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COMMENTARY
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Damn Yankees

By JOHN MOORES
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The baseball season is in full swing, and in towns across the country fans can pretend that their club has a shot to win the World Series this year. If only it were so. There are currently about a half-dozen clubs that dominate postseason play. Since the players' strike of 1994, the New York Yankees have appeared in five of seven World Series, and the Atlanta Braves have appeared in three. It is virtually impossible for a ball club to gain a World Series berth unless the club ranks in the upper fourth in payroll. In 2001, club payrolls ranged from $28 million to $116 million. Early data suggest that the payroll gap will be even greater this year.

Competitive Imbalance

This huge disparity in local revenue drives baseball's competitive imbalance. Last year, local broadcasting revenues from television, cable and radio ranged from a low of $500,000 (Montreal Expos) to a high of nearly $57 million (the Yankees). Most fans might think that visiting clubs split the "gate" (ticket and concession sales) with the home team. Not so. Baseball's fundamental economics were entrenched long before radio changed everything. Thus when the Yankees play the Royals in New York, the Yankees will keep most of their home revenues. The Royals, in a reciprocal arrangement, will keep most of their home revenues when the perennial World Series champions visit Kansas City. The Yankees come out ahead.
[[Illustration]]

A handful of clubs have adopted a fairly rational approach to deal with their revenue disadvantage. Unable to afford high-priced talent, these clubs have traded their veteran ballplayers away and opted for a "youth movement," hoping to catch lightning in a bottle. This is a risky strategy because it is extraordinarily difficult to determine which young talent will mature into competitive players. Furthermore, it's hard to retain the talent you groom. Just look at Jason Giambi, who moved this season from the small-market Oakland Athletics to the powerhouse Yankees.

Yet a handful of observers pretend that things couldn't be better for baseball. These Pollyannas ignore the obvious competitive balance problem, and focus instead on fictitious accounts of baseball's operating results. In truth, competitive imbalance lies at the heart of the major league's

economic woes, which are considerable. Last season, the league's 30 clubs sustained a combined operating loss of $232 million and had a net loss of $519 million. The 2002 season will be worse.

My ballclub, the San Diego Padres, had a cumulative operating loss of $43 million from 1998 to 2000, with a $10 million loss last year despite near-record attendance. The Padres are a small and uncomplicated business, like most clubs. Fans buy tickets, hot dogs and souvenirs. The club also gets paid to put games on radio and TV. National broadcasting rights are negotiated by Major League Baseball and distributed to all clubs through baseball's central fund. Finally, the Padres are paid by MLB under baseball's local revenue sharing system, which is far less extensive than those in other professional sports.

Unlike professional football and basketball, baseball has to bear the substantial expense of a "farm" system. It cost the Padres $18.4 million in 2001 to develop future players. This figure includes the cost of scouting and signing amateur players, the operation of our academy in the Dominican Republic, and many of the operating costs associated with six minor league affiliates. The total revenue received by Major League Baseball in 2001 from the minor leagues was $4,698,459. The Padres' share of this revenue amounted to $156,615.

Clubs also pay for travel, stadium costs, marketing and administrative costs. Stadium depreciation is a rather modest figure -- a mere $70 million in an industry that generates $3.5 billion in revenue and $3.8 billion in operating expenses. Many clubs, like the Padres, lease the facilities in which they play and therefore do not generate stadium depreciation expenses. In 2001, the Padres' total depreciation charge was $764,138 for things like furniture and office improvements. And, as a typical owner, I am unsalaried, as is my hard-working daughter.

The Padres are considered to be a well-managed ballclub. The club has won the National League West twice in the past six years, reaching the World Series in 1998. Attendance is well above the average. A new ballpark, partially publicly funded, was approved by 60% of the voters in 1998 and will open in 2004. While the team's payroll is well below industry average, it will increase in the new ballpark.

When the Padres lose money, I provide the capital to cover the losses through personal funds or commercial borrowing. Like most clubs, there is no entity related to the Padres that covers losses or creates business synergies. The Padres have lost over $100 million during the seven years I have owned the club -- and we're at the middle of the pack, with some clubs losing less and some losing more.

Some pretend that franchise appreciation makes up for operating losses. I purchased the Padres in late 1994 for about $85 million. A former partner and executive, who is considered one of the brightest lights in the game and is no shrinking violet, recently sold his minority interest back to me at a substantial discount from my purchase price. Franchise appreciation is a benefit that is available only to a limited number of high-revenue clubs.

In 1999, baseball commissioner Bud Selig assembled a blue-ribbon panel of distinguished Americans -- George Mitchell, Paul Volcker, Richard Levin and George Will -- to address the

league's problems. After studying the economics of the game, the panel found that increased revenue sharing and a system of payroll regulation are absolutely necessary for the health of the league. Regulation would be in the form of a "payroll zone" with a floor and a ceiling for each ballclub. The payroll zone, which would be enforced by financial disincentives, would deter ballclubs from exorbitant spending to buy a championship but would also increase player payrolls for many ballclubs.

Playing the Percentages

The fans and the media welcomed the recommendations. But the players' union, which must approve any changes to revenue sharing, has refused to sign off. Not surprisingly, the union is opposed to any action that creates even the slightest risk of reducing the rate of inflation in salaries. The union, it seems, prefers to pretend that a ballclub's payroll is not related to on-field success, and that a well-managed but poor ballclub can be quite competitive. Unfortunately, this simply isn't the case. From 1995 to 2001, the league's top payroll teams have won 219 of 224 post-season games; in other words, they're batting nearly 1.000.

There is, of course, some irony in the union's argument about the irrelevance of player salaries and the significance of good management in professional baseball. But pretending that winning in baseball doesn't require great players, and that great players aren't paid more than average ones, is anything but constructive. If that were the case, George Steinbrenner wouldn't be shelling out $120 million to have Mr. Giambi on his team. Mr. Steinbrenner doesn't need to pretend -- he knows the percentages.

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