Entrepreneurship a good play for NBA in China

ERIC DRUMMOND is head of international human resources for the National Basketball Association based in New York City. He has over 20 years of Fortune 500 experience with companies such as Ingersoll-Rand, PepsiCo, and Coors Brewing. His focus has been in the area of global human resources supporting various international business units. He has lectured at several institutions including the University of Colorado Denver, University of Geneve, NYU, and Yonsei University (Seoul) among others. He has lived in Europe, Asia, and the Middle East. A native of Detroit, he earned a master’s in labor relations from Michigan State University. Drummond serves on IIB’s Global Advisory Board.

The NBA entrepreneurial? Some would say No. After all, the National Basketball Association has been around since 1946 and is a well-established brand domestically and internationally. “Many of the players on the 30 NBA teams are known worldwide,” said Eric Drummond, a featured speaker at the Faculty Development in International Entrepreneurship (FDIE) program.

Pick a country – any country – and mention names like Kobe Bryant and LeBron James and watch faces light up in recognition.

International sales of NBA business units account for about 15 percent of the league’s revenues. Furthermore, said Drummond, “The NBA recruits talent from around the world. The 2008–09 season boasts 76 players from 31 countries.”

This does not sound like your typical entrepreneurial start-up operation.

Drummond suggested otherwise, pointing out that when a domestic company recognizes an emerging opportunity in another country and seeks to breathe life into it despite obstacles, an entrepreneurial vision and strategy are essential.

Such was the case in China, which a year ago represented the “Perfect Storm,” a confluence of conditions that made the NBA’s international marketing team, led by Heidi Ueberroth, move to plant its flag on Chinese soil. The NBA already had a presence in China through various programs such as exhibition matches, touring basketball events, and televised games. The league also had offices and employees in the country. But conditions now were ripe for something on a much bigger scale.

Unlike companies that have flocked to China in the last several decades, the NBA was not looking for low cost labor. In fact, Drummond said, “Wages are rising there and are now up to 50 percent higher than just five years ago.”

So if it were not about wages, it had to be about the market. And for the NBA, the market was and is enticing.

- 1.3 billion population
- A growing middle class; 400 million people moved out of poverty in the last 20 years.
- Basketball has been in China since the late 1890s; Chinese fans are almost as fanatical as those in the US.
- In the 15-24 age group, 83 percent identify themselves as fans of the NBA, up from 75 percent the previous year.
- In November 2007, at the start of the season, 200 million Chinese turned on their TVs at 8:00 in the morning to watch a regular season NBA game. This was because Yao Ming of the Houston Rockets and Yi Jianlian of the Milwaukee Bucks now NJ Nets) played against each other for the first time.

Oh, and let’s not forget the hugely successful Summer 08 Beijing Olympics and the new arena built to accommodate basketball and entertainment events during and after the official games.

Charting a different course

In its 62-year history, the NBA has grown by adding teams in the US and Canada, and maximizing profits through three main revenue streams:

- Sponsorships
- TV, broadcasting rights
- Merchandise sales

“But we asked ourselves if that were the best we could do to take advantage of this perfect storm,” said Drummond. “We came to the conclusion that if we concentrated on the same three revenue streams, we’d probably continue to make money but we’d miss the opportunity we saw developing in China.

“We shifted the paradigm from what we’d always done to what we’re good at: running a first class professional league and establishing the financial models to make that work.”

The international marketing team considered creating a second league which would function as a division of the NBA. But that had political ramifications “because it could be viewed by the China Basketball Association (CBA) as a rival.” The CBA has ties to the government and culturally to the people so that idea was quickly dropped.

“The choice came down to doing the same thing in the same way – exporting the NBA’s US business model intact – or figuring out a different way to make things happen in this particular market,” said Drummond. “This is where we became entrepreneurial and started thinking outside the box.”

The result was the formation of NBA China, a separate legal entity that is majority owned by the NBA but operates independently. It is headquartered in Beijing. Tim Chen was hired as CEO. Chen, most recently the head of Microsoft for China and previously the head of Motorola for China, “had the reputation that a brand like the NBA needed,” said Drummond.

The marketing team then contracted with Goldman Sachs to do valuation on the Perfect Storm. “We wanted them to put a dollar figure on what NBA China could look like five years out.” The number Goldman Sachs came back with? $2.3 billion.

Impressive, but not impressive enough to convince the NBA Board of Governors (the 30 team owners) in the US to provide the funding for a new venture. “They were focused on the States and not on making investments above and beyond what was already budgeted for China,” said Drummond.

Now what?

It was every entrepreneur’s biggest challenge: How to raise the funds to move forward. A stumbling block, yes, but the international marketing team had come...
too far to turn back now. “We did what no other sports league had ever done: We made a decision to do a private placement, to sell 10 percent of NBA China to outside investors,” said Drummond.

“There are no outside investors in the NBA so this was all new, a way to raise seed capital to grow this business exponentially without straining the 30 team owners.”

But 10 percent of what? Ten percent of the new entity’s current business wouldn’t amount to much; however, 10 percent of the $2.3 billion projected for NBA China five years out would be sizable. So the Goldman Sachs figures were used to attract investors. But not just any investors, not family and friends who are the traditional targets of entrepreneurs. Wanted were investors who had connections as well as capital to offer.

“We held 14 investor meetings in October 2007 to find Chinese strategic partners. We pre-selected 38, mostly companies in banking, media, and technology. Of the 38, 21 actually received the private placement memo.” The response? “We had more interest than we wanted,” said Drummond.

Although a good problem, it was a problem nevertheless, “because we had to pick and choose and not upset people who might become sponsors if not investors.”

This past January, NBA China received the support it needed when investors snapped up the initial 10 percent. ESPN, a division of The Walt Disney Company, became the anchor investor with 5 percent; Bank of China 2 percent; Legend Holdings Ltd. (parent of Lenovo laptop computers) 2 percent; Li Ka Shing Foundation 1 percent. There was one more investor NBA China couldn’t refuse: Another 1 percent went to China Merchants Bank because of its strategic importance.

“So we actually sold 11 percent ($253 million); the NBA retained 89 percent.”

**Joint venture**

According to Drummond the National Basketball Association will eventually run NBA China League “but it will be a joint venture with the CBA,” thus eliminating any potential rivalries and bad feelings.

“The NBA in the US came together bit by bit, adding elements as market opportunities grew.” In China, we’re starting with a blank sheet of paper that we can fill with franchise rights, league ownership, collective bargaining and innovative brand extension opportunities all up front.”

Drummond projects that in the next two years, the NBA will have 100 retail stores in China, some company owned, some franchiser owner. “This is nothing we’ve ever done before. In our US model we have only one store in New York City.” The biggest opportunity for brand extension is in arenas, he said (see sidebar).

There has been a paradigm shift, Drummond said. “We’re looking at using the NBA brand and NBA expertise for growth rather than relying on expansion teams. Because our best export is not a team but our knowledge. We know how to run a first class professional league and we know the financial models to make that work.”

NBA China is not just about the NBA, Drummond said. “Culturally it’s also about what we want to do for the country and for basketball.”

In addition to philanthropy, plans include a revamp of the entire provincial basketball system, a grassroots effort that consists of basketball academies and clinics “that will help manage how basketball is taught from high school to college.” If all goes according to plan, it is likely that NBA China will go public in three-five years.

And the owners? What do they think of NBA China now? “Brilliant,” they said at a recent board of governors meeting.

Despite the excitement about China in many corporate boardrooms, there is unease among some Americans who feel that the communist government could clamp down on foreign companies anytime they choose. Drummond does not share these concerns.

“I would submit there is no way the Chinese government can stop what is happening here now. They could perhaps put brakes on the economy, try to steer it, but that train has left the station.”

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**Beijing Olympic Basketball Arena**

Two years ago, kicking off the Perfect Storm, the NBA started advising the Beijing Organizing Committee for the Olympic Games (BOCOG) on the design of the Beijing Olympic Basketball Arena (BOBA).

“They came to us because they knew we knew about arenas,” said Drummond. “In order to incorporate the upscale elements they wanted, we advised them to increase their budget by many millions.”

There are many “firsts” attached to development of the arena. It is the first collaboration of its kind in Asia. The goal was to develop a world-class NBA-style venue that would remain an attraction for citizens and tourists long after the closing ceremony of the 29th Olympic Games.

By all accounts, the goal has been accomplished. The arena is twice as big as current CBA stadiums, with a capacity of nearly 19,000 seats, including club seats and 48 private suites, all with excellent views of the action. Furniture, light fixtures and audio-visual systems have been custom designed. Food and beverage options from around the world will satisfy a multitude of tastes. “After the Olympics the site will host NBA games, concert tours and shows, international and regional events, even a traveling circus,” said Drummond.

The arena will be run by a partnership of the BOCOG, NBA China, and AEG, a wholly owned subsidiary of the Anschutz Company and operator of facilities such as the Staples Center in Los Angeles. For the NBA it’s another first, their first venture into facility management in China.

“We’ve learned from the States; we’re doing this is Europe and now also in China. This arena in Asia is a first of its kind,” said Drummond, looking ahead to which city will want the next one. Will it be Shanghai, Chengdu, Guangzhou? “In China, they go from primitive to state of the art like this,” he said, snapping his fingers. “There is no in between.”

And in a country where basketball is a favored sport and a new billionaire pops up on a monthly basis, there will also be no shortage of funding.