

Skate's Art Market Research

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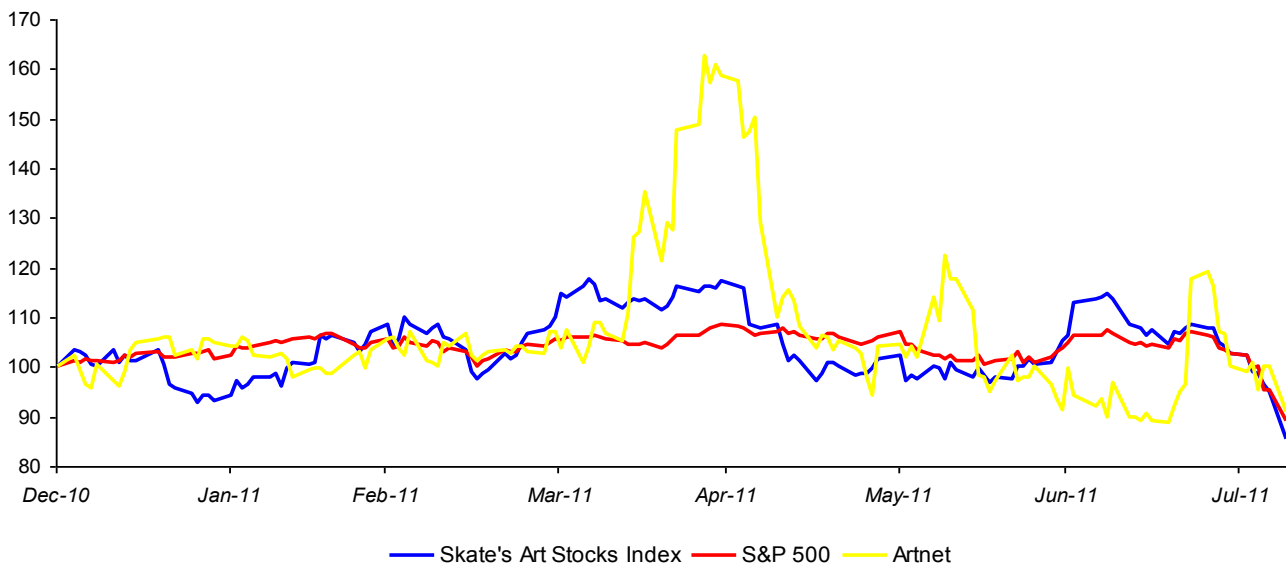
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Skate's Market Notes

artnet: Back to Red, Auction Volume Flat against Sotheby's 27% Same Period Growth, Price Database Profitability Down by 40%

artnet has reported its six months' financial results, and, unlike the Sotheby's numbers that we commented on last week (see [Sotheby's report](#)), its performance is disappointing. Revenue fell to the sum reported in the same period of last year, the firm returned to a net loss and its bet to grow on the back of its online auction offering is not (yet) working.

For more than three years, artnet has consistently said that while it faces declines in gallery membership and information sales, the firm's growth should come from the online auction business unit that it launched a few years ago. Unfortunately for artnet, the timing for the online auction launch largely coincided with the global economic meltdown of 2008, and the company's management asked for the benefit of the doubt on the question of whether its online art trading would prosper once economic recovery resumed.



Well, the time is up. Whether one believes that we are still in the same crisis, have entered a new crisis or are beyond the crisis, Sotheby's recent numbers stand as an excellent measure to benchmark artnet's performance. Sotheby's net auction sales are up 90.6% for the first six months of the year over the same period last year,

auction and related revenues are up 27% and the total global volume of art market trade has more than doubled compared to the first six months of 2010. artnet's auction segment has grown by only 11% in Euro terms, with total revenue of EUR 1.1 million for the first six months; this amount is less than Sotheby's average daily auction revenue for the same period and looks like a rounding error even when compared to the auction revenue of relative newcomers like China's Poly Auction (see [Skate's report on Poly](#)). And, unlike Sotheby's and Poly, artnet continues to lose money on its art auctions, operating its online auction segment at a 24% negative margin based on the first six months of the year.

Flat revenue numbers (down 0.3% for the first six months of the year in Euro terms), a net loss for the period and a non-performing auction business are not the only bad news to plague artnet. There are two more worrisome developments at the firm:

- 1) The Price Database, the only true cash cow in artnet's portfolio, suffered a dramatic profitability decline of 40% for the period. We expected artnet's profits from the price data segment to come under pressure due to the proliferation of various free art auction data sources, but this decline is happening too quickly and is too steep against the backdrop of growing art trading volumes. Frankly, we are at loss to see how artnet's management can reverse the trend.
- 2) artnet disclosed the magnitude of its problems at the artnet magazine unit by introducing this division as the fifth business segment in its financial report. The loss of EUR 471,000 on revenues of EUR 50,000 for the first six months of the year is truly depressing, and the fact that revenues are declining at a slower rate than the losses are increasing would console only a masochist.

Add to these woes a continuing decline in Galleries membership revenue (down 6.5%) and in the number of subscribers (down 2%)—which implies a decline on revenue per gallery—and one sees the complete picture of a business model that needs to change.

Some change has taken place already. Skate's has learned that earlier this year Bill Fine, a long-standing senior member of the management team, left artnet for rival Artinfo, a firm that never seemed to have much interest in making money anyway. artnet has overhauled its website, and it looks like a much more usable product with greater advertising sales potential than the long-standing previous version. The firm continues to expect a surge in its online art auction trading volumes.

But what if online art trading does not take off? The firm still has EUR 2.7 million in cash, and without debt it definitely has time to develop a new sense of direction. Would it not be a good time to think of a plan B in case the online art auction initiative continues to disappoint?

We stand behind our original recommendation of EUR 6.5 per share and look forward to new ideas from artnet's management.