

Skate's Art Market Research

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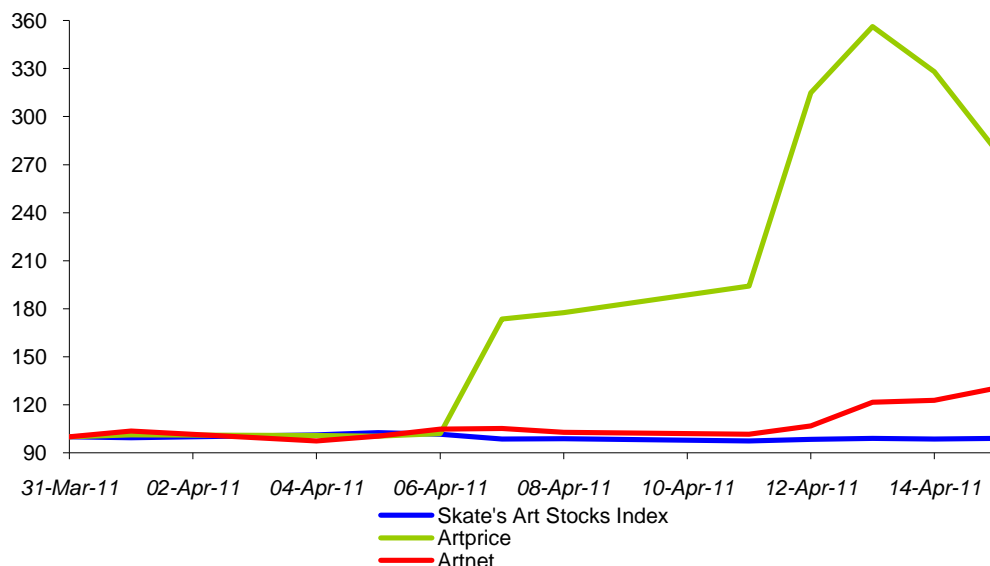
Skate's Market Notes

April 18, 2011

What's Happening to Artprice's Stock? Some Musings about the Future of the Chinese Art Market

Artprice, the Paris-listed art market data provider that is best known for its price database, flamboyant headquarters near Lyon named House of Chaos, and secretive financial reporting (the firm publishes only revenue values without disclosing either proper financial statements or any significant operational data), came on our radar last week due to the inexplicable surge in its share price. Artprice's share price tripled over the course of last week, which now makes the firm valued at \$142 million. This is four times above its major rival Artnet's market capitalization and about 20 (sic!) times its annual revenues (Artprice made EUR 5.4 million in sales in 2010, a modest increase of 11% over 2009). Artprice's business model is not nearly as well understood as Artnet's, and we can see no basis for either this share price rally or Artprice's valuation in general. The rally appears to have been triggered by an article in the local media (*La Tribune* newspaper) implying certain forward-looking statements such as an anticipated rapid increase in Artprice's sales. Skate's remains very suspicious of Artprice, as we do not like the lack of transparency in its accounting and are troubled by these rapid share price movements.

Artprice's Share Price Performance in the First Half of April versus Skate's Art Stocks Index and Artnet



Source: Skate's Art Market Research

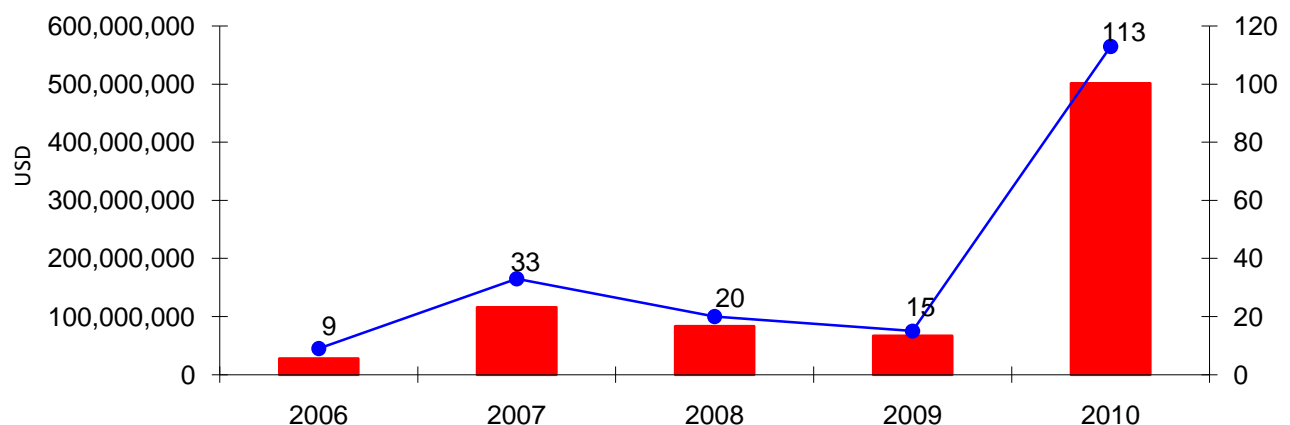
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Sensationalist reporting on Artprice's share price aside, the company has also made news with recent statements on the Chinese art market. Earlier this month, the company, which is led by its principal shareholder, an eccentric Frenchman by the name of Thierry Ehrmann, released its annual report on the outcome of the art market in 2010, using the Chinese flag as its cover page. The key conclusion of the report was that China has become a leader in the auction segment of the global art market ("electric shock to the world history of the art market," commented Artprice). Almost simultaneously, London-based ArtTactic published a report titled "China Art Market Confidence Reaches New High," which states that the company's measurements for the investment quality of different art market segments show that "the Chinese contemporary art market has moved into first place in terms of Market Confidence and is currently 21% above the U.S. & European market Confidence Indicator" (although what exactly "confidence" means remains unclear). Finally, the first week of April, traditionally the "Chinese Week" in the global auction market, once again proved the favorable situation for this segment by bringing 22 entries to Skate's Top 5000 (our ranking of the 5,000 most expensive works of art on the basis of auction prices). Of these 22 sales, three were repeat sales with annualized investment returns ranging from 19.7-93.8% (on a USD basis). In addition to all the market buzz in April, the arrest of one of the most recognized (though by no means the most valuable) modern Chinese artists, Ai Weiwei, only served to further emphasize the impetuous nature of the Chinese art market.

The chart below shows the sales growth rate of works by Chinese artists in the segment of Skate's Top 5000 (in USD and number of items).

Table 1 - Sales Volume of Chinese Artists



In our opinion, the Chinese art market is definitely seeing some turbulence, although it is still too early

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for it to be given the status of "global art leader." Going forward it seems that China has become the main center for speculation on the art market and perhaps the riskiest segment of the global art market. When it comes to the premium (investment) segment of the global art market monitored by Skate's Art Market Research, China is far from dominance by every indicator. The most valuable Chinese artist (Zhang Daqian) occupies the #62 spot in the ranking of global artists by market capitalization (the total auction value of works sold in the price range of Skate's Top 5000). Although the largest Chinese auction house (Poly International Auction) has challenged the world's third largest, Phillips, it still remains only the fourth largest auction house in terms of premium (investment) quality art sales. Finally, the total value of artworks by Chinese artists in Skate's Top 5000 is less than \$800 mln, which is far behind the market value of European and American artists, although it does exceed the aggregate market value of works by Russian artists by a factor of 2.5.

The main driving force behind the boom in the Chinese art market is a simultaneous increase in the number of wealthy people in China and their income growth, which is superimposed on the consequences brought on by the recent global financial crisis, especially the deep skepticism of many investors concerning the possibility of protecting and increasing their capital through traditional investment tools. The practice of art investment, which has deep historical and cultural roots, is widely recognized in China as a reasonable strategy for alternative investment. China's economic prosperity on the one hand (earlier this year, China officially became the second largest economy in the world after the United States) and an age-old proven global formula of value creation on the art market through a constant and significant source of demand (from medieval royal courts up to today's private museums) have indeed made China one of the world's most important art market centers. Yet, from an investment point of view, China is the global leader of venture capital and highly risky investment in "new art," but it is not a global center for art investment that aims for capital protection, something New York and London can more reasonably lay claim to.

When observing the enchanting variety of names, periods, themes and styles created by contemporary Chinese artists and consumed by the local art market (with a less significant share of foreign capital in the total volume of transactions), one of the most interesting things seems to be the swift creation of "new brands" on the Chinese art scene. Thus, in 2010 Zhang Daqian became one of the world's most frequently traded artists in the price segment above \$1.8 mln (i.e., the threshold of Skate's Top 5000). At the beginning of 2010, Zhang Daqian was represented by only two works in Skate's Top 5000 and statistically was barely different from several dozen other 20th century Chinese artists who were selling at similar prices. In a bit more than a year, the speculative Chinese market catapulted Zhang Daqian, making him the undisputed leader in this segment with a nominal market capitalization of \$97 mln and an average annual rate of return of 23.7% for repeat auction sales. During the "Chinese" auction week in early April, every fifth work sold above \$1.8 mln was created by Zhang Daqian.

Zhang Daqian's striking rise compared to his peer group of artists is very similar to the rapid growth in

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the markets for Andy Warhol, Jean-Michel Basquiat and Gerhard Richter. Does this mean that a Chinese art investment object comparable to Coca-Cola, General Electric and Siemens in terms of liquidity and investment potential has appeared? Probably not yet. Unlike China's CNPC oil monopoly and the world's largest mobile operator, China Mobile, Zhang Daqian and other most Chinese artists of his era lack an export component of ideas and images that would make it universally appealing to investors and collectors all over the world. The time test for the art market is the ability of art objects to occupy a permanent place in the pantheon of artistic heritage of world civilization, to become a part of the universal system of cultural and historical values of humanity. It remains to be seen whether Chinese artists will pass this time test.

Yet, the art market recognizes the importance of Chinese capital, and the most experienced dealers and gallery owners are trying to play a well-tested game of involving the "new bourgeoisie" (New Chinese) in the building of their own names and social roles through the patronage of the arts. But this does not mean that the global museums are willing to transfer substantial resources to Chinese contemporary art exhibitions or that international private collectors are ready to invest more time and money in the development of the Chinese cultural idea. Rather, a more natural strategy for the global establishment would be to export Western art and art market methods to China, obtaining significant income in exchange for recognition of China's economic power.

History is repeating itself, moving into a new geographic territory. Like China today, during the postwar years new industrial and financial elites in the United States attracted Europe's art elite and was the largest source of demand on the art market. Demand dominance gradually transferred into supply dominance as an American cultural environment and art market infrastructure produced and "sold to the world" names that symbolized the economic and intellectual leadership of the United States.

Today China is not the world's main art market; rather, it is the most rapidly growing source of demand standing at the T-intersection of the "Japanese" and "American" ways. If it turns to the right, strengthening its role in global politics and economics, China will be able to integrate its national culture into the modern global context for several decades, erecting its own Pollocks, Lichtensteins and Warhols (both in terms of fame and value). If it turns left, it will fall into the Japanese impasse, where artificial self-isolation, a society closed to foreigners and infantilism on the world stage have turned the Japanese miracle of the 1980s into the Japanese economic nightmare of today. This is manifested by Murakami's role as the most valuable Japanese artist of all time (only 128th in Skate's ranking) and Japanese art greatly trailing that of China, with Murakami separate from his countrymen of different ages, forgotten and out of demand.