A-Rod: A bargain at $300 million

Alex Rodriguez is the best player in baseball and his new contract will reflect that. Here’s why he'll likely be worth every penny for whichever team signs him.

A weekly column by Chris Isidore, CNNMoney.com senior writer
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NEW YORK (CNNMoney.com) -- Alex Rodriguez is about to do in November what he hasn't been able to do in October: Produce some real eye-popping numbers.

The New York Yankees' star third baseman, already the highest paid U.S. athlete in professional team sports, is likely to sign a new multi-year contract soon that could be between $300 million and $400 million.

A huge nine-figure deal is virtually certain. What's not known is where he'll sign.

But you don't have to be Scott Boras, A-Rod's uber-agent, to argue that a team can give his client a hefty raise and still have the deal be a good one.

In an interview with me on Saturday, Boras did in fact claim that.

He points to the changes in the overall economics of the game, and the improved market for player salaries that have resulted from these changes as the main reasons why A-Rod deserves another big payday.

"I think the logic of it is always based on demand, demand and the fact that this is now a much better business for many teams than it was in 2000," he said. "In 2000, you had to have a vision for what was going to unfold for the economics of the game. Now more teams have reaped those rewards."

Now even if you don't believe all of Boras' arguments about the economic benefits of lavishing money on his top client (and I don't), the changes in the market for players' salaries, and the improvement in the game's overall economic outlook, means it makes sense to sign the game's most productive player, even at top dollar.

First of all, A-Rod will bring in far more money to a team than the average fan bemoaning players' salaries might think.

Vince Gennaro, a consultant to numerous major league teams and the author of "Diamonds and Dollars," a book about the economics of baseball, has done an analysis that suggests A-Rod could produce $48 million per year in revenue and asset appreciation for the Yankees, allowing the team to pay him $34 million in salary, along with a 40 percent luxury tax, and still break even.

Gennaro's estimate includes an extra $3 million a year benefit to the YES Network, the regional sports network of which the Yankees own 36 percent, along with a $9 million a year in the estimated increased value of that stake.

CNNMoney.com sister publication FORTUNE has reported that the Yankees are looking at a possible sale of the team's ownership interest in YES, and that it could fetch $3.5 billion for the entire network. So re-signing A-Rod could be important for the Yankees in order to maximize the network's value.

Still, some take issue with the notion that YES would suffer if A-Rod leaves the Yankees.

The average number of YES viewers jumped during A-Rod's first year on the team in 2004, but fell each of the next two years. Viewership increased 9 percent this year despite the team's on-field struggles early in the season.

It is worth pointing out that even when the Yankees were slumping this year, A-Rod was on his way to putting up one of the best statistical seasons in history.

But Lee Berke, a consultant to regional sports networks, said that most of YES's revenue stream is already locked in through its industry-leading $2.15 monthly per-subscriber fee charged to cable and satellite TV operators that carry the network. Those long-term deals produce about two-thirds of the network's revenue, he estimates.

So let's assume A-Rod leaves and that in a worst-case, but probably unlikely, scenario, viewership dips by 10 percent. A corresponding drop in ad revenue would equate to only about a 3 percent drop in overall revenue for YES.

What's more, it already is clear that the YES Network's fortunes aren't exclusively tied to ratings success. Revenue increased even in the years that ratings were lower, rising to $340.4 million in 2006 from $321.3 million the year before, according to SNL Kagan, a media research firm.

Berke estimates YES has an operating profit margin of 60 percent -- twice the average for regional sports networks -- and this is why the network is worth so much.

"A-Rod is a contributing factor, like all the players are," said Berke. "But he's not a big factor. The brand is much bigger than A-Rod."

People tune into watch winning teams, not necessarily individuals. And Gennaro admits that as A-Rod gets older, he is less likely to have as much of an impact on how many games the Yankees win. So that means that if they end up paying him $30 million or more a year going forward, there's a very good chance that he will cost the team more than any extra revenue his presence brings in.

Still, there is a good economic argument for the Yankees signing A-Rod, even if the deal doesn't strictly pay for itself: Because they can.

The Yankees can afford to spend more than any other team. A new, albeit smaller, stadium is set to open in 2009 that will only greatly widen the revenue gap between the Yankees and the rest of the league.

Even though attendance will dip because the new stadium doesn't hold as many people, the Yankees estimate that ticket and luxury suite revenue will increase by $100 million a year from 2005 levels. Having a major star like A-Rod should help the Yankees meet or pass these estimates by keeping demand for the tickets high.

But A-Rod could also be a huge financial boon to many other teams, particularly those which have been underperforming in ticket sales or their television deals.

The team that might see the greatest economic boost from signing A-Rod could be the lowly Florida Marlins, which paid its entire roster about $30.5 million this year, and is in negotiations with elected officials about a new stadium deal.

If Miami-native A-Rod were to return to his hometown team, it wouldn't have to worry about paying 40 percent of his salary to the league as a luxury tax, as the Yankees would.

And if good young players there continue to develop, A-Rod might actually help lead the team back into postseason, producing revenue that could be worth between $2 million to $15 million a year. The Yankees have a far better chance of making the playoffs without A-Rod than would the Marlins.

"The Marlins are an interesting possibility," said Tim Mahon, principal for Anderson Economic Group, a business valuation service, who has studied team values. "I think it makes much more sense than it does for some of the other choices."

Mahon said that for deep-pocketed successful teams like the Yankees, Mets, Cubs, Red Sox or Angels, "there's a marginal economic benefit from bringing him in, even as fabulous a player as he is. But look at the upside for the Marlins, not just in ticket revenue but..."
also the structure of a new stadium deal."

Finally, there is one reason why giving A-Rod pretty much a blank check makes sense. A 10-year deal that may seem shocking today might be considered a bargain by the end of the contract.

Baseball's popularity is growing. Ticket sales are rising. Sports programming are increasingly important for advertisers in a world of TiVo and video downloads. Add in the increased dollars from new sources such as new media and international growth and that means revenue for all teams is likely to increase. Salaries should, and will, follow suit.

So expect A-Rod to score huge dollars, somewhere north of $30 million a year, when he signs a new deal soon.

But no team is likely to drastically overpay for him as the Texas Rangers did years ago. A-Rod would have to sign a contract worth more than $38 million a year in order for his salary to be as out of whack with the league's average salary as the $25.2 million a year deal he signed with Texas before the start of the 2001 baseball season.

When the Rangers traded him to the Yankees before the 2004 season, the deal seemed so expensive that Texas agreed to assume a portion of the contract and pay $71 million to the Yankees in the coming years. But four years later, there's no question A-Rod will now do better.

And his team, whichever one it is, is likely happy and better off writing those huge checks for years to come -- assuming they don't make the same mistake the Rangers did, writing the checks without keeping him on the team. ■

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