

2018

Gallery Swap

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GALLERY SWAP

DENISE SZEKELY

DECEMBER 2018

Executive Summary

In a world increasingly dominated by mega-Galleries like Zwirner and Gagosian with outposts in several continents, an international presence seems almost required for success. The rising cost of real estate in art capitals like London or New York is harming the gallery ecosystem, with less than half of the galleries reporting profitability. Smaller galleries, if they continue to run the current course, will never be able to compete with the likes of Hauser & Wirth or David Zwirner.

Art fairs are an expensive alternative to providing international reach, as they provide a small yet impersonal space in a different place for a few days, but unfortunately, the price is often exorbitant and the returns unclear. The explosion of art e-commerce sites like Artsy.com, which offer access to an international customer digitally, is another testament to the fact that everyone wants to be everywhere.

Independent galleries must come together if they want to continue to be able to attract top artist talent. Gallery Swap is one potential answer. Galleries with a space in New York, for example, should be able to share a part of their space for a period of time with a compatible gallery in Paris or London. Eight countries account for 95% of the global market: the United States, China, the United Kingdom, France, Switzerland, Germany, Italy, and Japan, and major cities in each of those would be Gallery Swap's target areas.

As a two-sided platform, like Airbnb, Uber or Etsy, Gallery Swap would need to please two key stakeholders in order to be successful: the host galleries and the visiting galleries. Even though it is the visiting gallery that pays Gallery Swap a fee to engage the host gallery, having a wide offering of different host galleries in attractive geographies is core to the company's value proposition, much like availability of host apartments is to Airbnb. The surveys I carried out to test galleries' appetite for this concept demonstrate that a critical mass

of host galleries available on the platform is essential to getting the growth engine started; nobody likes to take the first step when few others have registered. However, all galleries expressed that accessing a wider network of buyers and creating buzz locally by hosting overseas partners would add value to their businesses.

My projections contemplate ramping up the platform to host over 1,000 swaps per year after 5 years, generating \$1.4 million in revenue and \$0.6 million in EBITDA while capturing only 3% of the global number of art galleries. Given a relatively low initial invested capital of almost \$100k, Gallery Swap seems like a commercially compelling endeavor to pursue after graduation, although not without its risks. The most important risks to the model are: (1) the target customer is an independent gallery in a major city, and reports show these galleries are struggling financially, with closures outnumbering new openings; and (2) generating enough trust in the community to support deeper collaborations between galleries in far-away cities.

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Market Analysis

For a new concept such as Gallery Swap to be successful, the service must achieve product-market fit. Product-market fit, a moniker first introduced by famous venture capitalist Marc Andreessen,¹ is defined as whether the product addresses a customer's pain point.² Therefore, in envisioning Gallery Swap, I need to first contextualize what are independent galleries' most painful problems, and then evaluate if Gallery Swap addresses one or more of them.

According to the Art Basel and UBS Art Market Report, the number of gallery closures around the world in 2017 was bigger than the number of gallery openings.³ In fact, the ratio of gallery openings to closures in 2007 was 5:1, but has dropped to 0.9:1 in 2017.

This is a worrisome trend, as obviously, for many independent art galleries, cost is exceeding revenue. But what exactly is driving that?

Through my research and conversations with over a dozen NY-based gallerists, I have honed in on the following pain points:

1. Despite compelling headline growth in the fine arts market, moderately priced art pieces have underperformed relative to highly valuable art pieces

Artnet's 2018 Intelligence Report⁴ shows that the global fine arts market is growing at 19% per annum. Interestingly, the US fine arts market is the fastest growing market by far, at 49% per annum. This growth is partly being driven by increasing prices: in 2013, the average price

¹ Friend, Tad. "Tomorrow's Advance Man, Marc Andreessens Plan to Win the Future," *The New Yorker*, May 18, 2015. <https://www.newyorker.com/magazine/2015/05/18/tomorrows-advance-man>.

² Evergreen Business. Accessed October 2018, <https://medium.com/evergreen-business-weekly/product-market-fit-what-it-really-means-how-to-measure-it-and-where-to-find-it-70e746be907b>.

³ McAndrew, Clare. "The Art Market 2018," *An Art Basel & UBS Report*, https://www.ubs.com/global/en/about_ubs/art/2018/contemporary.html

⁴ Halperin, Julia. "Artnet Intelligence Report 2018," http://www.artnet.com/static/intelligence_report_290918.pdf.

of a work sold at auction was almost \$42,000; in 2017, it exceeded \$60,000, a compounded annual growth rate of 9%, which is over four times inflation over that period.

Looking at the data at a more granular level, the growth trends at higher price categories tell a different story than the lower-price categories. The fastest-growing segment comprised works priced between \$1 million and \$10 million and works priced at \$10 million and over. Both of these are growing at over 20% a year.

The slowest-growing sector, conversely, is growing at only 4% and is composed of objects priced between \$10,000 and \$100,000. Art pieces in this range make up the majority of independent art galleries' sales, while mega-galleries and auction houses sell the majority of highly valuable pieces. Not only are highly valuable art pieces growing in demand at a much faster rate, but they carry a much higher margin for the seller: the fixed costs are the same for selling a piece (shipping, labor, rent, etc.), so the higher price translates into a much better return on investment for the mega-galleries as compared to the smaller galleries.

Therefore, independent galleries feel stuck in a low-margin, low-growth segment of the fine arts market (see next pain point). The only way to succeed with low-margin product is to sell high volumes, and given their limited footprint, expanding their distribution becomes all the more important, for example through a Gallery Swap.

2. Independent galleries shoulder artist discovery costs, while the benefits are reaped by the larger galleries

Galleries generally split the sale of a work 50/50 with the artist. Galleries work closely with their artists and promote and develop their careers over time. They carry the costs of rent, marketing and promotion, installation and curating. Most importantly, they have to cover all these costs before making any sales. Galleries establish prices for the artist's work, support its production, control the supply, and act as important gatekeepers, administrators and

promoters, especially for artists that may not be well established. While there are many highly successful living artists with stable and high prices, looking at the primary market as a whole, prices tend on average to be lower and more volatile than the secondary market as it is made up of artists at various stages of their careers, with works appearing often before a consensus is established about the artist and the value of their work.

Up and coming artists generally start their careers being represented by the independent galleries, but once (and if) the artist gains recognition, she tends to switch to larger galleries that offer wider representation. As a result, smaller galleries take the first and most uncertain gambles, while the scaled galleries benefit by having their pick of the “market-tested” artists.

Taking into account that the percentage of artists in the independent galleries’ talent roster that become commercially successful is low, several gallerists pointed to the fact that the profit generated by “discovered” artists must often be re-invested in the careers of unproven artists to keep the funnel churning.

Independent galleries must find a way to internalize a greater portion of the profits generated by their talent discovery activities. If they were able to offer their artists a deeper base of potential collectors, for example through Gallery Swap, they would be able to keep the winners on the roster for longer.

3. An arms-race in art fair attendance, with declining returns, is driving increasing costs of doing business

As Julia Halperin from Artnet News reported, after asking a gallerist what he thought about attending art fairs, he responded “you can’t afford to go, but you can’t afford not to.”⁵

⁵ Halperin, Julia. “Art-Fair economics: Why Small Galleries Do Art-Fairs Even When they Don’t Make Money,” *Artnet News*, June 13, 2017. <https://news.artnet.com/market/art-fair-economics-small-galleries-gamble-989555>.

On average, a large gallery participates in five art fairs per year. These galleries reported that 46% of their sales took place at an art fair. Participating at a fair can cost anywhere between \$5,000 and \$100,000 (costs vary greatly depending on the fair, size of the booth, shipping and travel expenses).⁶ For many galleries, the cost of participating in art fairs has become their top spending category, especially when including production expenses such as building the walls, installations, lights, and other design. Such production expenses can more than double the gallery attendance fee.

The number of fairs per year has also multiplied. In 2000, there were 55 fairs worldwide according to the TEFAF 2017 Report, in 2017, that number had grown to at least 160⁷.

According to the Art Basel and UBS Art Market Report, dealers' share of sales occurring in art fairs has increased by 5% from 2016 to 46% in 2017, while overall sales only grew 4% over the same period. This means that art fairs have taken over a great part of galleries' foot traffic.

The shift has highlighted a change in buyer's habits. According to Marc Spiegler (via Bloomberg), global director of Art Basel, the explosion in art fairs can be explained by a demographic shift in wealth; patron's' wealth is more likely self-made than inherited.

Whereas before, buyers may have had time to travel the world in search of their preferred works, buyers today want to visit a space where they can efficiently be exposed to a large variety of artists, genres, and galleries, and get back to work⁸.

⁶ Halperin, Julia. Art-Fair economics: Why Small Galleries Do Art-Fairs Even When they Don't Make Money. ArtnetNews. June 13, 2017. URL: <https://news.artnet.com/market/art-fair-economics-small-galleries-gamble-989555>

⁷ Pownall, Rachel. "TEFAF Art Market Report 2017," *The European Fine Art Foundation*, <http://1uyxqn3lzdsa2ytyzjlaxmmmp.wpengine.netdna-cdn.com/wp-content/uploads/2017/03/TEFAF-Art-Market-Report-20173.pdf>

⁸ Tarmy, James. "Art Fairs are Popping Up Everywhere, Do They Make Any Money?" *Bloomberg*, March 6, 2018. <https://www.bloomberg.com/news/articles/2018-03-06/art-fairs-are-popping-up-everywhere-who-profits>

The oversaturation of art fairs has meant that independent galleries must carefully decide where to spend their limited resources, but at the same time, cannot afford not to attend as collectors are spending more time on the floors of major art fairs and less time in specific galleries.

Furthermore, dealers may find it frustrating to compare the short amount of time the art fair is open to the investment required to attend. They may also worry that their booth's location within the fair may signal inferiority to other galleries. A Gallery Swap would enable dealers to visit new markets with much lower upfront costs, and for a customizable period of time.

Competitive Analysis

Collaboration between galleries is a concept that already exists and has been successful.

Vanessa Carlos, a London based gallerist came up with the concept of Condo in 2016. It is an initiative through which London galleries lend their spaces for a month to foreign galleries to showcase their artists. The galleries join forces by promoting each other's artists, sharing contacts and sharing space. The visiting gallery does not even have to show up. They can send the art they want to exhibit and the host gallery can install and run the exhibit themselves.⁹ Condo has proven that it is an interesting new way to show artists without huge upfront costs. The organization has since expanded to other cities and had a successful run in New York last summer. Condo remains small, as the organization suggests a host and a visiting gallery to each participant. A platform would democratize this process and make it available to a wider gallery network. At Condo, shipping, insurance and installation costs are

⁹ Frieze Profiles. "In Profile: Condo. What is Condo? An interview with its founder Vanessa Carlos," Jan. 15, 2016. <https://frieze.com/article/profile-condo>

the responsibility of the visiting gallery. This would work the same at Gallery Swap, as the cost savings is in the use of the exhibition space as well as in manning the exhibit.

Vacation Gallery is another successful addition to the concept of established galleries using the space of another gallery at a different location for the length of a show. It is a gallery timeshare on new York's Lower East Side that hosts contemporary galleries from around the world on a rotating basis. During its first year in operation it is hosting galleries from L.A., San Francisco, Romania, Canada, Mexico City and Russia. It charges the visiting gallery one month's rent at cost¹⁰.

Okey-Dokey is another example of a successful gallery share program launched in Germany, in which 9 galleries from Cologne and Dusseldorf hosted galleries from Paris, New York, London and Mexico City among others.¹¹

Another innovative project which shows that the art world is looking for new business models to give galleries the option of reaching a wider audience is Cromwell Place. The project consists of the renovation of 5 adjacent townhouses in the central London neighborhood of South Kensington to convert them into flexible spaces for art related activities. There will be offices, storage facilities and gallery space. They will be available for monthly or weekly rental by international galleries or galleries located in other parts of the UK that want to be in central London for a few weeks. Galleries will pay a membership fee and a fee per meter of exhibition space. Even with fees the cost will be much lower than establishing an actual gallery in central London. Exhibition space will cost between \$3000

¹⁰ Vacation Gallery. <https://vacationgallery.nyc/> Accessed October 2018.

¹¹ Greenberger, Alex. "Okey dokey, A Gallery Share Program in the Vein of Condo to Launch in September," July 8, 2017. <http://www.artnews.com/2017/07/12/okey-dokey-a-german-gallery-share-program-in-the-vein-of-condo-to-launch-in-september/>

and \$7000 per week. It also saves gallerists the work and planning involved with a permanent space.¹²

Besides lessening costs entailed in participating in an art fair, the experience of art viewing is improved at a collaborative gallery exhibit. There is a possibility of showing more work when the space is not limited to a booth. There is more time to speak to the gallerists and also to revisit the works. The whirlwind extended weekend during which art fairs usually take place does not allow viewers to take in the works at an unhurried pace before deciding on a purchase.¹³

Competitor	Location	Term	Limitations	Cost to Attend
Gallery Swap	Global	Mutually agreed	Galleries registered on platform	\$1,000 per swap, host gallery allocated rent, plus 10% commission
Condo	NY, London, Shanghai, Mexico City, São Paulo	4 weeks	Galleries individually chosen by organization	\$700 participation fee
Vacation	New York	4-5 weeks	Space location on the Lower East Side	Rent-at- cost
Art Fair	Global	3-5 days	Booth size, location at the fair	\$5,000-\$100,000+
Cromwell Place	London	Weekly	80 galleries	\$3,000 - \$7,000 plus membership fees

¹² Cromwell Place. <https://cromwellplace.com/>. Accessed October 2018.

¹³ Carrigan, Margaret. "Done With Art Fairs, Dealers Invent New exhibition Models to liven Up Gallery Going," *Observer*, July 16, 2018. <https://observer.com/2018/07/condo-ny-shows-dealers-an-alternative-to-art-fairs/>

Business Model & Operational Plan

Gallery Swap will hone in on the aforementioned dealers' pain points to ensure that there is product-market fit. For visiting galleries, Gallery Swap seeks to offer the distribution and reach of an art fair at a lower cost and for a longer period of time. For host galleries, Gallery Swap aims to offer a way to increase buzz and foot traffic, and to lower real estate costs in upscale city locations through a synergistic sublet.

The key is collaboration between independent galleries - standing united will be the only way to compete with the mega-galleries, while continuing to perform the immensely important job of artist discovery. Collaboration through Gallery Swap can mean a lot more than simply offering a platform for transactional sharing; it can be the start of a community that shares resources and support in the same way as WeWork has been able to form an ecosystem of young, growing businesses.

Other examples of "sharing economy" businesses that demonstrate the success of sharing and collaboration include Airbnb, which enables hosts to maximize utilization of their homes, Lending Club, which enables those with surplus savings to lend peer-to-peer, and even Neighborgoods, which allows people to borrow resources directly from their neighbors.

A motif of these companies is that they are rarely the actual service provider; instead, they act as a dual sided marketplace, making the transaction possible, easy, and safe for both the provider and the user. They break down the barriers that exist to starting a business or maximizing fixed asset utilization for many people and make it both easy and lucrative to participate. In addition, the most successful examples have been able to harness the power of big data to develop algorithms that recommend new products or services to users based on their revealed preferences. I envision Gallery Swap will similarly be able to collect such data

and recommend visiting galleries new partners in other locations that are comparable in genre and clientele to previous partners.

One important chicken-or-the-egg question in dual-sided marketplaces is whether the startup should focus first on growing the demand side (its customers, or in this case, visiting galleries) or on growing the supply side (in this case, host galleries). Most research recommends focusing on growing the supply side, as the service offering becomes more attractive for customers, which join the platform organically. In fact, Airbnb focused first on growing its landlord options and Uber focused first on driver recruitment.¹⁴ Therefore, strategically, Gallery Swap will focus on making the offering highly attractive for host galleries, and bet that the demand will follow, which is why the visiting gallery pays the Swap fee.

Because dual-sided marketplaces are hard to police given the number of users, Gallery Swap will rely on the strength of reviews from both visitors and hosts to reward good users and punish bad ones, like Airbnb has been able to do. Review categories will be different between hosts and visitors, but example 1-5 star questions are: (a) host responsiveness & marketing efforts, (b) quality of location, (c) quality of space within the gallery, and (d) host commitment to selling visiting works.

Step-by-Step Operating Guide for New Members and Swaps

These are the detailed steps to register as a member of the Gallery Swap community:

1. Visit www.galleryswap.com

¹⁴Forte, Stephen. "Should You Target Demand or Supply in a Two-Sided-Market? *Redwhale*, July 5th 2016. <https://startupsventurecapital.com/should-you-target-supply-or-demand-in-a-two-sided-market-8e428bbeb29d>

2. Both hosts and visitors will fill out a registration form and upload several pictures of the gallery and the type of art exhibited. A sample form can be found in Exhibit A at the end of this section, but they center around: representative artists and works, target clientele, and details of the space and location. This step will facilitate hosts becoming visitors and vice-versa, as well as enable hosts to learn more about potential visitors.
3. Gallery Swap will offer professional photography services, for free or a subsidized fee to the first 50 galleries joining to make the platform attractive for visiting galleries.
4. Fill out a section for artist and landlord references to conduct background checks: Gallery Swap will need to verify the existence and legitimacy of each joining gallery through these calls / emails and online search. Although manual, this process will be critical in the beginning to avoid fraud or disappointing experiences with an unprofessional visiting or hosting gallery. As with all dual-sided marketplaces, Gallery Swap will be built on trust; if trust breaks down, the whole business is in jeopardy.
5. The registration form will ask for a copy of the host galleries' lease agreement and square footage available for sublet. Gallery Swap will then calculate the price of the sublet by multiplying the rent per sq. ft. of the given location times the footage available for sublet to the visiting gallery. This number will be increased by a 10% premium, to make it more attractive for hosts (the supply-side). Therefore, the hosting gallery will be able to reduce its occupancy costs with full transparency to the visiting gallery by: (days of sublet) times (area of sublet) times (occupancy cost per sq. ft. per day) times (1 + 10%).
6. If the lease agreement and background checks are satisfactory, the gallery will be admitted as a member and sent a "Congratulations" email for joining this "exclusive" community of independent galleries.

7. Member galleries that want to host must keep an up-to-date availability calendar on the site.

These are the detailed steps to complete a Gallery Swap:

1. Visit www.galleryswap.com
2. Visiting galleries will select the city they are considering *swapping* in, and be able to peruse the potential hosts that most complement or match the visiting gallery's style and ethos. There will be a map view of the hosts as well if the visiting gallery has a preference for an area within the city (e.g. Lower East Side, Upper East Side, etc.). (Although I propose the verb *swap*; however, note it is not necessarily an *exchange* of like-for-like sublet space, but rather, one gallery visiting another at one point in time).
3. The visiting gallery evaluates the occupancy costs and the amount of time it would like to *swap* for. It will be able to view the host gallery's availability calendar. If there is a match, the visiting gallery will submit its request to the host gallery.
4. The host gallery has 3 business days to review the offer, learn about the visiting gallery, and accept or reject the proposal.
5. Upon acceptance, Gallery Swap will collect a \$1,000 fee from the visiting gallery for use of the platform. Both galleries receive a "Congratulations!" email confirming the partnership, the dates, and the terms of use, duties and responsibilities of the parties, and a waiver of Gallery Swap's responsibility for success of the partnership. These legal terms will serve as a basis to avoid lawsuits and so everyone is clear.
6. The visiting gallery will also receive an email with a list of preferred logistics and installation service providers, in case they need them. Gallery Swap would collect a referral commission from the suggested logistics and installation providers if those are used.

7. The visiting gallery is responsible for paying shipping, installation, taxes, and any insurance associated with the visiting exhibition.
8. The host gallery must market the event to its clientele in the same way it would for one of its own shows, and in no event, less than two weeks ahead of time.
9. The visiting gallery conducts its installation of the works at a mutually agreeable time, or alternatively, the host gallery can charge a fee to install the works itself. Gallery Swap is not involved in these discussions.
10. The host gallery organizes an opening party for the visiting gallery, generating buzz and new foot traffic. The costs of this party are split 50-50 or in another mutually agreed upon manner. The host agrees to send pictures of the event to the visitor to demonstrate attendance if the visitor is not present. Gallery Swap will email reminders about this as well.
11. Because the visiting gallery, in most cases, will not be sending any staff to the host gallery, it will need to incent the host gallery to sell its works. Therefore, Gallery Swap will suggest that the visiting gallery pays a 10% commission to the host gallery for works sold.
12. After a successful *swap*, visitors will be responsible for taking back its unsold works and leaving the space in decent and acceptable conditions.
13. Visitors and hosts must leave each other ratings and reviews as previously discussed. Such ratings will be available on the site for future users.

To summarize, the host gallery will receive a subsidy on its rent, increased buzz and foot traffic, and a 10% commission if it sells visiting galleries' works. The visiting gallery will pay a \$1,000 swap fee, shipping, installation, and taxes, a part of the opening party costs, and the sublet / occupancy costs.

Below is a comparison between using Gallery Swap and going to a major art fair:

Visiting Gallery Cost	Gallery Swap	Major Art Fair	Visiting Gallery Revenue	Gallery Swap	Major Art Fair
Swap / Registration Fee	\$1,000	\$450	Number of Pieces Sold	5	6
Occupancy Expenses ¹	\$4,730	\$21,500	(x) Average Sales Price	\$5,000	\$5,000
Travel Costs (2 plane tickets)	–	\$1,400	Gross Revenue	\$25,000	\$30,000
Hotel Costs (4 nights)	–	\$1,000	Less: Commissions	(\$2,500)	–
Opening Party Costs	\$600	–			
Shipping	\$6,000	\$6,000			
Installation & Production	\$1,000	\$1,500			
Rental Furniture for Booth	–	\$300			
Total Costs	\$13,330	\$32,150	Net Revenue	\$22,500	\$30,000
Number of Days	30	4	Profit Before Taxes	\$9,170	(\$2,150)
Cost per Day	\$444	\$8,038	Profit per Day	\$306	(\$538)
<i>Multiple of Gallery Swap</i>	<i>1.0x</i>	<i>18.1x</i>	<i>Multiple of Gallery Swap</i>	<i>1.0x</i>	<i>(1.8x)</i>

1. For both, assumes a booth / sublet size of 430 sqft. For Gallery Swap, assumes host gallery pays \$10 / sqft / month (plus 10% premium), duration of 4 weeks. For Art Fair, assumes \$50 / sqft for the duration of the show (4 days).

As you can see in the illustrative calculations above, I assume that the average small gallery actually breaks even or loses a little money to go to the art fair. This is anecdotally what I have learned from the gallerists I have interviewed. With conservative assumptions around costs, I demonstrate that a successful gallery swap has a compelling value proposition: it costs 18x less than attending an art fair, and can be expected to generate a profit before tax of almost \$10,000. In this example, the host gallery makes \$4,730 in rent and a \$2,500 commission for a profit of \$7,230. The visiting gallery, conversely, makes a profit of \$9,170, vs. a small expected loss for attending an art fair.

Revenue Streams

Gallery Swap would generate revenue in a variety of different ways, not just the fee charged per swap.

- **Swap Fee:** Collect \$1,000 for each swap, regardless of value of works, location, or period. For the avoidance of doubt, if the visiting gallery and the host gallery want to do an actual swap, such that they are both hosts and visitors at each other's galleries at the same time, the fee would be charged twice (i.e. \$2,000).

- **Photography services:** Gallery swap will have a network of photographers that can take professional images of the Galleries that join the platform. It is very important for the visiting gallery to be able to picture their works in the space being offered. Assuming the typical photographer charges \$300 to shoot a space, Gallery Swap will charge the photographer a 10% commission for the referral (or \$30).
- **Ad space on website:** As traffic to the site grows over time, different vendors will be interested in advertising their products or services to art galleries. Notably, however, the ad space will not be offered in an obvious way which is not elegant, instead, the ad space will be presented in a way that is integrated with the structure of the site (i.e. “recommended partners” section, “providers near you” section, or other more subtle ways). The following businesses are examples that may be interested in participating on galleryswap.com:
 - Software providers for galleries (customer relationship management, inventory tracking, etc) such as Artlogic, Veevart or Masterpiece Manager
 - Shipping and logistics companies (see below)
 - Regional art fairs
- **Referrals for logistics and shipping companies:** Gallery Swap will create new business for art shipping companies such as Cadogan Tate and Crozier Arts. These companies can eventually pay Gallery Swap a commission for referrals.
- **Insurance:** Shipping companies offer insurance which will be added to shipping costs. In addition, companies such as Tata AIG and AXA Art offer different art insurance plans. Gallery Swap could also collect referral fees from insurance companies. Gallery Swap could also negotiate a policy for all its members bringing insurance costs down.

The range of offerings from Gallery Swap would also increase as soon as it gains enough momentum from economies of scale. For example, smaller galleries typically find themselves paying for short-term insurance that is proportionally pricier than a larger gallery's blanket policy. Gallery Swap contemplates the potential for negotiating such a blanket policy with insurance providers so that smaller galleries can benefit by bringing costs down. Similarly, there is scope for negotiating with shipping companies. Transport costs are the same for a \$10,000 work as a million-dollar work, however there is room for a blanket agreement once the company reaches enough scale. With scale, one could start a tender between shippers for a one-year contract for example, awarded to the best bidder.

Another service would be the possibility to provide temporary staff at discounted rates during the swap.

Challenges & Risks of the Business Model

Galleries may be apprehensive about exposing clients to other galleries: Traditionally galleries are very secretive about their client roster, and in my interviews, gallerists expressed some concern about sharing important clients with other galleries. However, this fear is misplaced, as the visiting gallery works will typically be sold by the staff at the host gallery, and in any case, the visiting gallery is based in another city, so “stealing” clients will be unlikely. In addition, galleries undertake this risk at a much larger degree when they participate in art fairs.

Galleries may fear losing their uniqueness: Galleries invest time and money in creating their brand. Visiting galleries may be concerned that the host gallery will not accurately reflect their brand and unique style. However, given the length of the show and the creative freedom the visiting gallery has guiding the installation in the sublet space, the visiting gallery will be able to keep the spark that makes them special.

Effort required to register: To ensure the trustworthiness of all involved, galleries have to enter a significant amount of information and photos to the Gallery Swap website. This commitment is necessary for the swaps to be a good experience for all involved. The new revenue stream that it can contribute towards covering real estate expenses is the real incentive for host galleries to want to be able to participate in a swap. In addition, this effort is only required once, so the marginal effort of every subsequent swap after the first one is minimal.

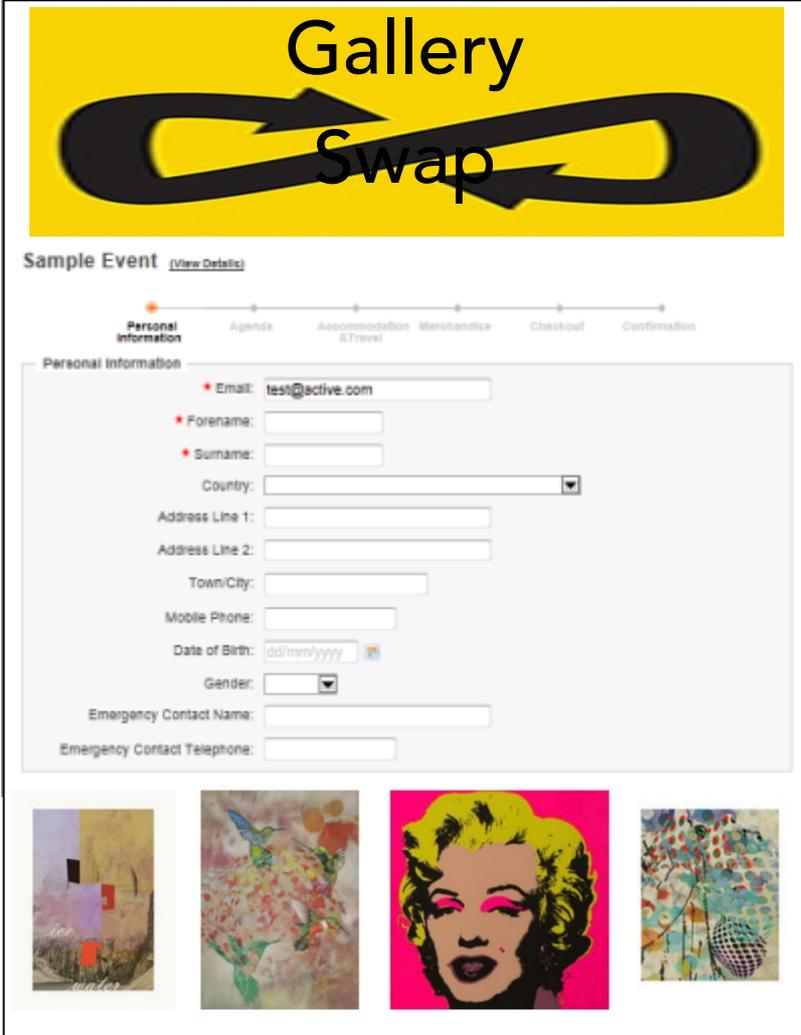
Type of works that can be swapped: Another issue that Gallery Swap needs to tackle, is that swaps might best be suited to works that can be transported easily. However, this risk is not unique to Gallery Swap, but to all art fairs.

Trust-eroding incidents: The art world is very small. Situations with bad actors can occur and quickly damage Gallery Swap's reputation. For example, a visiting gallery can provide non-authentic works, and thus damage the host gallery's image. Or a host gallery can mishandle the works and damage them in ways that insurance does not cover. In addition, host gallery staff may want to promote their own works more than those of the visiting gallery, despite the 10% commission. These risks are inherent in the business model and are not dissimilar from the trust-related risks that Airbnb or Uber had to overcome.

Exhibit A: Sample Registration Form

Fields to be populated:

- Address
- Photographs of the Gallery
- Total Sq. Ft.
- Sq. Ft available for visiting gallery
- Defining style or Gallery Program focus
- Available Dates
- Price range of works
- Pictures of the space
- Staff available
- Number of shows per year
- Contact details for Artist reference
- Landlord reference
- Lease Agreement
- Social Media



The image shows a registration form for a 'Sample Event' with a yellow header featuring the text 'Gallery Swap' and a black infinity symbol. Below the header is a progress bar with steps: Personal Information, Agents, Accommodation (Travel), Merchandise, Checkout, and Confirmation. The 'Personal Information' section is expanded and contains the following fields:

- Email:
- Forename:
- Surname:
- Country:
- Address Line 1:
- Address Line 2:
- Town/City:
- Mobile Phone:
- Date of Birth: 
- Gender:
- Emergency Contact Name:
- Emergency Contact Telephone:

Below the form are four small images of artworks: a colorful abstract painting, a painting of a hummingbird, a pop art portrait of Marilyn Monroe, and a painting of a globe with colorful dots.

Management (Why me?)

I plan to leverage my background, personal contacts, and education to push this project forward. With a law degree, a master's in Real Estate Development and a master's in Art Business, I believe I have the ideal background to be the founder of Gallery Swap. My law degrees (in Venezuela and the US) enable me to outline the potential liabilities ahead of time and introduce conflict resolution mechanisms in the swap agreements. A community based on trust will need good legal protection. My real estate knowledge, in turn, has helped me conceptualize the Gallery Swap business model, as it is, in essence, a real estate play: galleries in very upscale locations are struggling to pay rent and Gallery Swap is a way to better utilize a part of the store's square footage. Finally, my prestigious education at Sotheby's has opened a universe of galleries that was heretofore unavailable to me, and I feel I can further cultivate this network to convince the early adopters of Gallery Swap to take the risk.

I plan to recruit a part-time assistant initially to help with administrative tasks, customer service, and the website. Once the website gains traction, I would consider hiring one or two full-time positions with equity-based incentives: a marketing manager, responsible for new gallery outreach, and an operations officer, responsible for maintaining and improving the infrastructure that underlies the business, and making it possible to develop the different revenue streams mentioned above.

Most of the technical tasks like the website design will be outsourced to preserve flexibility without needing to hire a full-time developer. I will hire the software development company Art and Logic, www.artandlogic.com to develop the Gallery Swap webpage.

Go-to-Market Strategy

I believe a successful go-to-market strategy needs a step-by-step footprint. That is, unlike Condo, which went international immediately, I will seek to develop a density of participating galleries willing to host in each city so that there is an ample array to choose from for each visiting gallery before starting in a new city.

1. In order to reduce the risks outside of my control (like customs, transport over long distances, cultural differences, etc.), I will focus the first 6-12 months on targeting potential host galleries within the US. This will start with New York, LA, San Francisco, Chicago, Miami.
2. The outreach will be manual in the beginning. I will call to set up an appointment, present a slide deck with the value proposition, and offer to help them register on the site. I will also ask for referrals to other gallerists in the city, and if possible national and international ones as well to start growing the database. My aim is to add between 2 and 3 galleries per week to the membership.
3. International expansion will follow once the domestic US proof of concept is successful, with focus on Berlin, London and Paris, following the focused approach used in the US.

Marketing expenses will be for digital promotion of the platform. Ads on websites with a large number of gallery subscribers will be targeted. These include Artsy, Artnet and Instagram. Instagram is widely used by galleries. Ads on Instagram have an attractive cost of approximately \$6.70 CPM or per thousand clicks.¹⁵ Gallery Swap will use Instagram as its main advertising medium. Instagram's research shows ad recall from Instagram sponsored

¹⁵ Thrivehive. "How Much does it Cost to Advertise on Instagram?" Feb. 24, 2017. <https://thrivehive.com/how-much-does-it-cost-to-advertise-on-instagram/>

ads is 2.8x higher on average than ad recall from other social networks.¹⁶ In other words, the ads are more likely to be remembered by the target audience. Gallery Swap wants gallerists and collectors alike to engage with the platform and feel like they have heard and seen this concept before. Forrester did independent research on the platform's ads and found that consumers are 58x more likely to engage with branded content on Instagram compared to Facebook and 120x more likely compared to Twitter.¹⁷ Instagram was not only higher than other social media platforms, but the research showed that it was also higher than other channels such as email, referral traffic and paid acquisition. Lastly, because our marketing budget is limited, it is very important to make sure that the ads are being seen by the right audience, and Instagram allows just that. On Instagram, you can target by location, demographics, interests, and can also create custom audiences depending on the type of accounts the users follow.

I plan to engage a digital agency to create this high impact advertisement strategy as part of my marketing budget (which is around \$3,700 per month in the first year). This budget allows to engage even the most well-known agencies (that start at about \$1,000 per month, but the sky is the limit). An important benefit is that this can be turned down as soon as the strategy is in place and I feel like the rest of the work can be done in house (or by myself).

Gallery Swap will also present an opportunity to help galleries innovate their business models in a measurable way. As an add on service, Gallery Swap can help with the marketing of every swap, and even move upstream with innovative ideas that visiting galleries can take back home. Needless to say, they will also bring experience with them from what works well in their home markets.

¹⁶ Yotpo: "Instagram Advertising in 2018" Nov. 14, 2018.

<https://www.yotpo.com/blog/advertise-on-instagram/>

¹⁷ Forrester: "Instagram is the King of Social Engagement" Apr. 29, 2014.

<https://go.forrester.com/blogs/14-04-29-instagram-is-the-king-of-social-engagement/>

Highlights from Interviews with Gallerists

I presented the idea to a set of 20 different gallerists and conducted a survey to test the value proposition. Below is a summary of the most relevant insights gained from these conversations.¹⁸ Despite some hesitations, overall the feedback about the potential long-term was positive. However, I was unable to convince any of the gallerists to sign up for a pilot exchange. I believe this can be worked on with more time.

Josee Bienvenue from her namesake gallery, believes that a gallery swap can be successful if the gallery programs are complementary or compatible. She believes galleries are looking for new models as an alternative to fairs and their growing costs. A gallery is a physical location but also a network of contacts and clients. The biggest challenge would be for galleries that don't have anything in common to be willing to share their network of contacts and clients.

Ellie Rines from the Ceysson and Bénétierè Gallery would be hesitant to use an on-line platform that matches her with other galleries as she has worked very hard in developing her own brand and feels that she would have to sacrifice her gallery's individuality by being in a different space or hosting someone in her space. She is also concerned that if one gallery is interested in a swap and the other is not, that may affect relationships between them.

However, she also expressed that she attends art fairs regularly. Therefore, Gallery Swap may need to convince galleries with Ms. Rines' same preconceived notion that this risk is exaggerated.

Nicole Russo from the Chapter NY Gallery explained willingness to swap will vary greatly between galleries. She suggested if several galleries swap at the same time in a certain location, an energy similar to that of an art fair could be created.

¹⁸ Feedback based on email exchanges and extended conversations with the author in October and November 2018.

Rachel Rechner from Galerie Max Hetzler in Paris, thought the idea would resonate with galleries. She participated in a month-long exchange with a gallery in Berlin and then hosted the Berlin gallery in Paris. During this exchange the French and German embassies got involved, which shows the cultural significance that these exchanges can add.

Ko Sadakuni, Director of the Petzel gallery which participated in Condo New York last summer was very enthusiastic about the benefits of a gallery swap. They swapped spaces with the Nanzuka Gallery in Tokyo and both galleries had commercial success.

Financial Plan

Projecting the potential revenues of a new concept like Gallery Swap is very difficult – we must have some evidence grounded on reality to support projecting a number of swaps per year. Using a report with the total number of galleries by location, we can then assume that Gallery Swap, over five years, gains a certain % penetration of the total galleries in each city that become members. Each gallery, in turn, may do between 1 swap and potentially 3 swaps per year. Below is the analysis:

<u>Est. # of Art Galleries by Location</u>	<u># Galleries</u>	<u>Projected Gallery Swap Penetration</u>	<u>Projected Gallery Swap Members</u>	<u>Nr. Of Swaps / Year</u>	<u>Projected Market Size (# swaps)</u>
New York	1,140	20%	228	1.5	342
Los Angeles	570	15%	86	1.5	128
San Francisco	380	10%	38	1.5	57
Chicago	380	10%	38	1.5	57
Miami	190	10%	19	1.5	29
Berlin	760	10%	76	1.5	114
London	950	15%	143	1.5	214
Paris	570	15%	86	1.5	128
First Target Cities	4,940	14%	713	1.5	1,069
Other Cities in the US	3,800	2%	76	0.5	38
Other Cities in Germany	1,520	1%	15	0.5	8
Other Cities in the UK	950	1%	10	0.5	5
Other Cities in France	570	1%	6	0.5	3
Cities in Asia	1,710	1%	17	0.5	9
Other Cities Rest of World	5,510	0%	-	0.5	-
Total Market	19,000	4%	836	1.4	1,131

Source: The Global Art Gallery Report 2016 by Magnus Resch.

Taking as an example New York, our home base, there are around 1,140 art galleries. We assume that in 5 years, 20% of them, or 228 galleries, will sign up to be host or visiting galleries on Gallery Swap. We also assume that some galleries will do 1 swap per year, while others may do 2 or 3, such that the average number of swaps per year per gallery is 1.5. Therefore, the New York market represents a potential 342 swaps per year (incoming and outgoing).

For other target cities, we assume a penetration of between 10% and 15% in five years. For the non-target areas, our penetration rates are much lower (1-2%), and the average number of swaps per gallery per year is also lower (at 0.5). Adding it all together, we arrive at roughly 1,131 swaps per year as the total size of the market for Gallery Swap. This will drive our revenue assumptions.

Below are our financial projections. Assuming a target number of swaps in five years of 1,131, we ramp up to this number over time from year 1 to year 5 (that is the % achieved). The ancillary lines of revenue are very important drivers of profitability as well: we focus here on photography and shipping company referrals, and some adspace (“other”). We also assume that only half of the swaps use Gallery Swaps suggested vendors (leading to product commissions). For photography, there is a \$50 fee per referral, and for shipping referrals, the commission is much higher, at \$300. However, this is only 5% of the estimated shipping costs for the visiting gallery (\$6,000, as outlined in the Business Model section), so we are comfortable that this assumption makes commercial sense.

In addition, we assume employee payroll, marketing (and travel), IT, and rent comprise the operating costs. By year 5, there would be 2 full time employees. The model contemplates that I would not collect a salary, as the owner. My compensation would be the dividends.

We anticipate an initial investment of roughly \$90,000, which includes the initial development of the website, travel and marketing expenses for me to meet with galleries in the different cities personally and convince them to join the platform, as well as 3 months of office space rent. This amount, while not insignificant, I can raise from friends and family. In year 5, our model projects EBITDA of almost \$600,000, which represents an important return on the initial invested capital, assuming of course that the plan materializes.

ASSUMPTIONS

Fixed fee for swap	\$	1,000
Photography Commission for Referral	\$	50
Shipping Company Fee per Referral	\$	300
% of Swaps that take Referrals		50%
Other Revenue % of Swap Revenue		5%
Marketing spend % of Revenue		25%
Legal & IT spend % of Revenue		25%
Annual employee cost	\$	35,000
Office rent per year	\$	30,000

	Year 1	Year 2	Year 3	Year 4	Year 5
Target Nr. Of Swaps	1,131	1,131	1,131	1,131	1,131
<i>% Achieved</i>	<i>15%</i>	<i>35.0%</i>	<i>55.0%</i>	<i>75.0%</i>	<i>100%</i>
Total Swaps	170	396	622	848	1,131
Fee per Swap	\$ 1,000	\$ 1,000	\$ 1,000	\$ 1,000	\$ 1,000
Swap Revenue	\$ 169,575	\$ 395,675	\$ 621,775	\$ 847,875	\$ 1,130,500
Photography Referral Fees	\$ 2,120	\$ 9,892	\$ 15,544	\$ 21,197	\$ 28,263
Shipping Company Referral Fees	\$ 12,718	\$ 59,351	\$ 93,266	\$ 127,181	\$ 169,575
Other Revenue	\$ 2,120	\$ 19,784	\$ 31,089	\$ 42,394	\$ 56,525
Total Revenue	\$ 186,533	\$ 484,702	\$ 761,674	\$ 1,038,647	\$ 1,384,863
<i>Number of employees</i>	<i>1</i>	<i>1.5</i>	<i>2</i>	<i>2</i>	<i>2</i>
Employment costs	\$ 35,000	\$ 52,500	\$ 70,000	\$ 70,000	\$ 70,000
Marketing Spend	\$ 46,633	\$ 121,175	\$ 190,419	\$ 259,662	\$ 346,216
Legal & IT	\$ 46,633	\$ 121,175	\$ 190,419	\$ 259,662	\$ 346,216
Office Rent	\$ 30,000	\$ 30,000	\$ 30,000	\$ 30,000	\$ 30,000
Total costs	\$ 158,266	\$ 324,851	\$ 480,837	\$ 619,323	\$ 792,431
EBITDA	\$ 28,266	\$ 159,851	\$ 280,837	\$ 419,323	\$ 592,431

Start-Up Capital Invested

Initial IT Development	\$	30,000
Travel Expenses	\$	25,000
Marketing Expenses	\$	15,000
Legal Expenses	\$	10,000
First 3 Months Rent	\$	7,500
Total Capital Invested	\$	87,500

Cumulative Cash Flows \$ 1,480,709

Return on Investment	16.9x
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