ARSENAL HOLDINGS PLC
Commentary on STATEMENT OF ACCOUNTS & ANNUAL REPORT 2005 / 06 by Nigel Phillips

The last ever accounts for a season at Highbury certainly provide an interesting "bridge" between life as it was at Highbury and what it may be like at the Emirates Stadium. The accounts just published cover the period up to 31st May 2006, 11 weeks before the start of the current football season.

Total revenue was broadly unchanged at £137m (£138m) with ***profit before tax*** down to £15.9m (£19.3m). Profits from ***player trading*** were £19m (£3m) without which the Club would have lost £3.1m for the year (clearly demonstrating the importance of the Patrick Vieira sale.) ***Property development*** income fell but the income from ***football related activities*** increased by almost 15% to £132m from £115m. This income principally comprised four identified revenue streams, namely:

Broadcasting	£54.9m (£48.6m in the prior year)	42% of football revenue
Match day	£44.1m (£37.4m)	33%
Commercial	£22.8m (£20.7m)	17%
Retail	£10.2m (£8.4m)	8%

The run to the final of the Champions League generated £32.6m or 24% of total football income (£20.1m or 17% in the previous season with the first knock out round defeat by Bayern Munich) This uplift effectively accounts for all the additional football revenue.

Whilst not mentioned in the annual report it is estimated that football related revenue in the current season at the "sold out" new ground could increase further to £165m with perhaps an added £10m pa thereafter as the new three year TV contract becomes effective. This compares with Manchester United's football revenue in the 2004/05 season of £166m.

However, as income has risen so have costs. ***Total operating expenses*** (costs) increased to £141m from £121m and ***exceeded*** total turnover by £4m (Last year total costs were £17m ***less*** than turnover) This however includes a non-cash cost related to amortisation of player contracts and depreciation of £18m (£17m) ***Wages*** were the principal cost component and were significantly higher at £83m (£66m) despite the average number of playing staff being reduced from 61 to 49, the lowest total since the 48 reported in 1997. Apparently, increases in "key" player contracts have been balanced by reducing the squad size. Bonus payments related to reaching Paris will have accounted for possibly £5m of this increase. The wages to football revenue ratio was a reasonable 63% (57%)

Payments to agents are not disclosed but are thought to have been £4.4m (£3.6m) during the year. Salaries for directors, principally Keith Edelman, Ken Friar and David Dein, totalled £2.4m (£1.8m), a 33% increase.

Other operating (costs) charges increased to £38m from £28m and can only be partially explained by the costs associated with the stadium relocation. It would have been useful to have had more information on other operating charges as they represent 30% of all "cash" costs.

During the year a further £117m (£98m) was invested in the new stadium. This came from new debt and cash reserves. The ***total gross debt*** at the financial year end was £272m (£200m) with ***cash balances*** falling to £35.6m (£71.6m). It is not clear if any of this balance relates to deposits taken from the Highbury Square development, monies received in advance from the Emirates and Nike commercial sponsorships or pre-sales of boxes and Club seats in the new stadium. At the end of May

2005, 12 months prior to this financial year end, the cash balance included £16.4m in deposits / instalments on boxes and Club seats at the new stadium.

Post the financial year end Arsenal put £260m of its debt onto a longer term basis by issuing “bonds” to mainly UK based institutional investors (banks, insurance and investment companies.) £210m of this is at a fixed rate of interest with final maturity in 2031. A further £50m is at a floating rate of interest (the “base rate” has been fixed) It also has a 25 year maturity and it is expected that this will be repaid from the sale proceeds of the Highbury redevelopment. The bond investors are guaranteed to receive full principal and interest by an AAA rated insurance company, Ambac Assurance UK Ltd. Arsenal pays Ambac 0.65% pa on the amount of the loans outstanding for this insurance “wrap”, in addition to the interest paid to the investors. The cost of the refinancing was £19m and comes from breaking the original interest rate swaps on the old loan (£7.8m) and the unamortized costs of raising the original debt (£11.2m) These costs will appear in the 2006/07 accounts. £23.5m was received post year end for the sale of a development property at Drayton Park.

The ***refinancing*** has extended the number of years over which the loans are repaid and has lowered the annual interest costs. This appears to have been essential as meeting the debt service requirements on the original loans would clearly have been very challenging.

Intangible fixed assets, namely the net book value of ***purchased players***, rose to £66.6m (£29m) The addition of £53m during the year, before deposals, described as an all time record high for one season, would benefit from a more detailed explanation.

The ***Highbury Square development*** (711 housing units) is well under way with Sir Robert McAlpine (the new stadium builders) once again engaged. A £125m three year loan (in addition to the £260m) has been taken out to fund these works. It is stated in the accounts that only 70 units remain unsold of those that have been released but this figure expressed as a percentage of total available units is not disclosed. The successful completion of this development, planned to be in 2010, should repay the £125m loan and one assumes the £50m floating rate element of the £260m bond.

There were no movements in the ***shareholdings*** of the principal Directors during the year, during which the share price increased by £700 to £4,900 a share with trades during early 2006 at over £5,000 a share. This implies a market capitalisation of £311m.

Summary – Goodbye Highbury, hello Emirates! The figures presented are impressive and the annual report contains its normal Arsenal “style” with warm tributes to all departing players. There are however areas which would benefit from greater clarity (other costs, agents payments, player book values etc). The Highbury Square development seems crucial to Arsenal’s short term financial future although a full Emirates, attracted by classic Wenger football (contract expiry June 2008) together with sympathetic marketing, sensible pricing and the refinanced stadium debt should provide scope for further on field investment.

As an Arsenal shareholder if you have any comments on the financial accounts please get in contact with the Arsenal Supporters’ Trust either by using the enclosed reply paid envelope or by email at info@arsenaltrust.org.

These observations and comments seek to be objective and are a personal commentary by the author and do not represent an official statement from the Arsenal Supporters Trust.