

ARSENAL HOLDINGS PLC

Commentary on INTERIM ACCOUNTS for six months ending 30 November 2007

by Nigel Phillips

“A time to sow, a time to reap”

Eighteen months into the new stadium and one can see the financial impact of the move emerging. The Chairman sets out clearly in his commentary the key business objective of the Club:

- Development of long term stability and success for the Club through maintaining a business that **pays its own way**

Whilst **total revenue** fell slightly to £96.9m from £100.8m as income from property development fell substantially (£7.6m vs £23.7m) **football turnover** increased by 16% to £89.3m (£77.1m). Most of this increase comes from the new TV deals. **Profit before tax** was £20m (£12.9m excluding the £21.4m exceptional finance charge). **Operating profit (before debt service costs) from the football business**, excluding player sales and the cost of writing down the squad (basically depreciation of intangible assets – a non-cash cost) was £21.9m (£10.9m)

Arsenal's football income increased to £89m from £77m and comprised four separately identified revenue streams, namely:

Match day	£41.1m* (£38.0m)	46%	(49%) of football revenue
Broadcasting	£24.3m (£17.8m)	27%	(23%) of football revenue
Commercial	£15.7m (£14.1m)	18%	(18%) of football revenue
Retail	£7.8m (£7.0m)	9%	(9%) of football revenue

* 12 home games and Emirates Cup v 11 home games and Argentina vs Brazil

Football costs were broadly unchanged at £67.4m (£66.2m) and reflected the likely wages balance of the departure of Henry and Ljungberg v new squad members and improved contracts for others. The **wages to football turnover** ratio is likely to be close to a very reasonable 50% (£45m/£90m). There is no mention of whether the Club has yet reached agreement with David Dein over his employment termination payment (outstanding at September 2007). The non wages costs of running the Club (stadium costs, retail expenses?) are huge at about £50m per season and a more detailed breakdown of this significant amount would be very informative.

Cash balances. There is much talk about the current need for squad strengthening and the cash available. However of the £69.1m (£53.1m) period end cash, £25.5m (£26.3m) is pledged and acts as security for the stadium debt. It is unclear if the cash totals include the estimated £30m of deposits received from the Highbury Square apartment sales, or if these monies have been used to partially fund the development together with the loan facilities.

Debt levels rose as predicted as an additional £41m was borrowed to fund the property developments. The **total gross debt** now stands at £376m (£327m) of which £246.8m (£260m) relates to the new stadium, £103.8m (£44.6m) against Highbury Square and debenture subscriptions (the A, B, C and D bonds held by supporters) of £25.6m (£25.3m). The **net interest charge** was £7.7m (£6.8m).

The interest rates charged on the new stadium debt are either fixed contractually (on the £200m of the long term bonds) or by interest rate swaps (on the £50m of floating rate loans). Arsenal are also

Continued overleaf

These observations and comments seek to be objective but are a personal commentary by the author and do not represent an official statement from the Arsenal Supporters' Trust.

paying about £1.6m per year for “repayment insurance” to Ambac on the stadium debt. This insurance is in favour of the lenders / investors although it’s now of reduced value as the creditworthiness of the insurer has declined.

Accruals and deferred income (revenue received in advance of the accounting period to which it relates – essentially Club, box and commercial monies) remain high at £162m (£164m).

Property development remains vitally important to Arsenal’s future financial position. It is reported that over the next two financial years the completion and sales of Highbury Square (95% pre-sold) and Queensland Road will **generate funds of £350m**. With the current Highbury Square debt of £105m and rising and £30m of deposits received it is likely that the Club could net between £100m-£125m from these projects. The uncertainty in the financial markets and economy in general could impact upon legal completion on some of the Highbury Square apartments. It is difficult to predict at this stage how this could affect the Club. It is believed Arsenal are already re-marketing several apartments that have already been pre-sold.

Player trading figures are as always difficult to reconcile, as so many transfer deals are for “undisclosed” figures. The accounts show a profit on player sales of £19.6m (£12.2m). [Profit is the difference between the price paid / received and the book value of the player after amortisation charges]. Wenger’s ability to continually generate profits from his transfer dealings and keep the Club at the very top level (10 consecutive seasons in the Champions League) is amazing. From the figures disclosed related to the book value of players sold it appears that the signing-on fee paid to Henry at the time of his contract extension was substantial and probably in the region of £5m.

The accounts also show that Arsenal have a **maximum of £30.6m (£19.7m) still to pay in transfer fees** based on players achieving a specified number of appearances and other unspecified events. Of this amount £20m (£10.5m) is described as “probable” and £10.6m (£9.2m) has not yet been provided for.

Summary. Match day revenues are strong and are dependent on the football played and the stadium being full. The collectively negotiated broadcast income is also strong as the new three year TV deal becomes effective. However the commercial and retail revenue streams appear weak in comparison with other top-tier clubs. This is a legacy of long-term deals signed with Emirates (shirt expiry 2014/15 and naming rights expiry 2020/21) and Nike (expiry 2010/11) when cash was desperately needed “up front” to complete the Stadium. These deals are costing Arsenal at least £10m each year in revenue opportunity cost when compared to deals now being concluded by other clubs. The stadium debt deal looks an increasingly good piece of business as rates are fixed (and low) at a time when financial markets and lenders are under increasing amounts of stress.

Reaching completion of Highbury Square and Queensland Road during the next 18 months will be a major achievement. If all goes to plan and the level of completion defaults is low Arsenal should net at least £100m which will repay the £50m debt facility and one assumes be allocated to squad investment (to cover both transfers and wages). Of the near £70m of cash balances, £25m is unavailable as it is used to partially secure future repayments of the debt facilities and one also assumes some is set aside to meet the probable £20m of additional transfer fees payable on existing squad members.

This does however leave maybe £25m for the squad building (transfer plus wages) that appears all too necessary to sustain a season long challenge for honours on several fronts.

As an Arsenal Supporters’ Trust member, if you have any comments on the financial accounts please get in contact with us at info@arsenaltrust.org or on 07775 671345.

These observations and comments seek to be objective but are a personal commentary by the author and do not represent an official statement from the Arsenal Supporters’ Trust.