

Economic Organization of Sporting Competition

1. Why Leagues?
2. Evolution of Leagues
 - MLB from 1876-present
 - League Wars
3. Benefits & Costs of Alternative Organizational Structures
 - Internal Tradeoffs within the League
 - Externality Control
 - Revenue Sharing & Incentive Effects
 - Tragedy of the Commons
 - External Tradeoffs
 - Joint Actions Which Increase Consumer Value vs.
Joint Actions Which Increase Monopoly Rent

1. Why Leagues ?

Some competition occurs within a league structure

MLB, NBA, NFL

Leagues Within Leagues

UEFA Champions League

Some without: “Performance Based” Sport

Figure Skating

Heavyweight Boxing

Track & Field

Why Choose a League?

Odd Examples: Golf, NASCAR, Skiing, Tennis

All are essentially performance-based competitions

Why benefits do they realize from organizing?

Different Levels of Organization (1)

Unstructured

Parties agree to compete and define the rules of the match
College Football circa 1900

Governing Bodies

Define the rules of the game

FIFA

USGA; Royal & Ancient Golf Club of St. Andrews

May set up championship structures

FIFA World Cup

NCAA Men's & Women's Basketball Championships

Different Levels of Organization (2)

Associations of Competitors: ATP, LPGA, PGA

Entry Restrictions

Age, performance, conduct

Contracting Agents with Sites

Allocation of Revenue among Competitors

Leagues

Entry Restrictions

Open Systems (Non-U.S. Soccer) – play your way in

Closed Systems (Most U.S. Leagues) – buy your way in

Allocation of Revenue

Rules of Play on & off Field (those not set by Governing Bodies)

Scheduling & League Championship Structures

We will speak of leagues as the organizing unit, but there is significant variability across different sports.

Economic Objectives Addressed by Leagues

Define the Competitors: Who gets in?

Does a potential entrant add value to the competition?
..... to the other competitors?

Enhance Interest & Value of the Competition

Uniform & Value-enhancing rules

Scheduling & Championship Structures

Potential conflict between value of the sport and the league itself

Allocate the Revenue to Competitors

Sporting events are joint products

Who gets what?

How is revenue shared?

Avoid Rent Dissipation

Control behavior with negative externalities

2. Evolution of Leagues: Major League Baseball (1)

Mid-19th C Baseball was an adaptation of English cricket

Two Sets of Rules: Massachusetts vs. Knickerbocker Rules

Mass: Winner was first to score 100 runs (can take all day!)

Commercial development favored Knickerbocker rules

Knickerbocker rules codified by A. Cartwright, 1845

Towns formed teams & played each other

NABP (primarily NY) est. 1858

Key objective was to preserve "gentlemanliness" of the game (it failed)

Cincinnati Reds became openly professional in 1869

1st Barnstorming tour: went 56-0-1; 2nd: lost 4 games, abandoned

Barnstorming is unstable: interest requires a unique entity

Undefeated Goliath attractive; 75% winner is dull

Evolution of Leagues: Major League Baseball (2)

National Association: 1871-1875

Player-owned & managed

Number of teams grew from 9 to 15 in 1875, but ...

public confidence fell due to association with gamblers & liquor

National League est. 1876 with 8 teams

Owned & operated by businessmen

Standard rules & policies set for all teams to follow

Oldest surviving pro league in world, but not without threats

Merged with AL 1903 (another 8 team league)

Fought off the Federal League (1915)

Moved 2 teams to California to thwart Pacific Coast League Ambitions

Q: Is there any magic in the number 8?

A: Yes, sort of. See the economics of clubs

The Economics of Clubs and the NL Saga

James Buchanan – Nobel Laureate (1986)

Developed theory of the economics of clubs

What is right size of a “club”?

New members a new source of revenue

Also a drain – must share with one more

Add an opponent only if it raises the value of the club

National League limited to 8 in a growing economy

Feared too many teams would render some teams unprofitable

Problem: left NL vulnerable to entry

In 1901 AL entered “open” cities

Result: 1901-02 AL-NL War

1915: Entry of Federal League (-> anti-trust suit)

1950s: PCL Ambitions (-> Dodgers & Giants move west)

League Wars & The Economics of Clubs

Moral of the NL Saga

Limiting entry protects team profits from dilution

High profits create threats from rival leagues

Expansion can successfully thwart rivals

N. American Mergers of Rival Leagues

AL-NL 1903 -- 2 year war

AFL-NFL 1966 -- 6 year war

NBA-ABA 1976 -- 10 year war

NHL-WHA 1979 -- 7 year war

Why wars between rival leagues?

This is common in closed systems but very rare in open systems

Clubs keep # members low to protect profits per team

Some cities have room for more/new teams -> rival leagues

League wars end with death (Fed League, USFL, XFL) or merger

3. Benefits & Costs of Alternative Organizational Structures

Internal Tradeoffs

a) Externality Control

Externalities in CFB

Can play a weak schedule to increase chance at NT in CFB

This helps team w/ weak schedule but decreases value of the competition

More mismatches

Perception of competitiveness falls

BCS adopted to address this problem in part

Strength of schedule rewarded

Adds structure that leagues generally provide that CFB otherwise lacks

Control of field conditions

Grass height, muddy tracks to slow down teams

League control & sanctions limit this in NFL, MLB (but don't eliminate it)

Revenue Sharing & Incentive Effects

Old Days: Invitations to play coupled with negotiated prices

CFB again: non-conference games & appearance fees

Leagues:

Early on adopted rules for sharing ticket revenues

Varies a lot across leagues: NFL (much shared) vs. NBA (little)

Extension of sharing to media revenues

NFL: all TV revenue is league revenue, equally shared

MLB: Yankees, Braves, Cubs has extensive non-shared TV

Problems with Revenue Sharing -- See NFL

1. "The Bungles"

Incentive to field a quality team is diminished.

Keep low wage bill, lose, but get same share of media revenue as 49ers

2. Most revenue is pre-determined by TV contract

Incremental revenues come from stadium deals

-> threats to leave town for incremental revenue of highest bidder

Good for individual team, bad for league: every team left Los Angeles!

3. Luxury Box Revenues

Could there too many boxes with empty seats and no cheers?

Gate revenue is split 50-50.

Luxury box revenue is not shared.....

Sports Leagues & the Tragedy of the Commons

Tragedy of Commons

No single owner leads to excessive exploitation

Common grazing land in medieval England & 19th C U.S.
(Buffalo herds vs. Livestock)

Ocean Fisheries (Lake Hartwell too!)

Difficulty of controlling access -> excess fishing, lower stocks

Common Pool Problem in Oil Fields

Excessive investment in wells

Sub-optimal extraction rate -> poor recovery of oil from ground

The NFL as a Commons

Exploiters of the commons

Bud Adams (Houston to Tennessee)

Bill Bidwell (St. Louis to Arizona)

(the Redbird version of the Bungles)

Al Davis (in & out of LA)

Loss of teams' regional identity harms other owners

Jerry Jones

"Is there an NFL contract I can break?"

NFL exclusive contracts generate revenue for all owners

Coke contract barred teams from Pepsi deals

"Coke: official drink of the NFL"

Jones signed contract Pepsi & "Texas Stadium"

Stadium was a vehicle for getting Jones a bigger share of \$

External Tradeoffs

Joint action on rules, scheduling, etc increase value to consumers

But....Joint action can also benefit league owners at consumers' expense

How? Barriers to entry.

NFL has objective of limiting # franchises to keep share of media contract high per team

This limits # of teams.... i.e. without the entry restriction, LA fans would have a team. LA fans are clearly harmed by this aspect of joint action. Which leads us to the topic of Antitrust.

Misc Notes:

Notes re College Football:

CFB is less of a joint product as a rule than NFL: 100,000 show up at Michigan, & Tennessee regardless of the opponent

Some games more of a performance nature than a contest

Championship structure in CFB a problem in past

Weak schedule could win NT (undefeated BYU vs. 1-loss UW in 1984)

Bowl system still unstructured: want to play? (only pride at stake);
anachronistic relative to most revenue-generating sports contests