance value – the incremental attendance, merchandise sales, corporate sponsorship dollars, and broadcast revenues and valuation at YES, due to A-Rod’s role in making the Yankees a winning machine. It hits a low of $17-million per year early in the contract and peaks at more than $50 million per season in the middle years. Rodriguez’s cumulative performance value over the 10-year contract is estimated to be approximately $305 million in revenue and asset appreciation.

MARQUEE VALUE

Some believe that marquee value – or “iconic” value as Boras, calls it – is marketing fiction. The naysayers believe that fans root for the laundry, and as long as their team wins, fans couldn't care less about the players. After all, aren't they just sports? But not the fans of the New York Yankees. They love their men in pinstripes. The team is their institution, and the players are the human icons of the Yankees’ history.

My formula for measuring marquee value considers the value of the team brand and the player's personal attributes. It allot's a modest one-third of the appreciation in franchise value to the mega-stars on a team.

Beyond Rodriguez's impact on franchise value is his impact on the value of the YES Network. Boras is doing his typical Pinocchio act when estimating it at $500 million or more, but it is reasonable to say the YES Network will be a more valuable asset – $50 to $100 million more over 10 years – because Rodriguez is a Yankee.

The lofty $3 billion valuation experts have placed on the YES network is largely based on the popularity and appeal of the Yankees and the resulting industry high subscriber fees paid by cable and satellite providers. Along with shortstop Derek Jeter, A-Rod is an important asset who adds star power to the network, in addition to contributing to the Yankees winning ways. The potential for celebrating his many milestones, retiring his number, wearing a Yankees cap into the Hall of Fame, and bringing the all-time home run title back to New York can be centerpieces of YES programming for years to come and earn Rodriguez credit for a small piece of the network’s projected future growth.

A more tangible component of marquee value is as a drawing card from chasing personal milestones – becoming the youngest player to 600 and 700 home runs and chasing the career record in 2013 or so. If each of the five milestones referenced in his contract – Willie Mays’ 660 home runs, Babe Ruth’s 714, Hank Aaron’s 755, Barry Bonds’ final tally and setting the all-time mark – drew an extra 60,000 fans and netted a modest $1 million in merchandise sales, they would contribute $20 million to Yankee revenues.

Figures 3 and 4 summarize the calculations. The total revenue and asset value of A-Rod to the Yankees is at least $100 million greater than the value he could have

studying focus groups, researching fans and analyzing other factors, however, I'm convinced that marquee value is real – and adds to the financial value of players the caliber of Rodriguez.

Star players that are articulate, have a clean image and come off as likeable possess a value that carries over to the brand equity of the team. These players personalize the team brand and help build an enduring connection between the team and its fans that lasts long after they are gone. Though Rodriguez presents himself well, his appearance in the New York tabloids with a stripper and the perception of him as greedy for opting out of his original Yankees contract do raise questions.

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Figures 3 and 4 summarize the calculations. The total revenue and asset value of A-Rod to the Yankees is at least $100 million greater than the value he could have
generated for any other team. No other team has a comparable
fan base and revenue model. Combining the industry-leading YES Network with the highest priced tickets and New York-sized demand
for luxury suites means no team can move the financial needle like the Yankees.

Only the Cubs, Mets, Red Sox, Dodgers and Angels might have justified a contract of this magnitude and only on the condition that they
assembled a playoff-bound team without exceeding the luxury-tax threshold. Not only did A-Rod end up in the place where he could
generate the most value, but the terms of the deal are a win-win for both A-Rod and the Yankees.

Despite what appeared to be a roundabout route back to New York by A-Rod, the case can be made that everything went according to
script. Maybe he had to opt out to get the Yankees best offer on the table. Maybe the Yankees had to threaten to shut off negotiations after
the opt-out to restore their leverage. Maybe Boras had to excuse himself from the proceedings during the delicate period when his client
and the Yankees reconnected.

Yet there are no maybes when it comes to a healthy Alex Rodriguez. He will be worth every penny the Yankees pay him – and more.

Vince Gennaro is a consultant to several Major League Baseball teams and the author of “Diamond Dollars: The Economics of
Winning in Baseball,” an innovative look at the business of baseball. This followed a 20-year career at PepsiCo, where he was president
of a billion-dollar division. Gennaro teaches a graduate course on the business of baseball in the Sports Business Management program
at Manhattanville College. Send Vince a question or comment for potential use in a future column or webcast.

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