

Sotheby's (BID) – Owned By Tim Barakett and Steve Cohen

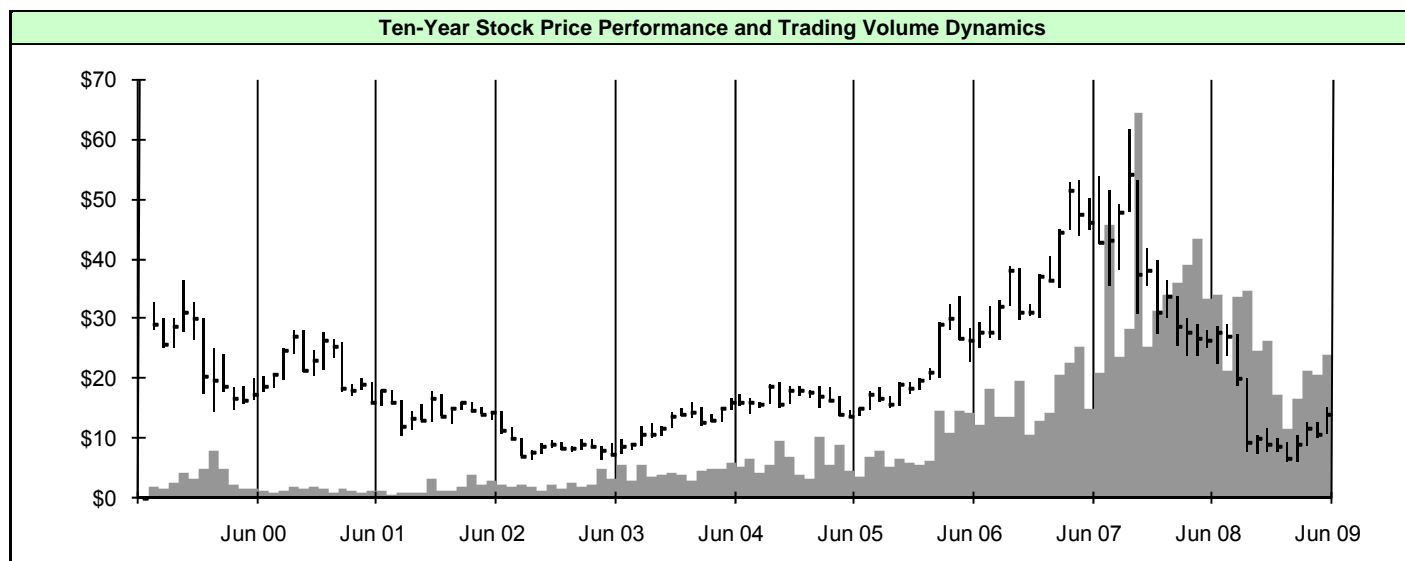
New York, NY, 212-606-7000

Services: Retail (Specialty Non-Apparel), Member of S&P MidCap 400

<http://www.sothebys.com>

Trading Data	Consensus EPS Estimates			Valuation	
Price: \$13.53 (as of 7/24/09)		Month	# of	P/E FYE 12/31/08	31.5x
52-week range: \$6.05 - \$28.98		Latest	Ago	P/E FYE 12/31/09	676.5x
Market value: \$906 million	This quarter	\$0.28	\$0.31	P/E FYE 12/31/10	48.3x
Enterprise value: \$1.4 billion	Next quarter	-0.31	-0.26	P/E FYE 12/31/11	n/a
Shares out: 67.0 million	FYE 12/31/09	0.02	0.04	EV / LTM revenue	2.2x
	FYE 12/31/10	0.28	0.28	EV / LTM EBITDA	19.8x
	FYE 12/31/11	n/a	n/a	EV / LTM EBIT	30.2x
	LT EPS growth	17.3%	17.3%	P / tangible book	1.8x
Ownership Data	Latest Quarterly EPS Surprise			Greenblatt Criteria	
Insider ownership: 3%	Date	Actual	Estimate	LTM EBIT yield	3%
Insider buys (last six months): 13	5/7/09	-\$0.53	-\$0.50	LTM pre-tax ROC	6%
Insider sales (last six months): 2					
Institutional ownership: 90%					
# of institutional owners: 375					

Operating Performance and Financial Position										
(\$ millions, except per share data)	Fiscal Years Ended							LTME	FQE	FQE
	12/31/02	12/31/03	12/31/04	12/31/05	12/31/06	12/31/07	12/31/08	3/31/09	3/31/08	3/31/09
Revenue	308	317	497	514	665	918	692	617	129	54
Gross profit	255	272	442	456	595	788	534	471	100	37
EBIT	(61)	(8)	127	120	197	276	80	46	(18)	(55)
Net income	(55)	(21)	87	62	107	213	28	6	(12)	(35)
Diluted EPS	(0.96)	(0.42)	1.00	1.02	1.73	3.25	0.43	0.08	(0.19)	(0.53)
Cash from ops	(17)	(48)	146	59	270	(37)	(176)	(180)	(161)	(165)
Capex	13	7	14	15	13	17	24	23	6	4
Free cash flow	(30)	(55)	133	44	258	(55)	(200)	(202)	(167)	(170)
Cash & investments	46	62	257	125	347	348	254	29	69	29
Total current assets	458	475	832	687	1,048	1,566	1,227	690	1,061	690
Intangible assets	13	14	14	13	48	34	18	17	36	17
Total assets	876	906	1,225	1,061	1,477	2,020	1,679	1,325	1,628	1,325
Short-term debt	0	20	0	1	0	0	0	0	100	0
Total current liabilities	448	393	620	545	789	1,075	564	247	687	247
Long-term debt	200	272	272	305	269	267	493	506	212	506
Total liabilities	735	779	989	935	1,176	1,416	1,126	806	990	806
Preferred stock	0	0	0	0	0	0	0	0	0	0
Common equity	140	127	235	126	302	604	554	519	638	519
EBIT/capital employed	-32%	-3%	53%	55%	>100%	>100%	16%	6%	n/m	n/m



BUSINESS OVERVIEW

Sotheby's, established in 1744, is one of the world's two largest auctioneers of authenticated fine art, antiques and decorative art, jewelry and collectibles.

SELECTED OPERATING DATA

FYE December 31	2006	2007	2008	1Q09 ²
Net auction sales ^{1,2} (\$mn)	3,235	4,626	4,190	200
Change (y-y)	37%	43%	-9%	-71%
Auction commissions (\$mn)	551	761	633	38
as % of net auction sales	17%	16%	15%	19%
Adjusted EBITDA ³ (\$mn)	218	314	94	-45
as % of revenue	33%	34%	14%	-82%
Loan portfolio (avg) ⁴ (\$mn)	158	171	186	158
<i>Operating expenses⁵ (\$mn):</i>				
Cost of services	63	80	95	9
Marketing	13	20	20	3
Compensation	226	294	240	48
G&A	136	167	176	30
D&A	23	22	25	5
Total opex	462	583	556	96
<i>Operating expenses as % of auction commissions:⁵</i>				
Cost of services	11%	11%	15%	24%
Marketing	2%	3%	3%	8%
Compensation	41%	39%	38%	125%
G&A	25%	22%	28%	79%
D&A	4%	3%	4%	14%
Total opex	84%	77%	88%	249%

Source: Company filings, *Manual of Ideas* analysis.

¹ Net auction sales represent the hammer (sale) price of property sold at auction excluding buyers' premium (which is currently 25% on first \$50k, 20% on next \$950k and 12% above \$1 million of the hammer price).

² Q1 net auction sales typically represent 9-14% of annual net auction sales.

³ Excludes restructuring and impairment charges and other special items.

⁴ Loan portfolio consists mainly of loans secured by works of art.

⁵ Excludes dealer cost of sales and restructuring charges.

INVESTMENT HIGHLIGHTS

- **Duopolistic industry.** Sotheby's global auction market share has ranged from 43-57% since 1989. Sotheby's and privately-held Christie's had market shares of 49% and 48%, respectively, in 2008.
- **Barriers to entry.** Client "skills" include trust, credibility, access, and fiduciary relationships. The company has significant intellectual and logistical capital, including import/export expertise, extensive appraisal history, and proprietary provenance databases that are more than one hundred years old.
- **Attractive model.** Sotheby's principally functions as an agent accepting property on consignment. As an intermediary, Sotheby's primarily derives revenue from charging the buyer a commission ("buyer's premium") based on the hammer price. This is a capital-light, high-margin business.
- **Breakeven "well below \$2 billion in net [auction] sales,"** reflecting cost savings of \$160+ million in 2009 (~30% opex reduction). Net sales of \$1 billion in 1H09 make the \$2 billion figure achievable.

THE BOTTOM LINE

Sotheby's has significant earning power and tangible asset backing. While it's impossible to predict the timing of recovery in the global art market, management's attention to cutting costs and lowering capital intensity should create value despite a soft art market. Actions could be pushed along by pressure from shareholders, which include SAC, Atticus, Ariel, and Private Capital. Any sustained art market recovery or monetization of the brand through licensing would create strong upside.

- **Well-positioned to benefit from macro trends.** Long-term wealth creation and concentration trends, especially in emerging markets, favor Sotheby's. The company's owned real estate, i.e., New York and London premises, pricing power (as evidenced by an increase in buyer's premium in June 2008, and art's status as a natural inflation hedge bode well should the dollar's purchasing power collapse.
- **High earning power, low risk of permanent loss.** With prior peak EPS of \$3+ (2007), investors can afford to wait for a recovery in auction volumes. The downside is protected due partly to \$7.50 per share of tangible equity. The owned and freehold London real estate (97,000 sq. ft) is on the books for \$36 million but may be worth \$150+ million.
- **Shares trade at 2.2x trailing revenue and 1.8x tangible book value** (earnings are expected to remain depressed at least through 2010).

INVESTMENT RISKS & CONCERNS

- **Declines in auction volumes.** With management trying to right-size the operation, another significant decline in net auction sales would lead to further losses and erosion of value. Net auctions sales were less than \$1 billion at the previous trough in 1991.
- **Sub-par cash generation and capital allocation.** Sotheby's management has proven a poor steward of capital during the boom times and has been slow to respond to the crisis. Value creation will require deeper cost cuts, a more profit-driven remuneration structure, tighter management of working capital, and overall focus on lower capital intensity.
- **Leveraged relative to cash flow, with \$506 million of debt,** including NYC mortgage debt of \$213 million. Valuable real estate, favorable debt maturity profile (earliest maturity in June 2013) and re-negotiated, undrawn \$150 million credit facility (expiring in September 2010) mitigate this risk.

MAJOR HOLDERS

CEO 1% | Other insiders 2% | Ariel 10% | Private Capital 7% | SAC 6% | Atticus 5% | Apex 5% | MAK Capital One 5%

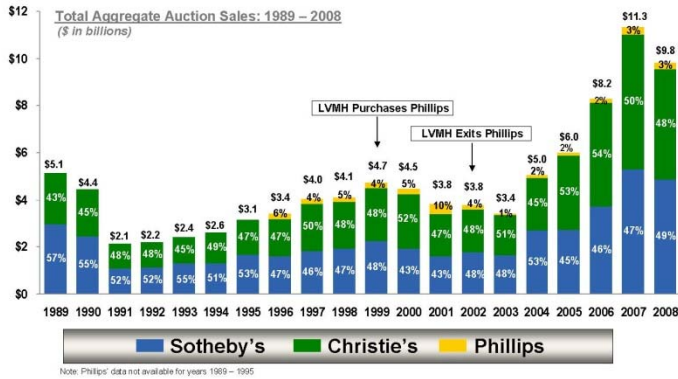
RATINGS

VALUE Intrinsic value materially higher than market value?	☆☆☆☆☆
MANAGEMENT Capable and properly incentivized?	☆☆☆
FINANCIAL STRENGTH Solid balance sheet?	☆☆
MOAT Able to sustain high returns on invested capital?	☆☆☆☆☆
EARNINGS MOMENTUM Fundamentals improving?	☆☆
MACRO Poised to benefit from economic and secular trends?	☆☆☆☆☆
EXPLOSIVENESS 5%+ probability of 5x upside in one year?	☆☆☆

...additional insight into BID:

SLIDES FROM COMPANY PRESENTATION, MAY 2009

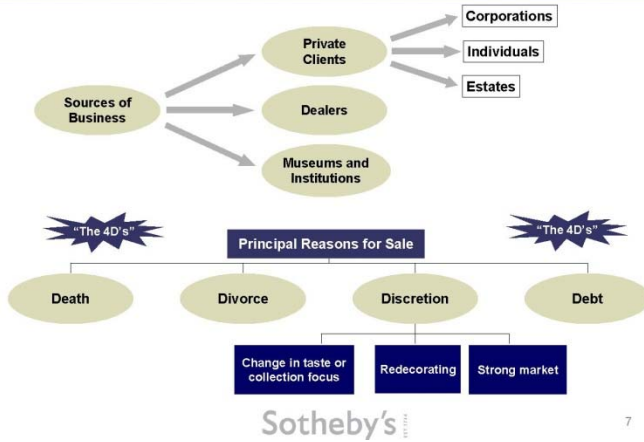
Historical Auction Market Share



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Relationships - Converting Auction Opportunities

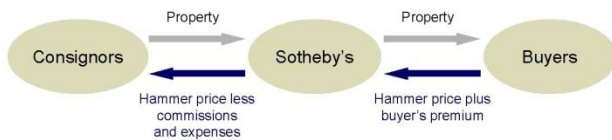


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The Auction Business Model

General Auction Transaction



"Agency Business"

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Auction Revenue Example

Hammer Price of \$1,100,000		Sotheby's Revenue	
• Buyers' Premium			
– 25% x \$50,000	=	\$12,500	
– 20% x \$950,000	=	190,000	
– 12% x \$100,000	=	12,000	
• Vendors' Commission			
– 0.5% x \$1,100,000	=	5,500	
• Recoverables	=	3,000	20% of hammer price
• Total Revenue	=	\$223,000	

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The Auction Business Model

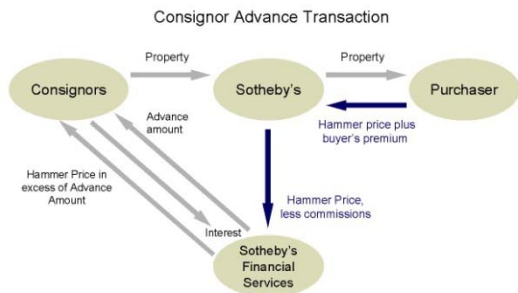


Sotheby's has dramatically curtailed the use of guarantees and only had \$1.1 million of net guarantee exposure outstanding as of February 2009.

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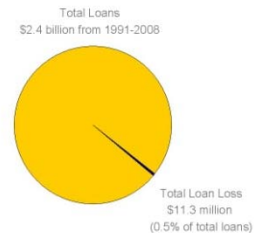


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Loan Risks and Historical Loan Loss

- Valuation appraisal error
- Macroeconomic decline
- Title defect
- Portability of collateral
- Prior liens
- Export/provenance claims
- Bankruptcy



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