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Dover Motorsports
Ticker Symbol – DVD

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Dover Motorsports is an interesting investment opportunity. I stumbled upon it while writing a report about International Speedway Corporation. Please refer to my report on International Speedway Corporation for background on NASCAR and the racing industry.

Dover Motorsports promotes NASCAR races. It owns four motorsports tracks which include Dover International Speedway in Dover, Delaware; Gateway International Raceway near St. Louis, Missouri; Memphis Motorsports Park in Memphis (recently shut down), Tennessee; and Nashville Superspeedway near Nashville, Tennessee. It generates revenues from admissions, concessions, television media rights fees, corporate sponsorship, advertising, royalties from licenses of trademarks, track rentals, and merchandise sales.

Unlike its competitor, International Speedway Corporation, Dover Motorsports does not possess any moat that would protect it from its competitors. It is actually at a disadvantage to its competitors. Not only that, the company is run by incompetent managers who did nothing but destroyed shareholders' value over the last decade. In my book, *Why Are We So Clueless about the Stock Market?*, I stress the importance of investing in companies that possess moats and are run by good managers. Why would I want to invest in a company that lacks these two characteristics? Let me give you some background on this company before I answer this question. The company owns four tracks that are like four separate businesses. Even though the company as a whole has no moat, Dover International Speedway is extremely valuable and does possess a moat which I will describe in more detail later in this report. First, I want to discuss the performance of the current management.

Let's look at some metrics illustrated below.

	2001	2002	2003	2004	2005	2006	2007	2008
Revenues	$86,551	$93,731	$93,626	$93,617	$90,999	$91,274	$86,052	$84,279
Net earnings	$6,871	-$27,195	-$22,138	$2,440	$3,975	$35,345	$3,744	-$5,679
Shareholders' equity	$244,519	$160,533	$137,372	$138,466	$113,277	$74,260	$76,116	$67,447

Revenues remained mostly flat from 2001 to 2008. Net earnings fluctuated widely, but on average they were negative $9,166. The shareholders' equity was destroyed from $244,519 in 2001 to $67,477 in 2008. The stock price was as high as $8.95 per share on April 10, 2002. Today, it is trading at around $1.80 per share.

How did the management achieve this "fabulous" performance?

On October 3, 1996, the company was taken public by Merrill Lynch under the name Dover Downs. It only had one racetrack, Dover Downs International Speedway. However, racing contributed only 30 percent of the revenues. The other 70 percent came from gambling. In March 2002, the company spun off its gambling division as a separate company – Dower Downs Casino.

Beginning in 1998, the company acquired three Midwest racetracks: Nashville Superspeedway, Gateway International Raceway, and Memphis Motorsports Park. These tracks turned out to be financial losers. Since the company was unable to obtain another Sprint Cup race from NASCAR (which shows just how difficult it is to be awarded additional Sprint Cup races from NASCAR) for one of these facilities, it was never able to operate these facilities with profitability. You might think that the management would finally either sell these assets or shut them down to stop the bleeding, but this was not the case here. The management used the cash flow from profitable operations and kept wasting shareholders' money by keeping unprofitable operations open. As a result, the company had to make impairment charges to assets and goodwill. The list is long. Take a look.

2002 Goodwill Write down	$28,606,000
2003 Goodwill Write down	$13,362,000
2003 Asset Impairment	$2,867,000
2003 Asset Impairment	$4,309,000
2006 Asset Impairment (Gateway)	$37,357,000
2006 Asset Impairment (Memphis)	$7,882,000
2006 Asset Impairment (Nashville)	$16,170,000
2006 Goodwill Impairment (Midwest)	$2,487,000
2008 Asset Impairment (Nashville)	$3,140,000
2008 Asset Impairment (Memphis)	$2,150,000
2008 Asset Impairment (Gateway)	$7,505,000
2009 Asset Impairment (Memphis)	$7,478,000
Total	**$133,313,000**

The management wrote down over $133 million against income for its mistakes. I understand when a company has to write down one or two mistakes. Even International Speedway Corporation, a competitor, had an impairment charge in 2009. No one is perfect, and even the best managers get it wrong on some acquisitions. But to be wrong on every single one is just mind-boggling. To put this in perspective, the entire market capitalization of this company is $65 million as of the date of this report. The amount of money the management wasted was double the current sale price of the entire company.

You might think that after their failures, the management would acknowledge their mistakes. Again, this was not the case. The managers are in complete denial as demonstrated by a comment made by Denis McGlynn, the company's CEO:

"We're still a successful company here, doing very well. Only because somebody is now comparing us against Speedway Motorsports, which is a megamonolith, and ISC [International Speedway Corporation], do we get criticized. But we are still the same successful company that we were before. So life is not bad here. And we're doing fine."

Source: http://www.scenedaily.com/news/articles/sprintcupseries/Do_Dover_and_Pocono_have_a_future_in_NASCAR.html

Shareholders' Criticism

As you can probably imagine, the shareholders are not too thrilled with the management. Mario D. Cibelli, the managing member of Marathon Partners L.P., has been a major shareholder of Dover Motorsports for approximately seven years. Cibelli has run out of patience and expressed his frustration in the letters to the Dover Motorsports' board of directors. You can access these letters at www.sellthecompany.com. He is pressuring the management to sell the company or liquidate its unprofitable assets.

Cibelli owns 16.3 percent of Dover Motorsports, but controls only 1.3 percent of voting stock. Henry B. Tippie is the Chairman of the Board of Directors and controls in excess of fifty percent of the voting power. This means that he can determine the outcome of anything he wants including the election of directors or other corporate actions. His actions don't seem to illustrate that he cares much about what shareholders want. After repeated complaints from Cibelli and other shareholders, he further aggravated shareholders by eliminating the question and answer session during the company's quarterly conference calls. I guess he grew tired of listening to shareholders' complaints. What is so ironic about Tippie is that he is a CPA, so he should have no problem understanding finance and shareholders' value. The University of Iowa named its business program after him – The Henry B. Tippie College of Business.

In one of the letters, Cibelli included Tippie's comments to students at the Tippie College of Business:

"We're in much faster-moving society today. If you go back to the '30s, '40s or even the 1950s, change was fairly slow in coming. Today, change is much more rapid and you must change with the times. If you don't change, you're going to get 'left at the gate,' so to speak."

It would be nice if Tippie followed his advice with Dover Motorsports and sold the company or closed down its money-draining operations. As Cibelli said, the days of independent racetrack operators are gone. Bigger players, such as International Speedway Corporation or Speedway Motorsports, have more resources and can run individual racetracks much more efficiently than independent owners.

Why Do I Think Dover Motorsports is a Good Investment?

It is obvious that the management is terrible and we cannot count on them to create shareholders' value. Why do I think that Dover Motorsports is a good investment? Because it possesses something extremely valuable in relation to the sale price of the company.

As mentioned before, the company owns four motorsports tracks which are as follows:

Dover International Speedway in Dover, Delaware
Gateway International Raceway near St. Louis, Missouri
Memphis Motorsports Park in Memphis, Tennessee (recently shut down)
Nashville Superspeedway near Nashville, Tennessee

As of December 31, 2008, the company has the following simplified balance sheet. I am using the 2008 figures because more disclosure is provided in comparison to the latest quarter. In any event, the balance sheet is not that much different now from what it was on December 31, 2008.

ASSETS		$155,179,000	**LIABILITIES**	$87,732,000
Dover International Speedway	$69,651,000			
Gateway International Raceway	$10,000,000			
Memphis Motorsports	$10,000,000		**SHAREHOLDERS' EQUITY**	**$67,447,000**
Nashville Superspeedway	$51,500,000		Equity per Share	$1.88

When acquiring any company, you are taking possession of all the assets and liabilities and their ability to generate future income. By purchasing all of Dover Motorsports, you would be getting over $155 million worth of assets. But just as a single-family home can have an existing mortgage, Dover Motorsports comes with $87.7 million of liabilities. This means your equity would be $67.4 million. How much would you be paying for this equity? Based on the current stock price, the market capitalization is $65 million. If you bought Dover Motorsports, you would be paying $65 million and getting $67.4 million of equity. You would be paying almost exactly what the company is worth. But it gets better. In the above chart, assets are equal to over $155 million and most of that value comes from the four racetracks which are valued at $141,151,000 ($69,651,000 + $10,000,000 + $10,000,000 + $51,500,000).

The problem is that these values are not correct because they follow accounting rules under GAAP (Generally Accepted Accounting Principles) that require properties such as racetracks to be recorded at cost and not market value. You know very well that just because you paid $100,000 for your house, it doesn't mean that this is how much your house is worth today. A house purchased for $100,000 years ago could be worth $300,000 or even more today.

As I mentioned before, Gateway International Raceway, Memphis Motorsports, and Nashville Superspeedway are financial losers. They do not operate profitably and they drag down the profitability of the entire company. Maybe these three facilities are worth what the company's balance sheet indicates, but since they are losing money, I will treat them as if they were worthless.

Dover International Speedway is a diamond. As shown above, it is valued at $69,651,000. This is way too low. Based on my research, this track is worth between $200 and $300 million. I will explain my valuation analysis in the next section. If I create a scenario using these values, we arrive at the following estimate.

ASSETS		$300,000,000	**LIABILITIES**	$87,732,000
Dover International Speedway	$300,000,000			
Gateway International Raceway	$0			
Memphis Motorsports	$0		**SHAREHOLDERS' EQUITY**	**$212,268,000**
Nashville Superspeedway	$0		Equity per Share	$5.91

In this scenario, I assigned Dover International Speedway a value of $300 million and all the other tracks and assets a value of $0. After subtracting all the liabilities, we are left with shareholders' equity of over $212 million. Remember that we can purchase this company for $65 million. In other words, the shareholders' equity of $212 million is the same as equity per share of $5.91. Today, the stock can be purchased for $1.80 per share. Is this a good deal? I think it is, but let's rerun the numbers more conservatively, assuming that Dover International Speedway is only worth $200 million.

ASSETS		$200,000,000	LIABILITIES	$87,732,000
Dover International Speedway	$200,000,000			
Gateway International Raceway	$0			
Memphis Motorsports	$0		**SHAREHOLDERS' EQUITY**	**$112,268,000**
Nashville Superspeedway	$0		Equity per Share	$3.12

In this case, all the other assets were assigned a value of $0 and Dover International Speedway a value of $200 million. This translates into shareholders' equity of over $112 million or $3.12 per share.

The stock of Dover Motorsports is worth between $3.12 and $5.91 per share. If you buy it at $1.80 per share and the more conservative scenario plays out, you almost double your money, and if the less conservative scenario plays out, you may be able to more than triple your money. The downside is limited because the company's value is backed by hard assets.

Why Do I Think Dover International Speedway is So Valuable?

NASCAR sanctions different types of races but the Sprint Cup series is the major league. This is where you get to see Jeff Gordon and Dale Earnhardt, Jr., race each other. This is where all the money is made by the track owners. Racetracks without Sprint Cup races are not very profitable, if they are profitable at all. Dover Motorsports' three financial losers (Gateway International Raceway, Memphis Motorsports, and Nashville Superspeedway) are examples of tracks without Sprint Cup races.

There are a total of 38 Sprint Cup races and they are allocated in the following way:

International Speedway Corporation	21
Speedway Motorsports	12
Pocono Raceway	2
Indianapolis Motor Speedway	1
Dover Motorsports	2
Total Sprint Cup Races	**38**

Note: Dover Motorsports holds two Sprint Cup races at one facility – Dover International Speedway.

International Speedway Corporation and Speedway Motorsports control more than 86 percent of Sprint Cup races. They have been acquiring racetracks with Sprint Cup dates for years. These two companies simply dominate the industry. Because of economies of scale, they are able to operate individual racetracks much more efficiently than independent owners. For example, they can offer multi-track sponsoring agreements to major corporations. Individual track owners are at a disadvantage.

NASCAR could add more Sprint Cup races, but the organization wants to limit the supply of these races to make them more valuable. Refer to my previous report on International Speedway Corporation to fully understand the rationale behind this. The bottom line is this: there are only five Sprint Cup races left and Dover Motorsports has two. This is significant particularly because Ponoco Raceway expressed on numerous occasions that their racetrack with two Sprint Cup dates is not for sale. It is family-owned, fully paid off, and intended to be passed onto the owners' grandchildren through trusts that have already been established. Indianapolis Motor Speedway has a long tradition of racing aside from NASCAR's influence. It is highly unlikely the owners will ever sell its facility or the Sprint Cup date. So there are only two Sprint Cups that remain and they belong to Dover Motorsports. This is the last prime racing real estate available that International Speedway Corporation and Speedway Motorsports can get their hands on. There is a really good chance that the management will finally give in and sell because it does not have the luxury of being a private company such as Ponoco Raceway and because it is constantly being pressured to do the right thing for its shareholders.

According to Burton Smith, Chairman and CEO of Speedway Motorsports, Dover International Speedway is for sale. He said that he spoke with Henry B. Tippie of Dover Motorsports and it is all about the price. Tippie does not want to give it away because he knows that Dover International Speedway is the last piece of the industry's consolidation puzzle and Smith does not want to pay too much. But Smith will have to pay up if he wants it. He is a motivated buyer, and here is why.

In December 2008, Smith acquired Kentucky Speedway for an incredibly cheap price of $78 million. He said that it was the best deal he ever made. He bought it from the owners who failed to get a Sprint Cup race and therefore sold him the facility at a cheap price. His goal is to put a Sprint Cup there. Smith knows that without another Sprint Cup date, his purchase is not worth much. He also wants another race for his Las Vegas facility. The only way he can get it is through another racetrack acquisition. Since he needs two additional Sprint Cups, acquiring Dover Motorsports or Ponoco Raceway would solve his predicament. As mentioned before, Ponoco Raceway is not for sale. The current owners said that even if it was for sale, it would be sold to the France family at International Speedway Corporation and not to Smith. Just to illustrate how much he might pay for a racetrack with Sprint Cup dates, it is helpful to go back to 2007 because that's when he paid $340 million in cash for New Hampshire International Speedway which had two Sprint Cup races. This facility had 40,000 fewer seats than Dover International Speedway. This transaction is the best comparable to show what price might be appropriate for Dover International Speedway. But since we are in 2009 and the economy is not as great as it was in 2007, we might have to adjust the price downward. It is not unreasonable to think that Dover International Speedway can be sold on the low end for $200 million and on the high end for $300 million. Who knows, maybe it can even be sold for $400 million. It all depends on how badly Smith wants its two Sprint Cup dates.

But using just one comparable sale to value Dover International Speedway might not be a good idea. Let me use another comparable sale. In 2007, International Speedway Corporation paid $215 million for Chicagoland Speedway in Joliet, IL. This facility had 75,000 seats and only *one* Sprint Cup race. Dover International Speedway has 135,000 seats and *two* Sprint Cup races. This sale comparable indicates that my low end estimate, $200 million, of Dover International Speedway is probably too conservative.

Dover International Speedway is a unique one-mile track. Unlike some superspeedways, it offers fans a superior, unobstructed view of the entire track. The speedway surface is not asphalt like the surface of other Sprint Cup tracks; instead, is all concrete. The facility is known for its race called "the Monster Mile." Its mid-Atlantic geographic location is excellent because it serves Philadelphia, New York City, Baltimore and Washington, D.C. The company has had its Sprint Cup date for 40 consecutive years.

It is really hard to predict whether the management will sell the company or not. If it does sell, then the shareholders would benefit greatly from this decision. How much they would benefit depends on the sale price. Smith claims that the company is for sale depending on the price. The management stated that they don't want to sell at the bottom. Even though the company's earnings per share are negative, it is not losing money. The company is cash flow positive, but because of various impairment charges against income, it seems as if it is not profitable. However, those impairment charges are for past mistakes and they do not affect cash flow.

At the current price of $1.80 per share or market capitalization of $65 million, it would not take much for the management to cause the stock price to double from these levels even if they chose not to sell. Based on Cibelli's letters the three unprofitable tracks are losing approximately $6 million per year which means that by simply closing them down, the company could save $6 million per year. By using a multiple of 10, this amount of savings is worth $60 million which would make the company be worth twice as much as what it is selling for today. I believe that there is hope and I am saying this because the company put its Memphis facility up for sale at a price of $10 million. The deal did not close and therefore, the management recently decided to shut it down. This is the first smart move that they have made in a long time.

I think that there is a chance that the management is trying to clean up its act and increase its share price so that when they do decide to sell the company, they are in a position to ask for more money. Since the company is cash flow positive, they are not in a hurry to sell which is good and bad. The good part is that they will not be forced to sell at a cheap price. The bad part is that they might not want to sell at all. What is encouraging is that there are willing buyers for Dover International Speedway and Dover Motorsport's stock. Cibelli already owns almost 3 million shares and recently, he made an offer to buy 8 million shares for $2.35 per share. Tippie purchased $239,928 worth of Dover Motorsports' shares just in November 2009. While he didn't impress shareholders with his capital allocating skills, I think that he's got it right this time by purchasing shares of Dover Motorsports for his personal account at these levels.

Conclusion

Even thought Dover Motorsports does not possess a companywide moat, Dover International Speedway does. This facility on its own is worth more than what the entire company is selling for on the stock market. Although management is incompetent, I believe that the positives far outweigh negatives. The way I feel about this company can be best described by Warren Buffett's words of wisdom:

"I try to buy stock in businesses that are so wonderful that an idiot can run them because sooner or later, one will."

Disclosure:

I, or persons whose accounts I manage, own shares of Dover Motorsports at the time of this report. This report is not a solicitation to buy or sell securities. Neither Mariusz Skonieczny nor Classic Value Investors, LLC, is responsible for any losses resulting from purchasing shares of Dover Motorsports. You are advised to consult your financial advisor or conduct the due diligence yourself.