

NIKE'S BIG RISK

Star endorsement costs rising to \$1.63B

By HILARY KRAMER

Nike's stock has been on the run lately, but the brand that made the Swoosh synonymous with star athletes may be taking investors' money for a whirl.

LeBron, Tiger, Serena, Lance, Michael, Mia — they're so big that last names are simply unnecessary.

Nike athletes are everywhere, covering a multitude of sports, from traditional to now even extreme ones.

And the company leaves nothing to chance, employing every form of media and using every opportunity to let you know that these stars wear Nike.

In fact, Nike practically invented the modern concept of marketing athlete endorsers, thanks in no small part to basketball legend Michael Jordan.

But even as Nike boasts to the public the number and caliber of its athletes, the company seems oddly vague about its long-term financial commitments to them.

The actual annual cash payments for endorsement contracts appear to be factored into Nike's creatively titled "demand-creation expense."

The long-term implications of these contracts, however, are even more complicated to figure out.

In November 2002, FASB issued interpretation No. 45: "guarantor's accounting and disclosure requirements for guarantees, including indirect guarantees of indebtedness of others."

That's "accountantese" for saying that, in this case, Nike has to recognize and disclose the fair value of the endorsements it issues.

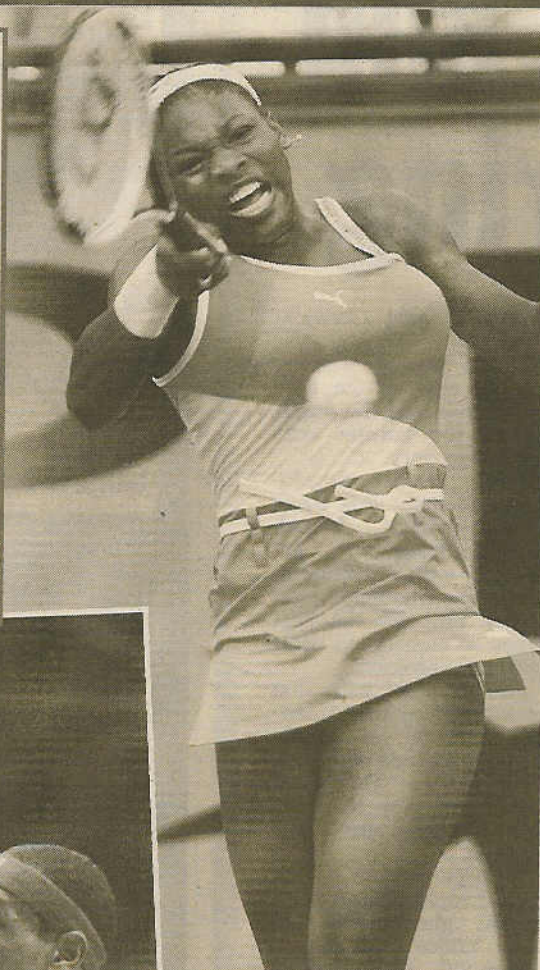
But Nike won't break down all of its endorsement commitments as

Is it the cash?

Nike has been on a roll lately, but investors are starting to worry about whether the \$1.6 billion it's paying for star athletes' endorsements will become a drag on its results. Nike's collection and how much they cost:

■ **Serena Williams \$40M**

■ **LeBron James \$90M**



Photos: AP; Reuters

Cash payments due on endorsement contracts: *

2004	\$197.2M
2005	\$323.6M
2006	\$275.8M
2007	\$266M
2008	\$166.1M
Thereafter	\$405.7M
TOTAL	\$1.6B

* Approximate amounts, but actual payments will likely be higher due to bonuses; SEC filings, Jan. 12, 2004

cash reserves and an 18 percent growth in net income for the recent quarter.

Still, this success has apparently emboldened the company to commit to new endorsements at a stunning rate and then defer most of the payments until after 2008 when it's unclear what the company and the world's economic environment will look like.

Nike's \$1.63 billion in total endorsement commitments is up \$192 million, or 13 percent, in just six months since Nike's May 31 fiscal year-end.

Just for perspective, Nike's entire property, plant and equipment value is around that amount (\$1.61 billion), as are its total inventories (\$1.9 billion).

Noted Sal Galatioto, Lehman Brothers managing director of its sports advisory group, "Some of the contracts can be lowered if an athlete can't perform, but there is still residual economic risk to the company."

Nike's current endorsement commitments are even on top of the 32-percent rise in endorsement commitments for Nike's full 2003 fiscal year.

The further out its endorsement contracts extend, the greater the risk that the money won't be well spent.

Added Galatioto, "It's difficult to predict the performance of an athlete over time and so there's inherent risk for the company giving the endorsement contract — a lot of risk."

With all the recent accounting problems surrounding risky off-balance sheet items, companies have an obligation to improve their corporate governance by increasing the transparency of their accounting. Nike, too, should just do it.

line items, so it's difficult to know which commitments are included and to what extent its accountants are booking

the full commitment amounts.

What is known, however, is that the amount that has been revealed is

already large enough to be significant.

To be sure, Nike is currently a healthy company with nearly \$1 billion in