THE SPIN-OFF REPORT

February 13, 2019 11:58 AM EST

The Madison Square Garden Company (Pre-Spin)
(BUY)

Current Share Price (2/12/19): $290.39	Ticker: MSG
Fair Value Estimate: $362 per share	Dividend: Nil
Shares Outstanding: 23.8 million	Yield: N/A
Market Capitalization: $6.9 billion	

MSG Entertainment

Fair Value Estimate: $221 per share	Ticker: TBD
Shares Outstanding: 23.8 million	Dividend: Nil
Market Capitalization: $5.2 billion	Yield: N/A

MSG Sports

Fair Value Estimate: $139 per share	Ticker: TBD
Shares Outstanding*: 36.0 million	Dividend: Nil
Market Capitalization: $5.0 billion	Yield: N/A

TBD – To be determined. N/A – Not applicable.
*Based on one-for-one share distribution ratio to MSG shareholders of record, and includes MSG Entertainment retaining a 33% ownership stake in MSG Sports.
Note: Market capitalization is based on fair value estimate for post-spin entities and current market cap for pre-spin MSG.

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INVESTMENT THESIS

On June 27, 2018, after the market close, The Madison Square Garden Company (NYSE: MSG) announced that its Board of Directors had authorized the company's management to explore a possible spin-off that would create a separately traded public company comprised of its sports businesses, including the New York Knicks and New York Rangers professional sports franchises. On October 4, 2018, MSG issued a press release announcing that the company had confidentially filed an initial Form 10 registration statement with the SEC related to the sports business spin-off.

It should be noted that the proposed transaction follows the company's spin-off of its sports broadcasting businesses into MSG Networks (NYSE: MSGN) in September 2015. Preceding the announcement of the current sports businesses spin-off, activist investor Silver Lake filed a 13-D with the SEC indicating that the company had built a 6.3% ownership stake. Silver Lake has subsequently increased its position to 9.7% of Class A shares.

If the company proceeds with the spin-off of its sports businesses, it would be structured as a tax-free transaction to all MSG shareholders. Upon completion of the contemplated separation, shareholders of record of MSG common stock would receive a pro rata distribution, expected to be equivalent, in aggregate, to an approximate two-thirds economic interest in the pure-play sports company. The remaining common stock, expected to be equivalent to an approximate one-third economic interest in the sports company, would be retained by the entertainment company. These shares are expected to be used to raise capital and/or be exchanged for the common stock of the entertainment company. James L. Dolan is expected to be the Executive Chairman and Chief Executive Officer of both companies.

One company would be a leader in live entertainment, with a growing portfolio of assets, including state-of-the-art music and entertainment-focused venues, MSG Productions, other strategic entertainment joint ventures, approximately one-third interest in the post-spin sports company, and approximately $1 billion in cash. The live entertainment company will also continue to move forward with the development of MSG Sphere. The first MSG Sphere is expected to open in Las Vegas around the end of calendar 2020, followed by a second MSG Sphere in London approximately one year later.

In terms of rationale, the separation of Sports from Entertainment makes sense as the Entertainment company looks to expand its portfolio of owned venues to drive earnings growth. The posited structure of the separation, with Entertainment retaining a 33% stake in Sports and approximately $1 billion in cash, will allow the company to largely finance its ambitious Spheres project without having to tap the debt markets or dilute Entertainment shareholders. The Entertainment business will be a hybrid of an asset-based stock (derived from the ownership of venues) and operating assets consisting primarily of a growing events promotion business that leverages the prime assets of the company (e.g. Madison Square Garden and the planned Spheres) and majority interest in the TAO Group.

The Sports business will be driven by the value of the NY Knicks and NY Rangers NBA and NHL franchises. Historical increases in the value of professional sports teams, and comparable sales transactions should provide a stable, yet growing, asset-based valuation at MSG Sports. Further, if the Dolan family were to sell an ownership interest in either of the sports franchises (or potentially take one or both teams private), significant upside optionality would arise, given the "whisper numbers" that have been reported on team valuations.

On a pre-spin sum-of-the-parts basis, shares of MSG are fairly valued at $362 per share. With our fair value estimate approximating 25% upside potential from the current share price, shares of MSG are recommended for purchase prior to the spin-off. The fair value consists of $151 per share in value assigned to post-spin MSG Entertainment and $211 per share derived from post-spin MSG Sports. The post-spin fair value estimates are subject to change. It should be noted that in more bullish scenarios additional value could be realized. This could include valuing the air rights above MSG, which could be worth $25 per share alone, or monetizing the Knicks and/or Rangers. Although the latter is highly subjective, if the Dolan "whisper number" for the Knicks is used, this would add $1 billion in fair value to the pre-spin sum-of-the-parts assuming the Rangers were valued at just the adjusted Forbes estimate, which excludes any value associated with the arena. That said, the typical rebuttal on the valuation of a sports franchise is that it is only worth what someone will pay, and that is dependent on the current owners' willingness to sell. In the absence of two willing parties, the sports franchises will likely be valued at a reasonable valuation approximating the Forbes value.

COMPANY DESCRIPTION

The Madison Square Garden Co. (NYSE: MSG) was first publicly traded in 2010 following its spin-off from Cablevision Systems Corp. (previously traded on the NYSE under the symbol "CVC"; was acquired by Altice NV in 2016). MSG controls various sports and entertainment franchises, including the National Basketball Association's (NBA) New York Knicks and the National Hockey League's (NHL) New York Rangers franchises. In addition, the company produces and promotes various live events, including the *Radio City Christmas Spectacular* starring the Rockettes. MSG owns or operates a number of entertainment venues, including Madison Square Garden Arena (The Garden), the Hulu Theater at Madison Square Garden, Radio City Music Hall, The Beacon Theatre (New York City), The Chicago Theatre, the Wang Theatre (Boston), and the Forum (Inglewood, California).

CVC came into being in the 1960s, when founder Charles Dolan began building cable systems in Manhattan and launched the cable channel HBO, both of which were eventually sold to Time Life Inc. Dolan funneled the proceeds from the sale into new cable systems in Long Island under the Cablevision brand name. Through a series of transactions, CVC expanded its cable systems across the country and began investing in other assets.

The majority of MSG's operating assets and franchises were initially acquired in 1994, when Viacom (NASDAQ: VIA, VIAB) sold its interest in the Knicks, Rangers, and related assets to a partnership between CVC and ITT Corp. for $1 billion. VIA itself had acquired the properties earlier in 1994 via the acquisition of Paramount Communications, and decided to sell The Garden, Knicks, and Rangers in order to pay down debt associated with the purchase. In 1997 CVC bought out ITT's 50% ownership in the partnership for $650 million.

James Dolan, the current Chairman and CEO of MSG, is the son of Cablevision founder Charles Dolan. MSG has a dual class structure. Class B shares carry 10 votes per share and elect 75% of the Board of Directors. Class A shares have one vote per share and elect the remaining 25%. Class B shares do not trade; as of September 30, 2018, they are 100% owned by the Dolan Family Group, which also owns 2.9% of Class A shares.

In F2018 (June 30 year-end), MSG generated $1.6 billion in revenue and $193.8 million in earnings before income taxes, depreciation, and amortization (see Exhibit 1). The company operates under two reportable segments: MSG Sports, which controls the sports teams; and MSG Entertainment, which promotes live entertainment in MSG-owned/leased venues. Depreciation on owned venues (The Garden, the Hulu Theater at Madison Square Garden, and the Forum) is reported under "Corporate & Other."

Exhibit 1 The Madison Square Garden Company: Historical Operating Results
($ in millions; fiscal years ending June 30)

	F2015	F2016	F2017	F2018	1H F2018	1H F2019
MSG Entertainment						
Revenue	$ 414.2	$ 415.4	$ 506.5	$ 780.7	$ 435.5	$ 479.5
Adjusted Operating Income	41.2	(14.6)	22.0	117.0	100.5	110.0
Depreciation and Amortization	10.3	9.9	11.3	18.5	8.5	8.3
Capital Expenditures	(5.7)	(5.0)	(11.5)	(24.4)	(11.1)	(14.3)
MSG Sports						
Revenue	$ 656.7	$ 699.1	$ 812.0	$ 778.7	$ 346.0	$ 371.2
Adjusted Operating Income	98.0	131.0	143.0	149.5	82.1	49.2
Depreciation and Amortization	19.1	11.0	9.3	7.5	3.8	3.9
Capital Expenditures	(4.5)	(4.6)	(2.4)	(4.6)	(1.6)	(2.1)
Corporate & Other						
Revenue	$ 0.7	$ 0.9	$ -	$ (0.3)	$ -	$ -
Adjusted Operating Income	(20.5)	(48.1)	(67.3)	(72.8)	(33.5)	(38.6)
Depreciation and Amortization	79.3	81.6	83.6	78.4	39.9	38.2
Capital Expenditures	(53.9)	(62.2)	(30.4)	(163.0)	(115.0)	(64.6)

Source: Bloomberg and company reports.

MSG Entertainment

MSG Entertainment presents and hosts concerts, family shows, and special events at MSG-owned or long-term leased venues, including The Garden (owned), the Hulu Theater at Madison Square Garden (owned), Radio City Music Hall (lease expires in 2023), The Beacon Theatre (lease expires in 2026), The Chicago Theatre (owned), and the Forum (owned). The company also has a booking agreement with the Wang Theatre in Boston. In addition, the company produces a limited number of shows, such as the *Radio City Christmas Spectacular*. Of note, while MSG owns The Garden arena, the platform that The Garden is built on, as well as the transferable development rights (air rights) above it, the company does not own the ground underneath the arena and in fact operates under a NYC permit. In 2013, the operating permit for The Garden was extended for 10 years.

The company completed a $1 billion renovation at The Garden in late 2013 and reopened the Forum in January 2014, after acquiring the latter property in 2012 and investing an estimated $100 million (in addition to the $24 million purchase price) to renovate the arena. The "Transformation" (as the company refers to it) at The Garden took three years to complete, with work done mostly during the summer months to avoid disruption to the NY Knicks and NY Rangers seasons, and it should allow The Garden to better compete for entertainment events with newer stadiums such as the Barclays Center in Brooklyn, NY. Enhancements include improved amenities and luxury suites. Similarly, renovations at the Forum have allowed the venue to take market share of concerts in the Los Angeles area away from newer venues such as the STAPLES Center (according to Pollstar data).

In July 2016, MSG Entertainment acquired a controlling interest in Boston Calling Events (BCE), which operates the Boston Calling Music Festival, a three-day indie and pop rock music event that began in 2013. The festival was most recently held on May 25-27, 2018, in Harvard University's athletic complex; the line-up included acts such as Eminem, The Killers, Queens of The Stone Age, and Tyler, the Creator. While the financial terms of MSG's purchase of BCE were not provided by management, other than to say that it was at an "attractive" valuation, MSG filings indicate that BCE contributed $13.7 million in revenue in F2018.

In January 2017, the company acquired 62.5% of TAO Group, which generated pro forma revenue of $235 million and adjusted operating income (AOI) of $43 million in calendar 2016, for $181 million (plus potential earn-outs of $25.5 million over five years). Including debt and a small preferred equity component, the deal valued TAO at ~$400 million, implying a ~9x AOI purchase multiple. TAO operates dining and nightlife venues in New York City, Las Vegas, and Sydney, Australia, under well-known brands including TAO, Marquee, Lavo, Avenue, The Stanton Social, Beauty & Essex, and VANDAL. As part of MSG, TAO Group's operating results, which are primarily comprised of food and beverage sales, are recorded on a three-month lag basis. TAO's founders retain a 37.5% stake and continue to manage the operations under five-year employment agreements (which include global non-compete clauses). MSG is eager to expand the TAO footprint, with contracts to open five new venues in New York City and eight additional locations in new markets, including Los Angeles, Chicago, and Singapore.

Revenue is generated from licensing venues to third-party promoters and, to a lesser degree, from promoting, co-promoting, and/or producing shows at MSG venues. The company does not promote shows at venues not owned, leased, or under long-term booking contracts. Ancillary revenues are generated from facility and ticketing fees, concessions, sponsorship, and a portion of merchandising. Expenses consist of performers' salaries and costs to set up, promote, stage, and put on performances.

The Entertainment business generated $781 million in revenue and adjusted operating income of $117 million in F2018 (see Exhibit 2). Revenue increased 54% in F2018, which was a direct result of the inclusion of revenues from the TAO Group ($209 million), partially offset by a decrease in revenue ($11 million), as the New York Spectacular did not take place (the project was short lived and was cancelled). Through 1Q F2019, revenue in prior years includes the TAO impact; revenue in 1Q F2019 was virtually flat versus the prior year, with fewer live events held at MSG's venues and slight accounting rule changes offsetting higher per-event revenue in the previous year.

Exhibit 2 The Madison Square Garden Company: MSG Entertainment Segment Historical Operating Results
($ in thousands; fiscal years end June 30)

	F2016	F2017	F2018	1Q F2018	1Q F2019
Revenue	415,390	506,468	780,726	164,281	162,953
Direct Operating Expenses	341,637	378,325	483,263	105,564	107,785
SG&A	96,204	120,496	192,929	44,391	48,969
Depreciation and Amortization	9,884	11,339	18,515	4,161	4,482
Operating Income	(32,335)	(3,692)	86,019	10,165	1,717
Reconciliation to Adjusted Operating Income					
Share-based Compensation	7,870	14,323	12,500	3,901	2,841
Depreciation and Amortization	9,884	11,339	18,515	4,161	4,482
Adjusted Operating Income	(14,581)	21,970	117,034	18,227	9,040

Source: Company reports.

MSG Sports

The MSG Sports segment owns and operates various sports franchises, and promotes, produces and/or presents other live sporting-related events. Owned franchises include the New York Knicks (NBA), New York Rangers (NHL), Westchester Knicks (NBA Development League), and the Hartford Wolf Pack (American Hockey League). Other live sporting events include the presentation of professional boxing, college basketball, professional bull riding (PBR), and e-sports, among others.

Franchise sports teams are subject to numerous limitations enforced by the respective leagues. The most notable are collective bargaining agreements (CBAs), particularly with respect to salary cap restrictions and organized labor of players. The NBA imposes a "soft salary cap," whereby the cap on any given team's total player salaries can be exceeded, but the team then has to pay a multiple of the excess over the cap (in a tiered rate structure) as a so-called luxury tax. The Knicks historically were a luxury tax payer, with expenses totaling $8.3 million, $38.1 million, and $5.1 million in the 2012-2013, 2013-2014, and 2014-2015 seasons, respectively. However, the Knicks did not pay a luxury tax in the 2015-2016, 2016-2017, and 2017-2018 seasons; in those years, the Knicks recorded proceeds of $2.5 million, $500,000, and $2.2 million, respectively, from luxury-tax-paying teams. The NHL imposes a "hard salary cap," whereby a team's total player salaries are not allowed to exceed a pre-defined amount based on league-wide revenue, and thus the NHL does not impose a luxury tax. Both the NHL and NBA have revenue-sharing programs whereby a pool of funds from teams with above-average net revenue is distributed to teams generating below-average net revenue.

The NBA's current CBA expires after the 2023-2024 season, with an option (for either the NBA or the NBA Players Association) to terminate following the 2022-2023 season. The NHL's CBA expires in September 2022, with an option for the league or Players' Association to terminate the agreement following the 2019-2020 season.

Failure to negotiate CBAs has caused issues in the recent past. In 2012, following the expiration of the NHL's CBA at the time, the NHL declared a player lockout, causing a delayed start to the 2012-2013 season. The 2012-2013 NHL season was shortened by 41% to just 48 games (versus 82 in a full regular season), while the 2004-2005 season was completely cancelled due to labor difficulties. The NBA was disrupted in the 2011-2012 season, which was shortened to 66 games, and the 1998-1999 season had only 50 games due to a player lockout. The NBA regular season is typically 82 games.

Revenue is generated primarily from ticket sales and license fees for suites at The Garden, proportionate shares of NHL and NBA television contracts and revenue sources, venue signage, and sponsorship, concessions, and merchandise sales. In addition, MSG Sports sells the telecast rights for the owned team's home and away games. The largest Sports expenses are player and team personnel salaries, league operating expenses, revenue sharing, and the luxury tax.

In F2018, MSG Sports generated $779 million in revenue and adjusted operating income of $150 million (see Exhibit 3). Through 1Q F2019, revenue decreased by nearly 32%, while adjusted operating income totaled $588,000 (see Exhibit 3). F2018's revenue decline of 4% versus the year prior was primarily attributed to the NY Rangers missing the playoffs, resulting in six fewer post-season home games, an NHL expansion fee, and a decrease in non-recurring league distributions from the NHL. Despite the F2018 revenue decline, adjusted operating income benefited from lower SG&A expense, which was due to lower employee compensation due to a severance cost that occurred in F2017. It should be noted that the change in the revenue recognition rule primarily relates to suite license fees and network TV deals, with revenue now being recorded based on events occurring, versus the previous straight-line recognition over the course of the fiscal year. This change will likely result in more lumpy revenue quarter to quarter based on sports and other event schedules. Management did comment that it expects revenue recognition to increase in 2Q F2019, likely based on the number of events scheduled versus 1Q F2019. Prior-year periods have not been adjusted to reflect the accounting change.

Exhibit 3 The Madison Square Garden Company: MSG Sports Segment Historical Operating Results
($ in thousands)

	F2016	F2017	F2018	1Q F2018	1Q F2019
Revenue	699,062	811,984	778,653	80,934	55,352
Direct Operating Expenses	396,220	473,590	457,694	16,728	15,319
SG&A	182,131	209,941	186,914	41,976	42,217
Depreciation and Amortization	10,957	9,319	7,481	1,906	1,942
Operating Income	109,754	119,134	126,564	20,324	(4,126)
Reconciliation to Adjusted Operating Income					
Share-based Compensation	10,316	14,548	15,498	4,236	2,772
Depreciation and Amortization	10,957	9,319	7,481	1,906	1,942
Adjusted Operating Income	131,027	143,001	149,543	26,466	588

Source: Company reports.

While e-sports is not a current earnings contributor, a potential earnings stream arises from the rapid growth of the business. MSG acquired Counter Logic Gaming ("CLG") in November 2017. CLG is an American e-sports team organization that fields premier video game players for CLG's teams. Teams compete in a number of popular video games, including League of Legends, Fortnite, and Smash Brothers, among others. With e-sports rapidly changing to more closely resemble traditional sports, with leagues and teams, MSG's acquisition looks to position the company to capitalize on the hugely popular and growing business of e-sports. While it is difficult to value CLG, a notable data point for game manufacturers has been the sale of franchises, which in turn have received sizeable valuations from bankers. According to Forbes, Riot Games (the developer of League of Legends) sold franchises for $10 million each in the summer of 2017; Activision Blizzard sold Overwatch League franchises for similar amounts. Depending on city, country, and the likely success of the franchises, valuations have reached as high as $80 million. It is estimated that global e-sports revenue could grow from a current estimate of $906 million to $1.65 billion in 2021. Sponsorship, advertising, and media rights all present a burgeoning opportunity akin to the early days of monetizing traditional sports franchises.

MSG Sphere

In April 2018, MSG held an event at the Los Angeles Forum where James Dolan unveiled plans to create a new concept for multimedia entertainment venues, dubbed the MSG Sphere. The Sphere, which promises a "new way to tell stories," will include innovative audio and visual capabilities to entertain guests within a 350-foot round dome that is 100% covered in wraparound LED screens with resolution 100 times today's HD TV technology. Additionally, the outside of the Sphere will be able to display visual images ranging from artwork to the actual performances occurring within. Sound capabilities include what is being described as targetable audio, where each attendee receives customized sound, with features including being able to broadcast in different languages to people standing next to each other without the use of headphones and with no sound bleeding between the two guests. Technologies used in construction and operation of the Sphere are being internally developed, acquired, and licensed, with few details divulged at this point. In November 2017, MSG announced that it had purchased Obscura Digital, a creative studio that was responsible for digital content used in the company's Christmas Spectacular show. It appears that Obscura's technologies will be heavily used in the LED video panels that will cover both the inside and outside of the Sphere.

While the company has not put a price tag on Sphere construction, it has been estimated in the media that each Sphere would cost $1 billion to fully construct. Currently, MSG is in the process (albeit in early stages) of constructing two Spheres: one in Las Vegas, where ground was broken in summer 2018 with an expected opening date of New Year's Eve 2020; and one to be built in London, which is currently posited to be open a year after the Las Vegas Sphere.

Separation of Entertainment and Sports Businesses

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Upon separation, MSG Entertainment is slated to include:

- World-class venues: New York's Madison Square Garden, the Hulu Theater at Madison Square Garden, Radio City Music Hall, and Beacon Theatre; the Forum in Inglewood, CA; The Chicago Theatre; and the Wang Theatre in Boston;
- MSG's bookings business, which fills MSG's venues with a wide variety of the most popular entertainment events. This business would also include the company's bookings of live sporting events such as college basketball and professional boxing, the results of which are currently reported as part of the company's MSG Sports segment;
- Productions, which includes the Radio City Rockettes and the Christmas Spectacular, the nation's number-one live family holiday show;
- Majority interests in TAO Group, a world-class hospitality group, and Boston Calling Events, producer of New England's Boston Calling Music Festival, a preeminent live music event;
- Strategic entertainment joint ventures—e.g., Tribeca Enterprises;
- An approximately one-third economic interest in the pure-play sports company; and
- Approximately $1 billion in cash on hand.

Notably, prior MSG Entertainment segment reporting (see Exhibit 2) does not include the "bookings" business related to sporting events, and little disclosure has been provided on the actual revenue and profit contribution of that business. Commentary surrounding the "bookings" business suggests that it had a highly successful F2018, which "delivered yet another year of increased venue utilization with a record-setting number of events … [with] double-digit increases in both multi-market and multi-night engagements." Additionally, the depreciation charges that are associated with the owned arenas (The Garden, the Hulu Theater, and the Forum) are not included in the Entertainment segment's results, and are instead embedded within results for the corporate segment.

The pure-play sports company would include:

- The New York Knicks professional NBA franchise and its development team, the Westchester Knicks;
- The New York Rangers professional NHL franchise and its development team, the Hartford Wolf Pack;
- Knicks Gaming, the official NBA 2K e-sports franchise of the New York Knicks, and a majority interest in Counter Logic Gaming, a leading North American e-sports organization; and
- A professional sports team training center in Greenburgh, NY.

Outlook

ENTERTAINMENT

Following the separation, the Entertainment business's valuation will largely be derived from the underlying value of the physical assets (venues), and to a lesser (yet not insignificant) degree from the value of earnings generated from the bookings business, TAO Group, and BCE, among other promotional businesses. Earnings growth will be a function of the number of events held at MSG venues, revenue per event, and the number of venues. It is assumed that utilization of the venues is fairly high (1Q F2019 saw a decline in utilization), so that earnings impact becomes a function of cost control, increased fees, or venue expansion. It has been noted that multi-night and multi-city engagements (for example, Phish's "residency" at The Garden for 13 nights in the summer of 2017) generate higher margins, as costs are leveraged over the multiple nights. It is unreasonable to expect consistent similar long-run engagements, which suggests that increased fees are currently the key revenue growth component. Management has commented that the live touring business has never been stronger, mostly as a factor of acts (bands, comics, etc.) being financially motivated to do so, implying that there could be room for increased revenue per event. However, that will eventually receive pushback, necessitating new venues to promote. MSG Sphere appears to be management's solution to this, albeit at what in all likelihood will be a hefty, as yet unquantified price tag.

It should be noted that it is assumed that the air rights associated with the MSG arena will remain with the entertainment company. While there is no exact information on number of square feet and the ultimate value of those air rights, those questions have been a constant subject of discussion among investors. Interestingly, on MSG's May 2018 conference call, the possibility of combining those air rights with Vornado Realty Trust's (NYSE: VNO) development rights to redevelop 2 Penn Plaza in New York City was brought up. Anecdotally, an investment thesis on VNO has focused on Vornado's potential redevelopment of the area around Madison Square Garden, which would lend credence to an opportunity for MSG Entertainment to raise liquidity for the Sphere project.

Funding for the Spheres will be available from the expected $1 billion cash position and the one-third of MSG Sports that will be retained by the company. It can be noted that there is minor debt (~$105 million) associated with the TAO Group. Management has commented that the timing and method of disposition of the MSG Sports shares has yet to be determined; however, a sale or exchange for shares of MSG Entertainment are distinct possibilities. The final method of share disposal will depend on the respective valuations of MSG Sports and MSG Entertainment, which could present an opportunity to raise capital without tapping the debt markets. The company currently has two untapped revolvers that are tied to the sports teams—$150 million for the Rangers and $215 million for the Knicks.

SPORTS

Clearly, annual operating results at the Sports segment can be lumpy, depending on a wide range of factors, including team performance and player compensation. Reflecting that, we think the estimated values of MSG's two core sports franchises, namely the New York Knicks basketball team and the New York Rangers hockey team, are the more relevant metrics for investors to consider with respect to the segment's potential valuation. On that front, Forbes magazine publishes an annual list of sports team valuations; the most recent list estimates the value of the Knicks and Rangers at $4.0 billion and $1.55 billion, respectively, based on four key factors, including the franchise's value attributable to revenue-sharing agreements, city/market size, the franchise's arena, and its brand (see Exhibit 4). For context, these estimates suggest the Knicks and the Rangers are the most valuable franchises in their respective sports (ahead of the Los Angeles Lakers, valued at $3.7 billion, and the Toronto Maple Leafs at $1.45 billion, also shown in Exhibit 4).

Exhibit 4 MSG Sports: Valuation Breakdown of NY Knicks and NY Rangers
($ in millions)

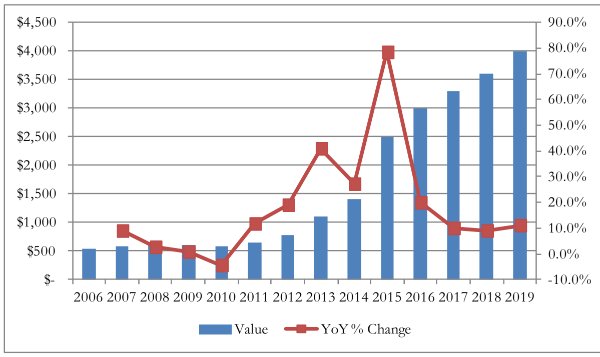
	Knicks	Lakers	Rangers	Leafs
Sport	$ 611	$ 587	$ 148	$ 151
Market	1,831	1,866	668	672
Arena	995	573	518	411
Brand	563	674	215	216
Total	**$ 4,000**	**$ 3,700**	**$ 1,549**	**$ 1,450**
Revenue	$ 443	$ 395	$ 253	$ 232
Multiple	**9.0x**	**9.4x**	**6.1x**	**6.3x**
EBITDA	$ 155	$ 147	$ 107	$ 94
Multiple	**25.8x**	**25.2x**	**14.5x**	**15.4x**

Source: Forbes.

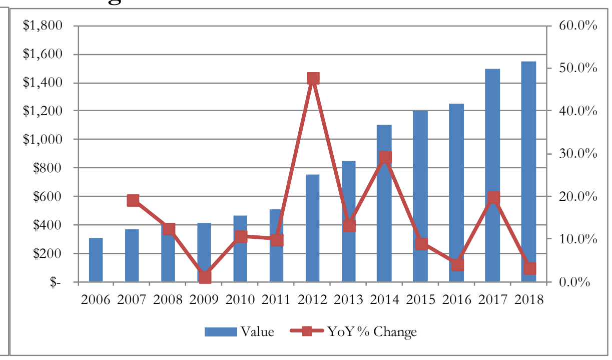
Notably, the value of both franchises, as estimated by Forbes, has steadily increased in recent years; in fact, since 2006, the estimated value of the Knicks and Rangers has grown at a compound annual rate of ~17% and 14%, respectively (see Exhibit 5). In our view, this has been driven not only by high-profile deals at higher than expected valuations but also by more sophisticated pricing strategies (for tickets, luxury suites, and sponsorships) and increasingly lucrative national and local TV contracts. On the latter, the NBA's television deal with Walt Disney Co. (NYSE: DIS) and Turner, which extends through 2024, saw its annual receipts jump to $2.7 billion (from $930 million) in its most recent renewal. Similarly, when the NHL renegotiated its deal with NBC in 2011, annual payments to the league jumped to $200 million (from $77.5 million), and we see the opportunity for a similar increase when that agreement expires in 2020, tangentially increasing payments to the Rangers.

Exhibit 5 The Madison Square Garden Company: Historical Estimated Value of NY Knicks and NY Rangers
($ in millions)

NY Knicks



NY Rangers



Source: Forbes.

Even as valuations have steadily risen in recent years, the vast majority of recent comparable transactions have been consummated at a significant premium to their most recent Forbes valuation. In the past seven years, those premiums have been 42% for professional basketball teams and 35% for professional hockey teams (see Exhibit 6). In our view, this phenomenon speaks to the scarcity value of what are undoubtedly considered trophy assets. Indeed, since 2004, the number of global billionaires has grown, according to Forbes, to 2,754 (from 587), and during that time the overall number of NBA and NHL teams has remained stagnant. Amid this ongoing global concentration of wealth (and increased focus on broadening the appeal of U.S. sports worldwide), sports assets have seen an increased influx of foreign investment. As an example, in 2016, Jiang Lizhang, a Chinese real estate investor, purchased 5% of the Minnesota Timberwolves from owner Glen Taylor at a reported valuation of about $1 billion, which was ~30% higher than the team's most recent Forbes valuation. As well, on October 27, 2017, it was reported that Brooklyn Nets owner Mikhail Prokhorov reached a deal to sell a 49% stake in the team to Joseph Tsai, the co-founder of Chinese-based Alibaba (NYSE: BABA), at a reported valuation of $2.35 billion (or almost 30% above Forbes' 2017 valuation of $1.8 billion). (Notably, the deal is said not to include ownership of the Barclays Center, the arena in which the Nets play; however, it does include an option to buy a controlling interest in the team within three years.) Underlying the growing number of potential purchasers for a limited number of sports properties, we would also highlight that U.S. sports teams possess advantageous tax attributes that allow ~90% of the team's purchase price to be allocated toward intangible assets, which can then be amortized against the owner's total income.

All things considered, we would not be surprised to see incremental upward revisions to the franchise values of both the Knicks and the Rangers when the next Forbes valuation lists are released in February 2020 and November 2019, respectively, which could serve as ancillary upside catalysts for the shares of MSG.

Exhibit 6 The Madison Square Garden Company: Recent Transactions Compared to Most Recent Appraisal Value
($ in millions)

Team	Date	Sale price (millions)	Forbes' estimated value	Premium/ Discount
Brooklyn Nets (49% stake)	Oct-17	$2,300	$1,800	27.8%
Houston Rockets	Sep-17	$2,200	$1,650	33.3%
Minnesota Timberwolves (5% stake)	Jun-16	$1,000	$770	29.9%
Atlanta Hawks	Apr-15	$730	$425	71.8%
Milwaukee Bucks	Apr-14	$550	$405	35.8%
Los Angeles Clippers	Aug-14	$2,000	$575	247.8%
Sacramento Kings	May-13	$534	$300	78.0%
New Orleans Hornets	Apr-12	$338	$285	18.6%
Memphis Grizzlies	Jun-12	$377	$263	43.3%
Detroit Pistons	Apr-11	$325	$360	-9.7%
Washington Wizards	Apr-10	$550	$313	75.7%
Golden State Warriors	Jul-10	$450	$315	42.9%
Average premium				*57.9%*
Avg. premium, ex-Clippers				***41.7%***

Team	Date	Sale price (millions)	Forbes' estimated value	Premium /Discount
Phoenix Coyotes	Dec-14	$305	$200	52.5%
New Jersey Devils	Aug-13	$320	$205	56.1%
St. Louis Blues	May-12	$180	$157	14.6%
Toronto Maple Leafs	Dec-11	$1,000	$521	91.9%
Dallas Stars	Nov-11	$240	$227	5.7%
Atlanta Thrashers	May-11	$170	$135	25.9%
Buffalo Sabres	Feb-11	$165	$169	-2.4%
Average premium				***34.9%***

Source: Company reports, Bloomberg, and Institutional Research Group estimates.

While less quantifiable to the value of a sports franchise, it would be remiss not to mention that the legalization of sports gambling in states outside of Nevada has garnered a great deal of interest. Seven states currently allow sports betting, two states have partial laws in place pending further action, and 15 states have filed bills for the current legislative session to legalize sports gambling. While the ultimate impact on the value of a franchise from legalized gambling is unclear, and is most certainly not a doubling in value as Dallas Mavericks owner Mark Cuban has suggested, increased revenue from gambling-related advertisers has already been commented on by MSG management. Additionally, the ability to further engage team fans either in the arena or offsite appears to be attractive from a monetization standpoint, while acknowledging that the ultimate form of monetization has yet to be fully fleshed out.

VALUATION ANALYSIS

The following valuation analysis has been derived without a public Form-10 filing covering the financials of the MSG Sports standalone company. Given the lack of transaction details typically provided within the SEC filings, the analysis assumes: (i) no additional debt is to be raised prior to the separation, with the majority of the current cash balance remaining with MSG Entertainment; (ii) shares of MSG Sports are distributed on a one-for-one basis to MSG shareholders; and (iii) MSG Entertainment retains a 33% ownership stake in MSG Sports, resulting in MSG Sports shares outstanding of 36 million. Management's latest commentary suggests that the company is still working out details on a long-term venue license agreement between The Garden and the Knicks and Rangers. The fair value estimates derived below are subject to revision based on finalization of intercompany agreements, finalized capital structures, and capital allocation policies.

MSG Sports

The value of MSG Sports will be primarily based on the valuation assigned to the New York Knicks and New York Rangers. The most easily accessible and widely used benchmark for valuing sports franchises is the annual publication of values in Forbes magazine. In the 2019 publication, the Knicks were valued at $4.0 billion, while the Rangers were valued at $1.55 billion in the most recent NHL valuations. As noted earlier, a component of that valuation includes what Forbes refers to as "value attributable to its arena." While Forbes does not provide specifics on what exactly that arena value is derived from, it does not appear to be from the ownership of the arena, as other franchise teams that do not own their stadiums also appear to have a piece of their valuation tied to their arenas. In the spirit of conservatism, and given the view that if the MSG's sports franchises were to be located in a different arena, this value attribute would certainly change and most likely decline, we view it as appropriate to adjust the valuations for the arena component. Forbes assigns $995 million and $518 million to the arena for the Knicks and the Rangers, respectively, resulting in an adjusted valuation for the Knicks and Rangers that total $4.0 billion, or $112 per share based on assumed 36.0 million shares outstanding (see Exhibit 7).

A valuation of MSG Sports would be incomplete if future growth in value were not considered. The Knicks have grown on average at 18.2% annually since 2016, representing a 16.6% CAGR. Included in the averages are the 78.6% and 41.0% increases in value in 2013 and 2015, with 2017 through 2019 increases of 10.0%, 9.1%, and 11.1% (excluding the two large outliers, the annual average increase in value drops to 10.5%). The Rangers' valuation increased, on average, approximately 15% over the same time period, with a 2018 increase of 3.3%. Assuming growth of 10% and 5% for the Knicks and Rangers, respectively, which approximates the most recent reported values growth, the sports teams together would be valued at $4.4 billion, or $122 per share based on assumed 36.0 million shares outstanding (see Exhibit 7).

While James Dolan, MSG's Chairman (whose family controls 71% of the voting shares through the ownership of all the Class B shares), has not expressly indicated a desire to monetize the company's sports assets, we think his public comments suggest a belief that sports team revenue, generally, will decline as MVPD (multichannel video programming distributor) bundles continue to unwind. In addition, Mr. Dolan has shown a willingness to monetize assets, as demonstrated by the sale of Cablevision to Altice in 2015 and prior news reports suggesting that MSG Networks (NYSE: MSGN) has been exploring a potential sale. (Notably, Mr. Dolan's concerns regarding the impact of bundling seemingly reflect a long-term horizon, as MSG's current national cable deals with the NBA and NHL do not expire until 2025 and 2021, respectively, and include annual escalators. As well, MSG's local rights deal does not expire until 2035 and also includes annual escalators.) Assigning historical acquisition premiums of 30% and 25% to the Knicks and Rangers, respectively, would result in a $5.7 billion valuation, or $157 per share based on assumed 36.0 million shares outstanding (see Exhibit 7).

While the path to a sale of one (or both) of MSG's sports teams is unclear in the near term, the potential for a minority investment from a foreign partner as a way for MSG Sports to unlock value as well as continue to broaden its appeal abroad could be an ancillary possibility. As recently as December 2018, following an ESPN profile on James Dolan, it was reported that parties interested in purchasing the Knicks had sent out "feelers" in the range of $5 billion. In the same article, Dolan was quoted as saying that there were no bona fide offers and that the Dolan family ownership does not want to sell the Knicks and Rangers, yet he has a fiduciary duty to his shareholders. While reports are unclear as to whether the $5 billion figure included The Garden (differing reports have unclear and divergent phrasing, we assume it did not), if the $5 billion was for the Knicks alone, it would equate to a $139 per share valuation for MSG Sports based on assumed 36.0 million shares outstanding, and imply zero valuation for the Rangers in our fair value estimate. Notably, the Rangers at the latest Forbes valuation (with no adjustments) would add $43 per share in value to MSG Sports based on assumed 36.0 million shares outstanding. Anecdotally, James Dolan commented that feelers are "…like a stock price. It's only important if you're going to buy or sell."

Exhibit 7 MSG Sports: Fair Value Estimate of Sports Franchises Based on Adjusted Forbes Valuation, Growth, and Acquisition Premium

($ in millions, except per share amounts; shares in millions)

	2018/ 2019	Arena Value	Adj. Value	Annual Growth	2019/ 2020	Premium	Bull Case	"Whisper Number"
New York Knicks, ex-arena	$ 4,000	$ 995	$ 3,005	10.0%	$ 3,305.5	30.0%	$ 4,297	$ 5,000
New York Rangers, ex arena	1,549	518	1,031	5.0%	1,083	25.0%	1,353	*N/A*
Total Value	$ 5,549	$ 1,513	$ 4,036	*8.7%*	$ 4,388	*28.8%*	$ 5,650	$ 5,000
Shares Outstanding	36.0							
Value per Share	**$ 154.15**		**$ 112.12**		**$ 121.90**		**$ 156.96**	**$ 138.90**

N/A: Not applicable. Source: Company reports, Forbes, and *The Spin-Off Report* estimates.

It should be noted that our fair value estimate of $139 per share for MSG Sports (based on the average of "2019" valuation and "bull case" scenarios) does not include any value for the various other businesses included in the standalone company. These include the company's e-sports teams (MSG acquired Counter Logic Gaming Inc in 2017 for an undisclosed sum), a professional e-sports team, and a training facility in Greenburgh, NY. Optionality from these businesses appears minimal in the near future; however, over the longer term they could prove valuable, although how valuable is not quantifiable to any reasonable degree at this point in time.

MSG Entertainment

Following the separation of MSG Sports, MSG Entertainment will have three main assets driving its valuation: (i) the owned entertainment venues; (ii) the operating businesses, which include owned productions such as the Christmas Spectacular and Boston Calling, majority ownership in TAO Group; and (iii) an approximate $1 billion in cash and $106 million in debt associated with TAO.

Given that the sports bookings business that will be included in MSG Entertainment, which handles live sporting events such as college basketball and professional boxing in MSG venues, is currently included in MSG's Sports segment, the following analysis, based on earnings of the operating businesses, is inherently conservative, in that it will underestimate the true earnings power of the bookings business overall. MSG has made a confidential Form-10 filing; when the filing is made available to the general public, we expect further details on the business, and at that point in time we will adjust our earnings estimates as needed.

The Entertainment business presents or hosts live events, such as concerts, shows, and other events, at its portfolio of owned and leased venues. MSG Entertainment primarily licenses its venues to third-party promoters for a fee (but in some cases takes on the economic risk of promotion). As well, the company collects facility and ticketing fees and generates revenue from concessions, sponsorships, and merchandise. Considering the lumpiness of MSG's concert/venue management business and its dependence on relationships with landlords, we think the company's owned real estate portfolio could be viewed as the Entertainment segment's most relevant source of value. Among its real estate assets, Madison Square Garden, located between 31st and 33rd Streets and 7th and 8th Avenues in Midtown Manhattan, has been dubbed "The World's Most Famous Arena." The complex, which includes both The Garden and the Hulu Theatre, was appraised at $1.2 billion by the New York City Independent Budget Office in a May 2014 tax assessment.

(Note: This analysis does not include any value for the so-called air rights, which are also known as development rights and refer to the transferable allowances of potentially buildable space, most commonly applying to the space above a building that could be used for additional construction. While MSG management implicitly concedes that its air rights have substantial value, it is quite cagey about the potential timing and magnitude of any monetization; thus, we exclude air rights from our valuation but urge investors to be cognizant of their potential as a valuable source of upside optionality. For context, we have seen estimates suggesting MSG could have 2.4-5.4 million square feet of potential development rights, and we note that, according to Tenantwise, air rights averaged $292 per square foot in 2016—with values in prime locations, such as the High Line, Hudson Yards, and Times Square, in the $400-$800 per square foot range. Notably, real estate website cityrealty.com states that the Department of City Planning has said that Manhattan air rights average $225 per square foot, but did not give a date for the data. This suggests to us that even at a conservative $250 per square foot, MSG's air rights alone could be valued at more than $600 million, or ~$25 per share.)

In 2008, MSG acquired The Chicago Theatre, with the iconic six-story CHICAGO marquee, for an undisclosed sum. The venue was previously purchased in 2004 by TheatreDreams Chicago LLC for $3 million, which for simplicity's sake is the value we assign, despite our contention that the replacement value is far higher. The Forum, which is in Inglewood, CA, and was the former home of the Los Angeles Lakers (NBA) and the Los Angeles Kings (NHL), was purchased by MSG in 2012 for $23.5 million. Subsequently, the company spent ~$100 million to renovate the venue into a world-class concert destination. We think MSG's investment could be used as a suitable baseline for valuation, which, again, is likely conservative relative to its replacement value, considering its proximity to the planned $2.6

billion Los Angeles Rams sports complex and reports that the T-Mobile Arena, a 20,000-seat venue in Las Vegas, cost ~$375 million to construct.

All told, our base-case valuation for MSG's owned real estate is $1.3 billion, or $56 per share. If one were to take a more bullish stance by applying some modicum of value to the potential air rights above Madison Square Garden as well as 25% premiums to the base-case values of the Forum and The Chicago Theatre, value of almost $2 billion, or $82 per share, could be derived (see Exhibit 8).

Exhibit 8 MSG Entertainment: Estimated Valuation of Owned Venues

($ in millions, except per share amounts; shares in millions)

Venues	
Madison Square Garden	$ 1,200.0
The Forum	123.5
The Chicago Theatre	3.0
Total	1,326.5
Shares Outstanding	23.8
FVE $ / Share	**$ 55.83**

Source: Company reports, Bloomberg, and *The Spin-Off Report* estimates.

Regarding MSG's other Entertainment assets, with stable attendance, high profitability, and minimal re-investment requirements, we view the Christmas Spectacular as a highly valuable asset for MSG. We note, however, that there is no direct comparison for valuation. Similarly, the investment made in TAO Group appears to be profitable and growing, at least in terms of the number of venues that the company is opening and operating, although management has noted that recent results have not met their financial expectations. In F2018, the MSG Entertainment segment generated revenue and EBITDA of $780.7 million and $117.0 million, respectively, representing a 15.0% margin. Through 1H F2019, the segment has increased revenue by 10% (primarily from higher event-related revenues) and operated with a 23.0% EBITDA margin. For context, the segment generated a 23.1% EBITDA margin in 1H F2018. Given this year's revenue trends, and an assumption of moderating top-line growth to 5% in F2020, it could be forecast that a standalone MSG Entertainment would generate $902 million in revenue in F2020. Assuming margin contraction in the back half of the year, similar to F2018, and accounting for estimated standalone corporate costs, we forecast that MSG Entertainment could earn $126 million in EBITDA. Applying a 9x multiple, in line with the price paid for the TAO Group ownership stake, MSG Entertainment's operating businesses would be valued at $1.1 billion, or $48 per share (see Exhibit 9). It should be noted that the margin contraction modeled for F2020 implies that approximately $30 million in corporate costs is assigned to the standalone entertainment company.

Exhibit 9 MSG Entertainment: Estimated Valuation of Operating Entertainment Assets

($ in millions, except per share amounts; shares in millions)

F2018 Revenue	$ 780.7
Growth	10.0%
F2019E Revenue	858.8
Growth	5.0%
F2020E Revenue	901.7
EBITDA Margin	14.0%
EBITDA	126.2
Multiple	9.0x
Total	1,136.2
Shares Outstanding	23.8
FVE $ / Share	**$ 47.82**

Source: Company reports, Bloomberg, and *The Spin-Off Report* estimates.

Based on the above valuation exercises for a standalone MSG Entertainment, and including roughly $1.1 billion in net cash and a 33% ownership stake in MSG Sports, we estimate that MSG Entertainment would be fairly valued at $5.2 billion, or $221 per share (see Exhibit 10).

Exhibit 10 MSG Entertainment: Post-Spin Sum-of-the-Parts Fair Value Estimate

($ in millions, except per share amounts; shares in millions)

Venues	$ 1,326.5
Entertainment Operating Businesses	1,136.2
Net Cash (Debt)	1,125.0
Sub Total	3,587.6
33% Ownership of MSG Sports	1,656.3
Market Capitalization	5,244.0
Shares Outstanding	23.8
FVE $ / Share	**$ 220.72**

Source: Company reports, Bloomberg, and *The Spin-Off Report* estimates.

The Madison Square Garden Company: Pre-Spin Sum-of-the-Parts

On a pre-spin sum-of-the-parts basis, shares of MSG are fairly valued at $362 per share (see Exhibit 11). With our fair value estimate approximating 25% upside potential from the current share price, shares of MSG are recommended for purchase prior to the spin-off. The fair value consists of $151 in value assigned to post-spin MSG Entertainment and $211 per share derived from post-spin MSG Sports. The post-spin fair value estimates are subject to change. It should be noted that in more bullish scenarios additional value could be realized. This could include valuing the air rights above MSG, which could be worth $25 per share alone, or monetizing the Knicks and/or Rangers. Although the latter is highly subjective, if the Dolan "whisper number" for the Knicks is used, this would add $1 billion in fair value to the pre-spin sum-of-the-parts assuming the Rangers were valued at just the adjusted Forbes estimate, which excludes any value associated with the arena. That said, the typical rebuttal on the valuation of a sports franchise is that it is only worth what someone will pay, and that is dependent on the current owners' willingness to sell. In the absence of two willing parties, the sports franchises will likely be valued at a reasonable valuation approximating the Forbes value.

Exhibit 11 The Madison Square Garden Company: Pre-Spin Sum-of-the-Parts Fair Value Estimate

($ in millions, except per share data; shares in millions)

MSG Entertainment (ex 33% stake in Sports)	$ 3,587.6
MSG Sports	5,019.2
Total	8,606.8
Shares Outstanding	23.8
FVE $ / Share	**$ 362.26**
Current MSG Share Price	$ 290.39
Implied Upside	***24.8%***

Source: Company reports, Bloomberg, and *The Spin-Off Report* estimates.

CONCLUSION

In terms of rationale, the separation of Sports from Entertainment makes sense as the Entertainment company looks to expand its portfolio of owned venues to drive earnings growth. The posited structure of the separation, with Entertainment retaining a 33% stake in Sports and approximately $1 billion in cash, will allow the company to largely finance its ambitious Spheres project without having to tap the debt markets or dilute Entertainment shareholders. The Entertainment business will be a hybrid of an asset based stock (derived from the ownership of venues) and operating assets consisting primarily of a growing events promotion business that leverages the prime assets of the company (Madison Square Garden).

The Sports business will value will be driven by the value of the NY Knicks and NY Rangers NBA and NHL franchises. Historical increases in value of professional sports teams, and comparable sales transactions should provide for a stable yet growing asset based valuation at MSG Sports. Further, if the Dolan family were to sell an ownership interest in either of the sports franchises (or potentially take one or both teams private), significant upside optionality would arise given the "whisper numbers" that have been reported on team valuations.

On a pre-spin sum-of-the-parts basis, shares of MSG are fairly valued at $362 per share. With our fair value estimate approximating 25% upside potential from the current share price, shares of MSG are recommended for purchase prior to the spin-off. The fair value consists of $151 in value assigned to post-spin MSG Entertainment and $211 per share derived from post-spin MSG Sports. The post-spin fair value estimates are subject to change. It should be noted that in more bullish scenarios additional value could be realized. This could include valuing the air rights above MSG, which could be worth $25 per share alone, or monetizing the Knicks and/or Rangers. Although the latter is highly subjective, if the Dolan "whisper number" for the Knicks is used, this would add $1 billion in fair value to the pre-spin sum-of-the-parts assuming the Rangers were valued at just the adjusted Forbes estimate, which excludes any value associated with the arena. That said, the typical rebuttal on the valuation of a sports franchise is that it is only worth what someone will pay, and that is dependent on the current owners' willingness to sell. In the absence of two willing parties, the sports franchises will likely be valued at a reasonable valuation approximating the Forbes value.