

# Art Fund Tracker

News and analysis from the global art & collectables investment market

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### EDITOR’S LETTER

## 2010 – A Year for Investment Vehicles dedicated to Passion

As investor interest in real assets has continued to grow throughout 2010 so has the emergence of investment vehicles dedicated exclusively to luxury and passion and including more than fine art. This year we saw the launch of several new funds focused on everything from wine and violins to vintage watches, rare letters and manuscripts, many of which were featured in the **Art Fund Tracker**.

In addition to fine art, there is currently a trend toward passion investment vehicles which could provide a highly fruitful avenue for investment strategies by HNWIs particularly in the current difficult economic climate. HNWIs are expected to increasingly explore the role that real assets can play in their portfolios in 2011 through opportunistic, tactical or strategic investment. While many investment professionals agree that these assets provide diversification benefits, there has been surprisingly little research into the appropriate allocation in an investment portfolio. For example, art and collectables used in the right way can enable investors to better tailor their investment strategies to address specific financial and investment concerns (e.g. controlling volatility, boosting returns, or hedging against inflation).

There is ample precedent of the role of art, collectibles and other investments of passion as a refuge for investors during times of economic uncertainty. Bad news is good news for collectors and sellers, and so it has been for a very long time. Not only does capital flee the stock market, but economic uncertainty forces out into the market art and other passion investments that otherwise might never have changed hands. Now, as in past stock market crashes, certain sectors of the art market and collectibles can offer investors a safe haven.

The value of many collectibles actually rose during the Great Depression. During the oil crisis of 1979, coins and

other collectable prices increased dramatically. Following the stock market crash of October 1987, the Dow Jones Industrial average took 15 months to recover its pre-crash level while investors cashing out of stocks put that money to work in the art market.

Like the financial markets, investments of passion respond to multiple factors, including supply and demand, world events, global and regional economic developments, and the personal behaviour and interests of individuals. The illiquidity and inefficiency of the art and collectibles market, rather than being a detriment to performance has historically had the opposite effect. The shorter term impact of negative world circumstances is less immediate and less pronounced on art and collectibles than on most other investments.

According to the Merrill Lynch/CapGemini World Wealth Report the global art market and luxury industry segments tend to be latecomers to economic downturns. It is therefore no surprise that over a year later did they begin to see the impact from the turmoil in the financial markets. Historically, investments in fine art and other high priced collectables have been more immune to economic downturns, as their UHNW buyers tend to be less adversely affected by such trends. Meanwhile, affordable and aspirational luxury goods, which are more accessible to HNWI's as well as to less affluent individuals, may suffer more of an impact if the downturn is sustained.

Despite these concerns, analysis suggests that new wealth and growing consumer demand in Asia-Pacific, Eastern Europe and the Middle East will continue to outweigh the pressures of the economic slump. In spite of recent market turmoil, we expect this trend to continue although tempered by a demand for lower volatility as private clients become more risk averse. Statistical arbitrage and heavy quant-driven trading strategies are going to find it tough and transparency will become essential to product design. There will be aversion to anything complicated and non-transparent and, while clients will shy away from products of great complexity (e.g. they will not buy what they cannot understand) there will be growing interest in real assets such as art, wine, collectables and other investments of passion.

*Randall James Willette  
Founder and Managing Director of Fine Art Wealth  
Management*

## INTERVIEW

# The Art Fund Association becomes first professional body dedicated to Art Investment



*Randall Willette interviews Enrique Liberman, President and Founding Member of the Art Fund Association (Art FA), and discusses his motivation behind launching the first professional body dedicated exclusively to art investment vehicles.*

**RW:** Enrique, as one of the founding members of The Art Fund Association (Art FA), can you explain why you decided to establish a professional body dedicated entirely to Art Investment Funds?

**EL:** Well Randall, they say that necessity is the mother of invention. Likewise, the establishment of Art FA finds its roots in the true necessity of the association. Art investment funds have been plagued by the same problems that have affected new forms of investment vehicles over the years. We see it in articles in the press that focus on the failures of certain early players in the industry and the limited operating history of art funds, which inevitably lead to a questioning of the viability of art funds. We see it around the art world where art market participants foment misperceptions about the intentions of art funds.

Accordingly, there is an essential need for a trade association that can act as a unified voice for the art fund industry and educate both the alternative investment community and the general public as to the importance and viability of art investment funds.

Beyond educational and promotional purposes, trade associations serve an important role of bringing together the various players that will help develop and grow the art fund industry. As a focal point for interactions between art fund industry participants, Art FA is needed to foster the development of best practices within the industry that, once established, can serve as a platform by which art fund managers will form, and investors will elect to invest in, art investment funds.

**RW:** As a trade association comprised of professionals, investors, and service providers to art investment funds,

what is the primary aim of the Association and what do you hope to achieve?

*EL:* The objectives of The Art Fund Association are similar to those espoused by the trade associations of other investment vehicles. First and foremost, we seek to be advocates for the art fund industry by promoting the value of art investment vehicles and their role both in the art market and as a growing component of the alternative investment industry to the investment community, general public, media and art world. Owing to the various restrictions on the marketing and advertising of privately offered investment vehicles, the art fund industry is forced to act largely outside of the eyes of the general public, thereby creating a negative mystique around art funds and their effect upon the art market. Art FA seeks to foster greater understanding, clarity and transparency around the activities of art investment funds and their practitioners.

Second, we recognize that our efforts to promote the importance of art investment funds to the art market and alternative investment community are irrelevant if art fund practitioners themselves do not operate according to the highest ethical standards and sound business practices. Accordingly, Art FA aims to develop best practices and professional standards of conduct to guide the art fund industry as it continues to grow and mature. Such practices and codes of conduct should reflect concerns from the perspectives of both art fund managers and fund investors. To that end, Art FA is in the process of forming a “Best Practices Committee” that will work to develop what we hope will be widely-used guidelines for the governance of art investment funds.

Finally, Art FA is dedicated to the professional development of its members and those interested in the art fund industry through educational and training events. Art FA will strive to be the principal point of contact for those seeking to learn more about art investment funds and the role they play in the art world.

*RW:* I understand you are a lawyer by background and are currently a Partner at Tannenbaum Helpurn Syracuse & Hirschtritt LLP in New York, where you chair the firm’s Art Law practice. What has been your experience working with art funds to date?

*EL:* My firm and I have been fortunate to be on the forefront of the development of the art fund industry. We have counselled clients in the formation and governance of art investment funds in many different contexts and from various perspectives. We have assisted art fund managers in the formation and structuring of their art investment funds, providing advice ranging from refinements to their

investment strategies and art portfolio composition to the character and content of investor disclosures and conflicts of interest-clearing mechanisms. We have represented prospective investors in art funds in connection with their due diligence of such funds and the terms of their investments. We have also represented art fund professionals in their compensation agreements and indemnification protections from the funds they serve.

*EL:* Who else are on your Board of Directors and what are their qualifications?

The Art Fund Association is proud to be able to draw upon the knowledge and expertise of a number of art fund professionals and art market participants among the members of its Board of Directors and other advisory committees. In selecting the various representatives to the Association’s governing bodies, we look for individuals who share our belief in the viability and importance of art investment funds as an alternative investment vehicle. Such individuals come from all manner of backgrounds from art fund managers, like Javier Lumbreras of the Artemundi Global Fund, to art market consultants and fund advisers, like Michael Sellinger of Cottelston Advisors, to noted private equity investors and art collectors like Michael Shvo. We find that it is important to have representatives from all aspects of the art market relevant to the formation and governance of art funds, including art insurance providers, art dealers, auction house representatives, placement agents, fund administrators, and art appraisers.

*RW:* Clearly, you have taken the view that art funds will become a mainstream alternative investment for private and institutional investors. Explain why?

*EL:* Randall, investments in fine art will, and already should, be a part of every accredited investor’s investment portfolio. The art market is the most unregulated industry in the world. With a lack of regulation comes great opportunity to generate investment returns to those with the knowledge and contacts to navigate the industry. Moreover, the art market is undergoing dramatic changes primarily as a result of its recent globalization to encompass new collectors from around the world such as Chinese and Indian collectors. The influx of these new collectors has driven, and will continue to drive, the prices of fine art higher in the coming years. Art is also well known to be a hedge against inflation, which in light of the current monetary policies of Western central banks and the rise of collectors from nations with appreciating currencies, further supports the value of investments in fine art.

As members of the investment community recognize the importance and opportunities of art as an investment class, they will generally look to art funds and their managers to guide them in crafting a diversified investment portfolio of fine art for their investors.

*RW:* Why do you believe so few art funds have been successful until now?

*EL:* Randall, as you know, art investment funds are a relatively new investment concept that has arisen in the last 5 years. For those art funds that have been able to raise the necessary funds to launch their operations, most have had the misfortune of making their investments immediately prior to the Great Recession, which as we all know resulted in a significant price correction in the art markets and in the drying up of the credit markets. Under such circumstances, it is not surprising to see the number of existing art funds diminish since 2008.

Those seeking to launch new art investment funds have at the same time been plagued by factors that hamper all new kinds of investment structures. Prospective art fund managers, while successful art dealers and collectors, are unable to use their past performance in marketing their proposed funds to investors because running an investment fund is a different undertaking with different costs and restrictions. While not being able to highlight their own track records, they have had to instead address the failures of certain of the early entrants into the art fund space, who bought art works at too high a price or charged their funds with exorbitant and unnecessary expenses.

Unlike other alternative investments, art funds have also had to cope with the misperception that art is a “collectable” and not an asset class. This of course is contrary to the realities of the art market that, like all other asset classes, has an entire industry dedicated to its maintenance and disposition. From art dealers, auction houses, art-specific insurance products, and art leverage financiers, the art market has a level of sophistication not seen with respect to traditional collectables. Unfortunately, this misperception extends to the various investment banks and other financial institutions that have been instrumental in seeding the early endeavors of other now established asset classes, but which continue to be reluctant to fund art investment funds.

Finally, the first art fund managers were art dealers and specialists. While knowledgeable about the intricacies of the art market, they had little experience as to how to manage an investment fund, which ultimately can derail the efforts of even the best investment manager.

With all of the foregoing working against them, it is not surprising that art funds have to date met with little success, despite the potential inherent to a properly structured and managed art investment fund.

*RW:* How many art funds do you believe exist globally today and are there a sufficient number to sustain a dedicated trade association?

*EL:* Well, it really depends on what you mean by an “art fund”. At its core, an art fund is a privately offered investment fund that seeks to generate returns through the buying and selling of art. However, many different kinds of investment vehicles meet that definition. Collectors of art often partner with each other and enter into co-ownership arrangements with respect to a work or group of works. In addition, many family offices segregate and hold the family’s art collection in special purpose vehicles for the purpose of generating investment returns. Then there are art investment clubs, art pension funds for artists and other art collectives around the world that would consider themselves art funds.

It is my contention that the focus should not be on counting the number of existing funds. If the concept of an art investment fund as a viable investment vehicle is correct, then the issue is not how many funds exist today, but rather identifying and circumventing those barriers that have kept the number of art funds, whatever that number maybe, from reaching their true potential.

*RW:* As I understand it, your aim is to have worldwide membership. How do you intend to attract art fund managers globally to become a member of your association? What are the benefits of doing so for an art fund?

*EL:* We believe that the opportunities to help foster the growth and development of the art fund industry will provide art fund managers and art fund service providers with the rationale to join and actively participate in the activities of Art FA.

Specifically, members of Art FA are afforded opportunities to come together with colleagues from around the world to share their experiences and challenges, exchange ideas and information, and discuss the latest industry trends and issues. Participation in Art FA events and activities offers access to an instant peer group of influential participants in the art fund space and opportunities to interact and network with such colleagues in an atmosphere conducive to fostering new relationships and ideas.

Art FA also offers its members a complete package of services necessary to forming and operating an art

investment fund, in most cases at preferred pricing or service levels. In doing so, Art FA offers a one-stop shop for individuals contemplating either starting or investing in an art fund.

Art FA members are also afforded the opportunity to attend conferences, educational seminars, and other events focusing on the art fund industry. In addition to the valuable information to be garnered from such events, participants are also afforded powerful tools to market themselves and their organizations through speaking opportunities at and sponsorship of such events.

*RW:* Who should become a member and how do they qualify?

*EL:* Art FA is actively recruiting those organizations and individuals who believe in the concept of art funds and wish to promote the growth and development of the art fund industry. Art FA is open to membership for art investment funds and their managers, art fund attorneys, art insurance providers and brokers, art dealers, gallerists, art appraisers, accountants, placement agents and fund administrators.

In addition, Art FA provides its membership with opportunities to serve on the Association's various advisory boards and steering committees, including its Best Practices Committee that will work during 2011 to formulate and publish codes of conduct and best practices for the industry.

Those interested in becoming members should send an e-mail to [join@artfundassociation.com](mailto:join@artfundassociation.com) for more information.

*RW:* Given that there already exist a number of professional organisations globally dedicated to alternative investments (for example here in the UK we have the Alternative Investment Management Association, AIMA) why should an art fund join your trade association versus one more established?

*EL:* The established organizations you speak of promote alternative investments in general and do not extol the virtues of particular investment vehicles at the expense of others. As the newest investment vehicle that is going through the rigors and difficulties of nascent investment structures, art funds require a voice focused on promoting their unique value and characteristics.

The specific attributes inherent to the ownership and disposition of fine art are yet another reason why a generalized approach to alternative investments is not enough to promote the growth of art funds. Investments in

art are inherently different than those of other alternative investments. Accordingly, art funds require their own set of best practices that can only be crafted by individuals with experience in investing in fine art.

Finally, art market service providers (including art dealers and art appraisers) do not as a general rule attend the events of traditional investment associations. An association with an art focus is necessary to bring art market participants to the events to learn about art funds.

This is of course not to say that the art fund community should not also join other professional organizations dedicated to alternative investments. In fact, participation in such other groups will further promote art investment funds to the investment community and the general public.

*RW:* I hear that Art FA has also recently launched a charitable organization for the art fund industry. Can you tell us about it?

*EL:* With the advent of a new kind of investment vehicle, there are opportunities for those managing or servicing such vehicles to make substantial monies. Accordingly, it is only fitting that those who profit from the art fund industry give something back to the community.

This was the rationale for the foundation of "Art Funds Give Back", which is the charitable arm of Art FA. Art Funds Give Back raises money through donations from art fund market participants and the proceeds from various silent art auctions it periodically conducts to fund art education programs in primary and secondary schools around the globe. We recently had our first event at St. Stephens of Hungary School in New York, where renowned artist, Sarah Hardesty, gave a presentation to the students on decorating their own paper mache masks and Art Funds Give Back made a donation to the art education program of the school. We have similar events planned in the U.S. and around the world in countries like Haiti, Egypt and India during 2011. We hope that your readers will join us in supporting this worthy cause.