

# Skate's Art Market Research

155 East 56<sup>th</sup> Street, 4<sup>th</sup> floor, New York, NY 10022 USA /phone: +1.212.514.6010

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## Skate's Market Notes

### Citibank Initiates Coverage of Sotheby's, Names Skate's Among Research Partners

Skate's is pleased to announce that Citibank, specifically the Citigroup Investment Research division, has recently launched investment coverage of Sotheby's (NYSE: BID). This marks the first time that this leading financial institution has devoted specific coverage to Sotheby's.

Citi's coverage of Sotheby's is welcome on several levels. First, it provides further acknowledgement of a reality that Skate's has long espoused, i.e., that art and the securities of companies that provide art-related products and services afford institutional and individual investors with a viable alternative asset choice. Second, as the largest publicly-traded art industry company in the world, the high liquidity of Sotheby's shares allows investors an excellent opportunity to invest in a leading participant in the art market without the costs and risks involved in actual art ownership.

Authored by Oliver Chen, CFA, and Kate McShane, CFA, Citi's research on Sotheby's—written according to top Wall Street standards—offers a refreshing and professional analysis of the auction house business model and its upside potential. Skate's fully welcomes any research and analysis from major financial institutions focused on the art industry. Although we remain a bit more bullish about Sotheby's, we find Citi's analysis extremely interesting. Citi's initiation of Sotheby's coverage is a very healthy event for the global art industry.

Below is a summary of Citibank's initial coverage of Sotheby's:

*Initiating With Neutral Rating — Sotheby's (BID) is a premier global auction house whose only major U.S./Europe competitor is privately held Christie's. Our \$35 target yields an expected +13% total return and a Neutral rating. Key positives include BID's high-trust agency model with low-inventory risk, substantial runway on growth in Asia, superb brand equity and client relationships, and duopolistic competitive structure. We see key risks on: BID's strong correlation to small-cap performance, supply constraints, EPS leverage on auction margins, lack of near-term catalyst, a need to prove an ability to drive consistent performance in new setting, and strong local Asian competitors.*

*High Trust and Leverage Auction Agency Model — a small degree of variable costs and salary fixed costs yield substantial operating leverage, which we compare to a retailer's sensitivity to SSS comps, based on our calculations. We forecast ~+1% in auction sales (+\$50mm) yields ~+5-7c in EPS given a 65% contribution margin rate.*

*A New Sotheby's is Theoretically Lower Risk — New BID is prudently focused on: lower debt amounts and associated interest expense, elimination of auction guarantee risk since 2009, reduced fixed costs, and has attractive net cash of \$3.50/share.*

*Asia Growth = Upside Opportunity, but Competitors a Risk — We see the potential for a major prize if BID can execute in Asia based on its current investment focus on Asia, 35-year history in the region, and Citi's +8-9% China GDP China estimate. We forecast BID ~\$0.9-1bn Asian auction revenues '11E (vs. US ~\$2bn) or ~+47% growth.*

*Top Brand, Capabilities, Clients — We like BID's substantial barriers to entry on analytical/global specialists teams; its century of valuation expertise, its logistical capabilities e.g. import/tax regulations; and its relationships with all top 10 billionaires.*

*Citi's Edge Includes — Partnerships with Top Ranked Art Market Experts: Citi's Private Bank Art Advisory Team, Skate's Art Market Research, & Artvest Partners LLC.*