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Skate's Art Market Research

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Skate's Art Stocks Review

April 2012

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artnet Posts Annual Results for 2011: Weak and Disappointing Performance Forces Introduction of New Product, Continued Focus on Online Auction Trading

On March 30, 2012, artnet disclosed its financial results for 2011, once again revealing that the company still has a number of issues to resolve. The signs of profitability that artnet began to show in 2010 continue to prove elusive. Instead, virtually all of the company's key performance figures have declined, frustrating artnet's expectations that its vast business development investments would be recouped. Yet, for all that, the company has still managed to achieve certain goals and bring several improvements that are expected to more fully materialize in the coming year. Below we take a closer look at the company's current situation and the efforts it is making to achieve a brighter future.

artnet's 2011 Results: Key Performance Indicators

EUR, thousands	12/31/2011	12/31/2010	Difference (balance)
Revenue	13,341	13,637	-2%
Profit from operations	-70	-27	-159%
EBIT	-211	-161	-31%
Net profit	31	153	-79%
Cash flow from operating activities	402	651	-38%
Staff (yearend)	114	105	9%
Cash and cash equivalents	2,112	2,698	-22%
Gross accounts receivable	1,201	1,390	-14%
Less: allowance for doubtful accounts	-260	-259	0%
Net accounts receivable	940	1,131	-17%
Equity	4,752	4,315	10%
Total assets	7,437	7,111	5%

Source: artnet's 2011 Annual Report, Skate's Art Market Research

Last year artnet announced a significant decline in profitability (-79%), which stood at EUR 31,000 against EUR 153,000 in 2010. In comparison to last year, cash flow from operating activities showed a disappointing decline of 38%, with the company's cash position falling by 22%.

On the other hand, artnet managed to keep revenues almost on the same level, which stood at just over EUR 13.3 mln. artnet's management is particularly excited about having achieved one of its goals—exceeding EUR 2 mln in revenue from the Auction segment, which showed modest but nevertheless important growth of 7%.

Indeed, artnet's auction sales have finally started to attract more attention, especially since several have brought high prices. In comparison to last year's annual report, this year artnet elected not to highlight price records in the financial disclosure. Only the top sale was mentioned by Hans Neuendorf in his introduction—Andy Warhol's *Flowers*—which sold for $1.3 mln. So far this has been the only artwork to sell above $1 mln; the second highest result on artnet's online trading platform remains Richard Prince's *Last week*, which sold below its pre-auction estimate for $324,500.

Since artnet launched its online trading platform, the company still has not developed a core strategy to target a specific buying audience. By emphasizing its desire to sell higher-value lots—while at the same time stating that it serves the market for works priced below $10,000—and focusing most of its attention on lots by blue-chip artists, the company claims that its main goal is to widen its group of buyers, "offering art for everyone." Yet, in order to provide buyers with lower-segment artworks, the company will have to apply a different methodology of selecting artworks for sale, setting the average estimate range and working with particular artists of such a caliber. A similar model has been successfully applied by Saatchi Online, a trading platform that is not trying to impress anyone with brand-name artists. Instead, it sticks to the lower-value market model, often presenting young and relatively unknown artists. Such an approach has the potential to work at artnet as well, especially since the premium segment of the auction market is occupied by the duopoly of Sotheby's and Christie's.

artnet's view on the auction market's development touches on the controversy of whether online trading will eventually dominate. Stating that "it is only a question of time until all the art trade takes place online," the company fails to take into account the most recent trend of art market trading becoming an event driven industry, particularly on the premium scale. While it may be wise to conduct all lower-value art transactions online in order to minimize costs that sometimes exceed the value of works, the historical leaders of auction trading and international art fairs are not going anywhere in the near future. That said, should artnet start acting more in line with its well-chosen strategy of focusing greater attention on the lower segment of the art market, it has all the potential to succeed.

Looking at the 6% decline in revenue experienced by artnet's Price Database, one more thought comes to mind in terms of strategy. It is worth noting again that artnet's management continues to lack focus on each part of its product mix. The company's response to the challenges of increased competition continues to be diversification into other, completely unrelated areas. It is important to remember, however, that artnet has always been known primarily for its core strength—its comprehensive database. Although today it is becoming more difficult to attract customers to fee-based subscription product given the increasing amount of free information online, there is still no information provider on the art market that is able to offer such a wide range of international coverage.

The good news is that artnet has announced another service that if performed successfully would supplement all of its excising activities—artnet Analytics. Scheduled to launch in the second quarter of 2012, this service will include access to art indices and customized analytics reports. While artnet is entering a niche market characterized by intense competition among several leading companies, wise methodology, smart presentation and artnet's traditionally high level of transparency mean that artnet Analytics has every chance of becoming a competitive and successful product.

artnet's Business Segments

EUR, thousands	Revenue			EBT		
	01/01-12/31/2011	01/01-12/31/2010	Change	01/01-12/31/2011	01/01-12/31/2010	Change
artnet Galleries	4,885	5,176	-6%	610	277	120%
artnet Price Database	4,695	4,987	-6%	909	1,067	-15%
artnet Auctions	2,079	1,951	7%	-928	-704	-32%
artnet Advertising	1,584	1,461	8%	236	135	75%
artnet Magazine	96	97	-1%	-1,039	-936	-11%
Total	**13,341**	**13,673**	**-2%**	**-212**	**-161**	**-32%**

Source: artnet's 2011 Annual Report, Skate's Art Market Research

In the end, it remains surprising how a company with such a competitive and timely array of products continues to report negative financial results, failing to generate positive EBT on a segment basis and, for 2011, achieving a total loss of 32%. Over-diversification seems to be at the heart of artnet's troubles. The company's determination to succeed in auction sales is impressive, but it is disrupted by the losses incurred in other sectors, such as artnet Magazine, which ate more than EUR 1 mln in cash last year. The positive change this year, however, occurred in the artnet Galleries sector, which saw EBT growth of 120%, compared to last year's decline of 200%. This EBT growth happened despite the revenue decline of 6%.

Going forward, the current favorable art market conditions should serve to benefit artnet's activity. While it is in the process of introducing supplementary value-added services to strengthen its existing product base, artnet still has a lot of work to do in order to truly enjoy what should be a strong and competitive position.

Weng Fine Art Posts Annual Results for 2011: Amid Stagnating Revenues, Company Reports Financial Performance in Line with Expectations, Justifies Strategic Development Path

Weng Fine Art (WFA), an 18-year old international art dealer focused on B2B art trading, recently announced its financial results for the first time since its IPO on the Frankfurt Stock Exchange in January 2011. The company's annual report has been made in the best German tradition of meticulous and detailed analysis and covers not only the company's position, but also the entire art market in general.

WFA believes that despite the recent economic turbulence in the European Union, Germany is still in a strong position, which makes now the perfect time for the company to introduce fundamental changes.

Weng Fine Art 2011/2012 Profit and Loss Statement

EUR, thousands	2008/09	2009/10	2010/11	2011/12	Change
Revenue	6,443	5,007	6,685	6,518	-2.5%
Cost of sales	3,929	3,173	3,997	3,705	-7.3%
Profit margin	64.0%	57.8%	67.3%	75.9%	12.9%
Depreciation	542	201	312	120	61.5%
Gross profit	2,061	1,768	2,471	2,869	16.1%
Total costs	1,246	828	1,270	1,519	19.7%
EBIT	815	940	1,202	1,350	12.4%
Finance costs	445	301	198	244	22.9%
Profit before tax	372	653	1,007	1,111	10.3%
Income tax	131	211	315	348	10.7%
Net Profit	241	442	692	763	10.1%

Source: Weng Fine Art 2011/12 Annual Report, Skate's Art Market Research

In arguing that its decision to go public was made with a carefully planned strategy in place, the company highlights its ability to achieve the performance figures that it forecasted last year. Revenues were virtually unchanged (a decrease of 2.5%) at EUR 6.5 mln, which was the result of 936 artworks being sold over the 2011/12 fiscal year. Although this figure represents a 10% decline over the previous year, the average price of lots sold has increased.

WFA's management is particularly satisfied with ongoing profitability, noting that since its launch in 1994 approximately 96% of works have been sold at a profit. This trend continued over the past fiscal year, with WFA showing significant growth in its profit margin, achieving 75.9% (an increase of 12.9%).

WFA's business model and its way of looking at art as a commodity are reminiscent of the approach taken by

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the Fine Art Fund. In ignoring the visual characteristics of artworks, both companies are interested only in their financial qualities. But whereas previously Philip Hoffman had been virtually alone in the criticism he faced from art society, today such attacks seem appropriate and even fashionable. But in comparison to the Fine Art Fund, which has been discreet about its financial situation and has rarely announced high returns for resold artworks, WFA has promised to make comprehensive reports about its activity. Such transparent reporting would go a long way toward demonstrating the efficiency of this investment approach and its long-term sustainability.

We should note that WFA is not attempting to promote a national art legacy; instead, it targets internationally recognizable names. In 2011, only half of its sales (49%) took place in Germany, while 38% were conducted elsewhere in the EU and the balance in countries like the U.S. and Switzerland. Furthermore, the company is not aiming to support local art providers; it purchased 31% of its stock in Germany, 41% elsewhere in the EU and 28% in countries outside the EU. One of the primary reasons for maintaining such a wide network of sales is likely WFA's tendency to work with Christie's and Sotheby's, leaders that have not yet expanded into the German market, where a vivid and competitive trading arena made up of local players has dominated instead.

According to WFA's annual report, costs increased to reach EUR 1.5 mln, which was also in line with the company's predictions. The nearly 20% increase was largely related to the recent IPO that brought immediate benefit to WFA. These rising costs have not influenced the final EBIT, however. This indicator increased by nearly 13% to just under $1.4 mln.

After achieving the original target price of EUR 15, WFA's share price nearly doubled by the end of the fiscal year to EUR 29 and continues to rise (as of March 31, 2012 the price was EUR 35.50).

WFA believes that its IPO was the next step toward the company's long-term development. The amount of financing attracted thus far—WFA is currently backed up by seven banks from Germany and Switzerland—proves the seriousness of its intentions. By the end of 2012 WFA expects to achieve EUR 7 mln in sales and to exceed EUR 10 mln in 2013.

Responding to the growth of e-commerce in the art market, the company plans to launch Weng Fine Art Editions Ltd. in May 2012 as a separate online trading platform. The company remains confident in its strategy of targeting the lower-value segment of globally recognizable artists from a variety of movements.

Weng Fine Art 2011/2012 Fiscal Year Results

EUR, thousands	2008/09	2009/10	2010/11	2011/12
Fixed assets	156	130	68	80
Stocks	8,557	8,274	9,605	10,562
Receivables	193	206	178	82
Working capital	352	267	182	124
Cash on hand	35	22	5	13
Deferred taxes	0	0	0	70
Deferred	2	0	13	5
Equity	2,775	3,218	3,911	4,399
Provisions	267	378	525	688
Bank liabilities	3,267	3,003	4,843	5,721
Liabilities	2,986	2,300	772	128
Total assets	9,295	8,899	10,051	10.936
Equity ratio	29.9%	36.2%	38.9%	40.2%
Return on equity	8.7%	13.7%	17.7%	17.3%

Source: Weng Fine Art 2011/12 Annual Report, Skate's Art Market Research

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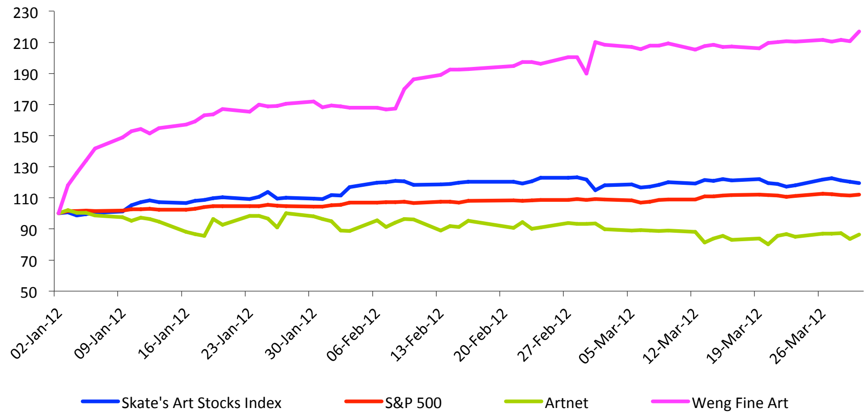
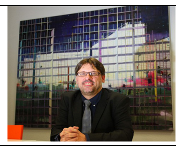
artnet vs. Weng Fine Art Stocks



artnet vs Weng Fine Art: Financial Metrics as of March 30, 2012

Company	artnet	Weng Fine Art
CEO	Hans Neuendorf	Rüdiger K. Weng
		
Revenue, USD	18,559,634	8,567,320
Profit, USD	43,786	1,003,950
Market capitalization, USD mln	25.24	24.61
Share price, USD	4.48	49.22
March 2012 performance	-7.3%	18.3%
YTD 2012 performance	-15.0%	137.3%

Source: artnet 2011 Annual Report, WFA 2011 Annual Report, Skate's Art Market Research

