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WHITE PAPER SERIES:

ESPORTS

The Big Business of Competitive Gaming

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INDUSTRY OVERVIEW

ESPN President John Skipper once declared competitive gaming as “not a real sport,” but it has evolved into a \$892 million juggernaut. Projected to be worth \$1.1 billion by 2018, according to estimates by SuperData and Newzoo, the esports industry is one that has captivated a rapidly growing global audience of almost 300 million people.

Broadly defined, esports describes competitive gaming, with the professional designation of the sport involving full-time, pro players rather than part-time amateurs. Much like in traditional sports, fans value skill of the players first and foremost and loathe seeing results influenced by outside factors (like the AI) rather than the talent and performance of the players.¹

The first esports event is widely considered to be the 1997 Red Annihilation tournament, with the winner taking home a new Ferrari.



Dennis “Thresh” Fong sits in the Ferrari 328GTS convertible he won in the Red Annihilation Quake Tournament at the 1997 Electronic Entertainment Expo (E3). Photo Credit: Dennis Fong

The first professional gaming league was also founded in 1997, when

entrepreneur Angel Munoz founded the Cyberathlete Professional League. It was not until 1999, however, after the Asian financial crisis, that esports began to take off. The South Korean government invested heavily in improving their broadband and telecommunications capacity to stimulate their economy. With improved Internet connectivity, online gaming took off in South Korea and spread to the rest of the world.² The early 2000s brought about additional professional esports organizations, such as the Electronic Sports World Cup in 2000 and Major League Gaming in 2002.³



Major League Gaming (MLG) hosts the Counter-Strike: Global Offensive Major Championship in Columbus, Ohio. Photo Credit: Wikipedia

Since then, the esports industry has continued to boom, prize pools have exploded from around \$300,000, to over \$67 million, with some players in the industry both domestically and internationally making well over \$1 million a year⁴, while the number of tournaments has grown from ten to over 4,000.⁵ This impressive growth shows very few signs of slowing down.

¹ SBNation
² Ibid
³ Adanai

⁴ eSports Earning
⁵ eSports Earning



GAMES & PUBLISHERS

The most popular games in the industry fall into the categories of Multi-Online Battle Arena (MOBA), Real Time Strategy (RTS), First Person Shooters (FPS), and Fighter. MOBA, the most popular of the gaming genres, describes a game in which each player controls a character on a team and works with teammates to destroy the opposing team's base, usually played in a 5v5 or 3v3 battle. Notable games in the category include League of Legends (LoL) and Defense of the Ancients 2 (DOTA 2). FPS, the next-most popular genre, includes games such as Call of Duty and Halo. FPS games simulate a firefight from the first-player perspective and can be played in both single and multiplayer mode. RTS games, the third-most popular genre including titles like Starcraft and Warcraft, involve a team building armies and buildings to overpower their opponent and destroy their assets. Rounding out the major four genres is fighter games, featuring classics like Street Fighter and the Super Smash Brothers. Fighter games are usually one-on-one close range battles, with each

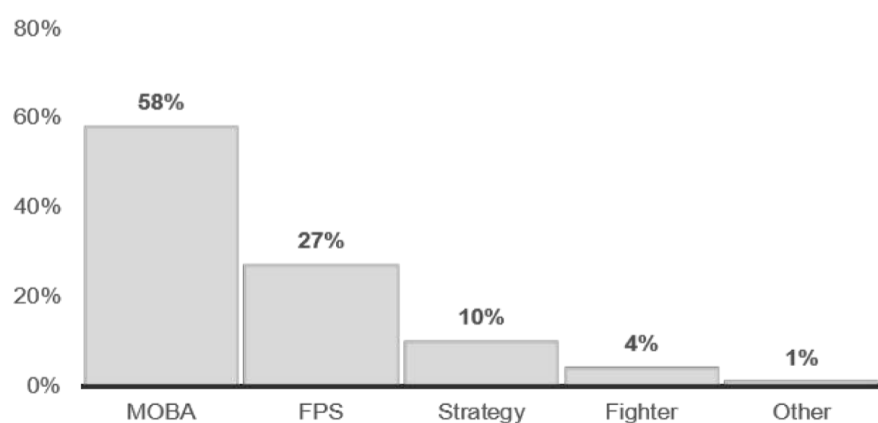


Exhibit 1: Distribution of time spent watching sports on Twitch in 2nd half of 2015, by genre

player striving to defeat their opponent in a short, winner-take-all format. These four genres accounted for 99% of all hours of content watched on the streaming service Twitch in the 2nd half of 2015.⁶ With the spiking demand for esports contests, tournaments awarded over \$66 million in prize money in 2015.

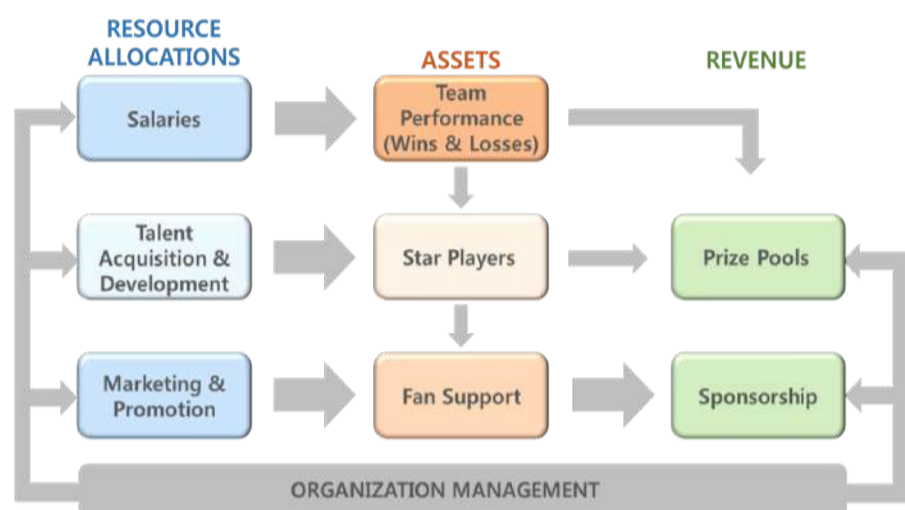


Exhibit 2: Financial Structures of esports Organizations

PROFESSIONAL TEAMS & LEAGUES

Professional esports teams make the vast majority of their money through sponsorships and prize pools, seeing less revenue from ticket sales, media rights, and other streams commonly realized by traditional sports teams.⁷ The top teams can generate over \$1 million a year in shirt sponsorships and several thousand dollars per month for directed social media posts and content.⁸ Prize pools are highly lucrative as well, with several tournaments offering north of \$1 million in prizes. The tournament with the largest prize pool, The International, offers nearly \$20 million in prizes, with over \$6 million going to the winner.

⁶ Exhibit 1: Statista
⁷ eSports Group
⁸ Mashable



PROFESSIONAL TEAMS & LEAGUES (CONTINUED)

To put that in context, the winner's share is larger than that of Wimbledon, The Masters, and the Kentucky Derby combined.⁹ In total, the top-earning team in terms of prize money, the Evil Geniuses, earned \$9 million in prizes in 2015. While publicly available and reliable data on esports team sponsorship revenue is scarce, esportsentrepreneur.com estimates that the five biggest teams in the esport industry are worth an average of \$30.4 million based on website viewership, stream impressions, social media following, sponsorships, merchandise product mix, and tournament winnings.¹⁰



Customized player chairs for the 2012 Premiere Hearthstone Summer Playoffs. Photo credit: Sammy Lam

Teams play in a number of leagues and tournaments across a variety of games, the most common being LoL, DOTA 2, and Counter Strike: Global Offensive (CS: GO). Some of the largest leagues and tournaments include the LoL League Championship Series (multiple locations), the International Extreme Masters (Poland), ESL One (CS: GO and DOTA 2—France), The International

(USA), and the esports Championship Series (CS: GO—England). All these competitions have multimillion dollar prize pools and attract tens of millions of viewers.¹¹



First place trophy at the 2012 Premiere Hearthstone Summer Playoffs, a UK based esports competition. Photo Credit: Connor Beattie

Sponsors are attracted to the esports industry due to its ability to captivate male millennials, who are otherwise difficult to reach through traditional marketing channels. Contrary to stereotypes, esports fans are often quite successful professionally and financially. As such, many large multi-billion dollar multinational corporations are currently esports sponsors, such as Coca-Cola, Red Bull, Microsoft, Sony, and several others.¹²

⁹ Euro Gamer
¹⁰ Lazy Gamer

¹¹ eSports Marketing

¹² Smart Launch

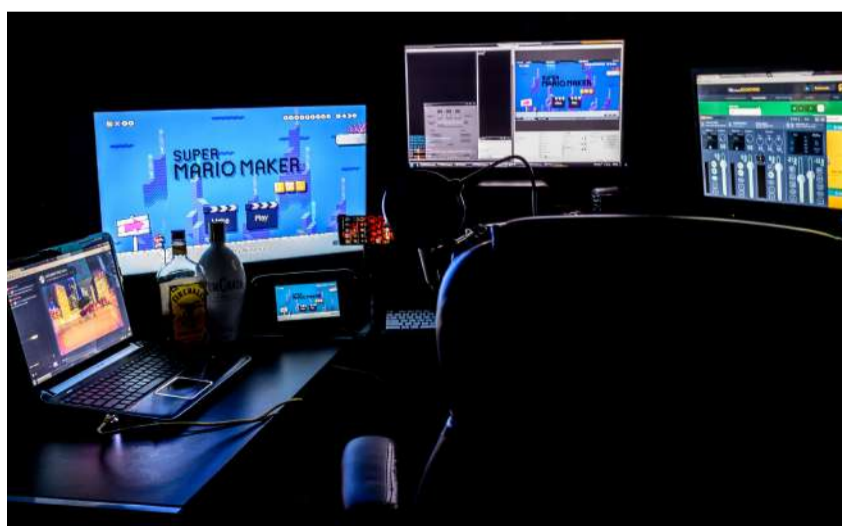


PROFESSIONAL TEAMS & LEAGUES (CONTINUED)

Numerous smaller brands such as MeUndies have entered the picture as well in an effort to grow their brand through exposure to a large and captive audience with the financial resources to spend on their products. As sponsorship values increase, prize pools grow, and growing speculation toward eventual monetization of media rights like most traditional sports, many investors are jumping at the chance to enter the esports industry in the short term with a view toward higher long-term return on investment.

STREAMING & MEDIA RIGHTS

The vast majority of esports content is consumed through streaming services. Roughly 70% of esports fans stream content through mobile apps, the most common being YouTube Gaming, which is used by 40% of U.S. fans.¹³ However, Twitch, which was recently acquired by Amazon in 2014 for \$1 billion, is largely considered to be the most prominent and popular name in the esports streaming industry.



A gamer's home set-up to stream his gameplay of Super Mario Maker for the Nintendo Wii U on his Twitch account.
Photo credit: Compfight

Beyond the two market leaders, who account for nearly 60% of all viewers, there is a crowded market with services such as MLG.tv, Instant esports, theScore, and over a dozen others competing for the remaining market share. These companies are able to earn revenue through advertisements, sponsorships, subscriptions, and donations.

Fan who use mobile apps to watch eSports (US)

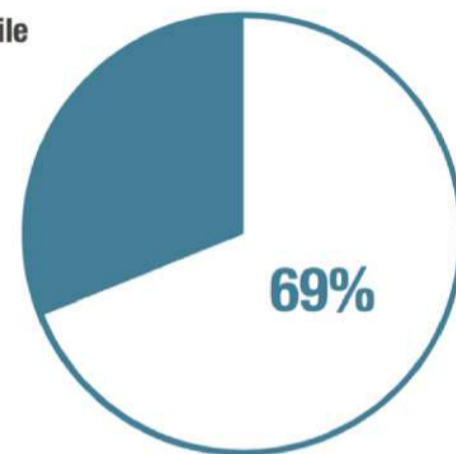


Exhibit 3.1: Fans who use mobile apps to watch esports. (US)

So far, traditional media companies have had little impact on the esports industry.¹⁴ Both Turner and ESPN have begun covering esports and streaming certain events such as the CS: GO Open Watch Tournament, 2016 Madden Championship, and the Street Fighter EVO Championships. As the industry grew on digital platforms with an audience that fled from traditional TV outlets, broadcasters have shown some trepidation that rights deals won't translate to high viewership or command high advertising prices. However, TV sports broadcasters have shown growing interest in the space. optimism for the industry's entry into additional media channels.¹⁵ This is especially appealing for esports league

¹³ Mashable
¹⁴ Euro Gamer

¹⁵ Lazy Gamer



STREAMING AND MEDIA RIGHTS (CONTINUED)

and team owners and investors as they look to traditional professional sports leagues that have generated a large percentage of their revenue through lucrative media rights contracts in recent years with the hope of replicating that within esports. The transition of esports to traditional media broadcast platforms is still in its infant stages; however, this progression will be one of the foremost drivers of the industry moving forward, with its impact felt at every level. It was recently announced that Major League Baseball's video streaming and technology services company BAMTech, partially owned by Disney, will pay Riot Games a minimum of \$300 million through 2023 for the streaming rights for League of Legends.¹⁶

via advertising sales and sponsorship deals. According to Trey Duffy, CEO of WOMP, an esports micro tournament platform, many esports teams and organizations will benefit with revenue sharing proceeds of up to 60% of the advertising revenues generated through these particular broadcasting deals.



A camera prepares to stream commentators discussing the Riot 2016 Season Championship Series of Europe's professional League of Legends league held in the Netherlands. Photo credit: Riot Esports

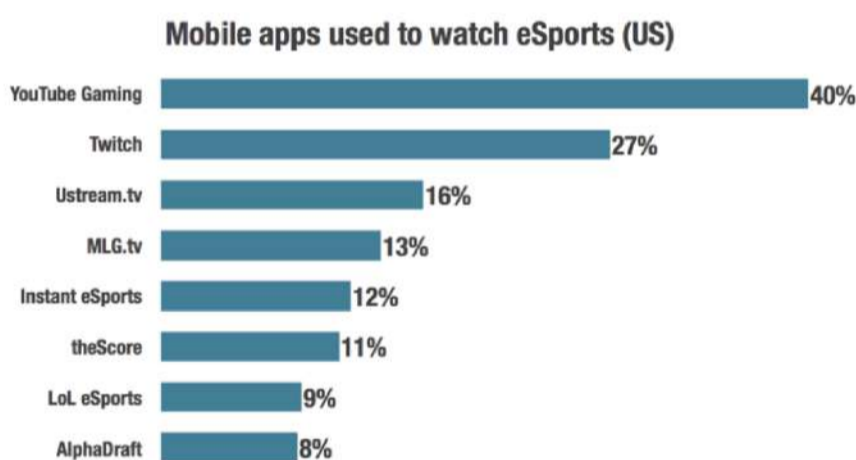


Exhibit 3.2: Mobile apps used to watch esports (US)

In 2017, the streaming application dedicated to League of Legends will be launched and available for both PC and smartphone users. As referenced in the exclusive rights contract, BAMTech is expected to monetize the platform

GAMBLING AND ANCILLARY BUSINESSES

Over the past several years, online gambling has taken off, offering new opportunities for those who want to get in on the esports action. There are two core verticals of third party esports gambling: cash gambling and skin gambling. Cash gambling involves betting on esports matches through third parties, broadly echoing the ways that millions of people bet on traditional sports. Within cash gambling are two primary product offerings: esportsbook betting and fantasy esports.

¹⁶ ESPN



GAMBLING AND ANCILLARY BUSINESSES (CONTINUED)

Esportsbook betting offers sports gamblers match bets, competitive outcome bets, in-play bets, and exotic wagers like parlays a mix of established online sportsbooks such as Pinnacle and Sportradar have added esports to their product mix, as have new operators focusing exclusively on esports. With Valve's crackdown on skin betting, this will likely increase the pace and scale of real money wagering for cash betting sites like Unikrn and Betway. Esportsbook betting is expected to see a major influx of customers, resulting in possibly the largest upside in the medium term of any esports wagering product. Overall, it is estimated that by the end of 2016, the esportsbook betting vertical will handle a total of \$550 million in betting and will continue to its trajectory into the future.¹⁷



Gamers compete on-stage at the Electronic Sports World Cup Pro Gaming Circuit at the 2013 Paris Games Week. Photo credit: James Cao

Fantasy esports took off in 2015 amid the wave of interest and enthusiasm around daily fantasy sports. However, as

many sites have been drawn into the larger legal and legislative issues surrounding daily fantasy sports leaders FanDuel and DraftKings, this trend has seen some market correction. In January 2016, one of the key players in fantasy esports, Vulcun, which raised \$12 million the prior year from marquee investors such as Sequoia, stopped accepting real-money fantasy wagers on esports events due to regulatory concerns. In July 2016, the company ended its skin/non-cash fantasy esports operations entirely amid the increasingly hostile legal environment.¹⁸



The International 2016 (TI6), an annually hosted Dota 2 esports championship, drew a live audience of thousands and over a million viewers worldwide. Photo Credit: Dota 2

Ultimately, whatever happens to daily fantasy sports betting will likely trickle down to fantasy esports. If more states challenge the legality of daily fantasy sports betting or pass bills increasing cost on fantasy esports operators, this category could face trouble ahead.

Skin gambling on the other hand generally doesn't involve any cash component. Instead, players compete—often with internal currencies—to win and bet skins, virtual bonus items and features that enhance gameplay.

¹⁷ [LinkedIn](#)
¹⁸ [Calvin Ayre](#)



GAMBLING AND ANCILLARY BUSINESSES (CONTINUED)

In today's world of esports betting, game developers allow skins to be exchanged only for game credit—not cash—but players sometimes go to secondary markets to convert those credits to cash. Over the past several years, the reason for the growth in the skin betting vertical is that skins are initially free. Players can unlock the skins through gameplay and receive \$100 in skins—which can be used later for gambling—in return for signing up and playing. This strategy has enabled the market growth within skin gambling.



Competitor gameplay is projected onto the big screen at the 2013 S3 World Championship Semi-Finals. Photo credit: Riot esports

Recently, many esports gambling sites have shifted their focus to online cash tournaments to stir up more traction and revenue. Unikrn, an esports betting company, introduced a new product this year called Connekt allowing players to earn Unikoins (virtual currency) simply for playing the games they already play, a similar platform to companies such as WOMP. With



A referee regulates fair gameplay at the 2013 S3 World Championship Semi-Finals at the ESL Arena in Cologne, Germany. Photo credit: Riot esports

viewership figures for esports significantly outnumbered by the volume of players, the core reason for esports betting companies to diversify into gameplay rewards is simple: gamers want to play games, not just watch them.

With 59% of fans tracking players or team statistics and half of them using stats to make fantasy wagering decisions, esports gambling will be an interesting segment to track going forward.¹⁹ Furthermore, third party betting, while a lightning rod for controversy and debate, should remain a major driver of viewership and fan engagement.

As esports increases its reach into new sub verticals, more consumers can enter the game in more ways. For example, esports requires the use of specialized equipment (just as in traditional sports), creating tremendous opportunities for manufacturers of

¹⁹ Super Data Research



GAMBLING AND ANCILLARY BUSINESSES (CONTINUED)

controllers, headsets, and other gaming agencies, training, and opportunities in virtual reality. With esports now obtaining approval from the Nevada Gaming Policy Committee to accept bets in Las Vegas, this opens the doors for other states as well as native gambling groups to eventually regulate esports as a wagering tool in their respective casinos.²⁰ Additionally, since few companies have the necessary understanding to take advantage of available esports sponsorship opportunities, industry veterans and consultants will look to monetize their expertise in one of the global economy's hottest industries. Finally, with companies launching new software and live training, esports players can improve their skills through targeted drill work and coaching through training platforms.²¹



Dota 2 team Alliance at Dreamhack in Jönköping, Sweden, Summer 2015

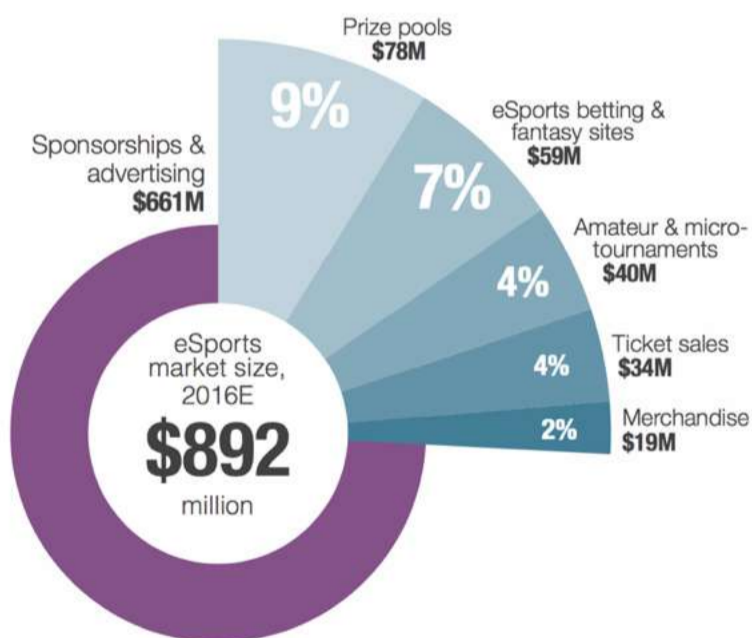


Exhibit 4: How Much Revenue Does Esports Generate

²⁰ Esports Betting Report
²¹ Super Data Research



ANALYSIS

So far, no mobile title has established itself as a clear frontrunner, as prize pools are dwarfed by those in PC games. Vainglory, the world's leading mobile esports title, is a multiplayer online battle arena (MOBA) title akin to League of Legends and Dota 2. Due to the increased demand, this past summer, Vainglory has begun offering six-figure prize pools for their World Championship.²² This gives room for several games to compete to establish themselves as a market leader and take advantage of the lucrative revenue potential in this relatively young segment of the industry. Mobile games to date have faced little in terms of regulatory headwinds, a key



A consumer tests a Virtual Reality (VR) headset at CES 2017, an technology and electronics trade show held in Las Vegas, Nevada. Photo credit: Compfight

differentiator from several other esports categories. Mobile games are already making headlines with massive exits. Tencent bought Swedish mobile game company, Supercell, the producer of Clash of Clans and Clash Royale, for

\$9.6 billion in 2015. This represents the largest transactions in the mobile game industry in the past two years. Opportunities in the mobile gaming industry are not limited to mobile titles, as there is room for growth in infrastructure (such as mobile-only streaming services and social media sites) and other subcategories.

Professional esports team ownership is another topic receiving increasing publicity, with public figures like Shaquille O'Neal, Alex Rodriguez, Rick Fox, and Peter Guber acquiring interests in teams. While valuations are on the rise, there are opportunities at what could end up as bargain values, evidenced by team owner Andrey Yanyuk in May of 2016 citing a cost of purchasing a team in the LoL Championship Series at \$1.5 million.²³



Team Fire wins the League of Legends All-Star Champion title at All Star Event 2015 in Los Angeles, CA. Photo credit: Riot esports

A newer trend and less occupied space within esports sees companies offering a wider range of gameplay opportunities for gamers of nearly all skill



ANALYSIS

levels who want to ladder up to professional esports. This format allows team owners to have a “first look” at player talent, while gamers can connect, socialize, and play video games on the big screen. While professional esports has achieved significant growth already, the “little leagues” and “minor leagues” of esports—which provide scouting opportunities for professional teams and larger markets for training providers—are some of the next key categories to monitor.



Dustin Beck, VP of eSports and Merchandise for Riot Games speaking about the past, present and future for League of Legends at GDC 2016



Gameplay screen for Supercell's Clash of Clans, a strategy video game. Photo credit: Compfight

The esports industry is one that is rapidly evolving, and it will be interesting to see the major developments continue. There are many industry newsletters available for interested parties as well as more and more events across the world focused on esports. As the industry continues to evolve in the upcoming years, it will be exciting to watch esports go head-to-head with traditional sports while also incorporating best practices and becoming a more formidable force in the global economy.

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ABOUT PARK LANE:

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