



# Sotheby's

## Fourth Quarter 2015 Earnings Call

26 February, 2016

# OVERALL PERFORMANCE



	2015	2014	Variance
Consolidated Sales	\$6.72B	\$6.74B	--%
Net Auction Sales	\$5.02B	\$5.15B	(3%)
Total Revenues	\$961M	\$938M	2%
Adjusted Operating Income*	\$255M	\$268M	(5%)
Adjusted Net Income*	\$143M	\$142M	1%
Adjusted Diluted Earnings per Share*	\$2.07	\$2.03	2%

\* Non-GAAP financial measure, see Appendix

# AGENCY SEGMENT

\$ in millions	2015	2014	Variance
Auction commissions	\$719	\$758	(5%)
Private sale comm.	\$61	\$60	2%
Auction guarantees, net	(\$12)	(\$15)	25%
Other agency revenues	\$23	\$22	4%
Inventory sales	\$100	\$60	66%
<b>Total</b>	<b>\$892</b>	<b>\$885</b>	<b>1%</b>

Auction direct costs	\$85	\$80	7%
Private sale expense	\$7	\$7	(2%)
Cost of inventory sales	\$103	\$59	74%
<b>Total</b>	<b>\$195</b>	<b>\$146</b>	<b>34%</b>

Agency gross profit	\$682	\$725	(6%)
<i>Auction commission margin</i>	14.3%	14.7%	(0.4%)

- The Taubman Collection brought Net Auction Sales of \$383 million in 2015 with no related auction commission revenues. For all other sales excluding Taubman, auction commission margin was 15.5% in 2015, which is an 80 basis point increase from prior year
- Changes in f/x rates contributed \$28 million to the overall \$43 million, or 6%, decrease in agency gross profit to \$682 million in 2015 as compared to 2014
  - Excluding foreign currency impact, 2015 Agency segment gross profit decreased by \$14.7 million, or 2%.

# FINANCE SEGMENT

\$ in millions	2015	2014	Variance
Finance revenues	\$65	\$47	38%
Cost of finance revenues	\$16	\$9	81%
Finance segment gross profit	\$49	\$39	28%
Average loan portfolio	\$733	\$583	26%
Finance revenue margin	8.9%	8.1%	0.8%
Finance segment leverage ratio	79.4%	69.1%	10.3%
Finance Segment LTM Return on Equity*	14.7%	N/A	N/A

- For 2015, the average loan portfolio balance was \$733 million, a 26% increase from the prior year
- As of the end of December 2015, the period-ending loan portfolio balance was \$682 million and credit facility borrowings were \$542 million, resulting in a leverage ratio of approx. 79%
- Finance segment revenues increased \$18 million, or 38%, in 2015, reflecting the growth of the portfolio, which can be attributed to the increased ability to fund loans through revolving credit facility borrowings, the relatively low nominal interest rate environment, and the improved global reach of Sotheby's art-financing business, all of which allowed Sotheby's to fund a number of significant new term loans during the first half of the year
- Finance segment gross profit, which is net of borrowing costs, increased \$11 million, or 28%, in 2015. The overall improvement in Finance segment gross profit is partially offset by the higher cost of revolving credit facility borrowings and financing of the loan portfolio with debt, which began in February 2014 and continued throughout 2015

\* Represents the return on Finance segment net income, excluding allocated corporate overhead costs, over the last twelve months, in relation to the Average Equity in the Loan Portfolio during that period.

## SALARIES AND RELATED COSTS

\$ in millions	2015	2014	Variance
Full-time salaries	\$146	\$150	(3%)
Incentive comp. expense	\$44	\$64	(30%)
Leadership transition severance costs	\$13	--	N/A
Share-based payment expense	\$29	\$23	22%
Payroll taxes	\$20	\$24	(13%)
Employee benefits	\$30	\$30	2%
Other comp. expense	\$20	\$20	(4%)
<b>Total salaries and related costs</b>	<b>\$303</b>	<b>\$311</b>	<b>(3%)</b>

- Salaries and related costs decreased \$8 million, or 3%, in 2015 as compared to 2014 largely due to a \$19 million reduction in incentive compensation expense and changes in f/x rates
- Excluding f/x impact, salaries and related costs increased \$5.6 million, or 2%, in 2015, which is primarily due to leadership transition severance costs of \$13 million

## GENERAL AND ADMINISTRATIVE EXPENSE

\$ in millions	2015	2014	Variance
<b>Professional fees:</b>			
Operations	\$25	\$25	(1%)
Legal and compliance	\$14	\$14	(4%)
Other	\$14	\$15	(2%)
<b>Total prof. fees</b>	<b>\$53</b>	<b>\$54</b>	<b>(2%)</b>
Facilities related exp.	\$43	\$45	(4%)
Travel and entertainment	\$28	\$28	--%
Telecomm. and technology	\$9	\$9	5%
Insurance	\$6	\$6	1%
Other indirect exp.	\$20	\$17	17%
<b>Total G&amp;A expenses</b>	<b>\$159</b>	<b>\$159</b>	<b>--%</b>

- Overall G&A expense was largely flat in 2015 when compared to 2014
- Excluding f/x impact, G&A expense increased \$7 million, or 4%, in 2015, when compared to the prior year, due in part to a client authenticity claim in the second quarter (shown within other indirect expense)

# APPENDIX

## **Use of Non-GAAP Financial Measures:**

GAAP refers to generally accepted accounting principles in the United States of America. Included in this presentation are financial measures presented in accordance with GAAP and also on a non-GAAP basis. The non-GAAP financial measures used in the presentation are: Adjusted Operating Income, Adjusted Net Income, and Adjusted Diluted Earnings Per Share. Sotheby's definition of these non-GAAP financial measures is provided in the following paragraphs.

Adjusted Operating Income is defined as operating income excluding leadership transition severance costs (recorded within Salaries and Related Costs), charges related to Sotheby's voluntary separation incentive programs, CEO Separation and Transition Costs, Restructuring Charges (net), and Special Charges (net). Adjusted Net Income is defined as Net Income Attributable to Sotheby's, excluding the after-tax impact of leadership transition severance costs (recorded within Salaries and Related Costs), charges related to Sotheby's voluntary separation incentive programs, CEO Separation and Transition Costs, Restructuring Charges (net), and Special Charges (net), as well as the income tax charge associated with the repatriation of pre-2014 foreign earnings. Adjusted Diluted Earnings Per Share is defined as Diluted Earnings Per Share excluding the per share impact of leadership transition severance costs (recorded within Salaries and Related Costs), charges related to Sotheby's voluntary separation incentive programs, CEO Separation and Transition Costs, Restructuring Charges (net), Special Charges (net), and the income tax charge associated with the repatriation of pre-2014 foreign earnings.

These non-GAAP financial measures are important supplemental measures used by the Board of Directors and management in their financial and operational decision making processes, for internal reporting, and as part of Sotheby's forecasting and budgeting processes as they provide helpful measures of Sotheby's core operations. These measures allow the Board of Directors and management to view operating trends, perform analytical comparisons, and benchmark performance between periods. Management also believes that these measures may be used by securities analysts, investors, financial institutions, and other interested parties in their evaluation of Sotheby's.

Management cautions users of Sotheby's financial statements that amounts presented in accordance with its definitions of these non-GAAP financial measures may not be comparable to similar measures disclosed by other companies because not all companies and analysts calculate such measures in the same manner.

A reconciliation of Adjusted Operating Income, Adjusted Net Income, and Adjusted Diluted Earnings Per Share to the most comparable GAAP amounts is presented in the following tables.

# APPENDIX

in thousands of dollars, except per share data

	<u>Three Months Ended</u>		<u>Year Ended</u>	
	<u>December 31, 2015</u>	<u>December 31, 2014</u>	<u>December 31, 2015</u>	<u>December 31, 2014</u>
Operating income	\$ 88,566	\$ 128,991	\$ 201,721	\$ 226,044
Add: Leadership transition severance costs	3,750	—	13,251	—
Add: Voluntary separation incentive program charges	36,938	—	36,938	—
Add: CEO separation and transition costs	—	7,591	4,232	7,591
Add: Restructuring charges (net)	3	(47)	(972)	14,238
Add: Special charges (net)	—	(80)	—	20,008
Adjusted Operating Income	<u>\$ 129,257</u>	<u>\$ 136,455</u>	<u>\$ 255,170</u>	<u>\$ 267,881</u>
Variance versus prior period - \$	<u>\$ (7,198)</u>		<u>\$ (12,711)</u>	
Variance versus prior period - %	<u>(5%)</u>		<u>(5%)</u>	



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in thousands of dollars, except per share data

	<b>Three Months Ended</b>		<b>Year Ended</b>	
	<b>December 31, 2015</b>	<b>December 31, 2014</b>	<b>December 31, 2015</b>	<b>December 31, 2014</b>
Net (loss) income attributable to Sotheby's	\$ (11,153)	\$ 74,003	\$ 43,727	\$ 117,795
Add: Leadership transition severance costs, net of tax	2,326	—	8,084	—
Add: Voluntary separation incentive program charges, net of tax	23,640	—	23,640	—
Add: CEO separation and transition costs, net of tax	17	4,453	2,581	4,453
Add: Restructuring charges (net), net of tax	28	(411)	(633)	9,017
Add: Special charges (net), net of tax	—	85	—	11,133
Add: Income tax expense related to repatriation of pre-2014 foreign earnings	65,732	—	65,732	—
Adjusted Net Income	<u>\$ 80,590</u>	<u>\$ 78,130</u>	<u>\$ 143,131</u>	<u>\$ 142,398</u>
Variance versus prior period - \$	<u>\$ 2,460</u>		<u>\$ 733</u>	
Variance versus prior period - %	<u>3%</u>		<u>1%</u>	

# APPENDIX

in thousands of dollars, except per share data

	Three Months Ended		Year Ended	
	December 31, 2015	December 31, 2014	December 31, 2015	December 31, 2014
Diluted (loss) earnings per share	\$ (0.17)	\$ 1.06	\$ 0.63	\$ 1.68
Add: Leadership transition severance costs, per share	0.03	—	0.11	—
Add: Voluntary separation incentive program charges, per share	0.35	—	0.34	—
Add: CEO separation and transition costs, per share	—	0.06	0.04	0.06
Add: Restructuring charges (net), per share	—	—	(0.01)	0.13
Add: Special charges (net), per share	—	—	—	0.16
Add: Income tax expense related to repatriation of pre-2014 foreign earnings, per share	0.98	—	0.96	—
Adjusted Diluted Earnings Per Share	<u>\$ 1.19</u>	<u>\$ 1.12</u>	<u>\$ 2.07</u>	<u>\$ 2.03</u>
Variance versus prior period - \$	<u>\$ 0.07</u>		<u>\$ 0.04</u>	
Variance versus prior period - %	<u>6%</u>		<u>2%</u>	

Note: The weighted average diluted shares outstanding used for the Adjusted Diluted Earnings Per Share calculation is 66.9 million for the fourth quarter of 2015 and 68.7 million for full year 2015.