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# The Economics of Hosting the Olympic Games: The Miscalculation of Cost-Benefit Analyses and Why Cities Continue to Bid

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Claremont McKenna College

**The Economics of Hosting the Olympic Games: The Miscalculation of Cost-Benefit  
Analyses and Why Cities Continue to Bid**

submitted to  
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and  
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for  
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## Chapter 1: Introduction

When a city decides to take in a professional sports team, build a new stadium, or host a “mega-event”, the overall economic impact must be taken into consideration in order to deem the investment worthy. To be considered efficient, there must be enough short and long-term benefits to outweigh the massive costs. Because of this, cost-benefit analyses are at the utmost importance when a city decides to take on a large scale sporting investment.

No other sporting investment reaches the utter scale and potential impact of the Olympic Games. Since its revival in 1896, the modern Olympiad has become arguably the world’s largest and most popular sporting event with over two hundred competing nations and upwards of four billion viewers worldwide.<sup>1</sup> The massive reach and diverse audience has made the Olympics an extremely attractive investment for cities seeking to reap the perceived benefits from international exposure.

While the substantial inflow of crowds and money is hard to dispute, so are the enormous costs. Throughout the latter half of the century, commercialization has caused the price tag on the Games to reach unimaginably high levels with the most recent Summer Games costing London close to \$15 billion dollars.<sup>2</sup> Yet, cities continuously overlook the enormous costs as they hope that they will be offset by the potential benefits. The financial success of the 1984 Los Angeles Games is widely believed to

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<sup>1</sup> John Horne and Wolfram Manzenreiter, *Sports Mega-Events: Social Scientific Analyses of a Global Phenomenon* 1st ed. Norwich: Blackwell Publishing, 2006. 33.

<sup>2</sup> Bent Flyvbjerg and Allison Stewart, *Olympic Proportions: Cost and Cost Overrun at the Olympics 1960-2012* (June 1, 2012). Saïd Business School Working Papers, Oxford: University of Oxford. 3.

have created the perception of the Games being a profitable endeavor and, now, when bidding time comes around, a plethora of nations line up hoping they will capitalize on the Games and become the next success story. However, no city since has been able to reach the same profit margin, and more times than none, when the Olympic torch goes out, the host city is left with massive financial debts and little to show for it.

In my thesis I will make the claim that the allure of hosting the Games is misleading due to errors on both sides of cost-benefit analyses. On one side, bidding wars push cities into paying a much higher price than anticipated resulting in massive cost overruns. On the other side, three common misconceptions concerning the potential benefits are leading candidate cities to overvalue the Games from an economics standpoint.

In the body of my thesis, I will break down the factors leading to underestimated costs and overestimated benefits. In chapter two, I will focus on the cost side and how the bidding process is causing candidate cities to overbid for the hosting rights. In chapter three, I will look at the potential benefits and explain the three common misconceptions cities are using in order to justify the massive costs. I will then conclude with a recommendation for the future of the Olympic movement. While many of the claims I will be discussing hold true for other mega-events such as the World Cup, I will focus solely on the modern Olympiad.

## **Chapter 2: Why are the costs underestimated?**

My thesis states that the costs of hosting the Olympic Games are often underestimated, while the potential social and economic benefits are overestimated. In this chapter, I will focus on the costs of hosting the Games, and attempt to explain why so many ex-post economic studies show much greater costs than the ex-ante estimates. I will start by examining the Olympic bidding process and the two phases of awarding the rights to host the mega-event. I will then explain why the auction-setting of the Olympic selection process creates the perfect environment for the winner's curse and is the primary cause for ex-ante cost underestimations and eventual cost overruns.

### **Bidding process**

Economic studies focus on the allocation of resources and who bears the costs. With a mega-sporting event such as the Olympics, an event that is only held every four years, the rights to host the Games can be thought of as a scarce resource that must be allocated to one of the cities or regions competing for those rights. The International Olympic Committee (IOC), a non-governmental organization, holds the rights to these games and acts as the monopoly seller, while the potential host cities act as competing buyers bidding for the Games.<sup>3</sup> In order to secure the rights to host arguably the biggest sporting event in the world, cities must endure a complex and drawn out process to promote their city or region for being the most attractive site. Not only must they prove

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<sup>3</sup> Brad R. Humphreys and Henry Van Egteren, "Mega Sporting Event Bidding, Mechanism Design and Rent Extraction," in *International Handbook on the Economics of Mega-sporting Events*. Eds. Wolfgang Maennig and Andrew Zimbalist. (Northampton: Edward Elgar, 2012). 17.

they are fit and willing to host the Games, but they must also guarantee their ability to meet the requirements and objectives of the IOC.

The process for selecting a host city is defined in Chapter 5, Rule 34 of the Olympic Charter. This rule maintains that the IOC has the sole authority for awarding the rights to host and that all applicant cities must submit detailed bids describing their plans for organizing the Games. Rule 34 also specifies that “these bids are legally binding, and requires that the government of the applicant cities must guarantee that the bid will comply with the Olympic Charter”.<sup>4</sup> Rule 37.1 of Chapter 5 goes on to further state that the IOC is not responsible for any of the costs associated with hosting. Rather, the Organizing Committee of the Olympic Games (OCOG) within the applicant city is responsible for all financial liabilities.<sup>5</sup>

The identification of potential host cities to the actual awarding of the rights is a two year process and involves two phases.<sup>6</sup> In phase 1, the Organizing Committees of the applicant cities are required to develop a preliminary bid to be presented to the IOC Executive Board. On top of the \$150,000 non-refundable “candidature acceptance fee”, the preliminary bid requires prospective cities to complete a detailed questionnaire providing information about all aspects of the Games, including in depth details regarding how the Games will be financed.<sup>7</sup> Cities hire financial analysts to value the project and create an ex-ante estimation of the costs associated with hosting the games. These costs include the construction of venues, housing for athletes, officials and media,

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<sup>4</sup> Brad R. Humphreys and Henry van Egteren 20.

<sup>5</sup> Brad R. Humphreys and Henry van Egteren 20.

<sup>6</sup> Brad R. Humphreys and Henry van Egteren 20.

<sup>7</sup> Brad R. Humphreys and Henry van Egteren 21.

security, transportation, communication, and any additional infrastructure costs.<sup>8</sup> It is within this questionnaire that “fiscal authorities of the host city and the country must agree to pay all costs associated with hosting, including cost overruns”.<sup>9</sup> The preliminary bid within phase 1 is designed to assess the local and national government of the applicant city’s willingness and ability to bear the costs that accompany hosting. The applicant cities with the best bids (or the highest willingness to pay) are chosen by the IOC to advance to phase 2 and become “candidate cities”.<sup>10</sup>

In addition to a second non-refundable fee of \$500,000, phase 2 of the bidding process is where candidate cities put together full bids in the form of “candidature files” or “bid books”<sup>11</sup>. The candidature files include full ex-ante budget plans and it is again stressed that the candidate city must guarantee to fulfill “all major capital infrastructure investments required to deliver the Olympic Games... and cover a potential economic shortfall of the OCOG”.<sup>12</sup> These bid books are submitted to the IOC Executive Board and are legally binding.<sup>13</sup> After each candidate city makes its formal bid presentation, the IOC awards the rights to host the Games through a voting process.

While the candidature files map out the candidate city’s financing plans, the forecast within the bid tends to be more of a guess than a calculated budget plan. The financial guarantees within the Candidature Files push bidding cities to essentially write a blank check to pay for the Games and force cities to take on an extremely risky

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<sup>8</sup> Brad R. Humphreys and Henry van Egteren 22.

<sup>9</sup> Brad R. Humphreys and Henry van Egteren 22.

<sup>10</sup> "IOC - International Olympic Committee." *Olympic Games Candidature Process*.

<sup>11</sup> Brad R. Humphreys and Henry van Egteren 22.

<sup>12</sup> Brad R. Humphreys and Henry van Egteren 20.

<sup>13</sup> Bent Flyvbjerg and Allison Stewart 4.

investment. The process of awarding the hosting rights is drawn out intentionally to give the host enough time to put the promised infrastructure and facilities in place. Yet, by the time all of the construction is complete, the final costs almost always turn out to be much greater than the proposed bid budget. A study by Bent Flyvbjerg and Allison Stewart at the University of Oxford examines the cost overruns of the Games since 1960. They were able to obtain data on the preliminary bid budgets and final costs of 16 of the 27 total Games held between 1960 and 2012. Their final finding show that of the 16 Games in the sample, host cities experience cost overruns 100 per cent of the time with an average real overrun of 179 per cent and an average nominal overrun of 324 per cent.<sup>14</sup>

Year	City	Type	Real Cost Overrun (%)	Nominal Cost Overrun (%)
1968	Grenoble	Winter	201	230
1976	Montreal	Summer	796	1266
1980	Lake Placid	Winter	321	502
1984	Sarajevo	Winter	173	1257
1988	Calgary	Winter	59	131
1992	Albertville	Winter	135	169
1992	Barcelona	Summer	417	609
1994	Lillehammer	Winter	277	347
1996	Atlanta	Summer	147	178
1998	Nagano	Winter	56	58
2000	Sydney	Summer	90	108
2002	Salt LakeCity	Winter	29	40
2004	Athens	Summer	60	97
2006	Torino	Winter	82	113
2008	Beijing	Summer	4	35
2010	Vancouver	Winter	17	36
<b>Average</b>			<b>179</b>	<b>323.5</b>

**Table 1** shows the real and nominal cost overruns

\*Primary data on final costs was not available for the Los Angeles Games as a private committee organized them.

**Source:** (Bent Flyvbjerg and Allison Stewart, 4.)

Because the majority of financing comes from public funding, such large overruns put a heavy burden on tax payers as they are forced to cover the host city's substantial financial deficits for sometimes decades after the Games takes place. In the case of the

<sup>14</sup> Bent Flyvbjerg and Allison Stewart 3.

1968 Grenoble Winter Games, local tax payers covered the financial deficit until 1992. Similarly, Montreal taxpayers were left to cover the substantial debt for 30 years following the 1976 Summer Games.<sup>15</sup> If the financial budget plans did not understate costs so dramatically there is a good chance public funding would not have been approved.

So why do the ex-ante budget plans continuously turn out to be much less than the actual ex-post costs of hosting? In the next section of this chapter, I will make the claim that this underestimation is deeply rooted in the auction-setting of the bidding process, and I will illustrate how the recurring cost overruns are a result of the unavoidable winner's curse.

### **The Winner's Curse**

As described in the previous section, ex-post costs of hosting the Olympic Games are always greater than the budget plan outlined in a host city's Candidature Files. In some cases, this is due to the stochastic component of the games. The time lag between the awarding of the rights and the actual production of the Games allows the opportunity for unforeseen events to significantly change the estimated costs. In 1970, Denver, Colorado was awarded the rights to the 1976 Winter Olympics; however, the terrorist attacks of the 1972 Munich Games caused estimated costs to rise by 300 per cent due to a dramatic increase in required security. In turn, Denver was unable to finance the games

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<sup>15</sup> Wladimir Andreff, "The winner's curse: why is the cost of mega sporting events so often underestimated?" in *International Handbook on the Economics of Mega-sporting Events*. Eds. Wolfgang Maennig and Andrew Zimbalist. (Northampton: Edward Elgar, 2012). 37.

and was forced to withdraw as host.<sup>16</sup> In many of the Winter Games, poor weather and lack of snowfall, like the case of the 2010 Winter Games in Vancouver, could force countries to take on infrastructure projects that are greater than anticipated, such as airlifting snow by helicopter, purchasing snow cannons, and covering the slopes with tubes of dry ice.<sup>17</sup>

These are two examples of how the stochastic component of the Games can be the cause of cost overruns; but this cannot be the sole reason as to why ex-ante costs are systematically underestimated. The source of these unexpectedly high expenses is embedded in the auction nature of the bidding process. In an auction, because of “incomplete information, emotions, or any other number of factors regarding the item being auctioned, bidders can have a difficult time determining the item’s intrinsic value”.<sup>18</sup> As a result, the bidder with the largest overestimation of an item’s value wins the auction. This economic theory is known as the “winner’s curse”.<sup>19</sup> Economists and financial analysts use this theory to explain lower than expected returns on investments made through competitive bidding. The theory originated when analysts sought to explain the low returns of oil companies.<sup>20</sup> In a situation where oil companies are competing for the rights to drill in a particular area, the winning bidder will always over pay for the lease. This is because the winning bid will always be higher than any likely market price due to incomplete information. Because the intrinsic value of the drilling rights is

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<sup>16</sup> Brad R. Humphreys and Henry van Egteren 24.

<sup>17</sup> Suzanne Goldenberg, "Canada's Mild Climate Leaves Winter Olympics Short of Snow." *The Guardian*. Media Limited (2010).

<sup>18</sup> Wladimir Andreff 39.

<sup>19</sup> Wladimir Andreff 43.

<sup>20</sup> Wladimir Andreff 44.

relatively uncertain, the oil company with the largest overestimate of the value will win the rights.

The process of allocating the rights to host the Olympics can be closely paralleled to the above example regarding oil companies. At the time when the IOC calls for the applicant cities to submit their Candidature Files, no one country knows the true intrinsic cost of hosting the next Olympics. The IOC simply defines the “assortment of sporting venues and infrastructure that must be completed and operational”<sup>21</sup> with no indication of the value of the potential costs. It is the responsibility of the candidate cities to meet these requirements and add in any additional infrastructure investments, such as transportation and urban development, they deem necessary to their own Olympic success. The IOC does not require these additional investments, so their costs are not specified in the Candidature Files.<sup>22</sup> This leaves much uncertainty when attempting to determine the actual costs and benefits that will come with hosting the Games. This is similar to the oil example and helps support the claim of the winner’s curse as the true, total value of the hosting rights is relatively uncertain.

In order to continue my comparison, it is important to point out several key aspects of the IOC and its intentions. Remember that Chapter 5 of the Olympic Charter states that the IOC is not responsible for any of the costs associated with hosting the Games, including cost overruns. The Charter also specifies that in the occasion of a surplus, any profits generated by the Games must be “applied to the development of the

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<sup>21</sup> Wladimir Andreff 52.

<sup>22</sup> Wladimir Andreff 52.

Olympic Movement”.<sup>23</sup> In other words, the IOC has claim to all (if any) profits. This is important to point out as it demonstrates that the IOC is not concerned with the high costs as long as the host city guarantees that it will provide the necessary infrastructure and sporting venues. The only stated objective of the IOC is to elect a host that will “maximize the overall quality of the project” in order to leave a “grandiose image of each Olympiad and an unforgettable memory”.<sup>24</sup> This presents a case of moral hazard as the hosting incentives of the IOC and the host city are misaligned. Because the IOC is protected against the risks that come with hosting, such as cost overruns, they are able to instigate aggressive overbidding between candidate cities. The IOC, in a sense, can and usually does, choose the most extravagant bid with the largest financial investment because they are not responsible for the costs (as seen in table 2).

2012 Summer Games		2016 Summer Games	
Bidding City	Announced Total Costs (\$m)	Bidding City	Announced Total Costs (\$m)
New York	10.68	Chicago	3.3
London	18.25	Tokyo	4.07
Madrid	3.64	Madrid	4.18
Paris	8.87	Rio de Janeiro	9.53
Moscow	11.86		

**Table 2** shows the ex-ante cost estimates of the bidding cities. The winning city is highlighted in yellow.

**Source:** (Wladimir Andreff, 52.)

The IOC’s attitude does not just provide the option for extreme overbidding; it appears to fundamentally encourage overbidding through the bidding process. By examining the objectives of both the supply side (the IOC) and the demand side (bidding

<sup>23</sup> Brad R. Humphreys and Henry van Egteren 20.

<sup>24</sup> Wladimir Andreff 53.

cities) of the auction, there is an apparent principle-agent problem as the IOC's best interests differ greatly than those of the hosting city. The IOC seeks to produce an extravagant, memorable event, as it will reap any of the profits without bearing the costs. At the same time, bidding cities know that in order to win the hosting rights they must outbid their competitors with ambitious project proposals. The objectives of both the IOC and candidate cities coupled with the principle-agent problem between the two create the perfect environment for the winner's curse.

The presence of the winner's curse is made even clearer after examining the 1984 Summer Games in Los Angeles. Following the hostage crisis of the 1972 Munich Games and the United States' boycott of the 1980 Games in Moscow, the Soviet Union and 13 other Eastern European countries refused to participate in the 1984 Games.<sup>25</sup> This left Los Angeles as the sole candidate for the Games and eliminated the auction style allocation of the Games. Without the incentive to overbid, Los Angeles was not forced to overbid for hosting rights and the 1984 Games became the most financially successful in the history of the Olympics (in terms of cost-benefit analysis) posting a profit of \$225 million.<sup>26</sup> It must be noted that the city's Organizing Committee was able to stage the Games by upgrading existing venues rather than building new facilities, greatly reducing infrastructure costs.<sup>27</sup> Yet, a city most likely would not win a competitive bidding process by proposing to merely upgrade existing venues, as opposed to building new lavish ones.

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<sup>25</sup> Alissa Walker, "How L.A.'s 1984 Summer Olympics Became the Most Successful Games Ever." *Gizmodo*. (2014).

<sup>26</sup> Alissa Walker, "How L.A.'s 1984 Summer Olympics Became the Most Successful Games Ever."

<sup>27</sup> Alissa Walker, "How L.A.'s 1984 Summer Olympics Became the Most Successful Games Ever."

All in all, without the possibility of the winner's curse, Los Angeles was able to avoid extreme overbidding and cost overruns.

In the current structure, cost overruns and huge financial deficits are an almost unavoidable fate that comes with hosting the Olympics. By comparing the preliminary bid budget to the actual ex post costs, it is evident that cities are underestimating the price of hosting the Olympics, causing cost overruns to drain public funds. Deeper examination of the bidding process of allocating the rights to host the Olympic shines light on how the winner's curse is leading to overbidding and underestimations of costs. In the next chapter I will look at benefit side of economic studies and explain the three misconceptions leading to the overestimated benefits of hosting the Games.

### **Chapter 3: Why are the benefits overestimated?**

In the previous chapter, I illustrated how the price of hosting the Olympic Games is almost always underestimated due to the winner's curse, leading to significant cost overruns for host cities. It has become all too common for the Games to end in massive financial deficits and a debt that must be repaid for decades following the Olympics. Given applicant cities' awareness of this long-standing trend, why do they continue to bid for the Games?

In the following chapter I will attempt to answer this question with the claim that cities are using three false beliefs as incentives for hosting the games. The first misconception is that the games have become a profitable venture for host cities. This skewed perception derives from the financial success of the 1984 Summer Games in Los Angeles – one of the only games to generate a significant profit. Yet, it can be argued that this case was a fluke as the single candidature nature of the bidding process eliminated the winner's curse and put Los Angeles in a rare bargaining position against the IOC. Cities have sought to emulate Los Angeles' financial plan but have failed as increasing division of revenues leaves most of the profits with the IOC.

The second belief misleading applicant cities is the idea that tourism brought by the Games will help local businesses and stimulate the economy within the region.

Evidence instead suggests that the claims of economic benefits are continuously overstated in cost-benefit analyses, due primarily to crowding out and leakages.<sup>28</sup>

The final misconception surrounding the games is that they will improve the city's infrastructure and contribute to a large-scale urban regeneration. While there have been successful developments – such as the case of the 1992 Barcelona games – most Olympic ventures have had a negative social impact on communities because of the misuse of funding and the unsustainable nature of the mega sporting venues.

### **Misconception #1: the Games generate profit for host cities**

Although the Olympics have the long-standing reputation of resulting in substantial financial losses for the host, cities continue to optimistically enter the bidding hoping that the mega-event will result in revenues. The idea that the Olympics generate a profit for the host city is a more modern concept, stemming in large part from the fiscal success of the 1984 Los Angeles Summer Games.

The terrorist attacks of the 1972 Munich games and the enormous debt Montreal accumulated after the 1976 Games made the Olympics an unattractive investment and put the future of the games at stake.<sup>29</sup> A series of crises discouraged many nations from submitting a bid for the 1984 Summer Games, and for the first time, the IOC experienced a single candidature with Los Angeles as the sole bidder. When Los Angeles was handed

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<sup>28</sup> Daniel M. Chin and Philip K. Porter, "Economic impact of sports events" in *International Handbook on the Economics of Mega-sporting Events*. Eds. Wolfgang Maennig and Andrew Zimbalist. (Northampton: Edward Elgar, 2012). 255.

<sup>29</sup> Mark L. Brace, "Revisiting Los Angeles: A Financial Look at the XXIIIrd Olympiad." *Southern California Quarterly* 83.2 (2001). 162.

the rights in 1978, the IOC recognized that the modern Olympic movement depended on the success of the 1984 Games.

The Los Angeles Olympic Organizing Committee (LAOOC) rose to the challenge and produced arguably the most successful Games in the history of the Olympiad. The 1984 Games was one of the only Games to record a profit (\$225 million) and set a record with 140 participating nations.<sup>30</sup> The financial success of the 1984 marked the beginning of the modern Olympic movement and forever shifted the perception of the Games. Cities now saw the Olympics as a money making endeavor and have since sought to recreate Los Angeles' feat. Yet, host cities have yet to generate profits anywhere close to what Los Angeles achieved in 1984 due to the fact that the majority of success can be attributed to a few unique circumstances.

As stated in my previous chapter, the winner's curse is at the source of eventual cost overruns for host cities. Because Los Angeles did not have to outbid any competitors, the effect of the winner's curse was eliminated, preventing overbidding for the hosting rights. The single candidature nature of the year also left Los Angeles in a very strong bargaining position against the IOC in terms of financial liabilities.<sup>31</sup> Without the revenue of the Games, the IOC would have surely gone bankrupt, and this forced them to comply with a number of the LAOOC's demands.<sup>32</sup>

The first of these demands was the refusal to finance the Games using public funding. The Olympics took on a "the games will pay for the games" approach and Los

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<sup>30</sup> Mark L. Brace 162.

<sup>31</sup> Mark L. Brace 162.

<sup>32</sup> Daniel M. Chin and Philip K. Porter 257.

Angeles was able to raise the necessary capital primarily through television sales, corporate sponsorships, and ticket sales.<sup>33</sup> The LAOOC sponsorship program “raised \$126 million in cash and in-kind commitments from twenty nine sponsors” including Canon, Coca-Cola, and IBM.<sup>34</sup> Furthermore, the LAOOC realized how much the games were worth to television companies and was able to initiate aggressive negotiations between networks. This strategy paid off and ABC agreed to a contract worth \$225 million.<sup>35</sup> By turning the Games into a private venture, the LAOOC was able to shift much of the financial liability of the Games away from the city, ensuring that the cost to taxpayers would be minimal.

Year	City	Total Costs (\$m)	Revenues (\$m)	
			TV	Domestic Sponsorship
1984	Los Angeles	413	286	219
2000	Sydney	3,000	1,318	492
2004	Athens	9,000	1,373	302
2008	Beijing	5,500	1,739	1,218
2012	London	14,800	2,569	1,150

**Table 3:** Total costs and revenues sources in US millions

**Source:** (Statista)

Los Angeles also refused to build any new athletic facilities or venues. The LAOOC recognized that the construction of large-scale facilities was a major drain on Olympic funds. The final cost of construction for the previous Games in Montreal reached an unprecedented figure of \$1.2 billion dollars.<sup>36</sup> With this in mind, Los Angeles kept the building to an absolute minimum, as the LAOOC knew that nearly all the

<sup>33</sup> Mark L. Brace 167.

<sup>34</sup> Mark L. Brace 171.

<sup>35</sup> Mark L. Brace 172.

<sup>36</sup> Mark L. Brace 167.

necessary venues for the competitions already existed in the region. They were able to use University of California Los Angeles and University of California Santa Barbra dormitories as Olympic Villages. Loyola Marymount provided weightlifting facilities, and various track and field events were held in the Los Angeles memorial Coliseum.<sup>37</sup> For any necessary repairs or refurbishments, the LAOOC was able to use money raised from corporate sponsors.<sup>38</sup>

The net profit of \$225 million dollars created a new outlook for the future of the Olympics. Los Angeles undertook the task of turning the games into a privately funded event and removed the financial burden from the public. Not only did corporate sponsors and a large TV contract provide the necessary funding for the Games, they also served as a significant revenue stream. In addition, they were able to utilize existing infrastructure to drastically cut down on construction costs. The Los Angeles Olympiad set a new standard for what Organizing Committees can achieve. Unfortunately, no other committee has been able to recreate the success of the 1984 Games as every committee since has posted a loss.<sup>39</sup>

Host cities have made attempts to emulate the LAOOC's model with little success, as they fail to recognize how Los Angeles was uniquely positioned. Nearly all the necessary venues for athletic competition already existed which enabled them to

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<sup>37</sup> Mark L. Brace 170.

<sup>38</sup> Stefan Kesenne, "The economic impact, cost and benefits of the FIFA World Cup and the Olympic Games: who wins who loses?" in *International Handbook on the Economics of Mega-sporting Events*. Eds. Wolfgang Maennig and Andrew Zimbalist. (Northampton: Edward Elgar, 2012). 275.

<sup>39</sup> Mark L. Brace 179.

spend minimal funds on infrastructure. Furthermore, without the auction-style allocation of the games, overbidding was avoided and Los Angeles had leverage over the IOC to rid themselves of much of the financial liabilities created by public funding. It is important to recognize that the unique circumstances of the 1984 Games made Los Angeles an exception to the Olympic fate.

Another reason that cities have not been able to reach the profit levels of the 1984 Games is because host cities are becoming entitled to increasingly less of the television right sales and corporate sponsorship funds. Article 21 of the Olympic Charter gives the IOC exclusive rights to negotiate broadcasting contracts and the distribution of those revenues.<sup>40</sup> The IOC has been gradually allocating itself larger shares of the rights to these revenues as seen in table 4. In 1984, the IOC was receiving one third of the

Period	Entity	IOC share %	Host cities share %
1948–1968		1–4	96–99
1972–1980		10	90
1984–1992		33	67
1996–2004		40	60
2006–2010		51	49

**Table 4:** Evolution of the distribution of revenue from television broadcasting rights  
**Source:** (Robert A Baade, and Allen R. Sanderson, 96.)

television revenues. Since the 2004 games, this share has jumped to one half of all revenues.<sup>41</sup> Sponsorship revenues have also been greatly divided since the Los Angeles

<sup>40</sup> Robert A Baade, and Allen R. Sanderson, "An analysis of the political economy for bidding for the Summer Olympic Games: lessons from the Chicago 2016 bid." in *International Handbook on the Economics of Mega-sporting Events*. Eds. Wolfgang Maennig and Andrew Zimbalist. (Northampton: Edward Elgar, 2012). 96.

<sup>41</sup> Holger Preuss, "Economic dimension of the Olympic Games." Centre d'Estudis Olímpics (Barcelona: 2002). 10.

Games. The Beijing Olympics raised \$2.1 billion in sponsorship revenue, but this was divided among the IOC, the OCOG, and the National Olympic Committee.<sup>42</sup> The sale of television rights and corporate sponsorships are one of the largest motivators for cities to bid for the Olympics. However, due to this increasing division of revenues between so many groups, host cities are overestimating the benefits of commercialization.

### **Misconception #2: tourism will stimulate the local economy**

The second misconception leading cities to continue to bid for the Olympic rights is the belief that tourism will help local businesses and will stimulate the host city's economy. In order to justify public subsidies for funding the Olympics, cities offer staggering claims regarding the amount of economic activity the mega-event can stimulate. When bidding for the 2012 Games, the chairman of the Dallas Organizing Committee claimed that the city would observe a \$4 billion impact that would "benefit most every business in the Metroplex – from hotels to restaurants, from real estate to transportation, from communication to health care".<sup>43</sup> Yet, cost-benefit analyses and traditional input-output economic models fail to account for crowding out and leakages that derive from the short-term nature of a mega-event like the Olympics. As a result, economic analyses greatly overestimate the economic benefits within the region.

In traditional input-output models, for economies with constant returns to scale, a steady increase in demand is met with an equal increase in supply. The economy should expand, more jobs should be created, and income should flow in. However, this theory

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<sup>42</sup> Holger Preuss 11.

<sup>43</sup> Robert A. Baade and Victor Matheson, "Bidding for the Olympics: Fool's Gold?" *Transatlantic Sport* (2002). 4.

does not hold for one-time, short duration events such as the Olympics. Instead of increasing steadily, the additional demand is concentrated in a short period of time, and supply cannot adjust. Businesses such as hotels respond by raising prices rather than hiring more employees or building more rooms. Higher prices cause locals or would-be visitors to go elsewhere, in turn, replacing new demand with the departure of already existing demand. This theory is known as “crowding out”.<sup>44</sup> By failing to account for the crowded out demand, cost-benefit analyses overstate the actual economic benefit of tourism. In fact, while the gross impact may seem large, crowding out offsets the benefits of new visitors until the net effect is practically zero.<sup>45</sup>

The majority of models also inaccurately estimate cash flows within a region during a mega-event due to leakages. In a normal, circular economy, spending becomes income for others, creating a multiplier effect.<sup>46</sup> However, during a mega-event, the economy is far from normal. While there may be a substantial inflow of spending during the Olympics, there is also a large inflow of temporary businesses. These businesses will flock to the city to make sales only to depart with any revenues once the Games are complete. As a result, leakages make it so only a small fraction of the income received as a consequence of someone’s spending is spent again within the region.<sup>47</sup> Due to this effect, much of the spending on services, goods, and entertainment leaves the region and has no positive impact on the local economy.

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<sup>44</sup> Daniel M. Chin and Philip K. Porter 257.

<sup>45</sup> Stefan Kesenne 273.

<sup>46</sup> Robert A. Baade and Victor Matheson 8.

<sup>47</sup> Robert A. Baade and Victor Matheson 8.

Another instance of leakages can be observed due to the fact that most large corporations within a host city are nationally owned chains. We know from national income accounts that over time “roughly one-third of income goes to capital and two-thirds to labor”.<sup>48</sup> Businesses such as hotels get much of their financing from international markets and are, therefore, not owned by the region. Because of this, when prices rise during a mega-event, models do not recognize the fraction of new profits leaving the local economy to shareholders outside the region. Again, this greatly reduces the multiplier effect of a circular economy leading to overstated economic benefits.

Cities continuously point to impact studies to provide rationale for public funding. By failing to account for the effects of crowding out and leakages, tax-payers are being misinformed of the realistic economic benefits of the Olympics, resulting in excessively optimistic appraisals. Local residents may not realize that the net impact of the Games may actually be close to zero.

### **Misconception #3: infrastructure investments lead to urban regeneration**

The last common misconception is the belief that the Olympic Games provide host cities with an ideal opportunity to instigate large scale urban developments, despite the huge infrastructure costs that come with it. Similarly to misconception #1 (the games generate profits for host cities), this misconception stems from the success of previous Games. Both Los Angeles in 1984 and Barcelona in 1992 were able to take advantage of the Olympics as an opportunity to stimulate urban regeneration and effectively rebranded themselves. Since then, cities have used these two cases as justification to take on the

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<sup>48</sup> Daniel M. Chin and Philip K. Porter 257.

enormous games-related expenditures. Yet, no city has been able to recreate a successful regeneration plan and most Olympics have actually had a negative impact on urban development.

Using the 1992 Summer Olympic Games as a catalyst, Barcelona was able to revitalize much of the urban development along its main waterfront areas. A combination of public and private funds was used to modernize neglected ports and neighborhoods, giving the entire district new life.<sup>49</sup> In terms of its financial strategy, Barcelona took on a different approach than previous games, using 83 percent of the total expenditure for urban improvements rather than for sport. The city spent billions on a modernized urban makeover and was able to fully redesign and upgrade transportation and telecommunications systems. There were also “4500 new flats provided by the Olympic Villages, five major nodes of new office development, extensive investment in the cultural sector (especially museums) and 5000 new hotel rooms”.<sup>50</sup> Barcelona set the standard for how a city can capitalize on the Games as an opportunity to make a positive change to its urban landscape and gain exposure as a major tourist destination.

The 1984 Los Angeles Games provide another example of a successful urban development model, although the LAOOC’s strategy was much different than that of Barcelona. While the city did not directly use the games to regenerate low-income districts, they were able to avoid the use of public funds, keeping them available for other social developments within the area. Furthermore, they limited the construction of new

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<sup>49</sup> "Barcelona: Event as a Catalyst," *Parks, Promenades & Planning: Brand Management with the 21st Century Urban Waterfront*, Rotch, 01 Dec, 2011, Web, 3 Dec 2012 .

<sup>50</sup> John R. Gold and Margaret M. Gold, "Olympic Cities: Regeneration, City Rebranding and Changing Urban Agendas," *Geography Compass*, (2008). 307.

facilities, significantly cutting infrastructure expenses. This cost-conscious model enabled Los Angeles to record a profit of \$225 million that was “channeled into American sports bodies and programs and injected an estimated \$2.4 billion into the Southern California economy”.<sup>51</sup> The Los Angeles Games are a unique success story in the sense that they were able to rejuvenate a community, not through a particularly effective strategy of building new infrastructure, but by freeing up funds for the social development of the city.

Certainly these two cases demonstrate how the Olympics can promote regeneration and boost the urban economy. However, the past two decades have seen more instances of how the Olympics can actually drain public funds. The increasing size and scope of the mega-event has led to numerous instances where heavy cost overruns on facilities have left a legacy that “tarnishes rather than enhances the reputation of the host city”.<sup>52</sup> The 1996 Atlanta Games are an example of how an attempt at urban renewal can lead to a negative social impact within a city. Atlanta took elements from both the 1992 Barcelona and 1984 Los Angeles Games when planning for the Games. The city saw a private consortium to organize the Games while simultaneously attempting to employ an urban regeneration strategy. This proved problematic, as the motivations of the private committee were not in line with those of the public. The Organizing Committee sought “urban improvements of a cosmetic nature”<sup>53</sup> and stressed beautification of the city rather than addressing social needs. As a result, the city “displaced poorer residents, closed hostels, and further designed the homeless of the landscape by means of such measures as

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<sup>51</sup> John R. Gold and Margaret M. Gold 306.

<sup>52</sup> John R. Gold and Margaret M. Gold 301.

<sup>53</sup> John R. Gold and Margaret M. Gold 308.

sleep proof benches and intermittent sprinklers”.<sup>54</sup> The city also failed to add job prospects, improve roads, or develop housing in the areas surrounding the Olympic venues. This led to a great deal of backlash and criticism for over-commercialization at the cost of the city’s underclass.

In addition to neglecting the needs of poorer communities, another negative social impact arises when examining the sustainability of the Olympic facilities. Peter Ueberoth, the president of the LAOOC, adhered to a strict management approach as he stated, “Where permanent construction was necessary, the emphasis was on facilities which would leave a lasting legacy for the future rather than service only the Games”.<sup>55</sup> In many cases, Organizing Committees fail to follow a similar approach and sporting venues are either destroyed or left “heavily underused and inaccessible to the public”<sup>56</sup> once the torch blows out. The 2004 Athens Games are recognized as one of the biggest failures in terms of post-Olympic venue use. The city spent billions building roughly two dozen facilities only to leave them covered in graffiti and surrounded by chain link fences just ten years later.<sup>57</sup> This failure sparked public anger and the Athens Olympics became “symbolic of the government’s waste” and a metaphor for Greece’s economic crisis.<sup>58</sup> In Beijing, the famous “Birds Nest” stadium, which costed \$480 million to build and \$11 million a year to maintain, has no regular tenant.

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<sup>54</sup> John R. Gold and Margaret M. Gold 308.

<sup>55</sup> Mark L. Brace 169.

<sup>56</sup> John R. Gold and Margaret M. Gold 309.

<sup>57</sup> Scott Stump and Eun K. Kim, "What Happens to Olympic Venues after the Torch Goes out." TODAY News, (2015).

<sup>58</sup> Binyamin Appelbaum, "Does Hosting the Olympics Actually Pay Off?" *The New York Times*, (2014).

Cities continue to use the possibility of urban regeneration as justification for hosting the Olympics, when in reality, the large scale infrastructure investments tend to do the public more harm than good. When attempting to use the Games to implement urban restructuring, it is not enough to replicate the strategies undertaken by past Olympic committees as each city has different needs. Cases such as the 1996 Atlanta Games show what can happen when regeneration strategies are not carefully planned around the ambitions of the community. Atlanta sought economic growth through beatification when it should have addressed some of the problems affecting the lower class. Cities also have failed to capitalize on the construction of mega sporting venues by leaving them underused following the games. The misconception of how Olympic infrastructure investments lead to urban regeneration sends cities down a dangerous path of negative social consequences and severe public scrutiny.

## Conclusion

Throughout this essay, I have supported my thesis that the costs of hosting the Olympics are almost always underestimated, while the potential benefits are overestimated. I illustrated how the bidding process opens the door for the winner's curse and unavoidable overbidding. This results in cost overruns and massive financial debts. Regardless, cities continue to enter the bidding war due to the misconception that the Games will generate a profit, stimulate the local economy, and lead to large-scale urban regeneration. However, it is clear that these benefits are vastly exaggerated by economic impact studies and are actually negligible.

As of late, this is becoming more apparent and it is becoming increasingly difficult for cities to justify hosting the Games. Recently, Boston terminated its bid for the 2024 Olympics due to resistance among residents.<sup>59</sup> Boston's mayor was quoted saying, "no benefit is so great that it is worth handing over the financial future of our city, and our citizens were rightly hesitant to be supportive as a result".<sup>60</sup> It is clear that cities are beginning to recognize that the immense costs are not worth the potential benefits that come with hosting. With the financial risks becoming more apparent, the IOC must proceed with caution in order to prevent the extinction of the Olympics.

In order to restore the legacy of the Games, I will suggest two ways to counteract the monopoly power of the IOC. First, is to eliminate the bidding process. The Los Angeles experience makes it clear that the absence of competing cities prevents the

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<sup>59</sup> Katharine Q. Seelye, "Boston's Bid for Summer Olympics Is Terminated." *The New York Times*. The New York Times, (2015).

<sup>60</sup> Katharine Q. Seelye, "Boston's Bid for Summer Olympics Is Terminated."

winner's curse and extreme overbidding. Furthermore, the single candidature puts the IOC on and the Organizing Committee on "roughly equal footing in negotiation the financial terms of the Games".<sup>61</sup> Some possible solutions for this could be choosing a few locations for the Games to rotate between or by fixing a site (such as Olympia). This would also help eliminate the problem of the underuse of large sporting facilities. Second, the IOC needs to do a better job of sharing the large profits produced by the Games with the host countries. Over the past couple of decades, host cities have become entitled to less and less of the revenues from the sale of television rights and corporate sponsorships. If the Organizing Committees of the host country had claim to a greater percentage of these revenues, it would help chip down the financial deficit caused by escalating costs.

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<sup>61</sup> Robert A. Baade and Victor Matheson 34.

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