

What is the true reason behind Christie's and Sotheby's increase in buyer's premiums?

Christie's executives claimed that it was a necessary measure taken because of the rising costs in the industry and that they made an effort to minimize the impact on buyers and sellers, however, it is evident that buyers will end up absorbing the additional costs. It is true that industry costs have risen and affected everyone; nonetheless the average prices of the lots sold at auctions have also increased. Moreover, despite having their expenses affected by inflation, Christie's stated that its total sales increased in 2012.

The truth is, that the only costs that are overflowing Christie's and Sotheby's financial statements come from the lower sector of the market. Their business model is becoming inefficient and obsolete in the sale of artworks priced below \$50,000 USD. They have perceived too much competition in the lower market and have decided to re-target their selling strategy by focusing in high-quality and high-priced sales. Smaller auction houses and online auctions are gaining market share and are competing with a more effective business model in the lower/mid markets. Sotheby's and Christie's operations can no longer compete with the 3-12% in premiums charged by online auctions.

In order to prove these statements, a statistical analysis was performed to 9,119 lots sold at auction houses during 2012. The analyzed lots were grouped into their corresponding price ranks, the buyers' premium charged for lots sold in Tier 1 is 25%, 20% for Tier 2 and 12% to Tier 3. The following charts show the share of lots sold in each tier and their respective share in value. The last column calculates the value of the premiums charged relative to the value of the sale in each Tier.

ANALYSIS OF LOTS SOLD USING PREVIOUS PREMIUM STRUCTURE

		Share by number of sales	Share by value of sales	% of premiums from value of sales
Tier 1	< \$50,000	37%	1%	0.3%
Tier 2	\$50,000 - \$1,000,000	53%	21%	4.2%
Tier 3	> \$1,000,000	10%	78%	9.3%
Total percentage of buyers premiums relative to the total sale				13.8%

ANALYSIS OF LOTS SOLD USING THE NEW CHRISTIE'S PREMIUM STRUCTURE

		Share by number of sales	Share by value of sales	% of premiums
C-Tier 1'	< \$75,000	47%	2%	0.6%
C-Tier 2'	\$75,000 - \$1,500,000	46%	24%	4.9%
C-Tier 3'	> \$1,500,000	7%	73%	8.8%
Total percentage of buyers premiums relative to the total sale				14.3%

ANALYSIS OF LOTS SOLD USING THE NEW SOTHEBY'S PREMIUM STRUCTURE

		Share by number of sales	Share by value of sales	% of premiums
S-Tier 1'	< \$100,000	54%	3%	0.8%

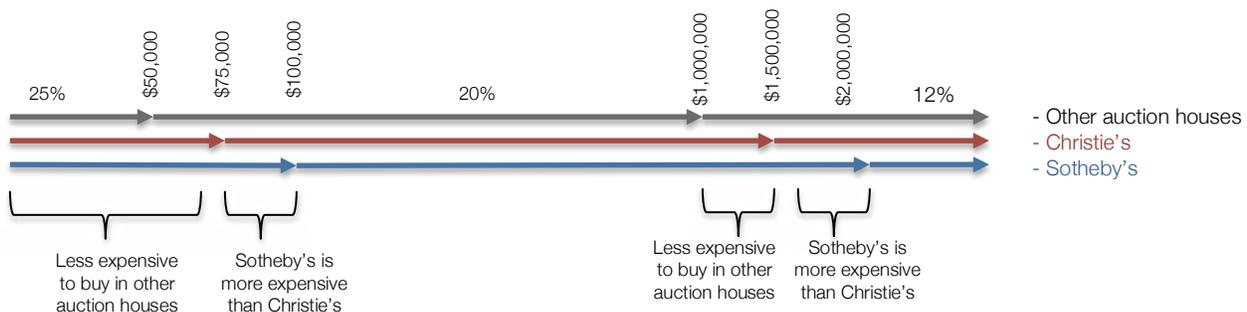
S-Tier 2'	\$100,000 - \$2,000,000	40%	27%	5.4%
S-Tier 3'	> \$2,000,000	6%	70%	8.3%
Total percentage of buyers premiums relative to the total sale				14.6%

Considering the lots studied, there were 13.8% in premiums from the total sale; with the new structure Christie's would have charged 14.3%. Is Christie's really going thru these changes just to gain an additional 0.5% (approximate) in premiums? Or is it trying to lure high-end market consumers and scare away the lower sectors? The same argument applies for Sotheby's; with its new structure it would only be adding 0.8% to its premiums.

If their ultimate interest were to increase profits by charging more to buyers they would have increased the premium rates and not the threshold amounts at which the premiums are calculated. Returning to the numbers analyzed, if instead of changing the premium structure they would increase the premiums to 26%, 21% and 13% (only one percent additional to each Tier) the total percentage of premiums charged would increase to 14.8%, compared to the 14.3% achieved by Christie's and 14.6% by Sotheby's with their new established structure. The numbers certainly prove that Christie's and Sotheby's interest is not to raise more resources, but to re-focus their selling strategy.

Although Christie's numbers are not public it is evident that they are avoiding the lower market sales because even if the premiums they charge are higher the transaction and administrative costs are too high to consider it a profitable sector. For an auction house, the costs of selling artworks are almost constant despite of their value, it doesn't matter much if they are priced at \$10,000 or \$1,000,000, the direct expenditures of a sale are almost the same. Although the seller directly absorbs the most important costs, the auction house is still responsible for some expenses like marketing, catalogue production and distribution, sale advertising and most of all administration. It is natural that if inflation is affecting costs in the industry, Christie's and Sotheby's are enabling the most profitable transactions: sales in the top end of the market.

The impact for buyers at Christie's and Sotheby's can be summarized with the following chart:



It is probable that in a short horizon there won't be noticeable changes, however Christie's and Sotheby's intentions on the long run are to change the preferences of their clients by attracting high priced sales, and avoiding the lower market where competition is growing stronger every day thanks to online auctions and selling mechanisms triggered by the everyday use of technology.