Professional Team Sports Clubs

Cases of soft budget constraints in capitalist economies?

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Professional Team Sports Clubs: Cases of soft budget constraints in capitalist economies?

Working paper, December 2010. Comments are welcome!

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Abstract: *Professional football in Europe is characterized by persistent deficits, growing debts and additional financial problems among the majority of the top league clubs. Despite these problems, these clubs have an abnormally high survival rate. This paper focuses on this apparent paradox and poses the question: Why do only very few European professional football clubs go out of business even though they operate chronically close to the edge of financial failure? By applying the soft budget constraint concept - originally developed by the Hungarian Economist János Kornai - to professional football in Europe, this paper argues that professional team sports clubs (PTSCs) are cases of an economic phenomenon normally found in socialist or post-socialist economies.*

Keywords: Soft budget constraints, European professional football, economics of sport

Introduction

The peculiar logics of professional team sports have puzzled economists for years now. Since Rottenberg (1956), Neale (1964), Davenport (1969) and Sloane (1971; 1980) took the first steps in their classic papers on the specificity of the sports business towards what has become a distinct, established discipline of sports economics, several academic insights have been applied to the understanding of the sport business sector.

However, it is clear that contemporary scholars examining the economy of professional team sports have not developed a satisfying understanding of the paradoxes that seem to be fundamental parts of the sector, such as: Why do European professional team sports clubs (PTSCs) chronically operate on the brink of insolvency without going out of business?; and: Why is the survival rate of PTSCs so high when the football business perpetually generates losses? It is also important to consider how we are to conceptualize these paradoxes.

To compensate for the lack of theoretical answers to these questions, this paper proposes an application of the concept 'Soft Budget Constraints Syndrome' (SBCS), developed by Kornai & Kornai et al. (Kornai, 1980a; 1980b; 1980c; 2001; 1998; 1979; 1986; 1985; Kornai, Maskin, & Roland, 2003) to understand the inefficiency of enterprises in socialist or post-socialist economies, to sports economics literature. It provides an explanation of the significant presence of the SBCS phenomenon to show how the concept can be applied to the business of professional team sports.

Structure of paper

The paper is structured as follows: Firstly, it goes through current research on the economics of European professional football focusing on the paradox of persistent losses and extreme stability (I). Secondly, it points to the missing theoretical conceptions of this phenomenon, suggesting the concept of soft budget constraints as a fruitful starting point in understanding the peculiar logics of professional team sports (II). Thirdly, it concludes by discussing whether the budget constraints of PTCSs can, or should, be hardened (III).

I: Persistent losses but extreme stability

Persistent losses

One of the inconvenient truths about European football is its significant lack of profitability and financial management. Even though the top five leagues' income has risen significantly over the last decade (see: Deloitte & Touche, 2000; 2001; 2002; 2003; 2004; 2005; Deloitte, 2006; 2007; 2008; 2009; 2010a), financial troubles have followed suit.

A large number of studies analyzing the development of European professional football point to a lack of profitable management or a 'winning' optimization approach in European football in contrast to the profit-orientated American leagues.[i] For example, in their discussions of Europe's most popular league, the Premier League, Walters and Hamil (Walters, 2007; Walters & Hamil, 2008; Hamil & Walters, 2010) find no evidence of any profit-orientated behavior among the European clubs. Despite significant revenue growth rates – more than 900 percent in the period between 1992 and 2007, and continued growth in the latest years – all of this money is used on players' salaries or transfers, leaving no profits.

In fact, since the foundation of the Premier League in 1992, there has been no year that has generated a collective pre-tax profit for the Premier League Clubs (Hamil & Walters, 2010, p. 354). On the contrary, the clubs usually operate way down in the red, with the international consultancy firm A.T. Kearny (2010) concluding that, comparing returns on assets with the ratio of equity to assets, the English Premier League under normal conditions would be only one year from bankruptcy. Recent research by Beech, Horsmann and Magraw (2008) on the English football clubs' numerous financial difficulties reaches the same conclusions.

The English situation is recognizable in other European football studies. Morrow (2006, p. 106), Szymanski & Zimbalist (2006, p. 140) and Hamil et al. (2010) see Italian football as a prime example of financial chaos and poor management. Baroncelli and Lago (2006, p. 20; 2006) also reveal an extreme increase in players' salaries of more than 700 percent in Juventus, Milan, Inter, Roma, Lazio and Parma from 1996-

2002 combined with persistent operating losses in all of the *Serie A* clubs, starting from an aggregate -€144.3 millon in 1996/97 increasing to -€982,2 million in 2001/02, thus clearly outlining a business sector on the brink of bankruptcy. In addition, over the 1996/1997-2006/2007 period the accumulated losses of Italian *Serie A* Clubs amounted to a total of €1355 million before transfer deficits were taken in to account (Hamil et al., 2010, p. 391).

Garcia and Rodriquez (Garcia & Rodriguez, 2003) and Boscá et al. (Boscá, Liern, Martínez, & Sala, 2008) show that Spanish football is another case of severe financial distress. Despite increasing revenues – the Spanish first tier currently has aggregate club revenues close to €1.5 billion (Deloitte, 2010a, p. 11) with FC Barcelona and Real Madrid both topping the Deloitte Football Money League[ii] (Deloitte, 2010b) – Spanish clubs are still spending larger and larger amounts on player wages and transfers, resulting in rising levels of debts. Even though Spanish football has had major financial injections, the first in 1992 from public Spanish football pools to cancel their debts and a second, five years later, from new television deals, several Spanish clubs have been threatened with closure due to overspending (Garcia & Rodriguez, 2003, p. 253; Lago et al., 2006; Barajas & Rodríguez, 2010).

According to Barajas and Rodriguez (2010, p. 57), close to a majority of Spanish clubs are vulnerable when measured on factors such as indebtedness, capacity to refund debts and expenditure on players seen in relation to operating revenues. Furthermore some 89 percent of the Spanish clubs in the first and second divisions had operational losses in 2008, with nine clubs being technically insolvent – due to regulations in Spanish law – thus operating under administration (Barajas & Rodríguez, 2010, p. 53). Seen from a historical perspective accumulated operating results in Spain have always been negative, and even though some clubs generate positive results from time to time, a breakdown of these data reveals that more than half of the clubs are operating in the red each year (Boscá et al., 2008, p. 170).

In the Scandinavian context, Gammelsæter and Ohr (2003, pp. 11,34) point out numerous financial problems in the Norwegian *Tippeligaen* (first tier) in their in-depth analysis of the development of Norwegian football. Many clubs have struggled over the years with low cash flows resulting in rescue operations (Gammelsaeter, Storm, & Södermann, 2010). Solberg and Haugen also confirm Norwegian football's dire financial situation. In 2007, the *Tippeliga* clubs' total operating losses amounted to NOK 80 million (Solberg & Haugen, 2010, p. 330).

There are also persistent concerns over the financial management of league clubs in Sweden. Escalating salaries in the 1990s resulted in equity requirements being put in place from the 2000-season onward (Carlsson, 2009). Although this licensing system reduced economic hardship in a number of Swedish clubs, it did not completely abolish the clubs' financial troubles. In 2009, for example, the three Stockholm clubs – AIK, Djurgården and Hammarby – were still experiencing significant problems (Gammelsaeter et al., 2010).

Denmark, being the leading Nordic league measured by revenue, had its initial steps towards commercialism characterized by financial hardship during the 1980s and 1990s (Storm & Magnussen, 2005). As in the rest of the European Leagues, all of the Danish clubs have been in financial trouble – some of them several times. In the first decade of the new millennium, FC Copenhagen and Brøndby IF stood out as the clubs which had the most proficient financial management. However, these clubs were the exception to the rest of the league's financial deficits (Storm & Brandt, 2008; Storm, 2009; Storm, 2007; Storm, 2010). In 2009 and 2010, following the credit crunch crisis, the majority of Danish league clubs faced significant losses amounting to a total of DKK 432 million in 2010. Leading clubs such as FC Copenhagen, Aalborg Boldklub, AGF (Århus), Brøndby and FC Midtjylland all experienced difficult times, some being close to financial collapse. It remains to be seen whether these current problems are over.

...but extreme stability

Despite the economic hardships outlined above, the history of European football is also a history of extreme stability. Szymanski (2009b) and Szymanski and Kuper (2009b; Kuper & Szymanski, 2009) show that the football sector is very stable when it comes to survival.

Compared with developments in the overall economy, the problems of football capitalism are trivial. For example, in 1923, the Football League consisted of 88 teams organized in four divisions. In the 2007/08 season, 85 of them still existed (97%), 75 remained in the top four divisions (85%), and 48 were in the same division as they were in 1923 (54%) (Kuper & Szymanski, 2009, p. 88f).

These statistics differ in relation to the survival rate of the English top 100 companies in 1912. By 1995, only 20 of these companies remained in the top hundred, 50 survived, seven were liquidated, six were nationalized, and 37 had been acquired by other firms (Szymanski, 2009b).

In comparison, the survival rate of Italian football clubs is also high. Of the 60 teams playing in the top Italian League from 1929-2010, only Legano and A.C. Ancona[iii] are out of business today. Although some Italian clubs in recent years – especially following the credit crunch crisis – have been relegated due to financial collapse, it is noteworthy that almost all of them have been reconstructed.[iv] Moreover, nine of the 18 (50%) teams playing in the top league during the 1929 season were also playing the best teams in the 2010-season. In the second-best division, however, only two teams from 1929 are present today. Nonetheless, it is remarkable that 20 of the 36 original teams (56%) are still playing in the two best tiers.

Spanish football clubs have also had high rates of survival, although not as high as in the English and Italian football leagues.[v] Most of the 59 teams that participated in Spain's first tier league since its establishment are still operating today. Furthermore, seven out the ten (70%) teams that played in this league in 1929 are also playing in this league in the current season (2010/2011).[vi] As with the Italian Teams, however, only two out of the ten teams that played in the second-tier in 1929 are playing there this season (there are 22 teams in this league today). Still, 13 of 20 (65%) teams being in the best or second best tier in 1929 is playing one of them today pointing to a high rate of survival.

In Danish football, even though several clubs faced severe financial problems between 1995 and 2009, only one league club, Lyngby FC, faced insolvency and relegation (Storm, 2009). More than 5879 firms in Denmark had to close in 2009 due to financial collapse. This figure rose 50 percent from 2008, which set a record for the number of bankruptcies in one year. In contrast, all of the Danish first-tier football clubs survived in 2009 and only two second-tier clubs (FC Amager and Køge BK) folded. This statistic indicates a high rate of survival in Danish professional football as well.

II: The peculiar logics of professional team sports: Towards a theoretical understanding

The above examples suggest that the survival rate of professional European football clubs, in comparison with the recent overall financial climate, seems extraordinarily high. Why is this so? And how are we to understand it? This paper proposes that by applying the idea of the soft budget constraint phenomenon, developed by Kornai, to the paradox of unprofitability and survival in European PTSCs, it is possible to identify a concept that provides valuable insights in the theoretical development of sports economics. This argument is enlarged below, giving an introduction to the concept followed by a discussion of the conditions that lead to soft budgets in the European PTSCs.

Understanding the soft budget constraint

Kornai introduced the concept of soft budget constraints in his article 'Resource constrained versus Demand-Constrained Systems' (Kornai, 1979) and his book *Economics of Shortage* (Kornai, 1980b), to describe a situation by which seemingly unprofitable firms or enterprises are bailed out by public authorities or creditors (Maskin, 1999, p. 421). Kornai saw the soft budget constraint as a significant factor in explaining certain characteristics of socialist economies, especially shortage and inefficient (public) companies (Li & Liang, 1998, p. 104). The concept is best understood when contrasted with its counterpart, the 'Hard Budget Constraint' (HBC), which, according to Kornai, is the dominating economic budget constraint in capitalist economies.

Hard budgets constraints

According to Kornai, the hard budget constraint is a form of economic coercion where "*proceeds from sales and costs of input are a question of life and death for the firm*" (Kornai, 1980b, p. 303; Kornai, 1979, p. 806). In addition, the budget constraint is hard if the growth of the firm is dependent on what it can derive from its own profits, or what it can take out from creditors for investment purposes under conservative conditions (Kornai, 1979, p. 807).

Furthermore, Kornai states that the following five conditions need to be met in order to guarantee 'perfect hardness' (see: Kornai, 1980b, pp. 302-303; Kornai, 1980c, pp. 233-237; Gomulka, 1985, pp. 2-3; se also: Kornai et al., 2003, pp. 1097-1098):

- H1: The firm is a price-taker for both inputs and outputs;
- H2: The firm cannot influence the tax rules: these rules base taxes on observable and measurable criteria; no individual exemption can be given concerning the volume of tax or dates of collection;
- H3: The firm cannot receive any free state or other grants to cover current expenses or as contributions to finance investment;
- H4: No credit from other firms or banks can be obtained: all transactions are made in cash;
- H5: No external finance for investment is possible.

According to Kornai (1980b, pp. 311-312; Kornai, 1980c, p. 237), the conditions of 'perfect hardening' are more or less theoretical, making the 'Almost Hard Budget Constraint' (AHBC) a more likely empirical case. Instances of AHBCs happen when primary conditions of the hard budget constraints, other than H2 and H3, which remain fixed, are relaxed. In such cases, the firm will always fulfill its obligations and take appropriate steps to adapt to changing environments. Price making exists within narrow limits, credits can be obtained on conservative and orthodox principles, and external financing for investment purposes can be derived on hard conditions (Gomulka, 1985, p. 3; Kornai et al., 2003, p. 1102).

Soft budget constraints

In contrast, 'perfect softness' is a state of affairs when differences between proceeds from sales and costs from production are not a matter of life and death (Kornai, 1980b, p. 308), when the growth of the firm is not tied to the present or future financial situation, or when the firm "survives even when investment entails grave losses" (Kornai, 1979, p. 807). In other words, 'perfect softness' occurs when several or all of above factors are relaxed. Of course, one can find intermediate stages between hard and soft constraints (Kornai, 1980b, p. 310; Kornai, 1980c, p. 237), thus making it difficult to measure exactly the degree of softness, but in general the relaxation of several or all conditions from H1 to H5 are signs of softness that are typical of companies in socialist or post-socialist economies.

Kornai does not deny that the SBC phenomenon can be found in capitalist economies, even though he believes that it is far more common in a socialist or post-socialist economy (Kornai, 1998, p. 12; 1980b, p. 314; 1986; Kornai et al., 2003, p. 1119; Blanchard, 1999, pp. 439-440; Gomulka, 1985, p. 1). However, examples of soft budget constraints in capitalist economies are not rare (Kornai et al., 2003, p. 1097; Röller & Zhang, 2005, p. 48). The public health care sector in Europe is often steered under soft budget constraints (Tjerbo & Hagen, 2009; Duggan, 2000). The same can be said for other public sector areas, such as the military or even the bank sector in some countries (Du & Li, 2007; Bergløf & Roland, 1995; Mitchell, 2000), where instances of soft budget constraints are found to be difficult to harden.

Maskin and Xu (2001) point to the existence of the SBC syndrome in the American context during the Savings and Loans crisis in the early 1990s and the Long-Term Capital Management Crisis in the late 1990s, where the US government conducted several bailed outs – an action that has been repeated during the recent credit crunch crisis, in which bailouts of American and European banks were made in order to prevent a fundamental collapse of western economies.[vii] As pointed out by Kornai, Maskin and Roland (2003, p. 1095), the collapse of the East-Asian banking sector in the 1990s can also be considered in relation to the SBC syndrome.

Why does the SBC syndrome appear?

According to Kornai, the SBC syndrome is likely to appear when a firm faces the possibility of negotiating refinancing, credits or subsidies *ex post* (Kornai et al., 2003, p. 1100). To put it more concrete, the question of (soft) budget constraints refers to the behavior and, in particular, the *expectations* of the future financial situation by a decision maker in a (public) firm standing in a principal-agent relationship to a financing (governmental) institution (Kornai, 1986, p. 4; 1980c, p. 240; 1998, p. 14; 1980b, p. 309f; 1985, p. 50; Tjerbo & Hagen, 2009, p. 337).

In short, decision makers and managers in firms that are expecting bailouts or support in case of financial trouble ex post have strong incentives to increase expenditure above the initial budget, leaving the additional costs – e.g. the firm deficits – for the principal to pay, thus resulting in a softening of their budget constraints.

If the expectation of support ex post does not exist *ex ante*, then a given project is very likely *not* to be undertaken by the firm, if the firm is not sure it can finance it alone in the future. In other words, ex ante expectations of future (ex post) refinancing or support are a primary key to the development of a soft budget constraint that is otherwise hard, almost hard or harder than the case where expectations of ex post support is institutionalized (Kornai, 1980b, p. 309f; Kornai et al., 2003, p. 1104).[viii]

How do expectations of ex post support grow?

In the classical case of the emergence of the SBC syndrome, typically established in socialist or post-socialist economies where a clear supporter-supported relationship exists, it is quite clear how expectations of ex post support are established in the SBC firm or organization. Normally, the SBC organization is producing a welfare good seen as important to the government and is thus established initially with public subsidies. Seen from the side of the supporter organization, Kornai draws attention to the dynamic commitment problem faced when the supporter organization is to decide whether to support a given project if it exceeds its costs in the future. The problem here is that ex ante it is very difficult for a potential supporter organization to select good projects from bad ones. Essentially, decisions in such cases are based on expectations of future performances, and one cannot predict these performances precisely. Information on which decisions can be made does not become evident until the project has run for a certain period of time. This being said, it is not necessarily clear that the information derived after a period of time is enough to make a correct decision to offer further support (or not). A potentially profitable project could eventually produce a lower return on investment than expected, and on the other hand, a project that seems inefficient in the short term could turn out to be profitable later. Therefore, information asymmetries can prompt bailouts or support.

Motivational factors behind organizations' decisions to support vary, according to the literature. Pun (1995, p. 335), Kornai (1979, p. 806; 1980b, p. 561ff; 1985, p. 50) and Kornai et al. (2003, p. 1111), point to paternalistic factors, which are relevant in many cases, whereas Kornai et al. (2003, pp. 1098-1099) point to other explanations, such as (un-)employment issues (see also: Li & Liang, 1998, p. 108; Schmidt, 1996), fear of political unrest, fear of losing previous investments (that are sunken), reputational (political) incentives (se also: Robinson & Torvik, 2009; Schmidt, 1996, p. 51), spillover effects, and even corruption.[ix]

In other words, certain structural, and perhaps even cultural, factors seem to be a prerequisite for the SBC syndrome to emerge. Understood in this way a soft budget phenomenon is not a solely financial matter – it is a socio-economic one (Kornai, 1986, p. 8). According to Kornai it primarily reflects a relationship between the state and the economic micro-organization in a vertical relationship (Kornai, 1998, p. 13). As a broader interpretation, a soft budget phenomenon can also be said to reflect a relationship between an organization and its environment (Kornai, 1980b, p. 321; Kornai et al., 2003, p. 1107).

In the translation of the conceptualization presented here, the element of vertical relations characteristic of a supporter-supported relationship is stretched to grasp a more complex situation where many types of stakeholders - not only public supporters, but also private investors, creditors or alike - in a firm (or organization) are interpreted by the firm (or the organization) as potential supporters, whereby expectations of ex post support can grow even though the vertical supporter-supported relationship does not exist ex ante.

It must be pointed out that, with organizations following the classical case above (with important societal assignments that serve or affect a larger number of people), such an approach entails that the PTSCs, to various degrees, take on a role as being ‘too big to fail’, behaving as if they can expect ex post support. As we shall see below this is exactly what many European PTSCs do.

Put differently, and without ruling out any of the above explanations of the emergence of the SBC syndrome, this paper want to suggest that in the case of the sports business, some specific characteristics, especially social attachments and emotions, have the ‘majority vote’ when the SBC syndrome is at play. This is because expectations of ex post support in European football usually grow due to the fact that football clubs serve as identification marks in their respective local communities or larger regions, and are successful in being such a mark.

By taking such a broad approach it becomes possible to understand the paradox of European football, because several stakeholders, private and public, from time to time play the role as supporters of their respective clubs, thus establishing the conditions of development of the SBC syndrome in a sector normally perceived as capitalist. We now turn to explain how this can be understood in more detail.

The soft budget environment of European football

In short, it can be argued that the emergence and persistence of the SBC syndrome in professional football is due to two main, interconnected factors: 1) The institutional mechanism of the football market and 2) the specific emotional logic of sport focused on winning. We will deal with the two main factors in turn, and then describe their interconnectedness.

The institutional mechanisms of the football market

According to Dietl, Franck and Lang (Dietl, Franck, & Lang, 2008, p. 366), European football clubs are facing severe financial problems due to the ruining conditions of competition in the European league structures enforced by: A) a more unequal distribution of the league revenue; B) an additional exogenous prize (e.g. participation in international competition) awarded to the winner of the domestic championship; C) a system of promotion and relegation; and D) increased inequality between the first and second divisions in the domestic league.

The problem of promotion and relegation (Factor C) is well recognized in the literature as a threat which places ever-increasing pressure on clubs to invest in player talent to avoid being relegated, excluded from the market, and thereby placed in a dire financial situation. Conversely, promotion increases revenues significantly (Solberg & Haugen, 2010, p. 337; Szymanski & Zimbalist, 2006, p. 4; Gammelsaeter & Ohr, 2003, p. 4). Thus, an increasingly unequal distribution of revenues (Factor A) and the increasing polarization between the first and second tiers (Factor D) amplifies the incentive to gamble for success.

Knowing that these mechanisms are actually at work in European football leagues (Szymanski & Smith, 1997, p. 148; Storm, 2009, p. 21; Football Governance Research Centre, 2005, p. 21; Szymanski & Zimbalist, 2006, p. 193; Barros et al., 2002, p. 7; Morrow, 2003, pp. 15-16), the overspending phenomenon is quite explainable. Typically, weaker performances or decreases in demand are not met with downward adjustments in costs (hardening) but the opposite: in order to be able to compete and raise performance clubs buy players, which indicates a softening of budget constraints.

It is not that a professional team sports club cannot be innovative or cannot develop more efficient 'lines of production' to cope with competition, but there is a general notion that sporting success can be achieved by hiring better players or a better coach, and that this is the precondition for gaining substantial income (Szymanski & Smith, 1997; Szymanski & Kuypers, 2000; Kuper & Szymanski, 2009). With these mechanisms at play, an expectation grows inside the PTSCs that if expenditure is high enough the investment will pay off, because there are major financial rewards in becoming successful on the field. But although there is some correlation between winning and increasing revenue, there is a limited - if any - connection between winning and generating profits (A.T.Kearney, 2010; Sperling, Nordskilde, & Bergander, 2010; Szymanski & Kuypers, 2000). All profits are typically competed away. The problem is that (false) expectations of increasing revenue and profit, seen on the level of the individual PTSC, add up to a sporting arms race on the aggregated level when the majority of clubs strive to make it to the top. The result is a demand on players and subsequently higher expenditures for all competitors involved.

As this sporting arms race is only further enforced with an exogenous prize (Factor B) - as the top level clubs compete for participation in the Champions League, where the income can be tremendous – it can be understood why the institutional mechanism of the football market is softening clubs' budget constraints.

But why are profits not possible?

It should be outlined here though, that Fort (2000) opposes the argument put forward by many scholars that PTSCs in the European context mainly optimize winning percentages, saying that European PTSCs are in fact profit maximizers, because it is not rational for them all to optimize winning percentages. He believes that the clubs are maximizing profits on behalf of a rational calculation of their 'real' or potential player talent set in relation to their financial capabilities. As the sum of winning percent is constant, which means that not all teams can win a league championship in a single year, and the teams know this, the teams with a lesser degree of financial strength will switch to a profit maximising approach thereby finding their place in the league hierarchy. They do this by only hiring the player talent that is necessary to reach the given profit maximizing optimum (Fort, 2000, p. 444).

Fort could be right if the clubs were willing to accept a sporting hierarchy among themselves that could lower the ruining competition conditions in the sector. What Fort overlooks, however, is that the game of overspending (e.g. the existence of softness of budget constraints) continues because the PTSCs have expectations of bailouts due to the second main factor in European professional football: Social attachments and emotions. This establishes the PTSCs as markers of identity in their respective regions, therefore providing them with resources to overcome the ruining competition of the sector.

When viewed from an economic perspective football clubs seem incompetent because they can afford to be (Kuper & Szymanski, 2009, p. 90). There is (almost) always someone – a bank, an investor, fans, public authorities, etc. – who is willing to step in and bail them out or find a (financial) solution to the problem (Lago et al., 2006, p. 6; Grant, 2007).

Furthermore, the prestige of being part of European football is significant, meaning that investors willing to risk their own money are likely to be attracted to this sector. This is particularly evident in the case of English football. For example, Russian oil billionaire Roman Abramovich has invested £700 million in the Chelsea Football Club since he took it over – money that will be extremely difficult get back (Hamil & Walters, 2010, p. 364). In this sense, a football club is more of a consumer good than an investment.

Moreover, according to Buraimo et al., the cultural significance of football in England has led even the hardest creditors into creating what Kornai would label as 'expectations of softness': "*English football has managed to sustain persistent losses that in other industries would have invited creditor reaction. The patience of banks, Inland Revenue, and other creditors is partly due to a reluctance to call in overdrafts and unpaid bills in recognition of community disapproval that would follow*" (Buraimo, Simmons, & Szymanski, 2006, p. 41).[x]

Clear cases of the SBC syndrome are also found in Italian football, where the cultural and political significance of the game is reflected in numerous examples of close connections between public authorities, politicians and clubs leading to permanent overspending, massive borrowing and searches for other financial 'solutions' to secure club survival.

The Lazio case in Italy is a prominent and interesting example of a club relaxing the H2 factor (described above). Around 2005 Lazio's managers reached an agreement with the Italian tax authorities to pay a €140 million tax liability over 23 years to avoid an immediate collapse of the club. Italian Prime Minister Silvio Berlusconi, besides being owner of AC Milan, excused the deal, stating: *"We are talking about a team that has a huge number of supporters and there could have been public disorder and grave consequences"* (Morrow, 2006, p. 105). Other leading politicians, such as the mayor of Rome, Walter Veltroni, replied to the support for the agreement like this: *"S.S. Lazio was a (...) national heritage for the sport and deserved to be bailed out simply on that account (...) the tax authorities were wise to help S.S. Lazio because the club had gone under it would have been a major blow to Italian sport*" (Hamil et al., 2010, p. 393).

Besides being a clear example of the SBC syndrome, the spirit of the Lazio case was instigated by the Salva Calcio decree ('save football') that was introduced by the Italian parliament in 2002 (Hamil et al., 2010, p. 374). The decree was designed to alleviate the Italian football clubs from financial reporting, regulatory and licensing problems, thus legally spreading the SBC syndrome to the overall football environment in Italy. The Salva Calcio decree allowed the Italian clubs to amortize players' transfer rights over a period of ten years instead of their respective lengths of contract, thereby improving the reported financial position and performance (Hamil et al., 2010, p. 393) in order to secure clearance from the Italian licensing agency, Co.Vi.Soc.

The Salva Calcio decree gives a clear picture of a very relaxed approach to the question of hardening budget constraints, which, in this case, was motivated by the weaving together of Italian professional football's (political) reputation and cultural matters. In this sense, some Italian clubs turn the horizontal relationship characteristic of the SBC-syndrome upside down. According to Hamil et al. (2010, p. 387) many Italian football clubs are owned by powerful families capable of exercising power in various social and political areas, and their survival can be seen as a result of simultaneous paternalism from the state and a perceived paternalistic care for the wider social welfare of the Italian people who stand alongside the football clubs' owners. In Italy the DNA of football is part of politics and power and vice versa.

With regard to Spain, the public interest in football is expressed in several rescue operations designed to help financially distressed clubs. In 1985 public authorities decided to help reduce debts in Spanish League clubs, which that at time exceeded €124 million. A few years later, in 1992, when the Spanish clubs faced a new economic crisis, the League organisation (LFP) closed a deal with the Surperior Sport Council in Spain and 192 millions of debts with public administrations were cancelled (Barajas & Rodríguez, 2010, p. 53).

In Spain, as in the case of the Italian clubs, the local government frequently steps in to bail out troubled clubs. For example: *(...) there is no chance that Real Madrid or Barcelona would ever be allowed to go bankrupt, whatever the financial problems of these big-spending clubs* (Lago et al., 2006, p. 8; see also: Barajas & Rodríguez, 2010, p. 64). As the clubs represent ethnic, geographical and cultural values (Ascari & Gagnepain, 2006, p. 77), and their fans and local communities take pride in that, the clubs are heavily backed by their respective regions, i.e. authorities and financial institutions (Barajas & Rodríguez, 2010, p. 53). Some of these regions sponsor the club or buy their stocks in order to support it. In other cases stadiums have been sold to a willing City Council for large profits.

These examples of support from local and state authorities – in the form of subsidies or cancelling debts – support the notion that Spanish top clubs seem to be immune to financial downturns. If the clubs cannot make it themselves others will fix the problem, either by providing the necessary credit (through the bank sector) or by injecting public subsidies into the clubs. As such conditions H3 and H4 are relaxed, showing the softness of budget constraints in European PTSCs.

Turning to the Scandinavian context, the political will to subsidize clubs is not as big as it is in Italy or Spain. However, several rescue operations of Danish football and team handball clubs have involved politicians and public support of various kinds. In some cases the City Councils have helped by sponsoring the clubs or by renting public stadium or arena facilities to the clubs at a very low price. The City Councils have even provided loans in order to secure liquidity in some of the clubs.

Support from public sources is not the only way in which conditions for softness appear in Scandinavian football. In the Danish professional football and team handball leagues, the use of soft loans – which, according to Kornai et al. (Kornai et al., 2003, p. 1102), are a way of relaxing hardness – is allowed in the license system and is frequently used as a means of boosting equity capital[xi] to match the licensing rules recommending that the equity capital in a professional Danish football or team handball club should be at least 25 percent of the amount spent on salaries. This clearly points to a practice of softness in the Danish context as financial risks are shared with external organizations – i.e. another relaxation of the hard budget constraint factors (Kornai, 1980c, p. 235).

III: Concluding remarks and perspectives

This paper has applied general insights from Kornai's work on the soft budget constraint to sport in order to understand the peculiar logics of professional team sports. It has shown that, with a few exceptions, European football clubs are operating with losses under conditions that can be understood by applying the concept of soft budget constraints to the phenomenon.

In many ways, European PTSCs share similarities with firms in socialist or post-socialist economies, and even banks in capitalist economies that are 'too big to fail', thus facing willingness from investors, public authorities and banks to bail them out or support them at times of financial trouble. In other words, PTSCs serve as central identification marks of local communities or large geographical regions to which stakeholders are socially attached to such a degree that the environment supports their survival – sometimes no matter what the economic costs. These bailouts, coupled with the lure of winning championships and trophies, reinforce the PTSCs' economically irrational behaviors. This in turn creates even greater economic problems which destabilize the sector and leave bills for others to pay.

Should and could the budget constraints be hardened?

While Kornai clearly points out that soft budget constraints are inefficient because the market is prevented from sweeping out inefficient firms when they are being subsidized by willing supporter organizations, the answer with regard to the sports business is less clear.

On one hand, the specificities of the sports business prevent it from becoming efficient – if 'efficient' means 'profitable' in a traditional sense. As pointed out by Kuper and Szymanski (Kuper & Szymanski, 2009, pp. 75-95), football clubs should learn that they are not businesses. They are sporting clubs whereby money is a means to an end. Making a profit in this sector is almost impossible.

On the other hand, grave financial problems are problems of moral hazards, meaning that many European clubs more or less irresponsibly gamble with money they do not have in order to stay competitive. If such actions are not sanctioned, then clubs that are making an effort to balance their books are punished in terms of their results on the field. Put another way, poorly operated clubs are rewarded for not being economically responsible because their spending enhances their chances of being successful – even though they are not entitled to such successes when measured financially.

This is of course not a fair situation, and with the amount of money now running through the European PTSCs, the sector is in need of being operated in a more businesslike way, e.g. the budget constraints must be hardened.[xii]

Fortunately, things are now taking a turn in the right direction in Europe as UEFA has reacted to the economic distress by initiating a Financial Fair Play program to improve the operational grounding of professional football. During the coming years European football clubs will be met with growing financial demands and a potential threat of being excluded from participation in the European club if they do not follow the new rules. So far all major football clubs have expressed that they will back up the initiative.

Judging by experiences in Germany, where a strict and enforced licensing system has been in place for a few years now, results of tighter control are positive. Besides growing interest from spectators and TV audiences, the German Bundesliga clubs are now reducing their debt portfolios, increasing their revenues and even making small profits. According to A.T. Kearney (2010), the French League is also operating under sustainable conditions.

Future studies must reveal whether the German or French model can be spread out to other European leagues and assess how effective the UEFA Financial Fairplay Program is in hardening the softness of European professional football.

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[i] On the contrast between the American profit maximization approach versus the European winning optimization please refer to: (Cairns, Jennett, & Sloane, 1986, p. 10; Solberg & Haugen, 2010, p. 331;

Downward, Dawson, & Dejonghe, 2009, p. 196; Szymanski & Zimbalist, 2006, p. 132; Kesenne, 2007, p. 4; Downward & Dawson, 2000, p. 27f; Lago, Simmons, & Szymanski, 2006, p. 5; Zimbalist, 2003, p. 504; Sandy, Sloane, & Rosentraub, 2004, p. 11; Barros, Ibrahímo, & Szymanski, 2002, p. 2ff; Ascari & Gagnepain, 2006, p. 77; Barajas, Fernández-Jardón, & Crolley, 2010; Szymanski, 2010, p. 32; Sloane, 2006; Szymanski, 2009a, p. 70f; Hamil, Morrow, Idle, Rossi, & Faccendini, 2010, p. 401).

[ii] FC Barcelona and Real Madrid have income streams of more than €400 million each in 2010.

[iii] Another team in Ancona, however, has taken over their logo, identity and plays under the name U.S. Ancona.

[iv] Clubs that have been relegated due to financial collapse are: Fiorentina (2002), Allessandria (2003), Como (2005), Perugia (2010), Venezia (2005 & 2009), Pisa (1994 & 2009), FC Pro Vercelli (2010), Pescara (2003 & 2008), Legano (2010), Ancona (2010) and Aurora Pro Patria (2009).

[v] The following Spanish clubs has been relegated due to financial trouble: CF Extremadura (2008), Real Oviedo 2003/04,Granada CF (2002/03), SD Compostela (2002/03, 2003/04), CP Merida (2000) was reconstructed as Merida UD (still operating), Real Burgos CF (folded in 1983 but was replaced by its reserve team; now operating under the name Burgos Club de Fútbol), CD Logrones (2000, 2004 and folded in 2009, but reconstructed as SD Logrones).

[vi] Today the Spanish first tier consists of 20 teams.

[vii] One can also point to the bailouts of the Finnish and Swedish banking system in the early 1990s (Kornai et al., 2003, p. 1123).

[viii] Kornai treats the terms “support”, “rescue” and “bailout” as synonymous actions to avert financial failure (Kornai et al., 2003, p. 1097).

[ix] It should be pointed out here that one instance of bailout alone does not make the SBC phenomenon appear. According to Kornai (1979, p. 807; 1980b, p. 568; 1998, p. 14), only if successive instances of support happens - for instance, if other organizations are being bailed out in the same sector or previous examples of support exists - expectations of future bailouts or support can grow.

[x] See Hamil et al. (2010, pp. 360-361) for a similar argument.

[xi] A similar practice is established in Spanish football (Garcia & Rodriguez, 2003, p. note 12).

[xii] This being said, it is impossible for the clubs to become cases of AHBCs should the system not be completely reformed into a copy of the profitable American franchise system of professional team sports. This, however, is not very likely to happen due to the European tradition of open leagues.