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Art & Finance Report 2021

7th edition

Solitário
Joana Vasconcelos ©Luís Vasconcelos/Courtesy Unidade Infinita Projectos - 2018

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Empower your art activities

Deloitte Private Art & Finance assists financial institutions, art businesses, collectors and cultural stakeholders with their art-related activities, and brings experience in consulting, tax, audit and business intelligence to the global art and finance ecosystem.

www.deloitte-artandfinance.com

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Introduction

00

Gardes
Luís Vasconcelos/Courtesy Unidade Infinita Projectos - 2012

Nathalie Tessier
Partner - Global Deloitte Private Leader and Global Audit & Assurance Growth Leader

Foreword

Art and collectible assets, such as fine art, classic cars, fine wine, collectible jewelry and watches, musical instruments and luxury handbags are the passion of the families that Deloitte Private serves worldwide. The wealth of ultra-high net worth individuals (UHNWIs) associated with art and collectibles was estimated at US$1,481 billion[1] in 2020, representing a sizeable portion of your or your clients' wealth. Governance, multigenerational planning, education, philanthropy, social impact, estate planning, legal agreements, asset diversification and family offices help preserve and expand the wealth and impact of your or your clients' collections.

This unique bi-annual publication aims to provide you with key insights on art and wealth management trends. You will discover that after 10 years of our analysis, art and finance is a growing and innovative industry that deserves our full attention, whatever your motivation and involvement with art and collectibles. You will understand how finance, art businesses and culture interconnect and can enable a better society. You will notice that technology, sustainability and regulation play an active role in the development of the art and finance industry. And, you will realize that the dynamic is global, spans all generations and is expanding.

Deloitte Private focuses on the specialized needs of the ultra-affluent, including families with multigenerational wealth, entrepreneurs, and closely held business owners. We understand that purpose is at the center of everything you do—fueled by core values, a strong vision, trust and legacy.

I wish you an enjoyable read of the seventh edition of the Deloitte Private Art & Finance report.

Nathalie

Nathalie Tessier FCPA, FCA, is the leader for Deloitte Private's Global practice with offices in more than 80 countries. She is a member of the Global Clients & Industries Leadership team. Deloitte Private's professionals focus on the needs of privately held companies, private equity firms, family enterprises, and high net worth individuals.

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Brise

1 Methodology: the new methodology uses Wealth-X and its reported regional UHNWI wealth (USD), which totaled US$35.45 trillion. Based on estimates from Knight Frank's Wealth Report 2020, the regional allocations to luxury investments (art, wine, cars, and jewelry) have been applied to the regional wealth figures, giving a total estimated value of art and collectibles wealth of US$1,481 billion in 2020.

Adriano Picinati di Torcello
Director – Global Art & Finance Coordinator, Deloitte Luxembourg

Anders Petterson
Managing Director, ArtTactic, London

We are delighted to present the seventh edition of the Deloitte Private Art & Finance Report

The 2021 edition of the Art & Finance report arrives at an uncertain and tumultuous time in our recent history. The world continues to feel the brunt of the COVID-19 pandemic as well as the effects of climate change, social injustice and gender inequality, to name just a few global challenges.

The question is, what role can art and culture play in tackling many of these challenges? On 30 July 2021, the G20 Ministers of Culture agreed for the first time in history on a G20 Declaration on Culture, which firmly positions culture as a major engine for sustainable socio-economic recovery in the wake of the COVID-19 pandemic.

In its modest way, the Deloitte Art & Finance initiative aims to be part of this change and transformation. Uniquely positioned at the intersection between art business, culture and finance, its goal is to elevate the dialogue between these stakeholders; encourage new models around finance and sustainable investment in art and culture; and amplify the role and importance of culture in improving our lives and society.

Since the Deloitte Art & Finance initiative was established in 2008, we have enjoyed an insightful journey with many significant moments and encounters. In 2011, we presented the first Art & Finance report during the fourth Deloitte Art & Finance conference in Miami, Florida.

After publishing seven editions of the report in collaboration with ArtTactic, our understanding of the art and finance ecosystem and its developments have greatly evolved.

We want to thank all the experts and their invaluable contributions over the years, and all the survey participants and art market stakeholders (wealth managers, collectors and art professionals) that continued to share their views and opinions on the art and finance industry. What started 10 years ago as an initial investigation into the role art could play within wealth management has gained significant momentum over the years.

We have now reached a stage where most wealth managers accept and understand the importance of art and collectibles as a strategic component of their holistic wealth management service offering. The emotional and financial value associated with art helps wealth managers create a deeper and more human relationship with their clients, allowing them to address personal, emotional and financial concerns around art and collectible wealth.

In this report, we take a unique 10-year retrospective look at our findings. It is clear that, despite challenges concerning lack of regulation and transparency, the art and finance industry continues to innovate and evolve—and is here to stay.

We hope this report will help you better understand the rich and complex nature of the art and finance ecosystem, the key drivers of change, and what role you can play in shaping its future.

Adriano Picinati di Torcello
Director – Global Art & Finance Coordinator
Deloitte Luxembourg

Anders Petterson
Managing Director
ArtTactic
London

We are honored to feature the outstanding works of renowned visual artist **Joana Vasconcelos** in this edition of the Art & Finance report. It is an immense pleasure and privilege to collaborate with her and her wonderful team.

Born in 1971, Joana Vasconcelos is a contemporary visual artist renowned for her monumental sculptures, whose 25 years of practice stretches to drawing and film. She updates the arts and crafts concept to the 21st century and incorporates everyday objects with irony and humor, bridging the domestic environment and public space while questioning the status of women, consumerism society and collective identity.

She received international acclaim at the first Venice Biennale ever curated by women with The Bride in 2005, followed by Trafaria Praia in 2013, the first floating pavilion in the Venice Biennale representing Portugal. In 2012, she became the youngest artist and only woman to ever exhibit at the Palace of Versailles, which featured a record-breaking 1.6 million visitors to become the most visited exhibition in France in 50 years. In 2018, Vasconcelos became the first Portuguese artist to exhibit at Guggenheim Bilbao with a major retrospective, one of the most visited in the museum's history and reaching fourth place in The Art Newspaper's annual exhibitions' Top 10. Her biggest show so far in the United Kingdom is currently ongoing at Yorkshire Sculpture Park until January 2022.

Pavillon de Thé
©Joana Vasconcelos - 2012

Introduction

A look back over 10 years of analysis

Since 2011, Deloitte Private and ArtTactic have published seven editions of the Art & Finance Report. This has provided us with a decade of data and research to look back on, which helps us get a better sense of what has changed and what our priorities should be going forward.

While the first five years of our research showed a gradual and steady evolution of the art and finance market, 2016 saw a significant shift in wealth managers' perception of the role and value of art and collectibles in a wealth management strategy and service offering. In 2014, only 53% of wealth managers believed art should be included as part of a wealth management service. However, this jumped to 78% in 2016, aligning the wealth management industry's opinion with those of collectors and art professionals for the first time in our analysis. This agreement has gone from strength to strength since then, with 85% of wealth managers saying so in 2021.

This suggests that the question is no longer whether art should be part of a wealth management offering, but rather how it can be implemented effectively.

The recent trends and developments covered in this report indicate that the art and finance industry will thrive from new innovations and technological advancement and adoption in the next five years, as well as a growing interest in art and collectibles. On a more macro level, there are strong signs that art and culture could become a key driver for socio-economic growth and help address many of our societal issues and challenges. This could open the art and cultural sector to a far broader spectrum of financial services, such as the growing market for impact investments, cultural bonds and new philanthropy models, which are underpinned by technology (i.e., blockchain and decentralized finance, or DeFI).

While the structure of this year's report follows previous editions, we have added two new sections dedicated to a) art and wealth protection, estate planning and philanthropy and b) culture and social impact investment and sustainability.

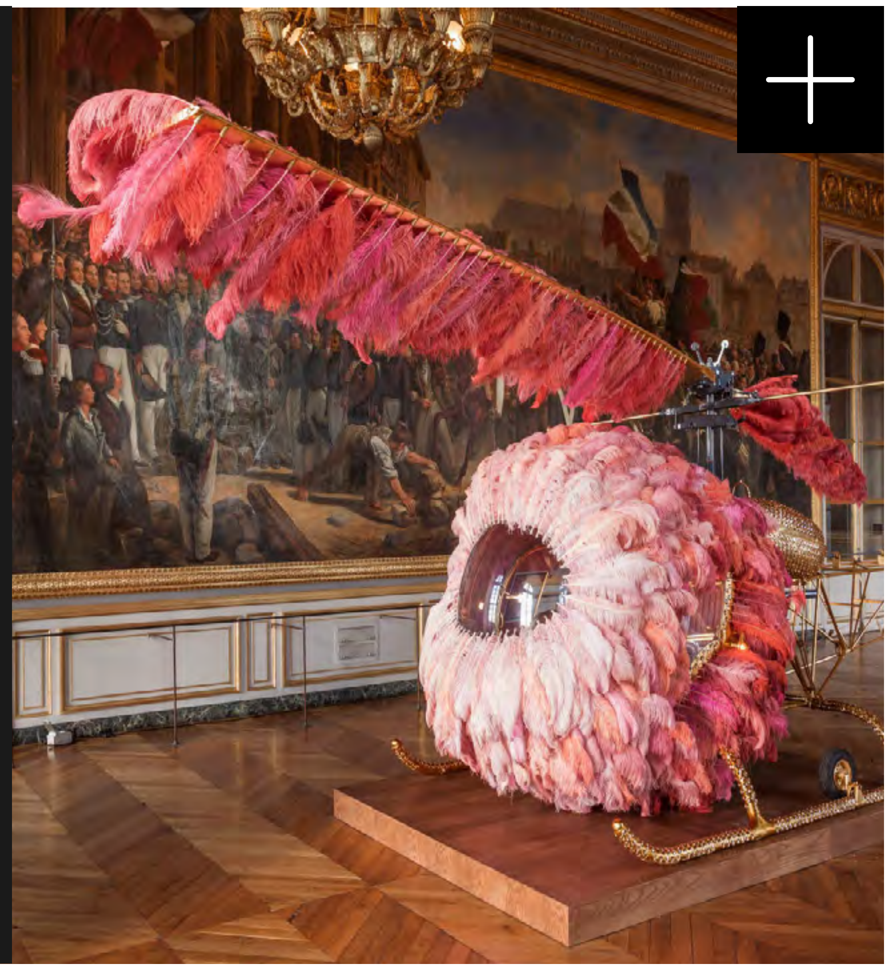
- Section 1: wealth and the global art market
- Section 2: art and wealth management survey
- Section 3: art and wealth protection, estate planning and philanthropy **(NEW)**
- Section 4: culture and social impact investment and sustainability **(NEW)**
- Section 5: art-secured lending
- Section 6: art and investment
- Section 7: art and technology
- Section 8: risk management and regulation

Also this year, we have started to differentiate between the opinions of younger collectors (under 35 years) from older collectors. This is to better capture the motivations and behavior of younger demographics, which already are and will increasingly become a force for change in the coming decade.

All previous reports can be found at www.deloitte-artandfinance.com. This year's edition is a digital version in line with our environment and energy policy, which sets out our commitments to minimizing our environmental impact.

We hope this year's report can inspire, encourage and act as a useful guide for those wishing to explore and help build a solid foundation between the visual art sector and more broadly with the creatives sectors, the cultural sector and the wealth management sector.

During the last 10 years, the role and value of art and collectibles in a wealth management strategy and service offering has evolved. The question is no longer whether art should be part of a wealth management offering, but rather how it can be implemented effectively.



Lilicoptère
©Luís Vasconcelos/Courtesy Unidade Infinita Projectos | Château de Versailles - 2012

Methodology and limitations

Figure 1. Survey sample 2021 - Geographical breakdown

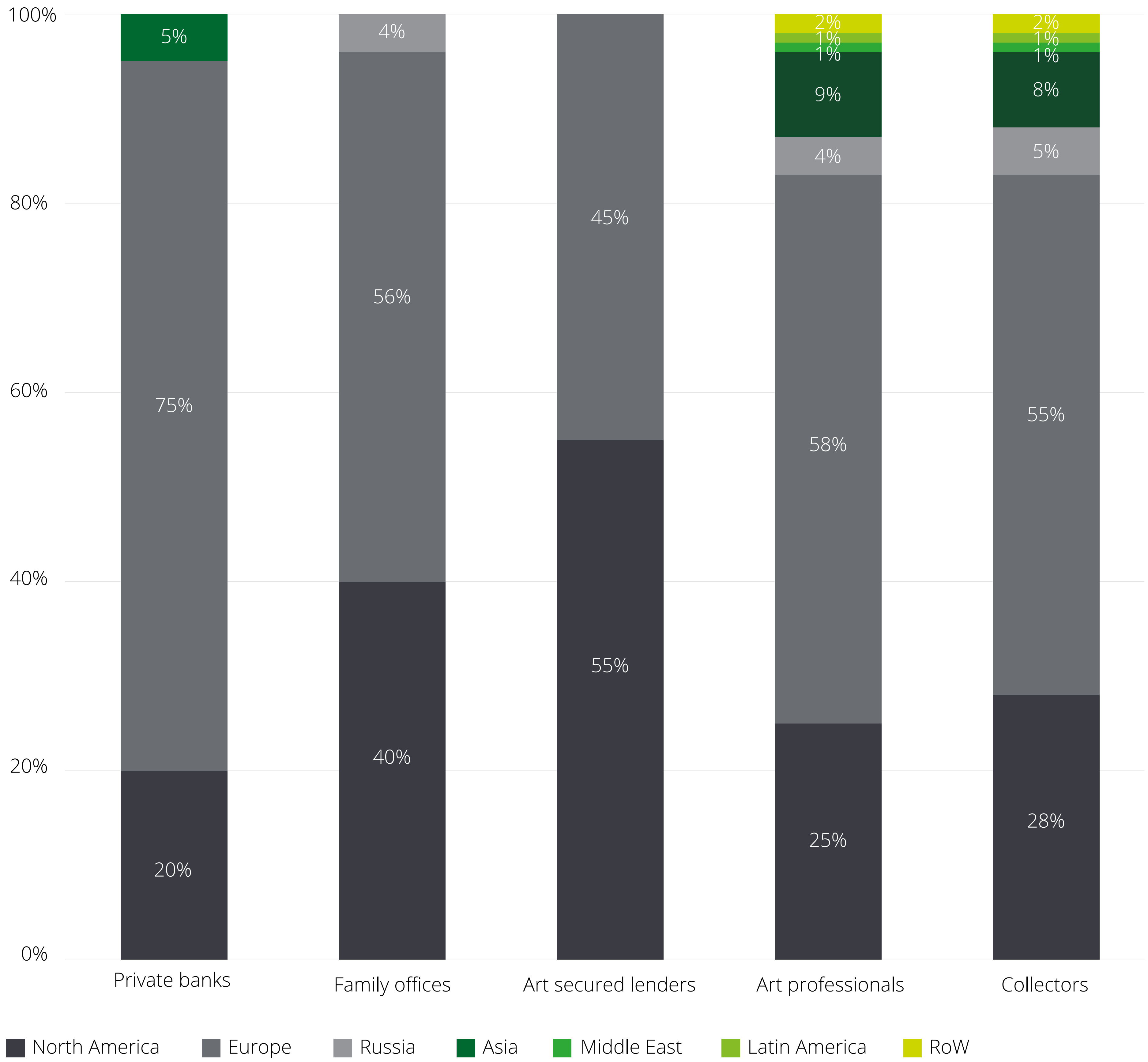


Table 1. Art & Finance report Survey participants by category

Sample	2011	2012	2014	2016	2017	2019	2021
Private banks	19	30	35	53	69	54	59
Family offices	0	0	14	14	27	25	21
Art collectors	48	81	90	94	107	105	115
Art professionals	140	112	122	126	155	138	182
Art secured lenders							11
Total	**207**	**223**	**262**	**287**	**358**	**322**	**388**

Deloitte Private and ArtTactic conducted the report's research between March 2021 and June 2021. We surveyed 59 private banks (up from 54 in 2019) and 21 family offices (down from 25 in 2019).

As in previous editions, we also surveyed important stakeholders in the art and finance industry, such as art collectors and art professionals (i.e., galleries, auction houses, art advisors, art lawyers, art insurers, art logistics specialists, etc.). A total of 182 art professionals (up from 138 in 2019) and 115 art collectors participated in the survey (up from 105 in 2019). These stakeholders from Europe, the United States, the Middle East, Latin America and Asia were surveyed on a variety of themes and topics related to art as an asset class, the role of art in a wealth management context, the impact of technology, new art investment models, as well as current and future challenges and opportunities.

Sample differences

each year's results may be affected by variations in the sample size and the geographical location of the wealth managers that responded to the survey. The first art and wealth management survey was conducted in 2011 and included 17 private banks from Luxembourg. In 2012, the sample expanded to 30 private banks, including banks from Poland and Spain. In 2014, the survey included 35 banks predominantly from Europe, the United States and Asia, and an additional 14 family offices from Europe and the United States.

In 2016, the survey included 53 private banks (38 from Europe, nine from the United States and six banks from Dubai) and 14 family offices (with eight from the United States). In 2017, we surveyed 69 private banks (of which five were art-secured lenders) and 27 family offices. In the last edition in 2019, our sample included 54 private banks and 25 family offices.

In this year's edition of the report, we surveyed 59 private banks (75% in Europe, 20% in the United States and 5% in other locations) and 21 family offices (56% in Europe, 40% in the United States and 4% in other locations). We initiated another survey among 11 art-secured lenders this year, which included four private banks and seven asset-based lenders.

We would like to express our gratitude to all the survey participants; without their support and enthusiasm, this report would not have been possible.

Deloitte Private and ArtTactic recognize that the findings are indicative and understand their limitations. However, we believe the results broadly reflect the current perceptions and attitudes of the global wealth management community, as well as art professionals and collectors.

Introduction

External data and analysis

Section 1 of the report also includes a 12-month outlook across various geographical art markets. These findings were based on a qualitative ArtTactic Art Market Confidence Survey conducted among 113 art experts in July 2021. Section 1 also features auction data analysis of various modern and contemporary art markets. This data is predominantly from Sotheby's, Christie's and Phillips, but the regional art market profiles also include other auction houses that represent major market shares in regions such as China, India, Africa and Russia. This year, we have also included data and market analysis of the nascent non-fungible token (NFT) market; this is based on data ArtTactic, non-fungible.com and CryptoSlam.

In the art investment section of the report (Section 6), we examine the performance, risk and correlation between art and other asset classes, drawing on data analysis from Artnet. For more information on the methodology used, please refer to p.15.

External contributions

In this year's edition, we are delighted to feature 72 leading experts contributing 41 articles. These provide our readers with new insights on a wide range of initiatives and models that tackle the opportunities and challenges facing the art market and the wealth management industry over the next decade. We are delighted to have collaborated with eight Deloitte offices that contributed 15 out of the 41 articles: Deloitte Luxembourg, Deloitte US, Deloitte UK, Deloitte Germany, Deloitte Japan, Deloitte Italy, Deloitte Russia and Deloitte Monaco.

The broad range and geographical diversity of these contributions align with our vision and goal to be an independent and neutral voice of the market. It also reflects our ambition to be truly international, as is the global art market itself.

Section 1

Collectibles in the time of COVID-19—how assets have weathered the pandemic,
Nannette Hechler-Fayd'herbe, Chief Investment Officer International Wealth Management and Global Head of Economics & Research, Credit Suisse AG

Japan: Race for the next art hub of Asia—tax reforms in the art market,
Yoshiyuki Umemura, Partner; Yuko Nishimura, Manager; Charlotte Lin, Senior consultant, Deloitte Japan

The State of the Art in Italy—results of the third survey on COVID-19's impacts,
Barbara Tagliaferri, Deloitte Italy Art & Finance coordinator; Roberta Ghilardi, Senior Sustainability Consultant; Mario Filice, Research & Editorial, Clients & Industries Deloitte Italy

THE 266-YEAR-OLD START-UP—an insider's view of the NFT boom,
Marcus Fox, Global Managing Director, 20th/21st C. Art, Christie's

The Brexit effect on the art market—legal aspects concerning the circulation of artworks between the EU and the UK,
Ida Palombella, Partner; Valentina Favero, Manager, Deloitte Italy

Who has fared best? Thriving in the post-Brexit art marketplace,
Simon Hornby, Senior Vice President, Crozier Europe

Growth opportunities at public auctions—key lessons for collectors trading at auctions,
Christine Bourron, CEO, Pi-Ex Ltd

Blue Champagne
Luís Vasconcelos/Courtesy Unidade Infinita Projectos | Château de Versailles - 2012

Section 2

Broadening horizons and pursuing new revenues—art advisory is no longer limited to the ultra-high net worth,
Eugenie Dumont, Art Collections Manager, Banque Degroof Petercam

Section 3

Art within wealth—a retrospective and look ahead,
Suzanne Gyorgy, Managing Director and Head of Art Advisory and Finance; Dominic Picarda, CFA, Head of Content Strategy, Citi Private Bank

New humanism and art insurance—how digitization shifts the focus of insurance in general, and art insurance in particular, towards human beings and their quality of life
Giovanni Liverani, CEO, Generali Deutschland AG Group Management Committee, Assicurazioni Generali SpA Global sponsor, ARTE Generali

The art and science of managing collectibles and luxury assets—key considerations for family offices,
Jutta Tornivaara, Director Audit & Assurance, Deloitte LLP

Philanthropy and the arts—what role can contemporary wealth management play?,
Laurent Issaurat, Head of Art Banking Services, Societe Generale Private Banking

A token gesture—can philanthropy benefit from the growth of blockchain technology?,
Bernadine Bröcker Wieder, Co-Founder & CEO, Vastari

Philanthropy & art—not as simple as it first appears
Micaela Saviano, Partner, Deloitte USA, Jared Lowe, Tax Senior Manager, Deloitte USA

Section 4

Corporate art collection as a contribution to society—by way of opening,
Alina Mukhina, Senior Manager, Tax and Legal Department, Transfer pricing services for CIS; Daria Rusanova, Manager, Deloitte Private, Deloitte Consulting LLC, Deloitte Russia

Impact investment—How art and culture can benefit from the drive towards more sustainable investment,
Anna Raginskaya, Financial Advisor, Blue Rider Group at Morgan Stanley; Bloum Cardenas, Trustee, Niki Charitable Art Foundation

From wellbeing to long-lasting cultural legacy—Therme art's social impact investment,
Mikolaj Sekutowicz, CEO, Co-Founder and Curator; Ilaria Peloso, Collections and Development Manager; Elena Fadeeva, Cultural Development and Partnerships Manager, Therme Art

So much talk, so little action... —business model innovation in the non-profit cultural sector,
Adrian Ellis, Director, AEA Consulting and Chair, Global Cultural Districts Network

Art and culture in Latin America—an opportunity for impact investing,
Carolina Biquard, Co-founder and CEO, Fundación Compromiso; Bárbara Russi, Director, Fundación Compromiso; Daniel Buchbinder, Founding Chair and CEO, Alterna; Ana Gabriela, Director of Strategic Alliances, Alterna

Social impact of culture: measuring for improving—new strategies for a more sustainable future,
Monica Palumbo, Sustainability Partner; Verdiana De' Leoni, Sustainability Senior Manager; Roberta Ghilardi, / Sustainability Senior Consultant, Deloitte Italy

The creative city dilemma—why creativity can kill cultural vitality and how to raise sustainable creative cities,
Pier Luigi Sacco, Professor of Cultural Economics, Rector Delegate for European Projects and International Networks, IULM University, Senior Researcher, OECD - CFE/LEED; Valentina Montalto, /Policy Analyst, European Commission

The cultural power of cities in a global cultural market,
Wondeur.ai Team

Section 5

Art lending in 2021—the evolution of the art wealth management space,
Dana Prussen, Vice President and Art Services Specialist; Drew Watson, Senior Vice President and Art Services Specialist, Bank of America Private Bank

Post-pandemic art financing in the non-banking market,
Joe Charalambous, President; Naomi Baigell, Managing Director, TPC Art Finance

Navigating a volatile market,
Aymeric Thuault, Director, Link Management; Aude Lemogne, Director, Link Management; Xavier Ledru, Managing Director, REYL Wealth Management

Managing liquidity risk in the art market—risk monitoring tools and the development of the art-secured lending market
Chen Chowers, Head of Operations, Overstone

Section 6

A post-pandemic look at the performance of art as an asset class,
Michaela Ben Yehuda, Senior Analyst, Business Intelligence; Robert Cacharani, Manager, Business Intelligence, artnet

The art market of the future—digital ownership of art on the blockchain,
Andreas Gerber, Head of New Business, Sygmun Bank

Security tokens + art—the FIMART value proposition,
Niccolò Filippo Veneri Savoia, CEO, Look Lateral Group

Section 7

Tipping point—the continuation of a beautiful relationship between technology and art,
Paul Lee, Partner & Global Head of Research for the technology, media, and telecommunications (TMT), Deloitte UK

The ArtTech phenomenon—technology's impact on art insurance,
Jean Gazançon, CEO, Arte Generali

Art & blockchain—unlocking new opportunities thanks to decentralized models,
Jesus Pena Garcia, Senior Manager; Giulia Pescatore, Manager, Antonio Victoria, Analyst; Kristijan Sacer, Analyst, Deloitte Luxembourg

From monetization to sector resilience—blockchain as social infrastructure?
Josephine Ayako Yamada, Manager, Deloitte Japan; Taihei Shii, CEO, Startbahn Inc; Kensuke Ito, Senior Researcher, Startbahn Inc

Cultural revolution—art's emerging digital ecosystem,
Chris Bentley, Head of Fine Art & Specie, UK & Lloyd's, AXA XL

Section 8

Transparency in the art market—are exchanges of information improving the situation?,
Pascal Noel, Director, Deloitte Monaco

Airing the laundry—direct and indirect anti-money laundering regulation of art markets
Patricia Pernes, US Counsel at Bonhams, and Michael Shepard, Deloitte's Global Financial Crime leader and a Deloitte Risk & Financial Advisory principal in Deloitte Transactions and Business Analytics LLP

Combating Financial Crime within the Art Trade—bridging provenance research and AML Compliance,
Victoire Louise Steinwachs, Manager, Deloitte Wirtschaftsprüfungsgesellschaft GmbH

What if... —financial institutions could monetize their experience in anti-money laundering while easing and securing art professionals' path towards compliance?
Maxime Heckel, Partner, Astrid Bandy, Senior Manager, Deloitte Luxembourg

Brave new media—collector risks in relation to the insurability and valuation of NFTs,
Megan Noh, Partner - Co-chair, Art Law, PRYOR CASHMAN LLP

Mitigating bankruptcy risk to artwork consignments in the United States,
Megan Noh, Partner - Co-chair, Art Law, PRYOR CASHMAN LLP

Collection management platforms: legal issues concerning the digitalization of art collections and the use of new technologies,
Ida Palombella, Partner; Federica Caretta, Director, Valentina Favero, Manager, Deloitte Italy

Key report findings 2021

Section 1
Wealth and the global art market

The rise in wealth in 2020 could find its way to the art market this year
Wealth creation in 2020 was largely immune to the global measures taken by governments and central banks to mitigate the economic impact of COVID-19. The increase of high net worth individuals (HNWIs) and their associated wealth could trigger new demand for alternative assets.

Asset diversification could drive further demand for art-related assets
The art market's ability to weather an unpredictable and unprecedented crisis has drawn further attention to art as an alternative asset class, with more collectors looking to diversify in times of heightened uncertainty.

Ultra-high net worth individuals' (UHNWIs) wealth associated with art and collectibles an estimated US$1,481 billion[2] in 2020
Art and collectibles account for a substantial portion of HNWIs' wealth and, therefore, requires services and management like any other asset.

Resilience and transformational change in the art market
Despite the severe disruption caused by the COVID-19 pandemic, the last 18 months have marked a period of transformational change in the art market, creating more resilient and innovative business models across the sector, which places the market on a better footing for future growth.

Changing landscape as the market shifts east
New York remains the dominant destination for global auction sales by Christie's, Sotheby's and Phillips. However, Hong Kong has asserted its presence with a series of record-setting auctions, positioning the market as the second most important location accelerating new developments and innovation in the region's art and finance industry.

Global online-only auction sales rocket, firmly establishing online as a strategic sales channel
The COVID-19 pandemic has catalyzed a seismic shift in online sales among the top auction houses.

Non-fungible tokens (NFTs) become an alternative art market channel
NFTs have created a new global "digital art and collectibles" market that was non-existent in the past or only accessible to a select few. It has allowed digital creators and artists to monetize their work and talent in a new and different way, and to potentially redefine the concept of ownership.

The COVID-19 pandemic has catalyzed a seismic shift in online sales among the top auction houses.

Petit Gâteau
©Luís Vasconcelos/Courtesy Unidade Infinita Projectos - 2011

2 Methodology: The new methodology uses Wealth-X and its reported regional UHNWI wealth (USD), which totaled US$35.45 trillion. Based on estimates from Knight Frank's Wealth Report 2020, the regional allocations to luxury investments (art, wine, cars, and jewelry) have been applied to the regional wealth figures, giving a total estimated value of art and collectibles wealth of US$1,481 billion in 2020.

Section 2
Art & Wealth Management Survey

A 10-year perspective
Between December 2011 and October 2021, Deloitte Private and ArtTactic published seven Art & Finance Reports. The results of our 10-year survey analysis of different art and finance stakeholders (wealth managers, collectors and art professionals) show encouraging and upward trends regarding art's role and importance in wealth management. We have seen a consolidation of the different stakeholders' narratives and motivations for including and developing art wealth management services. Client demand for art and wealth management services has grown over the last 10 years.

Turning point in 2016
six years ago, we saw a significant shift in wealth managers' perception of the role and value of art and collectibles in a wealth management strategy and service offering. **Now, the question is not so much if art should be integrated into a wealth management offering, but rather how to do it.** This interest in art and collectibles will continue as wealth managers move towards a holistic wealth management model[3].

Holistic wealth management
85% of wealth managers consider the need to develop a holistic advisory relationship with their clients as the main motivation for including art and collectibles in wealth management

Art as a capital asset
Over the last 10 years, art and collectibles have demonstrated their ability to maintain and appreciate in value, and we have seen stronger financial motivations behind art collecting. Although investment and diversification remain key drivers, the main focus in recent years has been preserving the capital allocated to art and collectible assets.

Broader spectrum of services
The spectrum of art-related wealth management services has gradually broadened over the last decade. These services fall predominantly into four categories: art and wealth protection, art and estate planning and philanthropy, art-secured lending and, to a lesser extent, art investment services. Social impact investment and culture is one of the newest trends emerging in recent years, and is likely to become an integral part of an art and wealth management service offering.

Collector needs and demand for art-related wealth management services have evolved over the last decade. The biggest interest is in collection management, estate planning and art investment services, as well as a growing need for art market research and information.

Valkyrie Crown
©Peter Mallet/Courtesy Haunch of Venison, London - 2012

3 Holistic wealth management coordinates all aspects of managing wealth

Over the last 10 years, the challenges of integrating art into wealth management remain, despite us seeing a slight improvement in recent years.

Strategic partnerships and closer relationships with art professionals
As the wealth management industry moves towards a more holistic approach regarding their service offering, over the last 10 years we have seen a strategic shift towards partnerships with external providers to deliver these services. In the context of art, a closer relationship between art professionals and wealth managers has emerged, particularly around services related to art advisory, valuation and art-secured lending.

Adapting to changing collector needs:
Collector needs and demand for art-related wealth management services have evolved over the last decade. The biggest interest is in collection management, estate planning and art investment services, as well as a growing need for art market research and information.

Younger collectors are driven by a stronger emphasis on the financial aspect of art ownership, but social impact and purpose-led investment ranks on par with the emotional value of buying art
There are signs that younger collectors are more motivated by financial considerations around art ownership compared with older art collectors.

Emotional value associated with art ownership remains key for collectors
Since we launched the survey in 2011, collectors' strongest motivation has consistently been the passion and emotional value associated with art ownership. It is an important aspect for developing deeper and more sticky client relationships in an increasingly competitive wealth management industry.

Obstacles to growth in the art and finance industry are slowly being addressed
Over the last 10 years, the challenges of integrating art into wealth management remain, despite seeing a slight improvement in recent years. The lack of regulation and transparency still dominates, but the share of wealth managers identifying these as key obstacles has decreased since 2017.

Increasing regulation in the art market could lead to a higher level of trust
With new AML regulations coming into effect this year, the broader art market was forced to comply with a new set of rules and regulations, which are likely to trigger changes in business practices.

Technology as a catalyst for future growth in art and wealth management services
The last 10 years have seen significant technological developments across all art market service areas.

Section 3.
Art wealth protection, estate planning and philanthropy

Global wealth transfer
The world is on the cusp of an unprecedented transfer of wealth: an estimated US$15 trillion[4] of wealth will be transferred to millennials and Generation Z raising important questions around art-related wealth and the next generation of art owners' tastes and priorities.

Art-related wealth requires stewardship
The preservation of artwork through wealth planning transcends tax and legal considerations.

Strong demand for research and information
Art market research and information identified as the most relevant art wealth management service.

Collection management and wealth reporting identified as the s**econd most relevant service** that wealth managers could offer.

Estate planning and art collections
Only 43% of wealth managers said their clients' estate plans sufficiently addressed their art collection (a steep decline compared with 67% in 2019). This presents an opportunity for banks to proactively identify and initiate discussions with their clients regarding their art collections.

Long-term estate planning around art is in its infancy
Very few (12%) of the collectors surveyed said they had formalized their estate documents with their estate planning advisors.

Lack of dialogue with heirs
Of the collectors who plan to leave their collection to their family, only 31% had specifically discussed the artworks they will bequeath and provided the means to care for the art.

Art and philanthropy
Cultural institutions need to rethink their reliance on traditional donations and individual-giving strategies and move towards a more purpose-led and impact-oriented giving and investment strategy, particularly as they become reliant on younger demographics.

4 Source: IQ-E, 'The Great Global Wealth Transfer', July 2020. Whitepaper, p.2.

Section 4.
Culture and social impact investment and sustainability

Culture, social impact investment and sustainability exist at the intersection between philanthropy and investment.
This is a relatively new domain for the art wealth management industry, providing wealth managers with a new client service focusing on social impact and purpose-led investment in the art and culture sector.

Investors see social investments as an opportunity, but art and culture still lag behind
According to a Global Impact Investing Network (GIIN) survey in 2020[5], 9% of respondents said they had directly invested in art and culture, but this only accounted for 0.1% of the sample assets under management (AUM).

Sustainable impact investment in the arts could become an attractive investment model
28% of collectors (50% of collectors under 35 years old) and 31% of art professionals identified sustainable impact investment in the arts as the most attractive investment model. This implies that wealth managers that expand their sustainable investment offerings are well-positioned to grow the highly attractive younger client segment in the future.

Art as a catalyst for social change and community cohesion
The power of the arts drives large-scale social change and helps tackle some of our biggest global challenges.

The cultural and creative sectors (CCS) constitute a key growth driver in many countries
While often perceived to be of little relevance to the overall economy, CCS are a key growth driver in many countries and represent some of the fastest-growing sectors in the world's economy. The United Nations (UN) has declared 2021 as the International Year of Creative Economy for Sustainable Development.

The international community has also recognized culture's role as a driver of sustainable development
The Agenda for Sustainable Development, includes several explicit references to cultural topics[6]. Cultural organizations represent a key driver for social change towards sustainable development, providing a platform for public debate and education.

There are signs the impact investment market is gradually opening up for the art and culture sector

New initiatives have been launched, such as "Creativity, Culture, and Capital: Impact investing in the global creative economy (CCC)", which aims to attract impact capital and investment to the creative economy.

Art and culture in a smart city strategy
Culture and impact investment could be influenced by the role culture can play in a smart city strategy. There is an increasing realization that urban smart cities must combine both technology and culture, because improving quality of life does not only require technology; it is also a question of connecting and inspiring people.

With the growing recognition that CCS can support cities to be "smarter", more sustainable investment products may develop
Culture impact bonds may become a reality in the future, helping develop a new generation of smart cities.

Maria Pia
©Luís Vasconcelos/Courtesy Unidade Infinita Projectos | Palácio Nacional da Ajuda, Lisbon - 2013

5 Global Impact Investing Network (GIIN) Research Institute, 'Annual Impact Investor Survey 2020', p.33.
6 In particular, SDG 11 aims to ensure that the cities of tomorrow are "inclusive, safe, resilient and sustainable" and target 11.4 focuses on protecting and safeguarding "the world's cultural and natural heritage". Moreover, the Agenda aims to ensure "inclusive and equitable quality education and promote lifelong learning opportunities for all", highlighting the importance of culture for sustainable development.

The way that collectors view their artwork has shifted in the last decade.

Brise
©Luís Vasconcelos/Courtesy Unidade Infinita Projectos - 2001

Section 5. Art-secured lending

Art-secured lending market
We conservatively estimate that the overall market size of outstanding loans against art could reach between US$24 billion and US$28.2 billion in 2021, a 10.7% average growth rate, and is expected to grow to an estimated US$31.3 billion by 2022.

The most significant change in the art wealth management space in the last 10 years
The way that collectors view their artwork has shifted in the last decade. Since 2009, we have seen the longest bull run in the history of the US stock market. The corresponding wealth effect, along with a prolonged period of low-interest rates, has fuelled the art market and benefitted collectors. In addition to collecting for aesthetic, intellectual and social reasons, collectors have increasingly been motivated by financial aspects, viewing their art as part of their overall balance sheet and a practical source of capital.

Most believe the art-secured lending market will remain niche
80% of art-secured lenders said they do not believe art-secured financing will ever become a mainstream product and that it will remain a niche market.

Jurisdictional challenges impede growth
The lack of a uniform legal framework across different global art markets, such as the uniform commercial code (UCC) in the United States, is a major impediment to growth. For example, the lack of a shared European legal framework for pledges requires a deep understanding of each European jurisdiction's specifics and legal limitations.

Demand for art-secured loans set to increase
Almost half (49%) of collectors this year said art-secured lending services were some of the most relevant services that wealth managers could offer, with 52% of art professionals echoing this view. Of the wealth managers surveyed, 74% said they expected the demand for art-secured lending services to increase in the future, with 72% of collectors and 74% of art professionals saying the same.

Section 6. Art and investment

Artnet's indices display strong short-term returns for art and more moderate returns in the long run.
Despite an unprecedented and economically tumultuous 2020, the Artnet Index for Fine Art bullishly recovered from the second half of 2020 into the first half of 2021. The index produced a 4.9% compound annual growth rate (CAGR) between 2005 and 2020, and even a mildly positive return of 0.8% from 2019 to 2020. Looking at the Fine Art market's returns trajectory, investment cycles both in the short-run and long-run depict the reliability of art as an asset class during economic turndowns.

Strong performance across most art collecting segments in the first half of 2021
All but two of the art movements monitored by Artnet have gained momentum in the first half of 2021, with indices increasing between 3% and 38% year-over-year. Two of the strongest categories were Post-War and Contemporary Art.

Art as a store of value
Art is regarded as a value-preserving asset class. The strong positive correlation between art and gold can indicate investors' perception towards art more as a value-preserving asset class than as an investment vehicle.

Direct investment and physical ownership of art remain core ownership models
Despite the increasing interest in new ownership and investment models for art and collectibles, 88% of collectors and 84% of art professionals believe that direct investment in art (i.e., the outright ownership of artwork) will be the most common form of art investment going forward, and 58% of wealth managers said the same.

New interest in alternative forms of art ownership
33% of wealth managers said their clients had expressed an increased interest in non-fungible tokens (NFTs), fractional ownership (29%), art investment funds (25%) and social impact investment in culture (21%). Interestingly, 64% of collectors said the COVID-19 pandemic had triggered a new interest in alternative art investment products, with 65% saying that NFTs had generated the most attention.

29% of wealth managers said they believed fractional ownership and tokenization of art and collectibles could become investment products of interest to their clients, with 26% of art professionals saying the same.

Younger collectors more tuned into recent developments in art investment products and services
64% of younger collectors[7] expressed a strong interest in NFTs (compared with 18% of older collectors) while 43% said fractional investment linked to artworks interested them, which is significantly higher than 17% of older collectors. During COVID-19, 86% of younger collectors had seen an increased interest in art investment products and services, compared with 61% of older collectors.

Social impact investment products
21% of wealth managers said social impact investment products in culture would be of interest to their clients (compared with 28% in 2019), with 28% of collectors and 31% of art professionals also identifying this as an area of strong interest. In line with global trends around social impact and an increasing focus on environmental, social and governance (ESG) investing, we are likely to see this interest grow in the future.

Fractional ownership and tokenization
29% of wealth managers said they believed fractional ownership and tokenization of art and collectibles could become investment products of interest to their clients, with 26% of art professionals saying the same. Collectors remain slightly more cautious, with 21% saying this would be an investment product of interest. This trend could attract a new investor base to the art market and support new philanthropic and social impact investment strategies like crowdfunding and co-ownership.

Security tokens and non-bankable art assets (nBAs)
A new financial infrastructure is developing around nBAs, which also includes art and collectibles. This could open up new opportunities for the wealth management sector to generate additional fee revenue, based on the estimated US$1,481 billion of art and collectible wealth held by ultra-high net worth individuals (UHNWIs) in 2020.

Section 7.
Art and technology

The digitalization of the art market has entered a new era
Over the last 18 months, the COVID-19 pandemic has sparked more digital innovation, experimentation and risk-taking than in the past decade alone, and the traditional art market is on the cusp of a new era, potentially redefining what it means to be a 21st-century art business.

The maturing art technology industry is a key enabler for the art and finance industry
In the art and tech ecosystem over the last 10 years, the number of specialized players addressing the various friction points faced by the art and finance industry continues to grow and gain maturity. The digital transformation sweeping the art market is likely to drive more efficiency and growth.

Technology could bring art and finance closer together
Art technology companies could help bridge the gap and address many of the current frictions between the art market and the wealth management industry.

Blockchain technology is going mainstream
Recent developments in and adoption of blockchain technology could solve many of the concerns raised by wealth managers and art market stakeholders—52% of wealth managers believe blockchain technology could have an important impact on their ability to further develop art-related services as part of their wealth management offering.

The growing market for decentralized finance (DeFi) could catalyze further integration between the art market and the wealth management industry
New developments in DeFi, such as security tokens, could accelerate wealth managers' interest in non-bankable assets like art and collectibles. This could boost the development of various art wealth management services, such as art-secured lending services, art investment, fundraising and new philanthropy models.

Collection management tools could help better integrate art in wealth reporting
53% of wealth managers said new and improved art collection management tools will help them develop an art-related wealth management service offering, and are closely associated with wealth managers' increasing focus on embedding art-related wealth in their client reporting.

Improved art due diligence tools and services
Wealth managers strongly believe that technology will improve the provenance tracking and traceability of art (80%), mitigate authenticity risks (67%), enhance valuation processes (61%) and boost the overall transparency of the art market (79%). This will facilitate a cost- and time-effective due-diligence process and could open up the market to more participants.

Most younger collectors believe technology will be a major game-changer in the art and wealth management industry
Overall, younger collectors think technological development will have a large impact on the art wealth management industry over the next two to three years.

7 The sample is based on 16 individuals out of 114 collectors surveyed in total. Although the sample size is small, these findings still highlight significant differences between the younger generation of collectors (under 35 years old) and the older generation of collectors (over 35 years old).

Section 8.
Risk management and regulation

The art market in need of rapid modernization
After 10 years of analysis, it is disconcerting that most stakeholders surveyed this year believe the art market's business processes still need modernizing, despite the acceleration of digital transformation, the growing role of technology and the increasing adoption of online markets. Although there are signs that certain problem areas are being addressed, some challenges remain. Lack of transparency, fear of price manipulation and anti-competitive behavior still linger among wealth managers' biggest concerns, alongside specific risks regarding authenticity and lack of provenance.

More government regulation may be required
Although self-regulation remains the art market's preferred approach to establish trust and credibility, it is unsurprising that more art market shareholders believe increased government regulation may now be required, as self-regulation has proven less effective. Significantly more collectors (47%) indicated their preference for government regulation this year, with 36% of art professionals saying the same. And, 44% of wealth managers this year believe government regulation would help restore trust in the art market.

Most wealth managers and art market stakeholders see transparency and regulation increasing in the art market in the next five years
One ray of hope is that 67% of wealth managers expect the art market to become more transparent and regulated over the next five years, compared with 55% of collectors and 67% of art professionals who said the same.

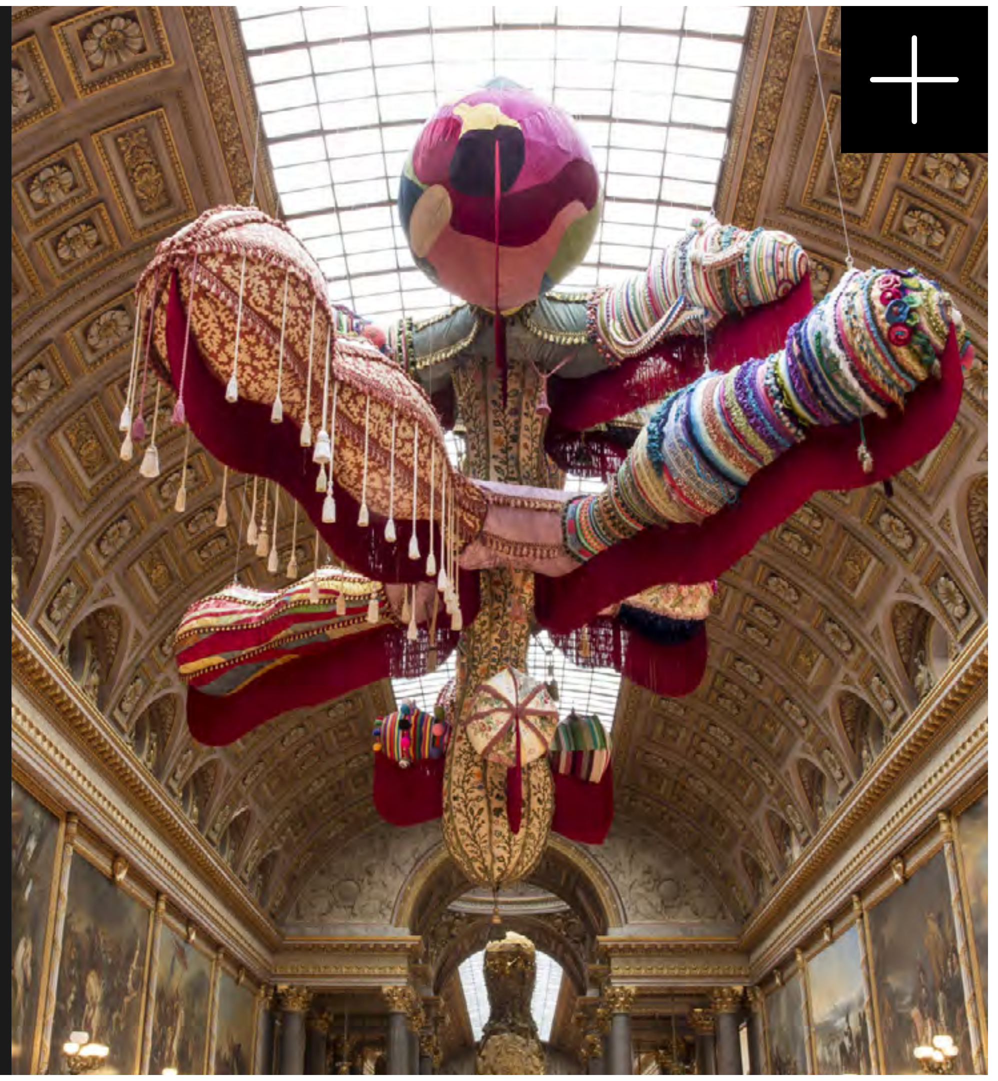
Transparency is the key to unlocking future growth in the art and finance industry and art market as a whole
83% of wealth managers said lack of transparency was a key factor that undermined trust in the art market. Both art collectors (74%) and art professionals (79%) also identified this as a major challenge.

New transparency requirements for offshore entities
New tax and anti-money laundering (AML) laws and regulations to improve transparency will affect collectors using offshore entities to buy, sell and hold art.

Money laundering remains a key concern despite new regulations
68% of wealth managers remain concerned about money laundering risks in the art market. The recent introduction of AML regulations in the European Union and the United States seems to have stemmed some wealth managers' fears. Both art collectors (65%) and art professionals (63%) continue to see money laundering as a great threat to the art market's reputation going forward.

Building trust in art market data paramount for further development of the art and finance industry going forward
The importance of trust in art market data is also essential for the future development of the art and finance industry, as it is the foundation of a robust valuation and risk management infrastructure around art and collectibles.

68% of wealth managers remain concerned about money laundering risks in the art market.



Royal Valkyrie
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Priorities

Regarding wealth managers

Art is an essential part of a wealth management offering—a strategic and collaborative approach to art and collectible wealth is required

The global wealth management industry has been evolving over the last decade—moving from an investment-focused client strategy to a holistic service offering, which addresses a broader set of client needs and assets, including art and collectibles. Over the last 10 years, we have been monitoring the evolution of clients' needs and demands for art-related wealth management services, as well as wealth managers' gradual adoption of these services. The question is no longer whether art and collectibles can play a role, but rather—how?

With UHNWI's worldwide wealth associated with art and collectibles estimated to be around US$1,481 billion in 2020 (an estimated 5% of their financial assets), there is significant scope to develop new client relationships and additional fees through wealth management services aimed at protecting, enhancing and leveraging art and collectible wealth. Wealth managers can achieve this through strategic partnerships and closer relationships with art professionals, including the growing number of art technology companies.

Like other assets, art-related wealth requires stewardship, which goes beyond tax and legal considerations. There is a higher expectation among collectors that wealth managers should offer a broader set of professional services, such as art advisory, research, valuation, collection management, estate planning, insurance, and arranging storage and security. The rationale for incorporating art in a wealth management offering is gaining traction—the last few years have seen healthy growth in the art-secured lending market, the emergence of new art investment models, and an increasing interest in social impact investment in the cultural and creative sectors.

Wealth managers repeatedly identify a lack of internal expertise as a major hurdle in developing a broader and more diverse service offering around art and collectibles. The solution is for wealth managers to work closely with art professionals and art market experts, striking the right balance between in-house services versus those outsourced to third-party experts. Sourcing expertise through reputable art professional networks and associations is vital, and with the advent of new online marketplaces matching art professionals with particular skills and expertise required by clients, we believe the wealth management sector's shortage of art-related skills and knowledge can be addressed.

Regarding the younger generation

The younger generation is a key driver for change—a new tech-focused art and wealth management strategy is needed for younger collectors

Our survey findings this year highlight distinct differences between younger collectors (aged under 35 years) and the older generation, both regarding their motivations behind art collecting and their demand for services related to art-related wealth. Younger collectors rank social impact and purpose-led investment in art as their highest motivation (alongside emotional value) at 86%, compared with 32% of older collectors. They also place a stronger emphasis on the financial aspect of art ownership.

However, the main difference between these generations of collectors lies in how these services are accessed, executed and delivered—and the importance of technology in achieving this. Overall, younger collectors believe technological development will greatly affect the art wealth management industry over the next two to three years. Most (85%) of the younger collectors surveyed stated blockchain technology could transform the way business is currently being conducted (compared with 52% of older collectors), while 85% of younger collectors believe that big data, analytics and artificial intelligence will have an impact on the art and wealth management industry going forward, significantly higher than 57% of older collectors.

Younger collectors are particularly tuned in to recent developments in art investment products and services, with 64% expressing a strong interest in NFTs (compared with 18% of older collectors) and 43% saying fractional investment linked to artworks would be of interest, significantly higher than 17% of older collectors.

To stay relevant and adapt to these new generational needs, wealth managers must align their future art-related service offering to meet these changing demands and behavioral changes, and understand the role of technology in this process.

Pavillon de Vin
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Regarding technology

Technology is and will remain a key driver of innovation and change in the art and wealth management sector over the coming years The art technology industry is maturing. Technology is already addressing many frictions in the art market, including issues around transparency, valuation, authenticity and provenance tracking. The advent of big data and artificial intelligence will likely catalyze the innovation of analytical tools, which can assist art valuation, risk monitoring and provide deeper insights and research into various aspects of art and collectible assets. These developments could also benefit existing art collection management systems and help integrate and consolidate art-related wealth data into existing wealth reporting tools. Wealth managers that partner and collaborate with collection management providers, data and research companies and new technology firms can seize the opportunity to develop a new range of tech and data-driven art-related services, which are particularly sought after by younger demographics.

Technology has also enabled new art investment and ownership models to emerge, which could attract new audiences and potential clients to the art market and the wealth management industry. The recent developments around tokenization, particularly security tokens, and the growing DeFi market could support incorporating non-bankable assets in wealth management. This could nurture new models around art-secured lending as well as philanthropy and patronage in the art market and the wealth management industry.

Technology could become the glue that binds the art market and the wealth management industry together. It could address and reduce many of today's frictions between different stakeholder groups (wealth managers, collectors and art professionals) and spark further development and growth in art wealth management services. However, technology is driving change at an exponential speed, so there is no time to waste—wealth managers must fully embrace these developments now, or risk losing a future generation of clients.

Regarding sustainability and impact investment

Impact investment in art and culture opens up new financial service models for the wealth management industry
The severe impact of the COVID-19 pandemic reset the priorities of the wealthy, sparking an increased search for meaning and purpose alongside a desire to contribute more to the world around them. For cultural institutions, the pandemic emphasized the need to shift their dependency on altruistic giving and support models towards a more purpose-led and impact-oriented giving and investment strategy. The need for this strategy shift will increase as they become more dependent on younger demographics for support.

The intersection between philanthropy and investment sees the emergence of a new space for social impact investment in art and culture. This relatively new area is likely to gain traction over the coming years, as investors shift their focus towards sustainable finance when deciding where and how to invest their wealth. Although art and culture have stayed on the fringes of what most sustainable finance investors would consider viable causes to support, the tide is now turning. Governments around the world are increasingly realizing the economic and social value of culture and creative sectors in our society.

The importance of cultural infrastructure and investment in smart city development and design strategies are being increasingly recognized, allowing new financial services related to cultural investment and finance to emerge. There are obvious opportunities for wealth managers that embrace these developments. By harnessing their existing expertise and services around sustainable investment, wealth managers are ideally positioned to drive new developments in social impact investment services around art and culture, merging collectors' growing interest in social impact investment and philanthropy.

Marilyn (AP)
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Regarding regulation

More regulation is needed: art professionals and wealth managers should take a more proactive approach to improve trust in the art market

The thorny topic of regulation has always split the art market into two camps—those who believe the market is best left to self-regulation versus those who think government intervention is required. Over the last five years, we have seen collectors shift towards a more "interventionist" approach. Almost half of the collectors surveyed this year (up from 28% in 2016) showed a strong preference for more government regulation to restore trust in the art market. To grow the art market beyond its current boundaries, it is critical to attract new audiences—and trust and transparency play an essential part in this process.

There is still plenty of work to be done, as the art market has been sluggish to evolve and adopt new business models over the last few decades. After 10 years of our Art & Finance Reports, it is worrying that most stakeholders (wealth managers, collectors and art professionals) still believe the art market needs to modernize its business practices.

Although there are some signs of improvement, with the pandemic catalyzing change and innovation, issues around transparency, trust in art market data, market manipulation, and authenticity, provenance and ownership risks are still among wealth managers' biggest concerns.

However, there seems to be light at the end of the tunnel. New regulations around ownership transparency and anti-money laundering (AML) are already affecting the art market and will force existing business practices to evolve. New technologies and data-driven art business models should also help to reduce information asymmetries and increase transparency.

Art professionals and wealth managers also play a role in this process. Wealth managers must continue to engage with art market stakeholders to help prioritize the issues that matter most to them, develop new tools, and modernize business practices that can help restore trust in the art market. This will enable more wealth managers to address their clients' art-related wealth, and help create new opportunities for closer collaborations between art professionals and wealth managers going forward.

Golden Valkyrie
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The big picture

Growth of an innovative art and finance industry

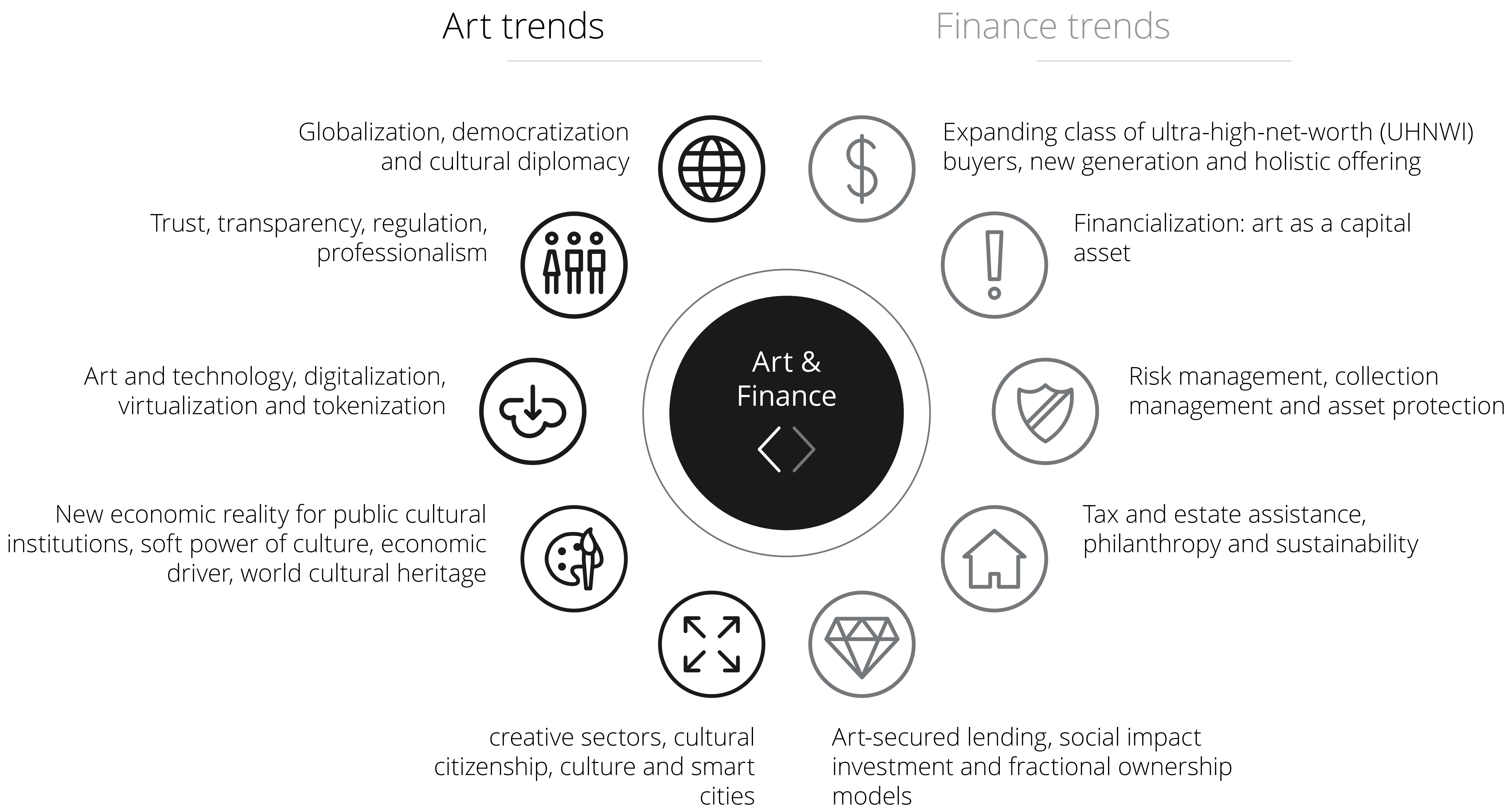
The transformation of the wealth management sector, the global art market and the cultural and creative sectors (CCS) is rapidly creating new needs and opportunities at the intersection of art and finance.

- As high-net-worth individuals seek holistic wealth management offerings;
- As art and collectible assets require the same attention as other assets;
- As a new generation introduces new values;
- As the need grows for new sustainable and innovative financial mechanisms for the culture and creative sectors;
- As purpose-led investment and innovation is increasingly demanded in the cultural sector;
- As trust, transparency and regulations rise up the agenda;
- As technology matures and offers new ways to do business;
- As culture is recognized as a major engine for sustainable socio-economic growth; and
- As all of this is part of a global phenomenon…

…there are solid elements to support the growth of an innovative art and finance industry in the years to come.

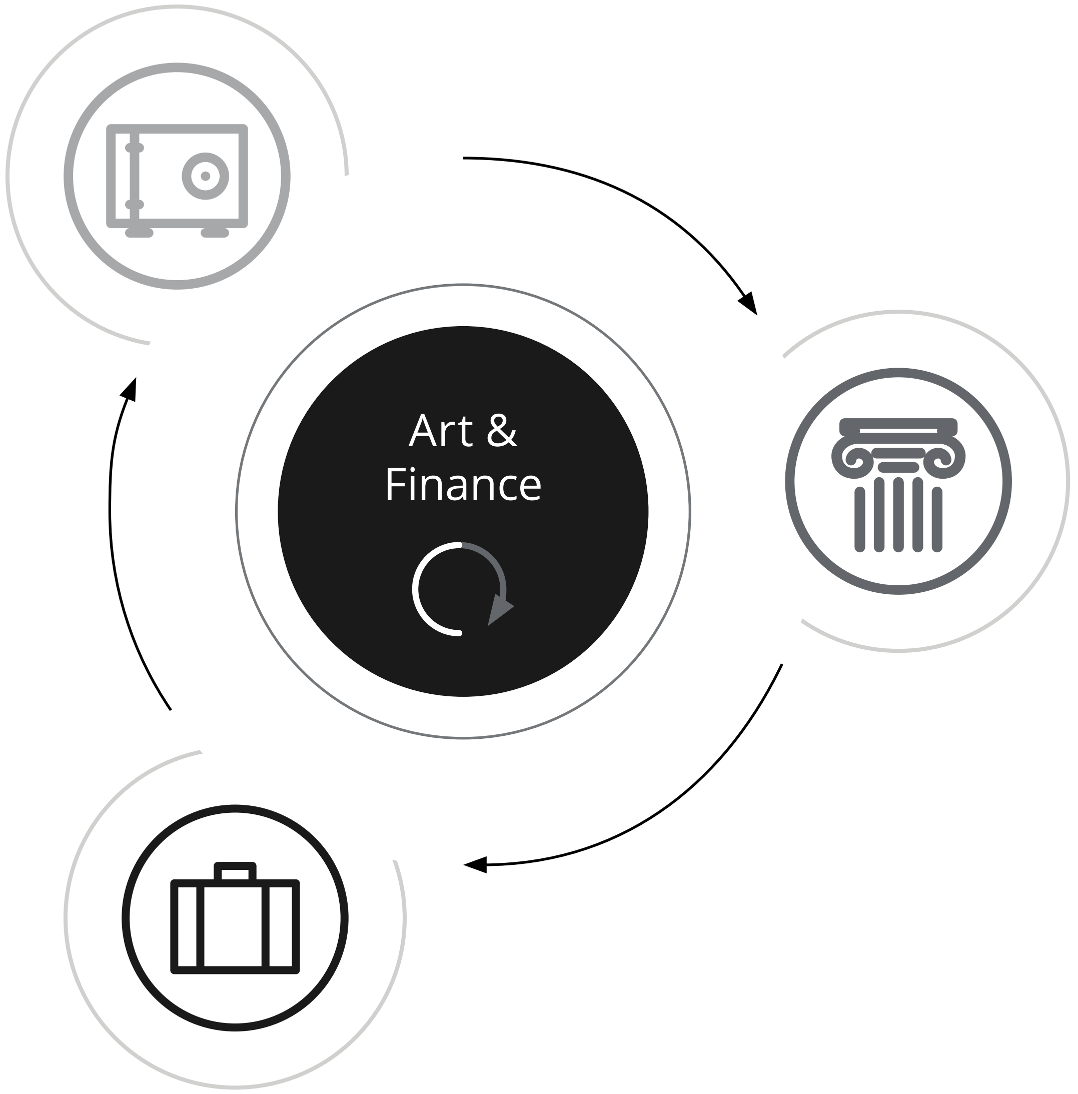
The big picture: a unique set of macro trends to a new art world

Growth of an innovative art and finance industry



Source: Deloitte & ArtTactic Art & Finance Report 7th Edition

The art and finance industry is uniquely positioned at the interesction of three interconnected sectors



Finance

- Private bankers
- Wealth managers
- Family offices
- Private investors/collectors
- Art/collectible fund promoters
- Art insurance companies
- Art trading companies
- Etc.

Culture

- Large public museums
- Private museums
- Corporate collectors
- Private collectors
- Public authorities (country, region, city, etc.)
- Etc.

Visual art sector

- Artists
- Companies selling art
- Digital art companies
- Art logistics companies
- Art fairs
- Art and media companies
- ArtTech companies
- Creative industries
- Etc.

Source: Deloitte & ArtTactic Art & Finance Report 7th Edition

Le Dauphin et La Dauphine
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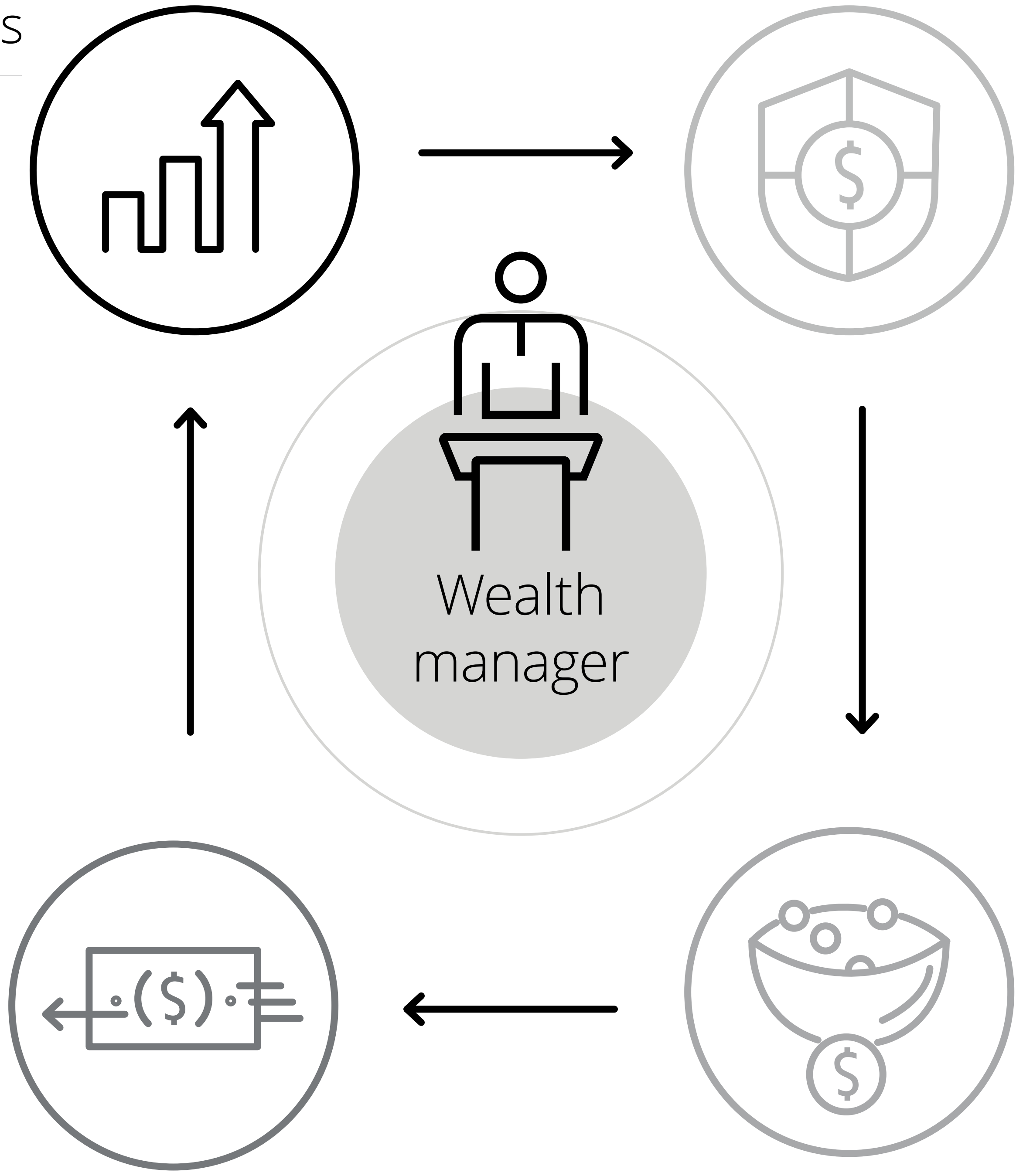
Illustration of art and wealth management services



Accumulating wealth growing assets

- Museums endowments
- Art investment
- Art funds
- Stock of art business
- Private Equity in start-ups
- Financing of art business
- Social impact investments
- Fractional investments/STOs

Protecting wealth managing risks

- Art advisory
- Valuation
- Assets consolidation
- Reporting
- Art insurance
- Reporting
- Art insurance
- Passive portfolio management
- Art collection management
- Tokenisation
- Family governance

Converting wealth to income - Creating an income stream

- Art-secured lending

Transfering wealth - Creating legacy

- Philanthropy advice
- Art related & estate planning
- Securization

Not included

- Client entertainment
- Internal education
- Art sponsoring
- Corporate collection

Wealth and the Global Art Market

01

Royal Valkyrie

Highlights

The rise in wealth in 2020 could find its way to the art market this year:
wealth creation in 2020 was largely immune to the global measures taken by governments and central banks to mitigate the economic impact of COVID-19. The increase of high net worth individuals (HNWIs) and their associated wealth could trigger new demand for alternative assets, particularly among investors looking to diversify in the face of rising inflation. Based on a recent report from Credit Suisse, 2020 marks the year when, for the first time, more than 1% of all global adults are in nominal terms US dollar millionaires[1]. These now number 56.1 million, or 1.1% of all adults, up 5.2 million from a year earlier[2].

Asset diversification could drive further demand for art-related assets:
the art market's ability to weather an unpredictable and unprecedented crisis has drawn further attention to art as an alternative asset class, with more collectors looking to diversify in times of heightened uncertainty. Of the collectors surveyed, 40% said portfolio and asset diversification was one of the key reasons they bought art, and 70% said this was one of the strongest arguments for why art should be included in a wealth management service offering.

Ultra-high net worth individuals' (UHNWIs) wealth associated with art and collectibles an estimated US$1,481 trillion[3] in 2020:
art and collectibles account for a substantial portion of HNWIs' wealth and, therefore, requires services and management like any other asset. Building a service offering around art-related wealth can help create new client experiences and develop a stronger personal and emotional connection with clients. New developments around tokenization of non-bankable assets could allow art and collectibles assets to be more easily integrated into an asset management allocation strategy.

Resilience and transformational change in the art market:
despite the severe disruption caused by the COVID-19 pandemic, the last 18 months have marked a period of transformational change in the art market, creating more resilient and innovative business models across the sector, which places the market on a better footing for future growth.

Art market confidence at a seven-year high as the art market stages a V-shaped recovery:
the latest ArtTactic Contemporary Art Market Confidence Report[4] in July 2021 shows a strong return to optimism in the art market, with the confidence indicator[5] reading at 80.6, up from 44.6 from the last reading in November 2020. This is the highest reading since January 2014, and up 89% from the pre-pandemic reading in September 2019.

A more agile and innovative art market could accelerate long-term growth:
despite a challenging year in 2020, the global art market has become more agile to adapt to the new environment. While Sotheby's, Christie's and Phillips reported a 25.9% year-on-year decline in sales in 2020, third-quarter 2020 sales were particularly strong. Auction houses expanded and extended their traditional low-activity summer season to drive in US$2.03 billion in public auction sales, compared with US$483 million in 2019. The second half of 2020's market momentum carried over into the first six months of 2021, with global auction sales from Christie's, Sotheby's and Phillips ending up at US$5.90 billion in the first half of 2021. This is a 230% year-on-year rise from US$1.79 billion in the first half of 2020 and also higher than US$5.70 billion in 2019. This growth in sales brings the premium end of the auction market back in line with pre-pandemic sale levels.

The latest ArtTactic Contemporary Art Market Confidence Report in July 2021 shows a strong return to optimism in the art market.

1 Credit Suisse Research Institute, Global wealth report 2021, p.20
2 Credit Suisse Research Institute, Global wealth report 2021, p.20
3 Methodology: The new methodology uses Wealth-X and its reported regional UHNWI wealth (USD), which totaled US$35.45 trillion. Based on estimates from Knight Frank's Wealth Report 2020, the regional allocations to luxury investments (art, wine, cars, and jewelry) have been applied to the regional wealth figures, giving a total estimated value of art and collectibles wealth of US$1,481 billion in 2020
4 ArtTactic Contemporary Art Market Confidence Report – July 2021
5 The ArtTactic Confidence Indicator moves between 0 and 100, where a confidence reading of above 50 implies that there is more positive sentiment in the art market compared to negative.

Changing landscape as the market shifts east:
New York remains the dominant destination for global auction sales by Christie's, Sotheby's and Phillips, with a 45.1% market share in the first half of 2021 (up from 44% in 2020 but down from 51% in 2019). However, Hong Kong has asserted its presence with a series of record-setting auctions, positioning the market as the second most important location (with a 22.2% market share) in the global auction market in the first half of 2021. The increasing demand for art and collectibles among Asian buyers is likely to drive future market growth, while also accelerating new developments and innovation in the region's art and finance industry.

Global online-only auction sales rocket, firmly establishing online as a strategic sales channel:
the COVID-19 pandemic has catalyzed a seismic shift in online sales among the top auction houses. Sotheby's, Christie's and Phillips' online-only auction sales broke through US$1 billion for the first time, ending up at US$1.05 billion in 2020, up from US$168.2 million in 2019. The strong growth in online-only sales continued into the first six months of 2021, with Sotheby's, Christie's and Phillips' online-only auction sales totaling US$670.6 million. This is up from US$394.7 million in 2020 and US$69.0 million in 2019.

Auction guarantees help shore up the auction market during the pandemic:
the overall share of guaranteed lots by value by Sotheby's, Christie's and Phillips increased from 37.1% in 2019 to 39.8% in 2020[6]. This share grew even further in the first half of 2021, with auction guarantees accounting for 40.8% of the total sales value of post-war and contemporary art evening sales, amounting to US$649 million. Auction guarantees have become an important "financial instrument" in today's auction market, helping stabilize the art market during a period of extreme uncertainty.

Non-fungible tokens (NFTs) become an alternative art market channel:
according to a Reuters article[7] citing data from crypto analytics platform DappRadar, NFT sales value of all categories reached just under US$2.5 billion in the first half of 2021, up from just US$13.7 million in the first half of 2020. The Reuters article also quoted another analytics platform, NonFungible.com, which reported a lower figure of US$1.3 billion in NFT sales in the first half of 2021, excluding around US$8 billion of decentralized finance (DeFi) NFTs. NFTs have created a new global "digital art and collectibles" market that was non-existent in the past or only accessible to a select few. It has allowed digital creators and artists to monetize their work and talent in a new and different way, and to potentially redefine the concept of ownership.

Already, we have seen major auction houses adopt NFTs as well as galleries such as PACE, who seem to be strategically positioning themselves for a future around digital collectibles, as a way to reach new audiences and create new revenue sources for their artists.

Asian art markets weather the COVID-19 pandemic with a positive outlook for 2021:
Whilst most of the regional modern and contemporary art markets studied in this report saw a significant fall in sales during 2020, a few markets bucked the trend. The market for Chinese contemporary art saw an increase of 23%, with the main growth coming from Mainland China. The majority (56%) of market experts surveyed[8] in July 2021 predicted that the Chinese contemporary art market would grow even further over the next 12 months. The South Asian art market saw a 6.6% decline in 2020, significantly less than the global average decline of 21%. However, as India was significantly affected by COVID-19 in the first half of 2021, this year's outlook for this market looks uncertain. Only 6% of market experts thought the Indian art market would see positive growth in the next 12 months, while 61% believed it would remain stable around current levels.

Amazônia
©Edouard Fraipont/Cortesia Casa Triângulo, São Paulo - 2014

6 Source: ArtTactic Analytics, and are based on data derived from post-war and contemporary evening sales
7 Reuters, NFT sales volume surges to $2.5 bln in 2021 first half, July 5 updated July 16, 2021
8 Source: ArtTactic Art Market Confidence Survey – July 2021

Introduction

This section's main aim is to take a closer look at how current and future trends in global wealth and the global art market are reshaping the landscape and context of the art and finance industry. Over the last 10 years, we have been able to monitor how the art market has adapted to global crises, such as the financial crisis in 2009 and, more recently, the impact of the COVID-19 pandemic. We are currently living in a time of extreme uncertainty but also of abundant opportunities.

We have highlighted some of the key trends and changes in the art market over recent years, and are also delighted to feature a series of global expert contributions providing insights into new developments and trends, such as:

1. Credit Suisse AG: Collectibles throughout the pandemic
2. Deloitte Japan: Race for the next art hub of Asia: tax reforms in the art market
3. Deloitte Italy: The state of the art in Italy: results of the third survey on COVID-19's impact
4. Christie's: The 266-year-old start-up - An insider's view of the NFT boom
5. Deloitte Italy: The Brexit effect on the art market: legal aspects concerning the circulation of artworks between the EU and the UK
6. Crozier Europe: Thriving in the post-Brexit art marketplace
7. Pi-eX Ltd: Growth opportunities at public auctions: key lessons for collectors trading at auctions

Over the last 10 years, we have been able to monitor how the art market has adapted to global crises.

Victoria
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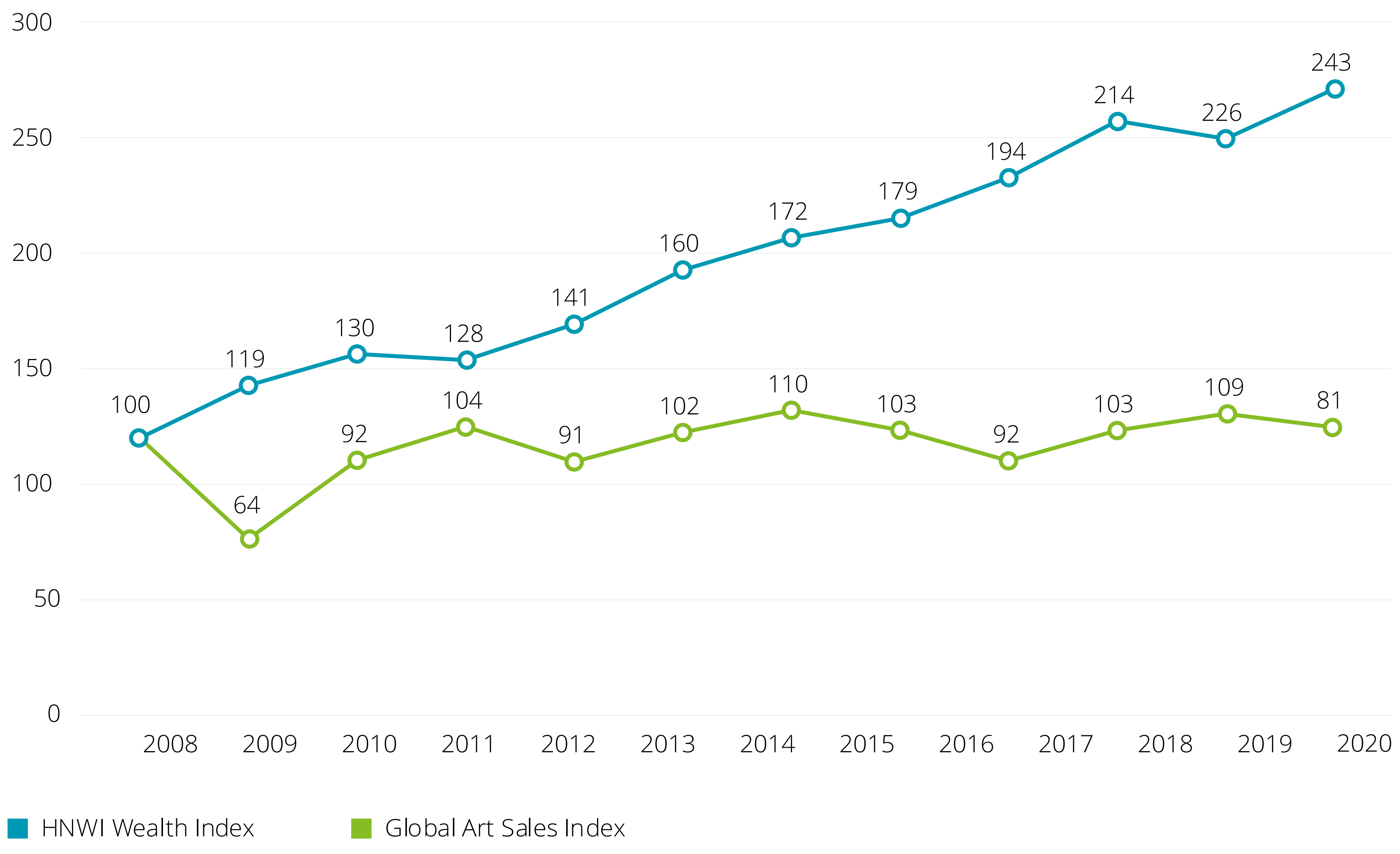
Part 1. Art and collectible wealth review

The findings of the Art Basel and UBS Global Art Market Report 2021[9] show that 2020's global art market sales were the lowest since the 2009 financial crisis, with global sales coming in at US$50.1 billion, down from US$64.4 billion in 2019. However, while the COVID-19 pandemic clearly affected last year's sales, the 10-year, pre-pandemic market trends between 2010 and 2019 still show an anemic nominal growth rate of just over 1.1% per annum. In real terms, this implies that the global art market has actually been shrinking over this period.

If we combine these findings with data from Capgemini's annual World Wealth Report[10], which shows global HNWI financial wealth almost doubling from US$42.7 trillion in 2010 to US$79.6 trillion in 2020 and the HNWI population growing from 10.9 million in 2010 to 20.8 million in 2020, it suggests that while art prices have reached new highs during this period, the overall art market has not. On the contrary, it seems that the global art market has failed to attract and keep pace with the wealth generated over this period.

Figure 2. HWNI wealth growth (US$) vs. global art market sales (US$) growth
Source: Art Basel and UBS Global Art Market Report, Cap Gemini, World Wealth Report 2021.



9 'The Art Market 2021', An Art Basel & UBS Report, Prepared by Dr. Clare McAndrew, Founder of Arts Economics
10 Source: Cap Gemini, 'World Wealth Report', based on figures from report editions published in 2014 and 2021

Is the widening gap between wealth creation and art market sales symptomatic of a deeper problem, and to what extent has the COVID-19 pandemic changed this?

The last 18 months have been extremely challenging for most industries and markets around the world, with some sectors more affected than others. The largely in-person event-driven art market—heavily reliant on physical auction sales, a dense global art fair calendar and gallery exhibitions—was understandably affected by the social restrictions and lockdowns imposed over the last year and a half. The reluctance to embrace technology and digital interfaces over the last decade was another factor that hit the art market hard. In the article p.57 below, Deloitte Italy shares some of the ways the pandemic affected the Italian art market's ecosystem, based on three surveys conducted at different stages during the last 18 months.

However, despite the challenging situation, the art market and many of its stakeholders have proven remarkably agile and innovative, and for the first time, it looks like the art market is catching up with other industries regarding digital transformation. By adapting to new technologies during the COVID-19 pandemic—whether embracing online sales and online platforms, virtual reality (VR) and augmented reality (AR), or the recent phenomenon of NFTs and the acceptance of cryptocurrencies—the art market has finally realized the importance of building audiences and communities outside its traditional client demographics. By opening and creating new channels of engagement, there is a real need and opportunity to broaden this audience and address the anemic growth of the global art market over the last decade.

Rise in wealth in 2020 could find its way to the art market this year

The growing number of HNWIs and their associated wealth could feed demand for all kinds of assets, especially stores of value, given that investors are concerned about diversification in the face of value erosion through inflation. According to a UBS Investors Sentiment publication global investors believe inflation will accelerate over the next 12 months[11].

Wealth creation in 2020 was largely immune to the strict measures taken by governments and central banks to mitigate the economic impact of COVID-19. Based on a recent report from Credit Suisse, 2020 marks the year when, for the first time, more than 1% of all global adults are in nominal terms US dollar millionaires[12]. They now number 56.1 million, up 5.2 million from a year earlier[13], or 1.1% of all adults.

The combined financial and non-financial wealth of HNWI adults, of which household debt is subtracted to reflect net household worth[14], has grown nearly four-fold from US$41.5 trillion in 2000 to US$191.6 trillion in 2020, and their share of global wealth has risen from 35% to 46% over the same period.

The UHNW group grew even faster, adding 23.9% more members, the highest rate of increase since 2003. Credit Suisse estimated the number of UHNWI at 215,030, with a net worth of more than US$50 million at the end of 2020. This is a 41,410 increase than the 173,620 recorded a year earlier[15].

Global wealth is projected to rise by 39% over the next five years. Unadjusted for inflation, the number of millionaires will also grow markedly over this same period to reach 84 million, an increase of almost 28 million from 2020. The number of UHNWIs should reach 344,000[16], adding 129,000 over five years, a rise of 60%[17]. See more about the impact of COVID-19 in the Credit Suisse article "Collectibles in the time of COVID-19—how assets have weathered the pandemic" (p. 40).

While the last 18 months have beset many industries with unprecedented challenges, for others, the COVID-19 pandemic has triggered a new set of growth opportunities. The wealth management industry is among the beneficiaries of the pandemic, as global financial wealth[18] increased 8.3% during 2020, according to a recent report from BCG[19]. The report cites some of the factors behind this boom being a spike in net new savings and a strong stock market performance fueled by highly supportive central banks. Cash and deposits grew by 10.6% over the previous year's numbers, marking the largest annual increase in 20 years.

Another recent wealth report by Capgemini showed unprecedented stock market gains amid a volatile global economy, which drove a 6.3% global HNWI[20] population increase and a 7.6% jump in global HNWI wealth in 2020 to US$79.6 trillion. North America recorded a 10.7% increase in its HNWI population and an 11.9% growth in total wealth. The second-fastest-growing region, Asia-Pacific, saw a 5.8% increase in their HNWI population and an 8.4% increase in wealth. The four jurisdictions contributing to this HNWI wealth growth were China (13.5%), Taiwan (9%), Hong Kong (12.1%), and South Korea (9.2%).

...the art market has finally realized the importance of building audiences and communities outside its traditional client demographics.

11 UBS Investor Sentiment Global 2Q2021, p.1
12 Credit Suisse Research Institute, Global wealth report 2021, p.16
13 Credit Suisse Research Institute, Global wealth report 2021, p.20
14 Wealth is typically held in financial and non-financial assets, of which household debt is subtracted to reflect net household worth
15 Credit Suisse Research Institute, Global wealth report 2021, p.22
16 Credit Suisse Research Institute, Global wealth report 2021, p.27
17 Credit Suisse Research Institute, Global wealth report 2021, p.36
18 The BCG report defines financial wealth as all financial wealth, and not exclusively linked to HNWI or UHNWI
19 BCG: https://web-assets.bcg.com/d4/47/64895c544486a7411b06ba4099f2/bcg-global-wealth-2021-jun-2021.pdf Pg. 4
20 Individuals with a net worth above US$30 million at the end of 2020

But how much of this wealth has entered the art and collectibles market? The Art Basel and UBS Global Art Market Report 2021 found that global art market sales were US$50.1 billion in 2020, a 22% decrease from 2019 and 27% lower than 2018, which suggests the wealth accumulation that took place in 2020 had little impact on the art market so far. However, the strong rebound in auction market sales in the first half of 2021 could mean some of this wealth is finding its way to the art and collectibles market, as individuals are looking to diversify some of their wealth in alternative assets. Our survey this year suggests that 40% of collectors bought art and collectibles as a diversification strategy, 36% saw it as an investment opportunity, and 40% considered collecting art as an impact investment opportunity.

New types of investment models and products regarding art and collectibles have emerged over the last 18 months, from social impact investment (see Section 4) to fractional investment models, tokenization and NFTs (see Section 6). By democratizing and facilitating access to investment products in the art and collectibles market, we could see the asset allocation towards art and collectibles increase in the future; thereby growing the size of the overall art market and the industry that surrounds it.

Art and collectibles and portfolio allocations during 2020

The UBS Global Family Report 2020 found that family offices allocated 3% to arts and antiques, on par with gold and precious metals. Knight Frank's The Wealth Report 2021 and Credit Suisse's 2020 report "Collectibles: An integral part of wealth" noted a global average of 5% allocated to art and other collectibles. Also, an average of 23% of wealth managers surveyed in Knight Frank's The Wealth Report 2021 saw an increase in their clients' spending on tangible investments of passion during the pandemic, such as art and classic cars[21].

A recent study among existing art collectors shows a significantly higher allocation of their wealth in art. According to the Art Basel and UBS Global Art Market Report 2021[22], 61% of HNWI collectors (with assets above US$1 million) reported an allocation of over 10% to art and collectibles. A minority of collectors (28%) also reported that over 30% of their wealth portfolio was accounted for by their art collections. Among a younger generation of collectors, the report found that 30% of millennial collectors had more than 30% of their wealth held in art, double the amount of some of the older collectors surveyed. This may be related to lifecycle factors and the buildup of other assets over time, but it shows the significant position of art in the wealth portfolios of some young collectors.

In the Marsh Family Office Benchmarking Study 2021, based on nearly 100 clients who have insurance programs with an average of more than US$500,000 in annual premiums, 69% of families surveyed owned a significant collection of valuables. Of this group, 91% own fine art collections, a leap from 50% in 2018. Jewelry is the second most common type of collectible, followed by antiques, automobiles, coins, and wine or spirits. While 16% collect other items, such as guns, furs, musical instruments, silverware, and classic boats[23].

In figure 2 we have assumed that UHNWIs' wealth (in US dollars) will grow at the same rate as the expected growth in the UHNWI population according to Knight Frank's The Wealth Report 2021. We have changed the average allocation of 6% used in the previous Art & Finance report to 5%[24] of financial wealth (not including non-financial assets) for 2020. We have also used this as an estimate of the average allocation in five years' time. However, as the growth rate in annual sales has failed to keep pace with increases in global wealth, this high-level estimate must be considered as indicative only.

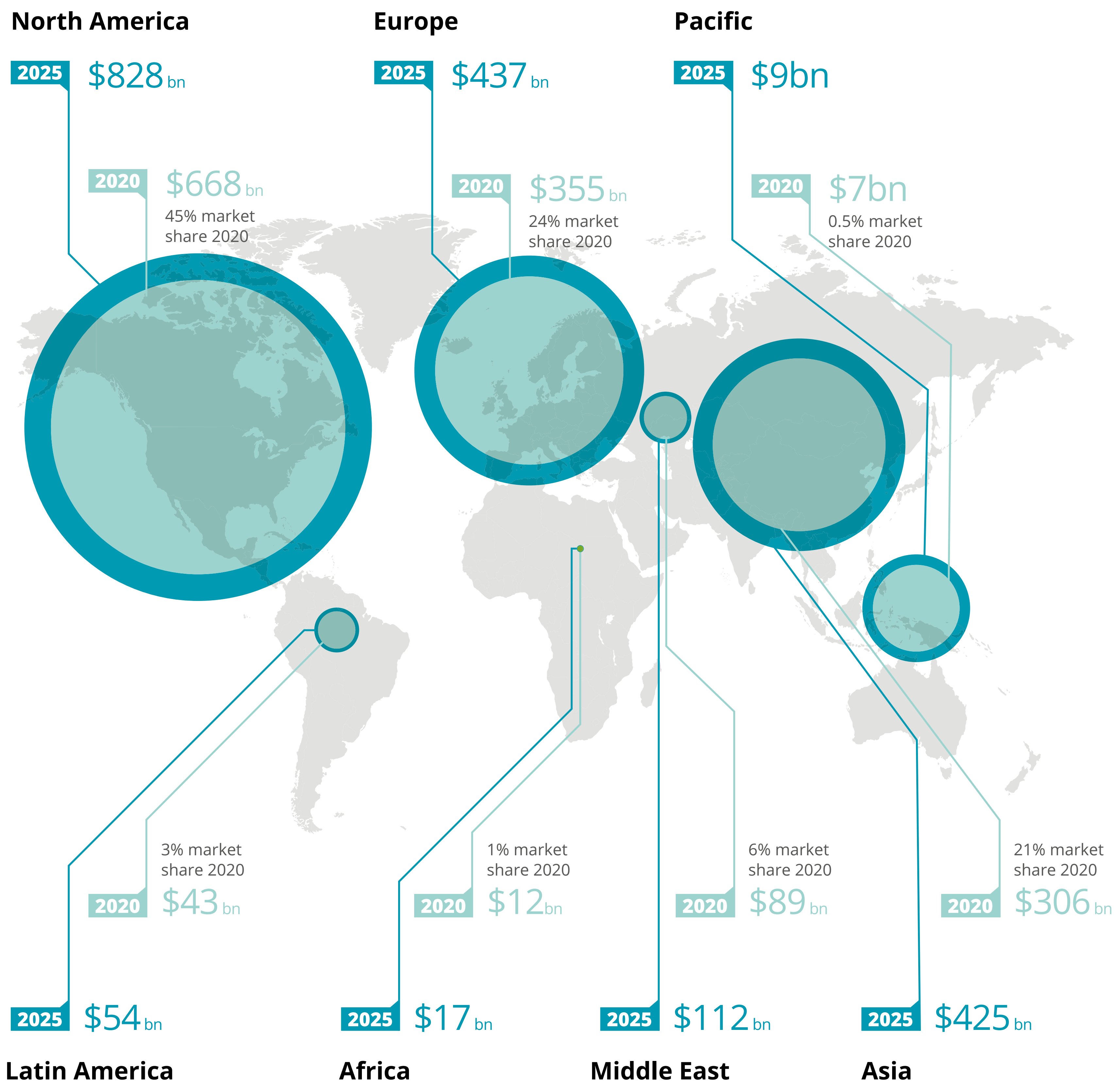
To better reflect regional differences in wealth allocation towards art and collectibles, we have changed this year's calculations of art and collectible wealth to incorporate regional allocations, instead of applying a global allocation average.

Based on these calculations, we estimate that UHNWIs' wealth associated with art and collectibles was an estimated US$1,481 trillion[25] in 2020. We project that, in 2025, this figure could grow to an estimated US$1,882 billion[26]. However, this projection assumes that the growth of art and collectible wealth will track the estimated regional growth in the global wealth population. But, as already discussed previously, the growth in annual art market sales over the last 10 years has failed to keep pace with increases in global wealth. Therefore, this estimate may be overly optimistic. However, the transformational change over the last 18 months in the art market, alongside the increasing access to new types of art investment products, could signal a closer alignment between wealth and art market growth in the future.

21 Knight Frank – The Wealth Report 2021, p.79
22 Source: UBS & Art Basel Art Market report 2021 p.290
23 Marsch, Family Office Benchmarking Study 2021, p.16
24 Knight Frank's Wealth Report 2020, p.102
25 Methodology: the new methodology uses Wealth-X and its reported regional UHNWI wealth (USD), which totaled US$35.45 trillion. Based on estimates from Knight Frank's Wealth Report 2020, the regional allocations to luxury investments (art, wine, cars, and jewelry) have been applied to the regional wealth figures, giving a total estimated value of art and collectibles wealth of US$1,481 billion in 2020
26 The five-year projection is calculated by assuming that art and collectible wealth will grow as a function of the five-year regional growth projections in regional wealth population (2020-2025) estimated by Knight Frank in its The Wealth Report 2021 (p.81)

Figure 3. Global UHNWI art & collectible wealth 2020 estimates

In this year's report, we estimate that UHNWIs' wealth associated with art and collectibles was an estimated US$1,481 billion in 2020. We project that, in 2025, this figure could grow to an estimated US$1.882 trillion.



Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021

Table 2. Art and collectible wealth 2020–2025

All figures are in US$ billion	North America	Latin America	Africa	Europe	Middle East	Asia	Pacific	Overall
Total UHNWI wealth in 2020[1]	13,359	860	312	8,880	1,489	10,202	357	35,459
Regional allocations to art and collectibles[2]	5%	5%	4%	4%	6%	3%	2%	5%
Total UHNWI collectible wealth in 2020	668	43	12	355	89	306	7	1,481
Total UHNWI collectible wealth in 2025	828	54	17	437	112	425	9	1,882

Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021
Wealth-X World Ultra Wealth Report 2021 and Knight Frank Wealth Report 2020

1 Source: Wealth-X World Ultra Wealth Report 2021
2 Source: Knight Frank Wealth Report 2020

When we look at the wealth associated with art and collectibles by UHNWIs, it is important to bear in mind how this relates to other financial assets. Compared with the total assets under management (AUM) of the asset management industry, art and collectible wealth accounts for 1,46%. This is based on a recent report from BCG[27], which reported that global AUM in 2020 ended at US$103 trillion. The Global Private Markets Review 2021, a recent report by McKinsey[28] found that private markets[29] (more illiquid investments such as private equity, real estate, private debt, infrastructure or natural resources) reached US$7.3 trillion in AUM in 2020, an all-time high, with private equity AUM increasing to US$4.5 trillion in 2020, about 61% of total private market AUM. Compared to private markets, art and collectible wealth accounts for nearly 20%.

Art and collectibles account for a substantial portion of HNWIs' wealth; therefore, it requires services and management like any other assets. Building a service offering around art-related wealth can help create new client experiences and develop a stronger personal and emotional connection with clients. New developments around the tokenization of non-bankable assets could allow art and collectible assets to be more easily integrated into asset management allocation strategies.

Following the Credit Suisse publication in October 2020 "Collectibles : An integral part of wealth", we are pleased to collaborate with Nannette Hechler-Fayd'herbe, Chief Investment Officer International Wealth Management and Global Head of Economics & Research, Credit Suisse AG and to present her views on **"Collectibles in the time of COVID-19 How assets have weathered the pandemic" in her article p.40.**

27 BCG, The $100 Trillion Machine, July 2021
28 McKinsey Global Private Markets Review 2021, A year of disruption in the private markets, April 2021
29 McKinsey defines private markets as closed-end funds investing in private equity, real estate, private debt, infrastructure, or natural resources, as well as related secondaries and funds of funds. We exclude hedge funds and, except where otherwise noted, publicly-traded or open-end funds

Dr. Nannette Hechler-Fayd'herbe
Chief Investment Officer International Wealth Management and Global Head of Economics & Research, Crédit Suisse AG

Expert voices

Collectibles in the time of COVID-19

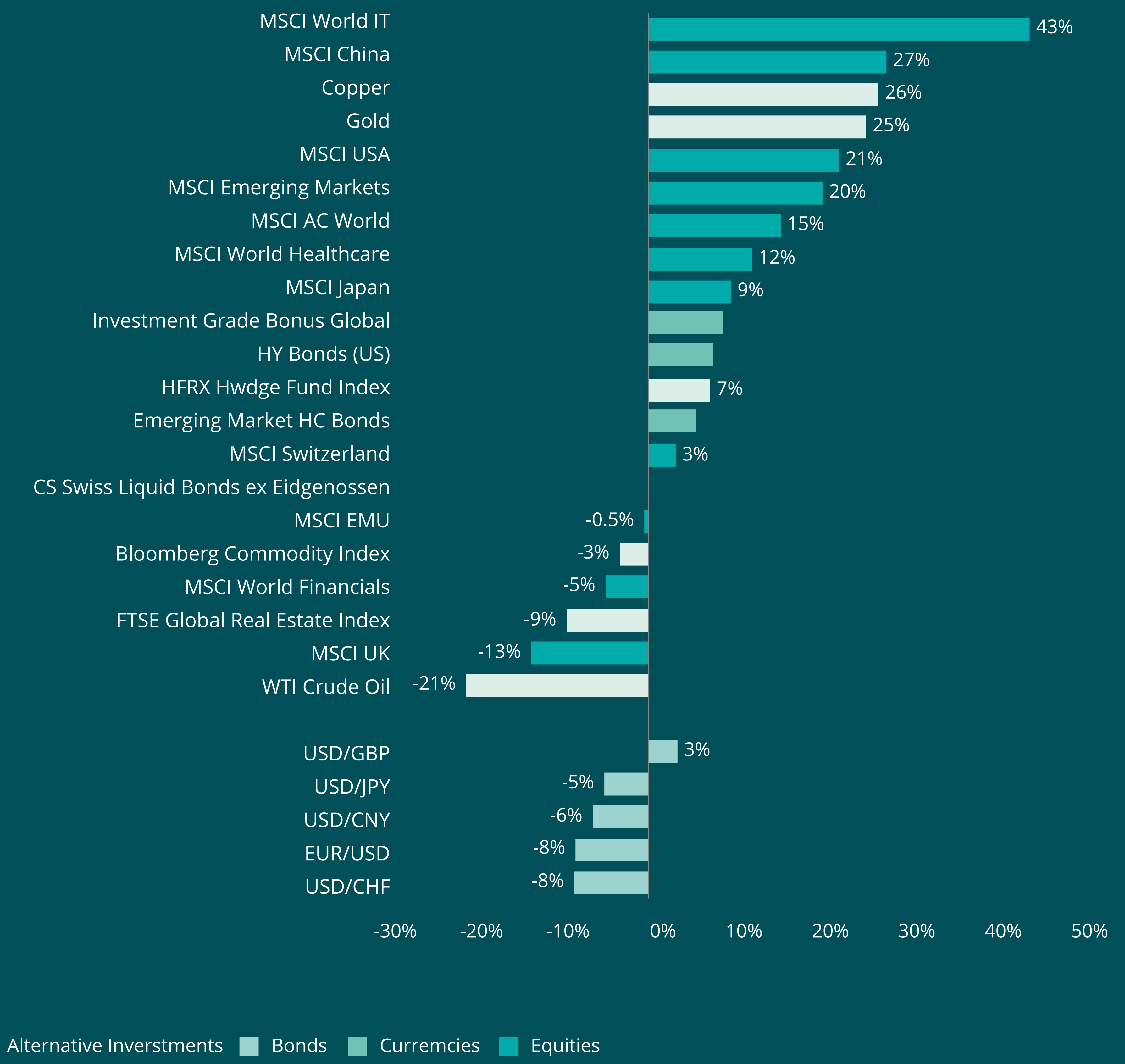
How assets have weathered the pandemic

2020, the year the COVID-19 pandemic took hold, was unprecedented in so many respects that it will come as no surprise that it also proved deeply transformational for the collectibles market. Although collectors, auction houses, galleries, Concours d'Elegance, and others were quick to resort to online channels to substitute for in-person events and sales, collectibles sales ended the year mostly down from 2019. Yet, the interest and engagement of collectors remains vibrant, and an increase in ultra-high net worth (UHNW) wealth in 2020 bodes well for a rebound in collectibles, along with a return to in-person events as global vaccination campaigns move along.

Global wealth defies the pandemic, increasing in 2020
Despite the global recession triggered by the COVID-19 pandemic, global household net wealth did not decline. In fact, quite the opposite is true, as the just-published Credit Suisse Global Wealth Report 2021 concludes: global net wealth increased by 7.4% from US$390 trillion in 2019 to US$418 trillion in 2020. Nearly half of this increase (3.3%) is attributable to the decline of the US$ against a number of other currencies, which inflates the measured wealth increase in dollar terms, but the remainder (4.1%) is increased household wealth. This makes 2020 an average year in terms of wealth increase and certainly puts it in a completely different camp from 2008, when global household wealth dropped by 4%.

The core reasons for the resilience of global wealth and the apparent disconnect between the economic impact of the pandemic and household wealth are clearly attributable to the rapid and unprecedented government and central bank interventions in advanced economies to support households and businesses. These interventions, coupled with optimism spurred by rapid progress in vaccine development, led financial markets to boom in 2020. Global equities, for example, ended the year up 14.7% from the year before. Global investment grade bonds were up 9%. Copper and gold bounced by 24-25% (see Figure 4).

Figure 4. Selected financial assets returns in 2020
Source: Credit Suisse, Bloomberg



Non-financial assets lag financial assets

Wealth is typically held in financial and non-financial assets, of which household debt is subtracted to reflect net household worth. The relative share of financial and non-financial assets varies substantially from country to country. In the USA, for example, the share of financial wealth is higher than in most European countries. It also varies across the various categories of wealth, being higher in the top echelons of wealth than in the lower categories.

Unlike in previous years, the global wealth increase in 2020 was essentially due to the increased value of financial assets, while non-financial assets played only a marginal role (see Figure 5). Non-financial assets include real estate as well as collectibles and other real assets. Surveys typically show that collectibles account for 5% of UHNW individuals' wealth.

Figure 5. Annual change in net worth and its components (%), 2000-2020

Source: James Davies, Rodrigo Lluberas and Anthony Shorrocks, Credit Suisse Global Wealth Databook 2021

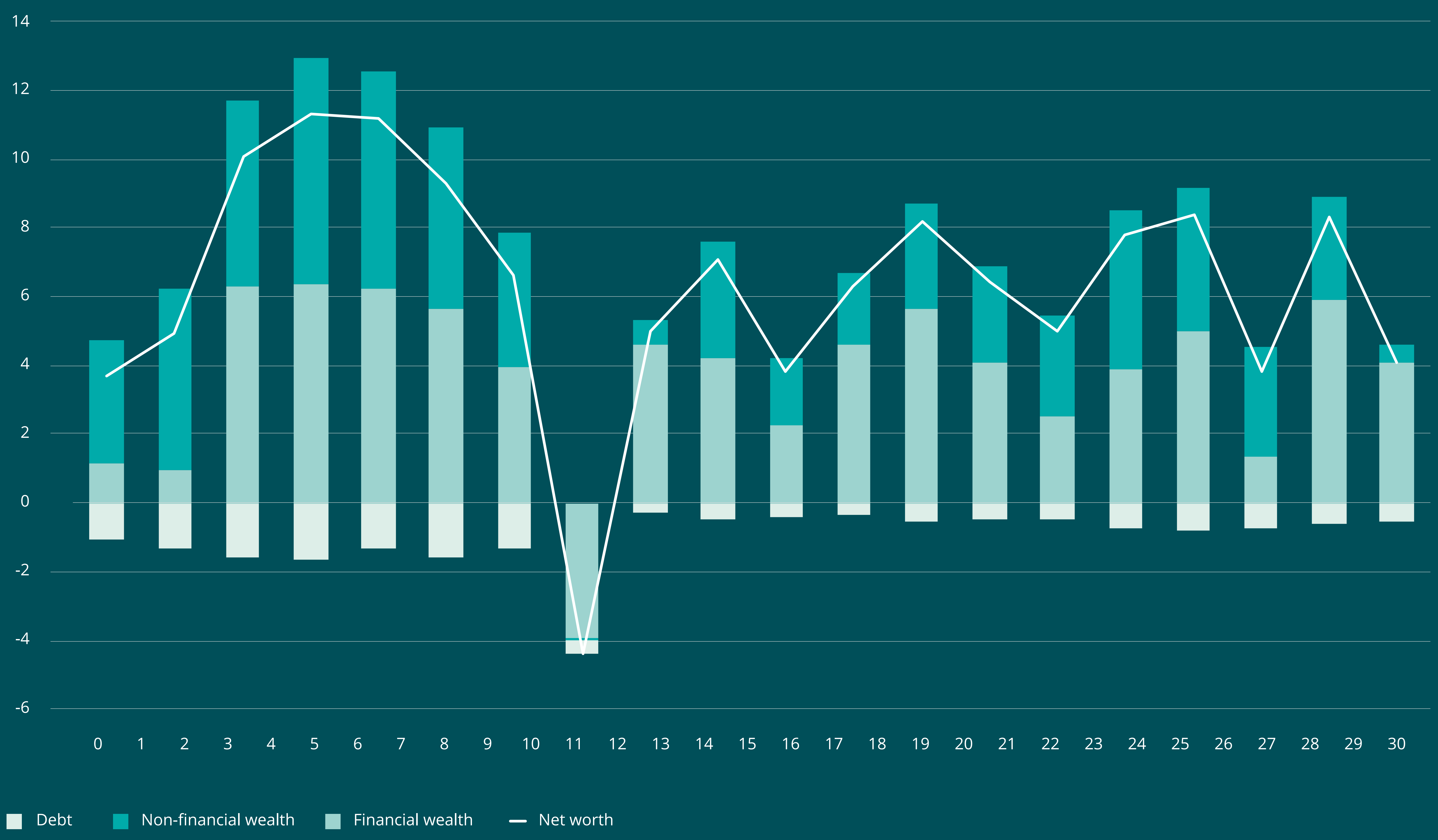


Figure 6. Illustrative price development of selected collectibles categories from 2010-2020
Source: Credit Suisse, Liv-ex, Sotheby's, HAGI

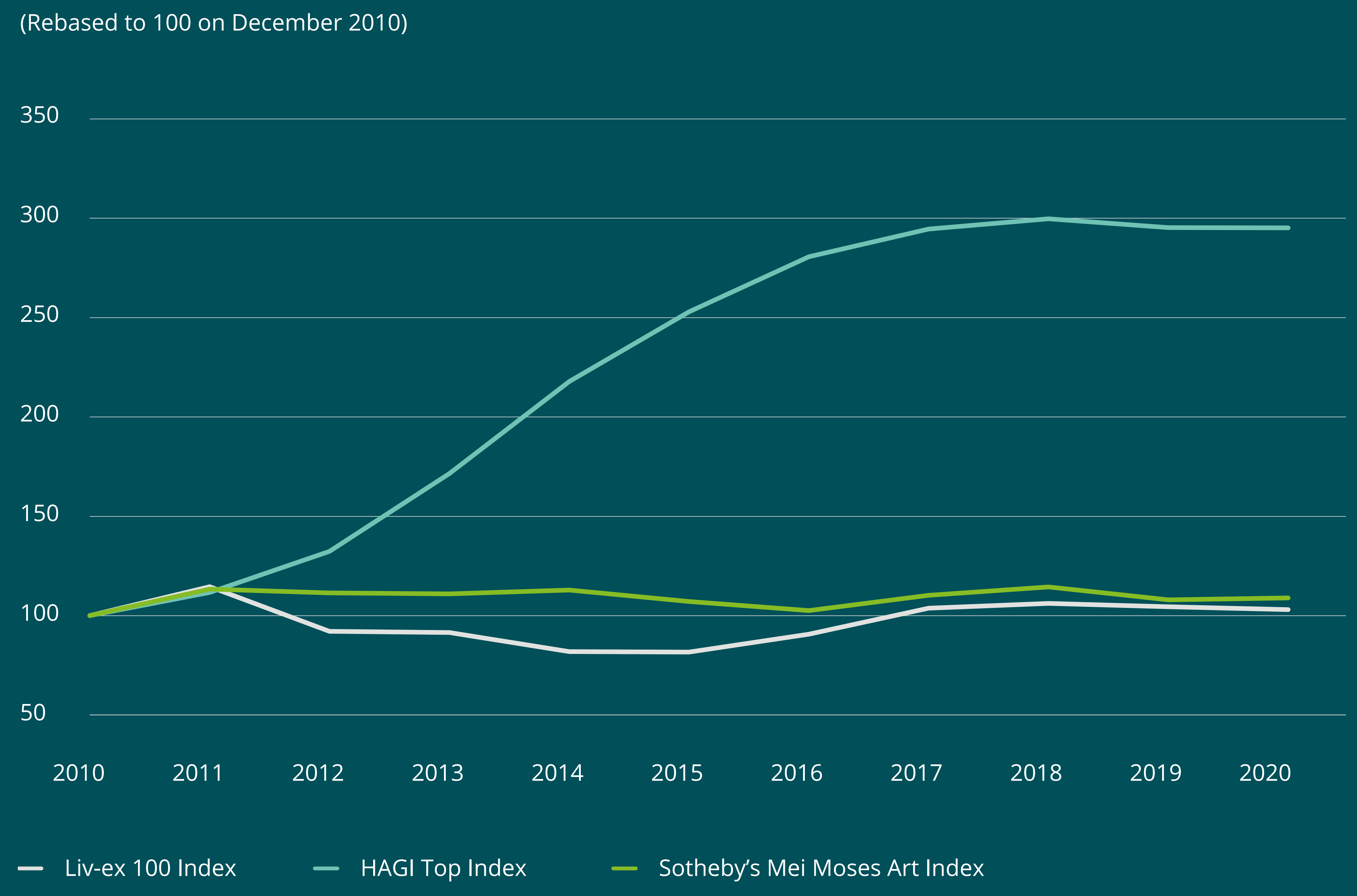


Table 3. Y/Y returns of selected collectibles

YoY returns	2019	2020	CAGR 2010-20	Historical returns
Liv-ex 100 Index	-1.5%	-1.4%	0.3%	5.70%
HAGI Top Index	-1.5%	0.0%	11.4%	11.40%
Sotheby's Mei Moses Art Index	-5.7%	0.9%	0.9%	8.40%

Source: Credit Suisse, Live-ex, HAGI, Sotheby's Mei Moses
* historical returns refer to 2001-2020 for Live-ex, 2010-2020 for HAGI and 1950-2020 for Mei Moses

Collectibles in 2020: Stores of value, not growth
Collectibles span a vast range of valuable items. Fine art is the most important category as measured by the size of annual sales (around US$50 billion in 2020, US$64 billion in 2019). Watches, jewelry, classic cars, and fine wines are of roughly similar size (about US$5 billion each in 2019). Niche collectibles such as collectors' music instruments or luxury handbags are a much smaller category.

Figure 6 shows the returns of selected collectibles (fine art, classic cars, and fine wines) measured by representative indices over time. It demonstrates that collectibles broadly maintained their value in 2020. Unlike financial assets, however, they were unable to benefit much from the boost various government support measures gave to households' net income and savings. Classic car values stayed flat, according to the HAGI Top Index; art was up a meager +0.9%, as measured by Sotheby's Mei Moses All Art Index; while fine wines were down -1.4% on average, according to the Liv-ex Fine Wine 100 Index. This compares to an average annual return of 11.4%, 0.9%, and 0.3% over the 2010-2020 period (see table 1) and 12%, 8.4%, and 5.7%, respectively, over longer time horizons (see table 3).

Collectibles thus had a difficult year of operation. Global art sales declined by more than 20% in 2020 as travel restrictions led to the cancellation of important fairs and in-person auctions. The classic cars market saw many of the traditional Concours d'Elegance and other exclusive collectors' events cancelled. Yet, auction houses and other market intermediaries were quick to react and switched to virtual events. As a result, online sales boomed, reaching record values in 2020, according to the three largest global auction houses Sotheby's, Christie's, and Phillips. They also opened up access to new clients, especially among the millennials. But the online collectors' experience is not equally suited for all collectibles. The year 2020 showed that it is a very successful platform for medium or lower-priced collectors' items, for example, but less so for top-priced items. Equally, classic car collectors, who often require not only visual but also mechanic, auditory, and even olfactory expertise to assess their objects, are more likely to favor private sales than online ones.

The increase in households' net worth in 2020 resulted in more than 5 million additional millionaires globally versus 2019 and 24% more individuals whose wealth exceeds US$50 million, according to the Credit Suisse Global Wealth Report 2021. This should feed demand for all kinds of assets, especially stores of value given that investors are concerned about diversification in the face of value erosion through inflation. A case in point, since the beginning of 2021, fine wines, which are among the more liquid collectibles (in every sense!), are up 8.6% as per End July 2021, according to the Liv-ex Fine Wine 100 Index.

Outlook beyond the pandemic

As the world emerges from the pandemic and some of the operational difficulties of 2020 subside with easing travel restrictions and a gradual resumption of in-person events, the outlook for collectibles is bright. The increase in households' net worth in 2020 resulted in more than 5 million additional millionaires globally versus 2019 and 24% more individuals whose wealth exceeds US$50 million, according to the Credit Suisse Global Wealth Report 2021. This should feed demand for all kinds of assets, especially stores of value given that investors are concerned about diversification in the face of value erosion through inflation. A case in point, since the beginning of 2021, fine wines, which are among the more liquid collectibles (in every sense!), are up 8.6% as per End July 2021 according to the Liv-ex Fine Wine 100 index.

Digital revolution

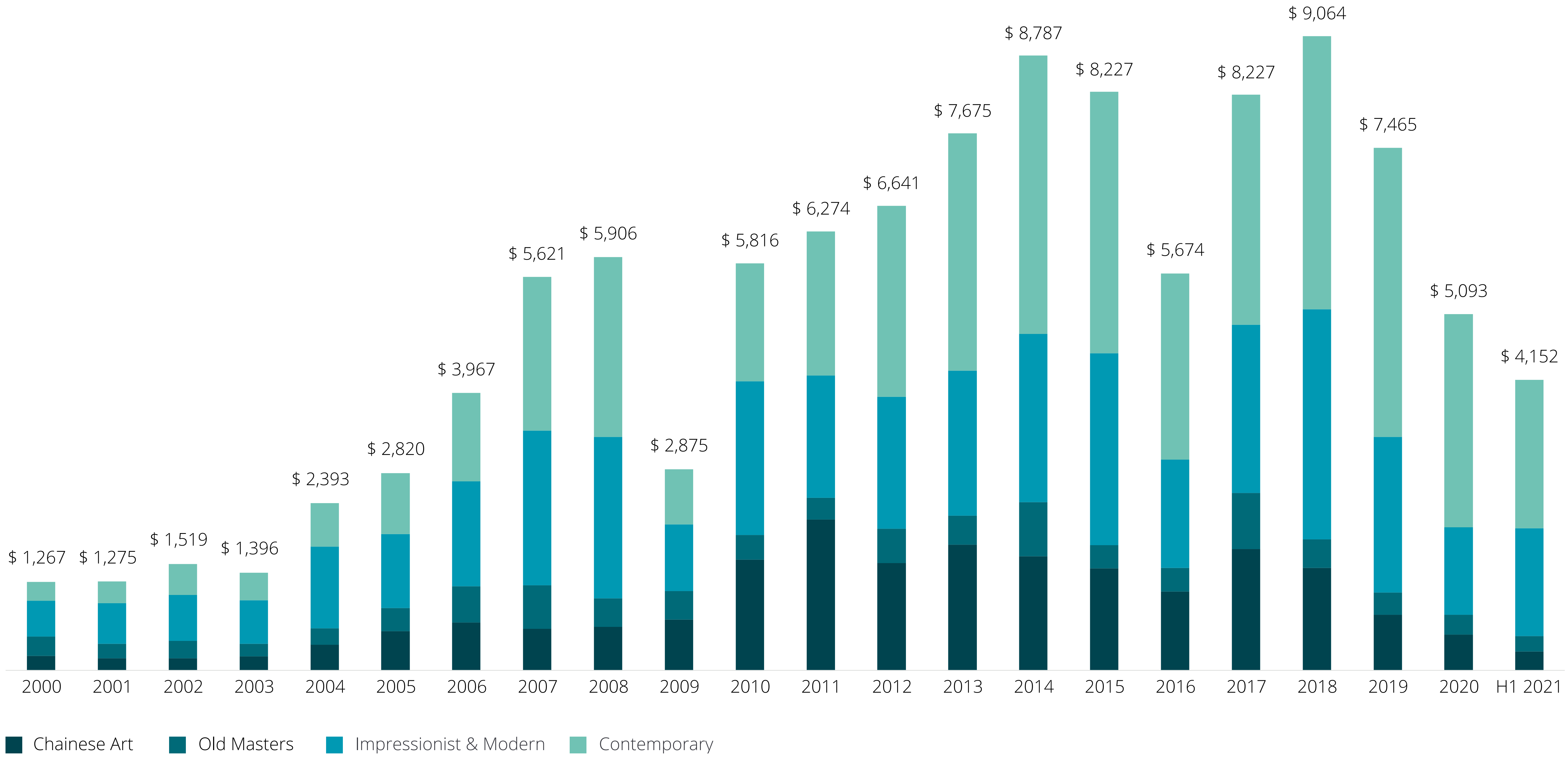
The digital revolution has long reached the world of collectibles. Yet, the COVID-19 pandemic took digital platforms to a new level, reinforcing the growing importance of Asia and China, in particular, in the collectibles market. Asia in general is more inclined to use digital transactions, which means that the shift of auction houses and collectibles professionals to the virtual world will likely open up greater access to new collectors in Asia.

Of course, however, the digital revolution is also adding a new dimension to art, given the advent of digital art and the growing market for non-fungible tokens (NFTs). A number of UHNWI now also look to digital assets when allocating their wealth. The Knight Frank Attitudes Survey, for example, shows that in 2020 UHNWI across all regions held an average of 1% of their wealth in cryptocurrencies. Yet cryptocurrencies themselves come with uncertainties due to very high volatility and sometimes substantial drawdowns. Since 2010, Bitcoin, for example, has not only achieved an average annual return of 246%, but also had an average volatility of 205% and three drawdowns of up to 80%. As experience with digital assets grows and the universe becomes more diverse, for example with NFTs, digital assets may well establish themselves in UHNWI and HNWI portfolios and lend the audio-visual art market in particular significantly more depth and liquidity. Whether for new non-financial tokenized assets or for already existing but limited-access asset categories like private markets, tokenization is potentially opening up the market for smaller and non-institutional investors with its global distributed network, transparency, and ability to develop peer-to-peer platforms across borders facilitating the emergence of new investors.

Part 2. Global art market review

Growth acceleration: can new business strategies in the auction market trigger higher growth rates and a new expansive phase in the global art market?

Figure 7. Auction analysis—top collecting categories at Sotheby's and Christie's 2000–2021 (first half) - US$ million
Source: ArtTactic

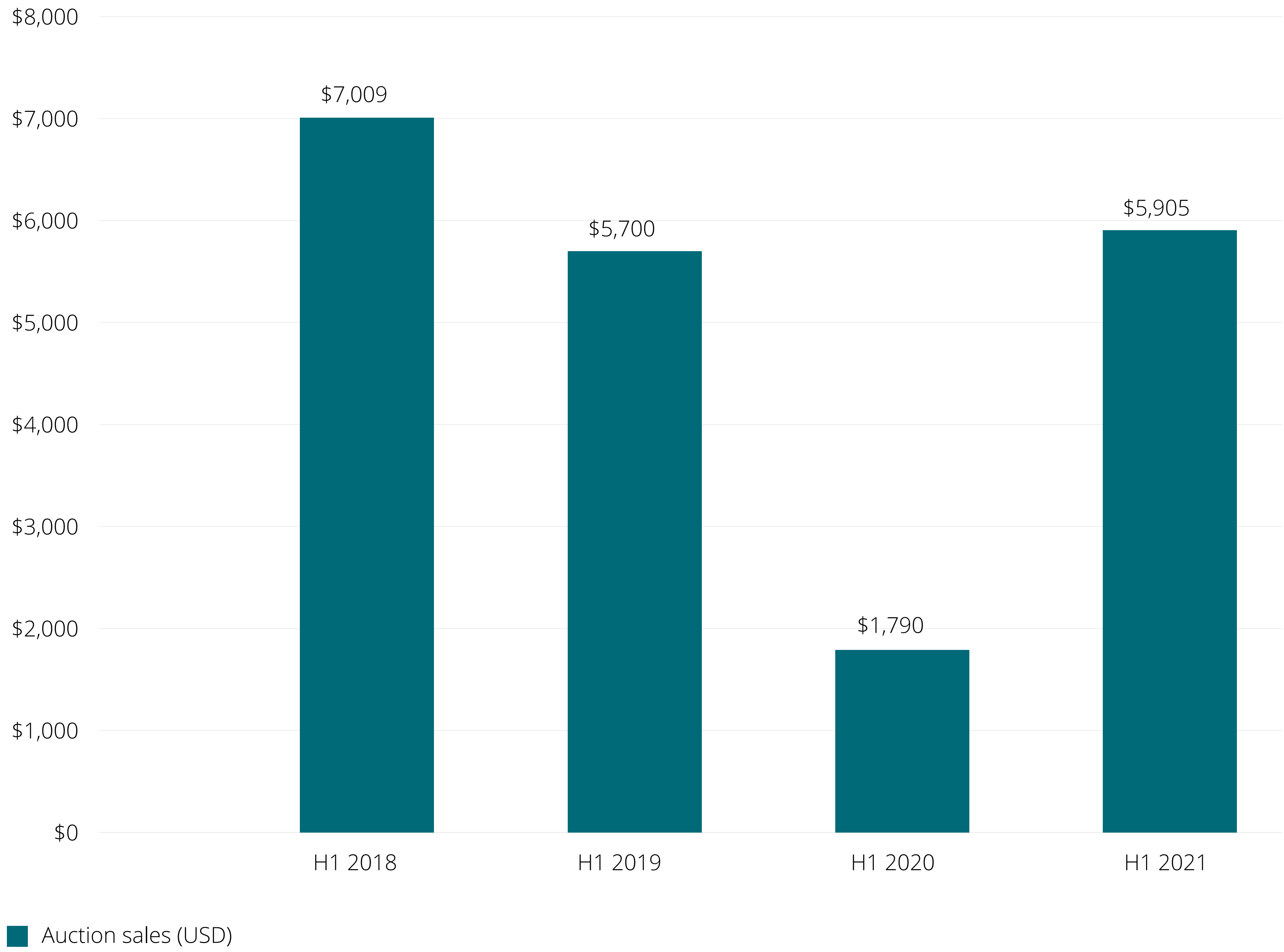


Auction market reached a peak in 2018, but recent transformations in the art market could accelerate long-term growth: auction sales based on the top-four fine art categories at Sotheby's, Christie's and Phillips peaked in 2018, with a combined sales value of US$9.1 billion, above the 10-year average sales value of US$7.2 billion. Since 2010, annual sales have fluctuated between US$5.8 billion and US$9.1 billion, but the art market's growth rates have not kept pace with the growth of wealth accumulation over the same period. Already before the pandemic in 2019, the art market was showing stagnating growth, which was further undermined by the impact of COVID-19 last year. However, the transformation taking place in top auction houses, introducing new collectibles and embracing digital sales channels and new formats, suggest that we may be at the cusp of a new phase in the global auction market. The significant recovery seen in the first six months of 2021 provides us with some insights into the new dynamic that could shape the auction market of the future.

Comparison: from pre- to post-pandemic

The global art market bounces back to pre-pandemic levels in the first half of 2021, as the art market adapts to a new reality.

Figure 8. Total auction sales in US$ milion (all categories) at Sothby's, Christie's, and Phillips
Source: ArtTactic



COVID-19 hit the art market hard in the first half of 2020, with global auction sales from Christie's, Sotheby's and Phillips tumbling to a 49% year-on-year decline. However, through ingenuity, innovation, and rapid adoption of digital channels, the three auction houses managed to recoup their losses. They saw a 30.1% year-on-year increase in the second half of 2020, ending 2020 with total sales of US$7.41 billion, down 25.9% from 2019. The "catch-up" effect in the third quarter was particularly buoyant, as auction houses expanded and extended their traditional low-activity summer season to drive in US$2.03 billion in public auction sales, compared with US$483 million in 2019.

The market momentum has carried over into the first six months of 2021, with global auction sales from Christie's, Sotheby's and Phillips ending up at US$5.90 billion, a 230% year-on-year rise from US$1.79 billion in the first half of 2020 and also higher than US$5.70 billion in 2019. This rise in sales brings the premium end of the auction market back in line with pre-pandemic sales levels.

Despite the severe disruption caused by the COVID-19 pandemic, the last 18 months have seen the art market transform, creating more resilient and innovative business models across the sector, and placing the market on a better footing for future growth. The need for the art market to modernize was expressed by 75% of collectors, 83% of art professionals and 69% of wealth managers in this year's survey—and it looks like it is finally happening.

The resilience seen in both art sales and prices during the pandemic and the strong rebound to pre-pandemic levels in the first half of 2021 has again demonstrated the "bounce-back" effect we saw after the financial crisis in 2009. The art market's ability to weather unpredictable and unprecedented crises has once again highlighted art as an attractive asset class, with more collectors looking to diversify in times of heightened uncertainty.

In this year's Art & Finance survey, 40% of collectors said portfolio and asset diversification was one of the key reasons why they bought art, and 70% said this was one of the strongest arguments for why art should be included in a wealth management service offering.

Going forward, the combined effects of the increasing modernization of art business practices, the introduction of new art investment models, and a resilient and growing art market, could catalyze further growth of the art and finance industry.

Sotheby's, Christie's and Phillips saw a 230% increase in year-on-year auction sales in H1 2021.

Overall H1 2021 versus H1 2020 versus H1 2019
(i.e., looking at the market from post-pandemic, pandemic and pre-pandemic perspectives)

H1 2021: US$5,905,439,652

H1 2020: US$1,789,879,696

H1 2019: US$5,699,646,778

Table 4. By collecting category (Sotheby's, Christie's and Phillips)
Source: ArtTactic

All Auctions at Sotheby's Christie's and Phillips	H1 2018	H1 2019	H1 2020	H1 2021
Post-war and contemporary art	2,207,107,293	2,296,427,845	793,843,568	2,122,964,488
Modern and impressionist art	2,351,783,307	1,588,791,480	393,681,972	1,534,740,496
Old master paintings and drawings	142,343,537	139,238,864	109,279,898	224,217,385
Chinese and Asian art	891,617,155	445,407,803	39,075,619	270,205,864
NFT	-	-	-	116,423,689
American art	202,152,675	78,656,814	44,109,387	38,539,576
Decorative arts and furniture	109,073,508	69,572,956	27,679,690	224,698,417
Jewels and watches	572,725,670	443,648,533	121,537,117	652,920,343
Cars	-	837,563	57,486,725	121,705,498
Other	532,334,595	637,064,920	203,185,720	599,023,896
Total sales value	**7,009,137,740**	**5,699,646,778**	**1,789,879,696**	**5,905,439,652**

Post-war and contemporary market bounces back to the top:
after suffering a 72% decline in sales during the first half of 2020, post-war and contemporary art auction sales rebounded to pre-pandemic levels in the first six months of this year. The market recorded US$2.12 billion in sales, up 167% year on year from 2020 and only 7.6% below 2019 levels, accounting for 35.9% of total sales (down from 44.3% in 2020). The lower market share is a result of auction houses adapting their sales strategies to incorporate a broader range of collectibles, including decorative arts, NFTs and classical cars.

Impressionist and modern art market recovers after a weak 2020:
impressionist and modern art generated US$1.53 billion in sales in the first half of 2021, almost quadrupling sales from 2020 and only 3% below the pre-pandemic 2019 level. Over the last 18 months, auction houses have changed their sales structure and started to amalgamate traditionally separate auction sales categories, including 19th, 20th and 21st-century works, a strategy that seems to be working.

Despite the severe disruption caused by the COVID-19 pandemic, the last 18 months have seen the art market transform, creating more resilient and innovative business models across the sector, and placing the market on a better footing for future growth.

Anjo
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Chinese and Asian art flourishes as auction sales jump 591% in first six months of the year: the Asian collector base's strength was evident in the first six months of this year, with auction sales of Chinese and Asian art reaching US$270 million, up from only US$39 million in the first half of 2020. This boost was largely due to cancellations or postponements of the major Hong Kong auction seasons in the winter and spring of 2020. The sales value is still significantly lower than 2019 (US$445 million) and could signal a shift in taste among Asian collectors towards Western art, particularly in the modern and contemporary segment (see the growth of Hong Kong sales later in the report p. 49).

Auction houses broaden their focus on new collectibles to attract new audiences: as auction houses strive to widen their client base and bring in new audiences, we have seen a renewed focus on different categories of collectibles. The growth of online sales has also allowed auction houses to experiment with both the sales format (smaller, curated auctions with fewer lots) and frequency of auctions. The collectible categories with the biggest surge in demand over the last six months are classical cars (US$121 million, +111% year-on-year), decorative arts and furniture (US$225 million, +711% years-on-year), jewels and watches (US$653 million, +437% year-on-year) and NFTs (US$116 million).

Table 5. By location, US$ million
Source: ArtTactic

All Auctions at Sotheby's Christie's and Phillips	H1 2018	H1 2019	H1 2020	H1 2021
New York	3,576	2,880	792	2,661
London	1,912	1,473	685	1,163
Hong Kong	956	892	39	1,310
Paris	267	231	151	417
Geneva	238	160	63	215
Other	60	65	59	140
Total sales value	7,009	5,670	1,790	5,905

Hong Kong has become a new hub for the higher end of the market: New York remains the dominant destination for the global auction market with a 45.1% market share in the first half of 2021 (up from 44% in 2020 but down from 51% in 2019). However, Hong Kong has asserted its presence with a series of record-setting auctions, positioning the market as the second most important location (22.2% market share) in the global auction market in the first half of 2021. London dropped to third place with a 19.7% market share in the first half of 2021, down from 38.3% in 2020 and 25.8% in 2019. There are signs that the European auction market could be shifting towards Paris, with its share of the market increasing to 7.1% in the first half of 2021, up from 4% in 2019 (pre-Brexit).

Contaminação
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Online sales—a driver for future growth

Figure 9. Online-only Auctions: Total Sales (US$) at Sotheby's, Christie's and Phillips
Source: ArtTactic

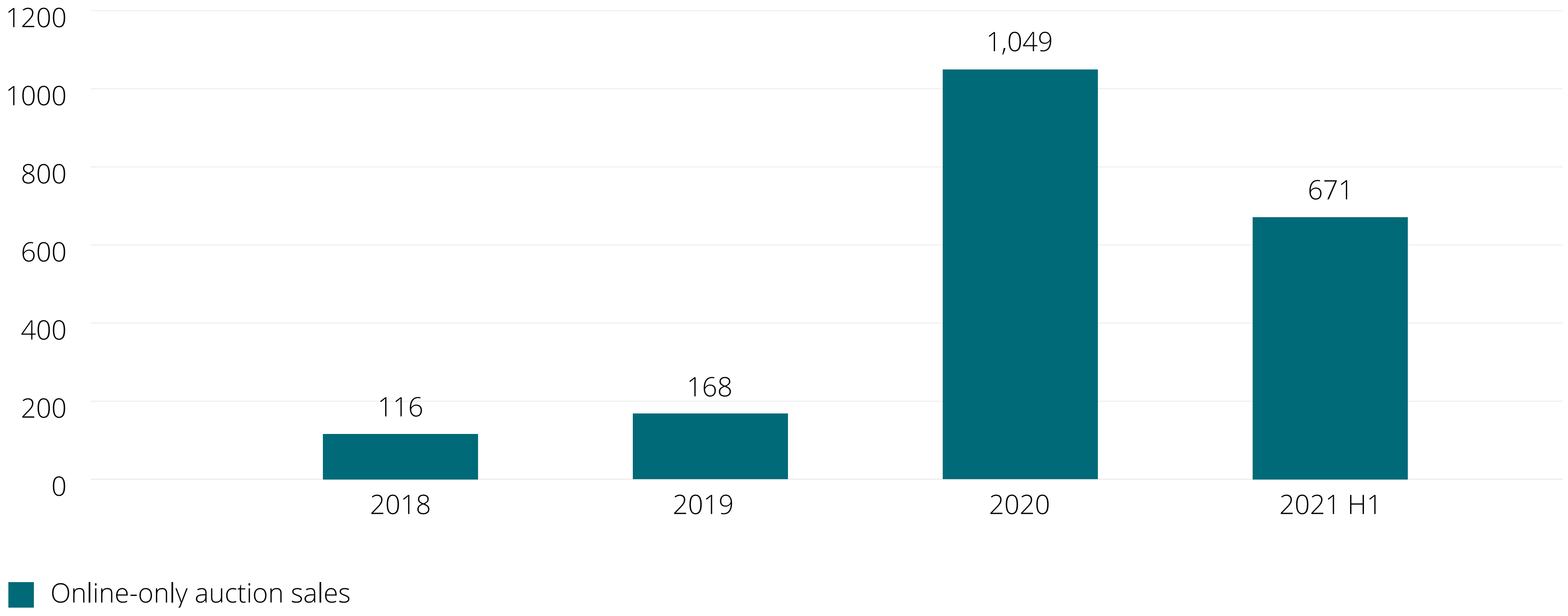


Figure 11. Online-only Auctions: Number of Sales by Auction House (Sotheby's, Christie's and Phillips)
Source: ArtTactic

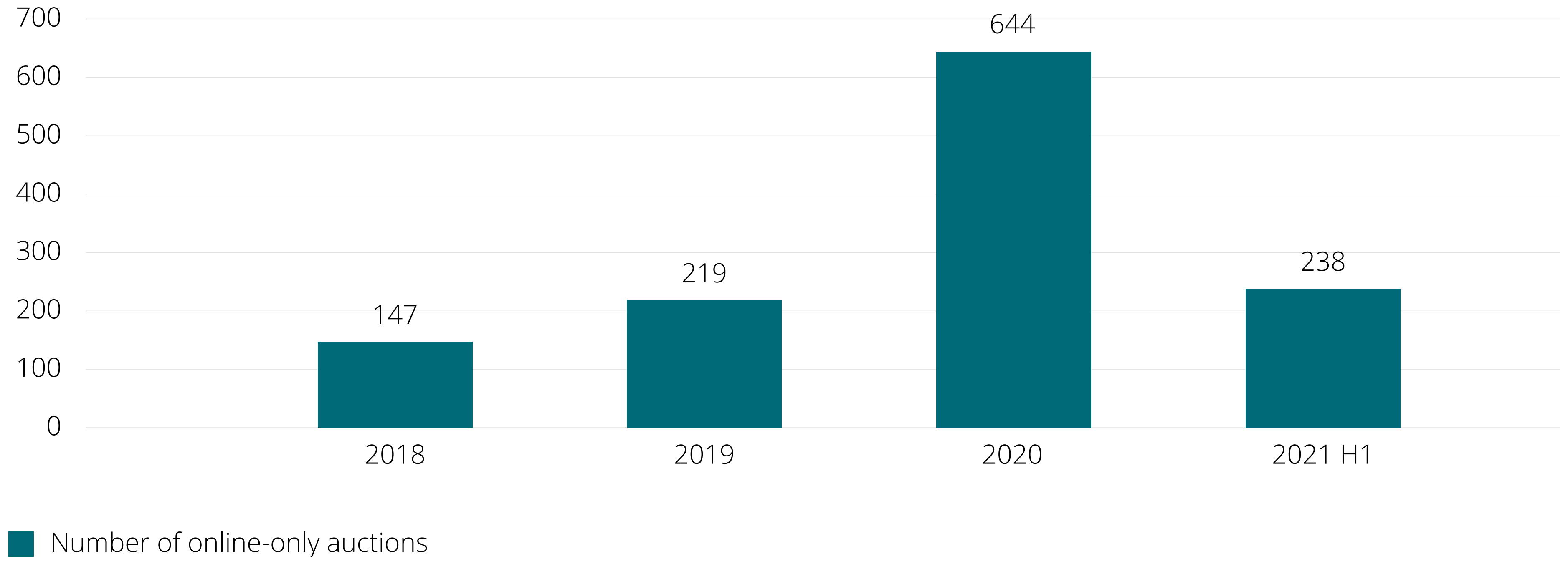
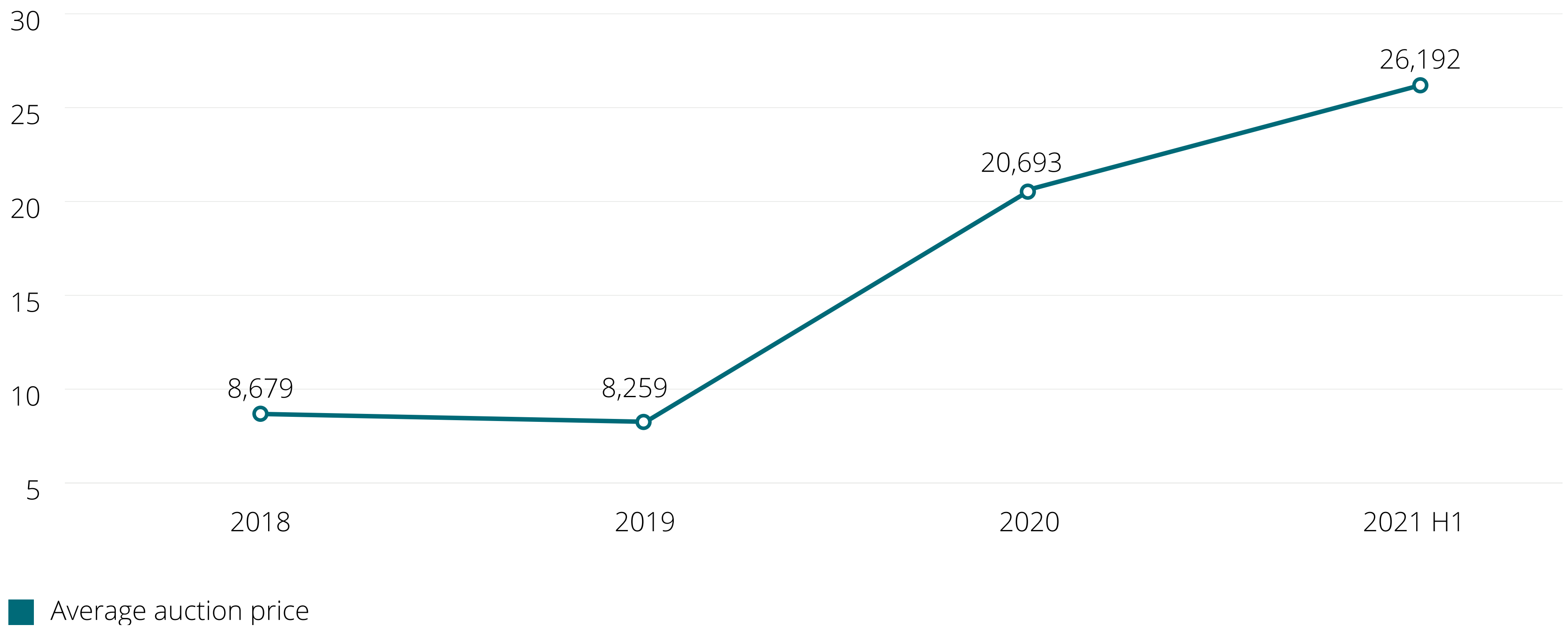


Figure 10. Online-only Auctions: Average Sales Price (US$) at Sotheby's, Christie's and Phillips
Source: ArtTactic



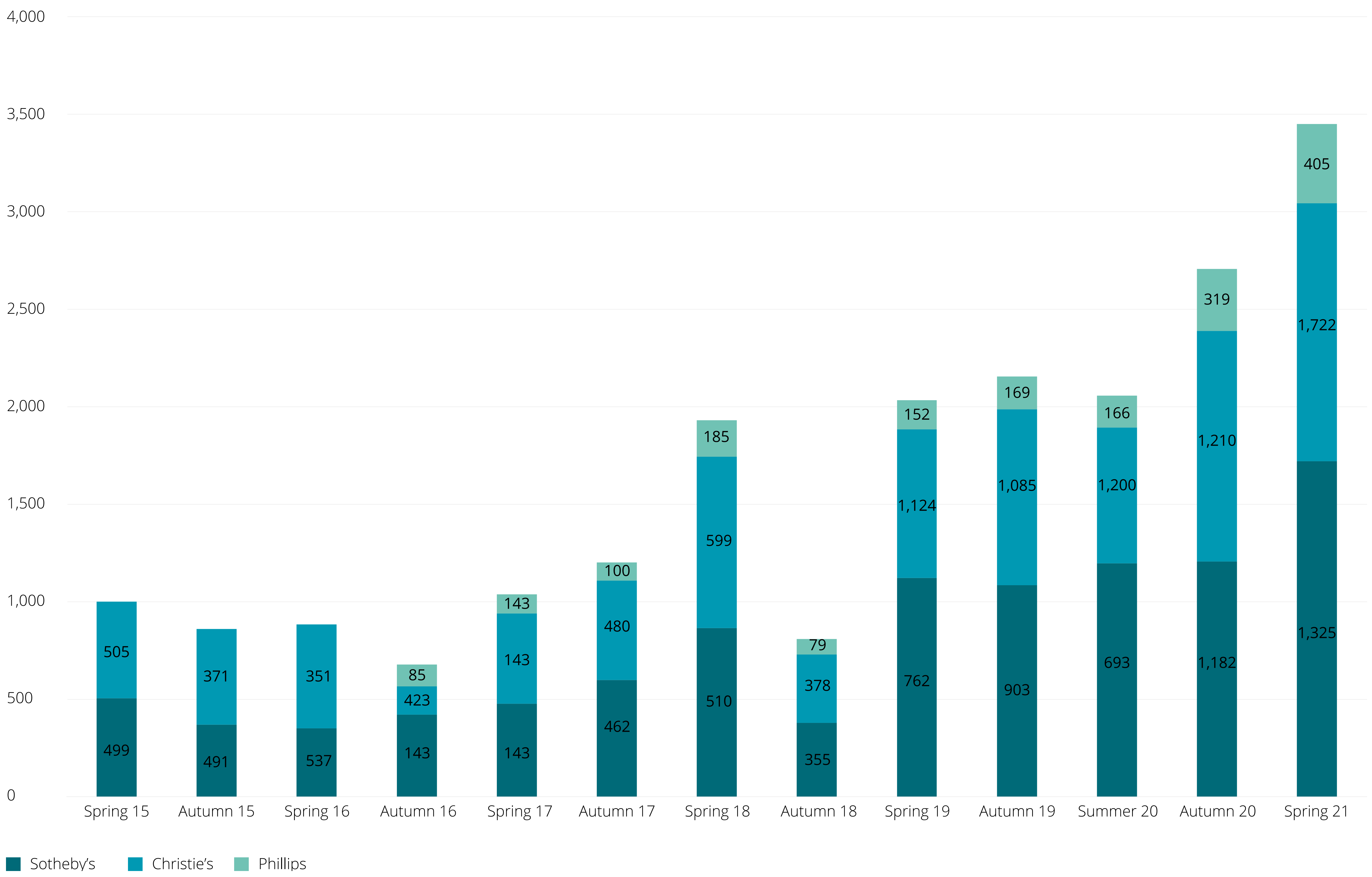
The online art market is here to stay:
The Hiscox Online Art Trade Report 2021 found online art sales reached a record $6.8 billion in the first six months of the year (72% up on the first half of 2020) and could hit a record-breaking $13.5 billion by the year end if sales continue at the same pace.

Global online-only auction sales rocket, firmly establishing online as a strategic sales channel:
The COVID-19 pandemic has catalyzed a seismic shift in online sales among the top auction houses. Sotheby's, Christie's and Phillips online-only auction sales broke the US$1 billion barrier for the first time, ending up at US$1.05 billion in 2020, up from US$168.2 million in 2019. The three auction houses organized 644 online-only auctions in 2020, up from 219 in 2019. The strong growth in online-only sales continued into the first six months of 2021, with Sotheby's, Christie's and Phillips online-only auction sales totaling US$670.6 million, up from US$394.7 million in first half of 2020 and US$69.0 million in first half of 2019. There were 238 online-only auctions in the first half of 2021, up from 216 in 2020 and 93 in 2019. Over the 18 months since the outbreak of the pandemic, online auctions have firmly established themselves in the art market and in the annual auction sales calendar, a sign that the move to digital is here to stay.

Online-only auctions take a larger share of the market:
Online-only sales accounted for 14.2% of total sales for the top three auction houses in 2020, up from 1.7% in 2019. As we enter a post-crisis "new normal", the market share for online-only auctions has fallen, but they still account for 11.4% of total sales at Sotheby's, Christie's and Phillips in the first half of 2021. With a total sales value of US$670.6 million, this was 871% higher than in 2019, when online-only auctions accounted for a market share of just 1.2%.

Buyer confidence online remains high as average prices are up 22.4% in the first half of 2021:
The rapid growth in the value of online-only sales was not only driven by an increase in the number of lots sold online, but also a 22.4% increase in average prices to US$26,192 overall in the first half of 2021. Average online-only prices peaked in March 2021 at US$44,785, up 197% from the previous year. The strong momentum in volumes of lots sold, sales value and average prices signals auction houses and buyers are more confident than ever when transacting online. However, as we revert to a more normal situation, we anticipate current growth rates to slow down, as buyers will start to return to physical and hybrid auction formats.

Figure 12. Hong Kong - Modern and Contemporary Art Auctions sales (HK$ million) at Sotheby's, Christie's and Phillips
Source: ArtTactic



Art market moving east: Hong Kong as the new global art market hub as Asian buyers move in:

The Hong Kong evening sales of Sotheby's, Christie's and Phillips of modern and contemporary art raised a total of US$725.5 million in 2020. This was 10.9% higher than the total sales in 2019, representing a new record year for the Hong Kong market. Despite the disruption caused by COVID-19 to most of the global art market, recent Hong Kong auctions are demonstrating confidence at the top-end of the market and Hong Kong's growing importance as a global art market hub.

The auction momentum that built up during 2020 continued into the spring sales of 2021—Hong Kong's evening sales of modern and contemporary art raised a total of HK$3.45 billion (US$443 million) against the total pre-sale auction estimate of US$382 million to US$542 million. This was 67.6% higher than the total sales in summer 2020, and 27.4% higher than the previous record season in autumn 2020.

Across all collecting categories, Hong Kong has become the second most important sales destination for the three major auction houses, with a 22.2% market share in the first half of 2021 (up from 15.8% in 2020) and ahead of London's 19.7% market share.

Japan is also undergoing a transformation in the race to become the next Asian art hub. To learn more, see the article from Deloitte Japan p. 50.

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Expert voices

Japan: Race for the Next Art Hub of Asia

Tax reforms in the art market

As interest in the art market rises, Japan is promoting initiatives to become the next art hub of Asia. With the recent changes to Hong Kong's political climate, Japan has found an opportunity to place itself in the center of Asia's art market.

The minister for regulatory reform, Taro Kono, is "determined to grow the art business in Japan, so that Japan will become a hub in Asia like Hong Kong," says Yasuaki Ishizaka, the chairman of Sotheby's Japan[30]. Through various regulatory reforms, Japan hopes to attract and encourage art businesses around the world to enter the Japanese market. This article will explore recent tax reforms and the potential impacts on the Japanese art industry.

Tariff reforms for customs areas (freeports)
In a race with other Asian cities to become the next art hub, Japan has started to take actions to attract international art businesses.

One of the most significant changes that could help achieve this goal is the recent tax reforms. Tax rules surrounding freeports have been drastically eased to encourage fairs and galleries to exhibit in designated areas, allowing foreign buyers to trade without tax burdens.

One of the reasons that Hong Kong became the center of the Asian art market was its lenient customs rules. There is no tax for foreign buyers to trade valuable artworks in Hong Kong, which easily attracts exhibitions, negotiations, or even auctions in the tax-free customs areas. However, Hong Kong's political climate casts doubts over the continuation of the flexibility foreign buyers enjoyed. For Japan to play the role of Asia's art hub, it is looking to model its customs tax rules after those that Hong Kong previously presented to foreign buyers.

30 Georgina Adam, "Tokyo aims to take art trade crown from Hong Kong," The Art Newspaper, June 7, 2021

To create a hub for both art and culture, where creators can gather and increase their awareness of their surroundings, barrier issues need to be addressed, and professional participants in the art market need to be increased.

Japan's former rules for customs areas were strict, with limited storage periods which made auctions and exhibitions difficult. Dealers previously had to pay a hefty tax when displaying or selling artwork brought from overseas to Japan's galleries or auction sites. "The tax system is burdensome and a complication to doing business," says Tim Blum, the co-founder of Blum and Poe, which opened a gallery in Tokyo in 2014. "Until now, if we imported art into Japan, we had to pay import tax of 10% upfront. It went into escrow; if the art was re-exported, then it was reimbursed, or the tax paid if it went to a domestic buyer."[31]

However, with the new tax reform designed to attract the global art community, Japan hopes to introduce more freeports where foreign buyers can trade artworks without tax burdens. Artworks sent abroad from customs areas can now be traded without import procedures and payment of duties and taxes, encouraging foreign art galleries, auctions and art fairs to be opened in these customs areas. In addition, improvements to infrastructure for safe transportation and storage of artworks at a lower cost are being considered.

For example, Haneda Airport is looking to be a hub for art as well as travel. Constructions are underway for a building, five minutes from the airport and within the free-trade zone. Upon completion in 2023, it will offer 30,000 sq. m of space, eventually with the aim of becoming a gallery hub.[32]

Of course, this reform of the tax-free zone alone is not enough to make Tokyo the new art hub of Asia, but it has kickstarted conversations to change the art market. Study groups are looking into tax reforms for inheritance, donations, depreciation, and so on. Many high-net-worth-individuals are also turning their focus to art investments, with increased interest in related tax incentives.

Inheritance and gift tax reforms for artworks

The recent tax reforms of Japan have also changed in favor of art collectors. Tax rules around inheritance and gifting of artworks in Japan present a heavy burden for collectors, who are potentially subject to a maximum of 55% tax charge when passing assets through generations. Recent tax reforms have sought to allow forward planning and to promote charitable giving, as well as to prevent an overseas outflow of valuable artworks and promote their exhibition at the art museums, particularly for important cultural properties and significant artworks.

Below outline the key recent changes that are sparking interests in investors to review their collections with tax experts.

(1) Grace period and exemption of inheritance tax on certain artworks (2018 tax reform)

Art collectors can conclude long-term deposit contracts with museums based on preservation and utilization plan approved by the Agency for Cultural Affairs. In the event of death of the owner, if the inheritor continues to deposit the artwork under the same plan, the inheritance tax payable will be deferred by 80% of the taxable value of the artwork. The deferred payment will be exempted when the heir also passes away.

31 Adam, "Tokyo aims to take art trade crown."
32 Adam, "Tokyo aims to take art trade crown."

This rule applies to artworks inherited after April 1, 2019.

(2) Artworks as payment-in-kind for inheritance tax (2020 tax reform)

Applying to cases where hurdles exist for monetary payment of inheritance tax, artworks can be accepted as payment-in-kind for inheritance tax subject to approval from Director of the Tax Office.

Statutory order is predetermined for assets acceptable as payment-in-kind by reference to liquidity. For example, government bonds and listed stock take the highest priority. Artworks, particularly those by living, contemporary artists, were classed as the lowest priority prior to the tax reform.

These changes raise the priority of certain artworks to being on par with government bonds and listed stocks, making the scheme more accessible and attractive to many. In addition to important cultural properties and significant artworks that were ranked as high priority prior to the reform, contemporary artworks can now benefit from this change if they are registered with the Agency for Cultural Affairs prior to owners' death.

This applies to artworks registered by the Agency for Cultural Affairs inherited after April 1, 2021.

Japan's action plan to promote its art industry

In order to promote Tokyo as the next art hub of Asia, Japan must first strengthen the foundation of its art market. Christie's Japan Managing Director Katsura Yamaguchi says "facilitating art deals with customs is meaningful, but it is necessary first to make a foundation of art in the country."[33]

Japan's art market has remained at a level of approximately $60 billion USD annually (approximately 7 trillion JPY) over the past 10 years.[34] While the notion of art and collectibles as alternative assets is growing in recognition, the lack of transparency in the industry has made it difficult for investors to consider art investment as an option. However, recent growth of young businesspersons purchasing artworks has progressively attracted attention primarily from real estate developers and wealth management community.

To create a hub for both art and culture, where creators can gather and increase their awareness of their surroundings, barrier issues need to be addressed, and professional participants in the art market need to be increased. Initiatives to facilitate this environment include:

- Introduction of new policy plans to bring foreign talent to Japan (i.e. freelance visas, art programs targeting domestic and international creators)
- Increase of international art industry professionals and talent (curators, advisors, appraisers)
- Consultation with industry professionals to establish new art-related policies
- Focus on recent global art trends, such as digital art and immersive AR/VR experiences

Yasuta Hayashi, Deputy Director of Cultural Economy and International Affairs Division for Agency of Cultural Affairs in Japan, declares that a collaborative effort involving multiple governmental institutions (Agency of Cultural Affairs; Ministry of Economy, Trade and Industry; Ministry of Foreign Affairs of Japan) will be essential to achieve these goals.[35]

With the negative impacts of the pandemic on the global art market (closures of museums and galleries, postponement of events, drastic decline in tourism, etc.), it is difficult to predict when Japan would potentially replace Hong Kong as the next art hub of Asia. However, there is no doubt that the recent changes in Japan's policy and regulatory landscape will steer the country in the direction of growing its art market to appeal to foreign art dealers and collectors from around the world. After the Summer Olympics in Tokyo, Japan is looking to future events, such as the 2025 World Exposition in Osaka and the opening of Integrated Resorts, to further attract international art collectors and businesses seeking to leverage newly introduced benefits.

**This article is based on Japanese tax laws and regulations that are valid as of the date of publication. Please note that this article will not be updated in response to changes in laws and regulations after the date of publication.*

33 Eri Sugiura, "Japan sculpts new tax rules in push to become Asian art hub," Nikkei Asia, April 31, 2021
34 Agency of Cultural Affairs Government of Japan, Japan Art Industry Market Research Report 2020, 2020
35 Yasuta Hayashi (Deputy Director, Cultural Economy and International Affairs Division for Agency of Cultural Affairs, Japan), interview, May 26, 2021

Art market confidence

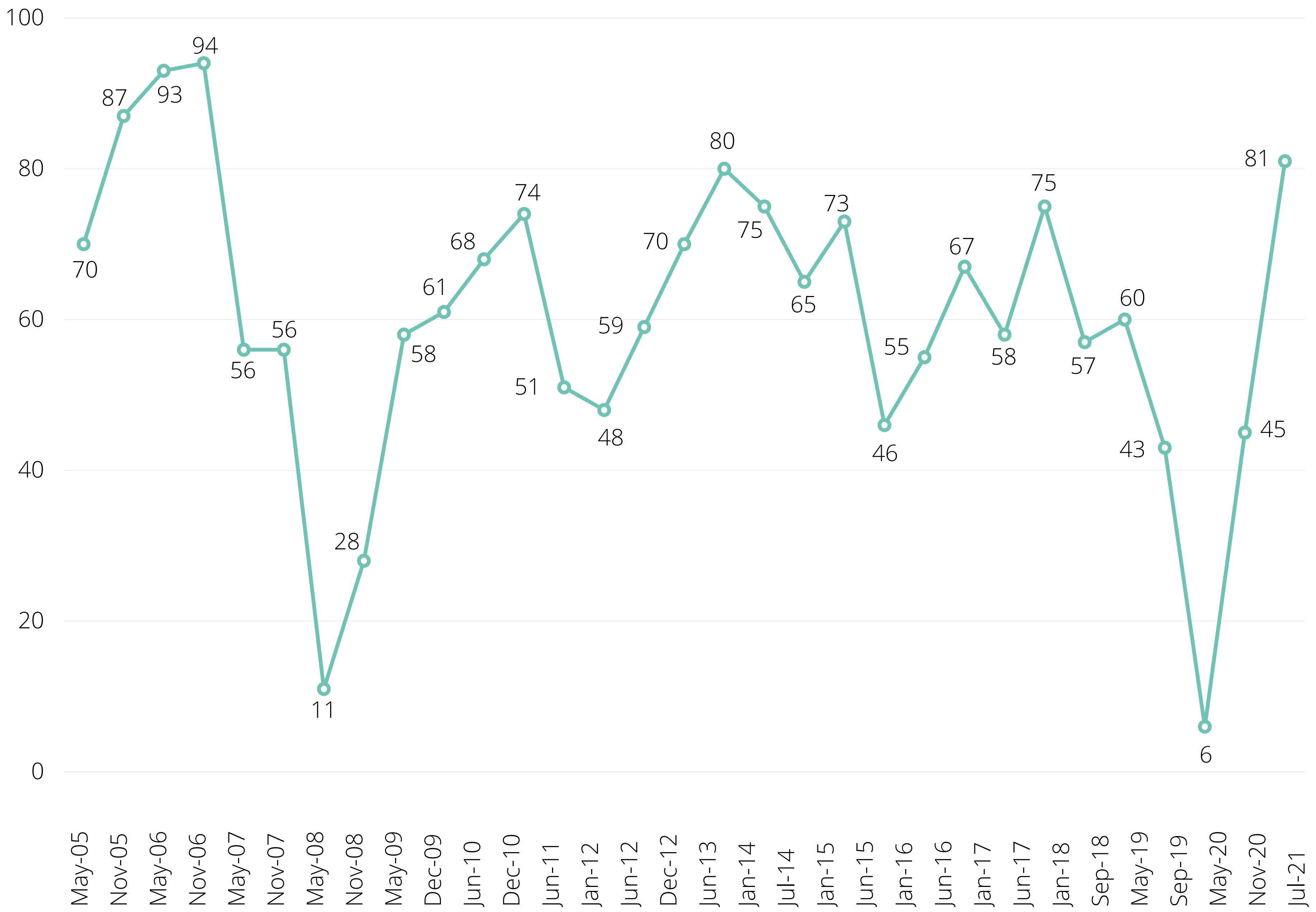
Art market confidence at a seven-year high as the art market stages a V-shaped recovery

The ArtTactic Contemporary Art Market Confidence Report in July 2021 shows a strong return to optimism in the art market, with the confidence indicator[36] at 80.6, up from 44.6 from the last reading in November 2020. This is the highest reading since January 2014, and up 89% from the pre-pandemic reading in September 2019.

Even before COVID-19, confidence in the art market had been steadily declining since January 2018. It reached an all-time low in May 2020, only months after the outbreak of the pandemic; however, ArtTactic's survey reading in November 2020 signaled a V-shaped market recovery. This was reflected in the auction sale boom in the first half of 2021, showing sales more than tripling for Christie's, Sotheby's and Phillips, and exceeding that of 2019.

This suggests that the COVID-19 pandemic, while causing severe disruption, has also catalyzed transformational change in the art market. It has created more resilient and innovative business models across the sector, placing the market on a better footing for future growth.

Figure 13. US & Europe - Art Market Confidence Indicator, May 2005 - July 2021
Source: ArtTactic



Positive short-term outlook for the auction market as sales increase 230% in first half of 2021

The latest Auction Confidence Indicator[37] shows a reading of 90, up from 56 in November this year. Positive sentiment (52%) outweighs negative sentiment (7%) in a ratio of more than 7:1, signaling that experts believe the auction market will continue to see a positive trend for the remainder of the year.

Auction houses were among the fastest out of the block when the pandemic hit last year, by rapidly switching their offline sales to online and adopting new hybrid formats. Many of these initial changes seem to have become permanent—the models adopted during the pandemic have evolved further in the second half of 2021, fueling new audience demand and reinvigorating the existing collector base.

Auction sales from Christie's, Sotheby's and Phillips came in at US$5.9 billion during the first half of 2021, up from US$1.79 billion in 2020 and exceeding US$5.7 billion in sales in the first half of 2019. With Q3 and Q4 historically accounting for the largest share of auction sales, 2021 could reach close to 2018's peak levels. This is a clear sign of strength, considering the market's difficult situation in the last 18 months. Primary market confidence rides on the wave of positive auction sentiment

Art market confidence at seven-year high as the art market stages a V-shaped recovery.

36 The ArtTactic Confidence Indicator moves between 0 and 100, where a confidence reading of above 50 implies that there is more positive sentiment in the art market compared to negative
37 ArtTactic, Contemporary Art Market Confidence Report – July 2021

With the prospect of a packed physical art fair calendar this autumn, experts interviewed by ArtTactic believe the auction market's positive trends are likely to spill over into the primary market over the coming months. The gallery sector's adjustment to the COVID-19 crisis helped restore confidence in the primary market—the Primary Market Confidence Indicator jumped from an all-time low of 3 in April last year to 39 in November, with a further leap to 76 in July 2021. Half of the art market experts surveyed felt the primary market would develop positively over the coming six months, whilst only 36% said the same in November 2020. However, the rapid rise in COVID-19 infections and the risk of new variants could delay a "return to normality" to next year.

Attention shifts to a younger generation of artists

The market demand for a younger generation of artists continued through 2020 and into the first half of 2021. Auction sales at Christie's, Sotheby's and Phillips of younger artists (aged 45 or below) saw sales of US$52.4 million in 2020 and US$144.6 million in 2021 (a 175.7% year-on-year increase in the first six months of 2021). The interest in younger artists could also correspond with buying trends among millennial collectors, which were the highest spenders in 2020, according to the Art Basel and UBS Global Art Market Report 2021[38]. The report found that their median spend was US$228,000, compared with the Generation X median spend of US$122,000 and the baby boomer spend of US$109,000. The report also found the number of millennials spending more than US$1 million increased from 25% in 2019 to 35% in 2020.

The younger generation of contemporary artists' outlook has undergone an even stronger positive shift in sentiment, with 61% of experts surveyed in July 2021 saying this market will continue to grow over the coming six months (up from 59% in November 2020). More impressively, 79% said this trend would continue well into the first half of 2022 (up from 54% in November 2020). Most believe the obsession with youth will continue into next year, as more younger collectors and buyers join the market boom, particularly from Asia.

However, there are fears that the market speculation for younger artists could threaten its future sustainability, as the Speculation Barometer came in at 7.4, above the historical average of 6.6. Some art market experts, surveyed by ArtTactic, view the speculation among younger artists as unhealthy and unsustainable—with the fear of missing out (FOMO) among collectors and investors looking for the next big thing pushing prices far beyond justified limits, given the stage of these artists' careers. Other experts continue to believe the growing attention on this younger generation of artists will likely benefit more younger artists of color, as well as young female artists that have traditionally been under-represented, particularly in the auction market.

Most believe the obsession with youth will continue into next year, as more younger collectors and buyers join the market boom, particularly from Asia.

It's Raining Men
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38 UBS & Art Basel Art Market report 2021 p.298

Auction guarantees

A financial instrument that has grown in influence at the premium end of the art market

Auction guarantees have become a popular financial instrument in the art market today. An auction guarantee is a pre-arranged agreement between the seller and the auction house and/or an external third party who agrees to pay a fixed amount for a specific lot coming up for auction. If the lot fails to sell, the auction house or the third party becomes the lot's owner and pays the seller the full guarantee. If the lot sells for more than the guaranteed amount, the winning bidder becomes the lot's owner and the auction house or the third party receives a proportion of the guaranteed amount's excess from the seller.

This type of financial arrangement serves several purposes. First, it helps the auction house attract consignors who may worry their artwork will not attract sufficient bidders and fail to sell (i.e., "burning" or tainting the artwork by creating an element of uncertainty around its value and quality). Second, auction guarantees help build market confidence by ensuring that as many of the high-value lots featuring in the auction are sold—resulting in a high sell-through rate, a closely watched ratio by art market observers. And third, it is profitable, attracting a growing number of third-party guarantors (investors) in recent years.

In this year's survey among wealth managers, collectors and art professionals, we found that opinions are divided about the role of guarantees in the art market. About a third of collectors (31%) and art professionals (34%) felt that auction guarantees are a threat to the art market's reputation, and that the instrument itself undermines market transparency. A much lower share of wealth managers, 17%, thought the same. However, most stakeholders see auction guarantees as a natural progression of the art market's increasing financialization.

> About a third of collectors (31%) and art professionals (34%) felt that auction guarantees are a threat to the art market's reputation...

Figure 14. Auction Guarantees: Post-War & Contemporary Art Evening Sales in London, New York and Hong Kong (Sotheby's, Christie's and Phillips, US$ million)
Source: ArtTactic

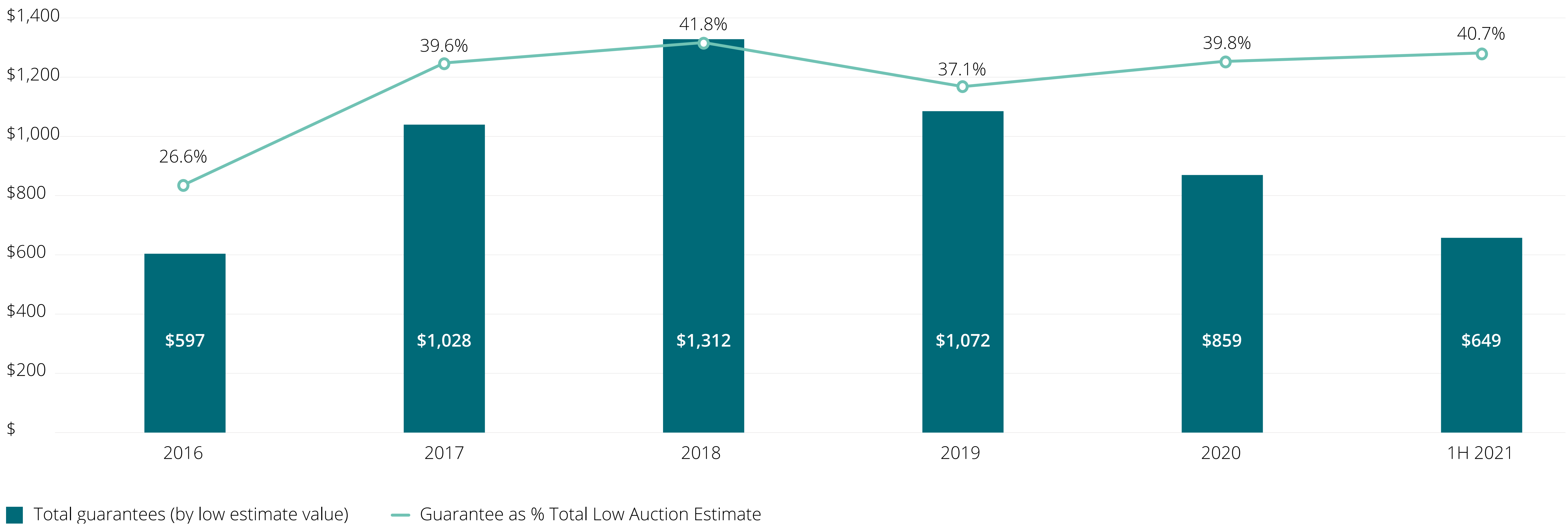
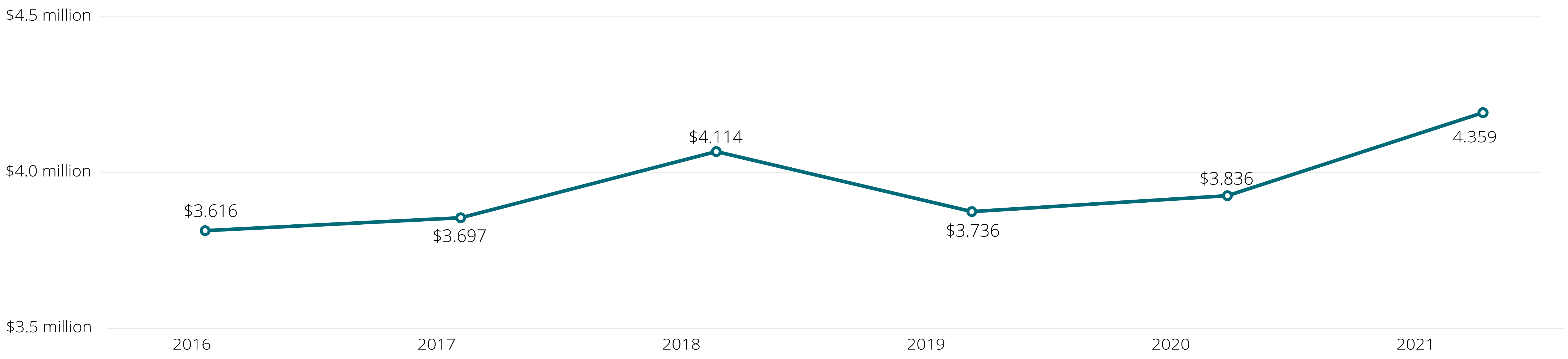


Figure 15. Auction Guarantees:
Average value of guaranteed lots (based on low estimate)
Post-War & Contemporary Art Evening Sales in London, New York and Hong Kong (Sotheby's, Christie's and Phillips US$ thousand)
Source: ArtTactic



Auction guarantees helped shore up the auction market during the pandemic: auction guarantees declined during 2020 by 20% to US$859 million. This followed a similar trend to the overall evening sales of post-war and contemporary art at Sotheby's, Christie's and Phillips, which saw a 30% decline in sales value last year. However, the three auction houses' overall share of guaranteed lots by value increased from 37.1% in 2019 to 39.8% in 2020. This share grew further in the first half of 2021, with auction guarantees accounting for 40.7% of the total sales value of post-war and contemporary art evening sales during the first six months of this year, amounting to US$649 million. If the current trend continues, we could see guarantees matching the peak of 2018, when US$1.31 billion worth of guarantees were offered.

Higher returns are likely to attract more guarantors this year: the estimated average return on guarantees increased to 16.2% in the first half of 2021, compared with 11.8% in both 2019 and 2020 . An estimated profit of US$105 million was generated on guaranteed artworks at Sotheby's, Christie's and Phillips post-war and contemporary evening sales in the first half of 2021 (hammer price versus low estimate). This profit is typically shared between the guarantors and the sellers. The higher average return on guarantees is likely to lure more third-party guarantors to the market, as confidence and sales increase.

Hong Kong becomes an important market for auction guarantees: guarantors are shifting their attention to the Hong Kong market, as strong auction performances offer superior returns compared with London and New York. The guaranteed sales in Hong Kong's modern and contemporary evening sales (based on the low estimate) increased from US$92 million in spring 2020 to US$185 million in spring 2021. The total hammer value of guarantees this season came in 24% above the low estimate, signaling a superior return for guarantors compared with London and New York. Out of 39 guaranteed lots this spring, 38 sold above the low estimate (with 11 of these selling above the high estimate).

Joujoux
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Expert voices

The State of the Art in Italy

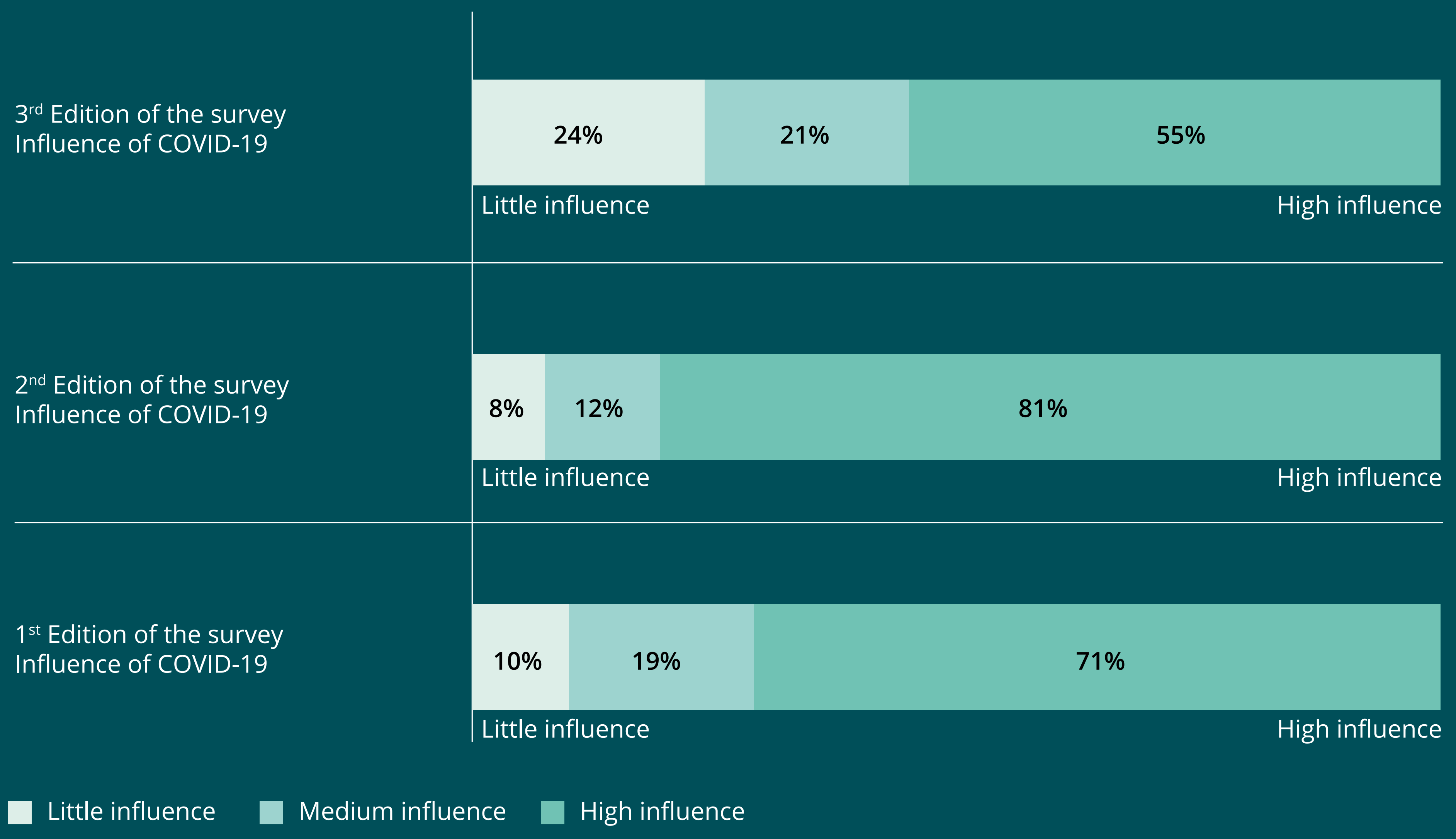
Results of the third survey on COVID-19's impacts

Since the outbreak of the COVID-19 pandemic, Deloitte Private in Italy has been monitoring the "Status of Art" of the artistic and cultural system. This brief paper aims at describing the results of the third wave of a survey that has involved the main stakeholders belonging to the artistic and cultural system in Italy to analyze the evolution of the impacts of the pandemic crisis on the sector, but also their expectations for the future, considering the relevance of the artistic and cultural places and sites in Italy and the presence of a wide range of operators directly or indirectly connected to the Italian art system for which a specific support has been assigned, together with tourism, in the Next Generation EU funding dedicated to Italy.

The first section of the survey, addressed to the entire panel of addressees, focuses on the main aspects of the experience of purchasing and enjoying art and collectables in the last few months, period during which the pandemic has weakened, allowing the organization of live events and the return to museums and exhibitions. This is a major change, in a sector that has survived only through digital initiatives and strategies that have been implemented to keep the pre-existing relational networks alive.

In fact, the respondents confirmed that in the last period the pandemic has had less impact on the fruition of art and culture, also if compared to the first two waves of the survey conducted in September 2020 and January 2021.

Figure 16. The influence of COVID-19 on the fruition of arts and cultural goods



Only 45% of the respondents affirms to have started again to enjoy the places of culture still open to public. This means that, even if access to these places is now possible, the public has felt partly discouraged to participate in live exhibitions at museums, galleries and other exhibition sites. According to the panel, among the factors that have discouraged the attendance of these places and may affect the future attendance is the reduced appetite for travels (30%), and the residual fear of being infected (24%), which however has decreased with respect to the previous editions of the survey. Yet the perception regarding the future fruition of arts of the 58% of the respondents has improved, if compared with the perception at the beginning of the pandemic crisis.

This result highlights how the artistic and cultural sector is still struggling, but on the right path to recover from the crisis, at least if we consider the perception emerged from the survey and the general context. In fact, the same conclusions can be drawn by internationally recognized organizations' analysis. According to ICOM (International Council of Museums)[39], which has carried out three surveys[40] involving museums around the world starting from spring 2020, impact has very badly affected museums professionals, with almost one in ten of the participating museums that had to lay off staff members because of the crisis. Comparing the data from the three ICOM surveys there is more confidence for the future – with the percentage of museums facing a permanent closure has fallen from 12.9% to 4.1% -. Yet, ICOM underlines that "without adequate financial relief measures, the pandemic will still have major repercussions in terms of reduced operational capacity, affecting opening hours, exhibitions and public programs." In the same way, a series of reports that deepen the impact of COVID on the sector published by UNESCO[41], calls for substantial public and private intervention, including policies that strongly support culture, to support places of culture and workers in the sector.

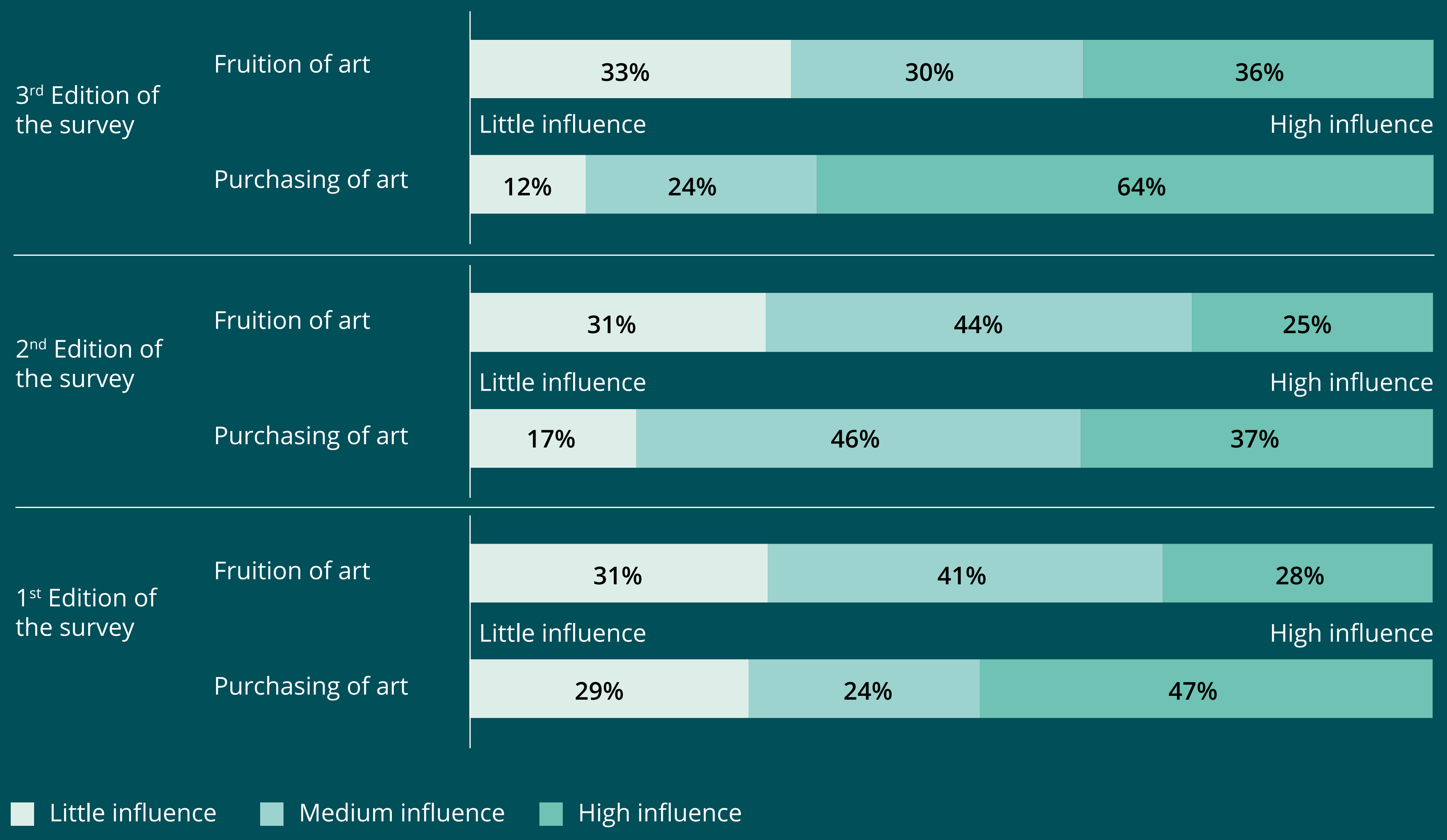
Nevertheless, the reports also highlight that digital strategies and tools have improved in the artistic and cultural sector, and this has been confirmed also by the results of our survey.

In particular, if we return to analyze the results of our third survey, respondents have confirmed the improvement of online tools for the purchase of works of art, as well demonstrated also by the increasing attention towards NFTs (Not Fungible Tokens[42]) and digital art.

Yet, even if virtual initiatives have exploded since the beginning of the pandemic, with regard to fruition of arts the perceptions of the respondents still show cautiousness in affirming that online tools will substitute live fruition. The emotional and social aspect of the live presence remains indispensable for art enthusiasts and professionals: only the 9% of the respondents declare that the online services will replace the live ones, while the 15% think online will not be able to substitute any live services at all, and the other respondents think that online services will only partially replace live services.

39 ICOM, Museums, Museums Professionals, and COVID-19: Third Survey, July 2021
40 The first survey has been carried out in spring 2020; the second one in early autumn 2020; the third one in spring 2021.
41 UNESCO, Disruption and Resilience: UNESCO reports reveal new data on impact of COVID-19 on culture, 17th June 2021, https://en.unesco.org/news/disruption-and-resilience-unesco-reports-reveal-new-data-impact-covid-19-culture
42 According to Forbes Advisor: "An NFT is a digital asset that represents real-world objects like art, music, in-game items and videos. They are bought and sold online, frequently with cryptocurrency, and they are generally encoded with the same underlying software as many cryptos. Although they've been around since 2014, NFTs are gaining notoriety now because they are becoming an increasingly popular way to buy and sell digital artwork.", https://www.forbes.com/advisor/investing/nft-non-fungible-token/

Figure 17. Effectiveness of online tools in the fruition and purchasing of art



Thanks to the reopening of the cultural places the use of online tools has decreased in the last weeks: 48% of the respondents did not use them, with a meaningful 12% that claims to not have used them for artistic purposes so far. It should be also considered that the 85% of respondents states that in the next 1 or 2 years online services may substitute live services up to 50%.

This is due to the major change that cultural organizations have recently been passing through: the vaccination campaign has improved the perceptions of the respondents, with 50% of them thinking that levels of fruition of arts and culture will return at the same levels of the pre-COVID-19 period. In order to do that, new regulatory instruments aimed at encouraging private support for the artistic and cultural sector, sector - such as tax concessions, which is the variable that according to respondents could give the sector more impetus (39% of the panel) - are needed. This could be particularly true for those categories that were not included in recovery funds and plans at a national and international level.

Funds are needed also for supporting the little organizations that work in the arts market, such as galleries and dealers, because “art” as an “asset class” has not lost the appeal of the market (89% of the respondents), but 7 out of 10 of the respondents affirms that volumes of transactions has decreased up to 50%. The expectations for future turnover are also negative: more than the 50% of the panel affirms that turnover will decrease up to 25% in 2021, if compared to 2019 (the last “not-COVID” fiscal year). According to more than 1 out of 3 respondents, 1 or 2 years are needed for recovering the market levels of the period before COVID-19.

Yet we can observe a positive opinion with regard to digital channels: the majority of the operators involved in the survey believe that online tools are very effective in substituting the offering of live services (73%), while 18% consider the effectiveness to be medium-level. The share of those who strongly support the relationship of person has decreased, but it is still relevant (9%).

In the opinion of the operators interviewed, the main impact that the Covid-19 pandemic will have on the art market system in the short term (1-2 years) will concern the rarefaction of trade fairs and the disappearance of minor appointments. This is a very plausible effect given the crisis experienced by the art fairs sector, which in recent years had seen the birth of hundreds of very specialized appointments, often proposed as satellite events of more established fairs, such as ArtBasel or Frieze.

In conclusion, the third analysis that Deloitte Private in Italy has carried out to deepen the impact of one of the worst economic and social crisis in contemporary history has proven once again the very broad and deep impacts of the pandemic on the arts and cultural sector. Nevertheless, the analysis has also proven how the pandemic has encouraged all the operators in the sector to find alternative channels for establishing a more meditated and complex relationship with the public. Moving digital has certainly been a form of survival, but what has happened is likely to affect the future dynamics, in which online and offline will hopefully coexist, enriching each other. Once again, the future of the sector depends on the development of the pandemic at an international level, but culture has proved its resilience now more than ever, making us confident for its performance in the post-COVID-19 era.

NFTs

What could the growth in the NFT market mean for the art and finance industry?
Over the last nine months, NFTs have broken through to the mainstream and the art market. The big auction houses jumped on the NFT bandwagon in March 2021, when Christie's established a new all-time NFT record of US$69 million for Everydays: The First 5000 Days by the artist Mike Winkelmann (aka Beeple).

According to a recent article by Reuters[43] citing data from crypto analytics platform DappRadar, NFT sales value of all categories reached just under US$2.5 billion in the first half of 2021, up from just US$13.7 million in the first half of 2020. The Reuters article also quoted another analytics platform, NonFungible.com, which reported a lower figure of US$1.3 billion in NFT sales in the first half of 2021, excluding around US$8 billion of decentralized finance (DeFi) NFTs.

NFTs have created a new global "digital art and collectibles" market that was non-existent in the past or only accessible to a select few. It has allowed creators and artists working in the digital medium to monetize their work and talent in a new and different way, potentially redefining the concept of ownership. From a buyer's perspective, the NFT market has democratized ownership of digital art. It builds an infrastructure that creates unique, traceable and undisputed ownership records of a digital artwork, which can be easily traded in the secondary market without requiring any traditional art market intermediaries. Therein lies the potential for disruption.

On the other hand, the speculative nature of the NFT art and collectibles market has become an issue, and was illustrated in a recent report[44] published by Hiscox and ArtTactic in October 2021. The report found that in August this year, NFT sales of crypto art and collectibles reached a new all-time high of an estimated $1.69 billion in sales, eclipsing the previous record month in March 2021 of $356 million. The surge in NFT sales over the last months were, according to the report, driven by crypto collectibles (such as CryptoPunks and Bored Ape Yacht Club), as well as generative art projects (such as ArtBlocks and BlockArt). However, the boom fizzled out in September 2021, as NFT sales dropped 69% to $520 million, showing the volatile nature of the current NFT art and collectibles market. (See also figure 18 on p.61)

But speculation is not the only challenge facing the NFT art and collectibles market. Cybercrime, legal considerations such as copyright, authenticity and regulatory uncertainty, as well as the environmental costs associated with minting NFTs are other concerns that also need to be addressed in the future.

Recent developments are raising the question of what role NFTs could play within the traditional art market and the museum sector going forward. Already, we have seen major auction houses adopt NFTs as well as galleries such as PACE, who seem to be strategically positioning themselves for a future around digital collectibles, as a way to reach new audiences and create new revenue sources for their artists. In the case of museums, the Uffizi Gallery and the State Hermitage Museum are raising funds by minting and selling NFTs of works in their holdings. See article from Bernadine Brocker Weider p.150 in section 3. See article from Megan E. Noh, Brave new media - Collector risks in relation to the insurability and valuation of NFTs pg 304 in section 8.

Material_Girl
©Thierry Bal/Courtesy Phillips, London - 2015

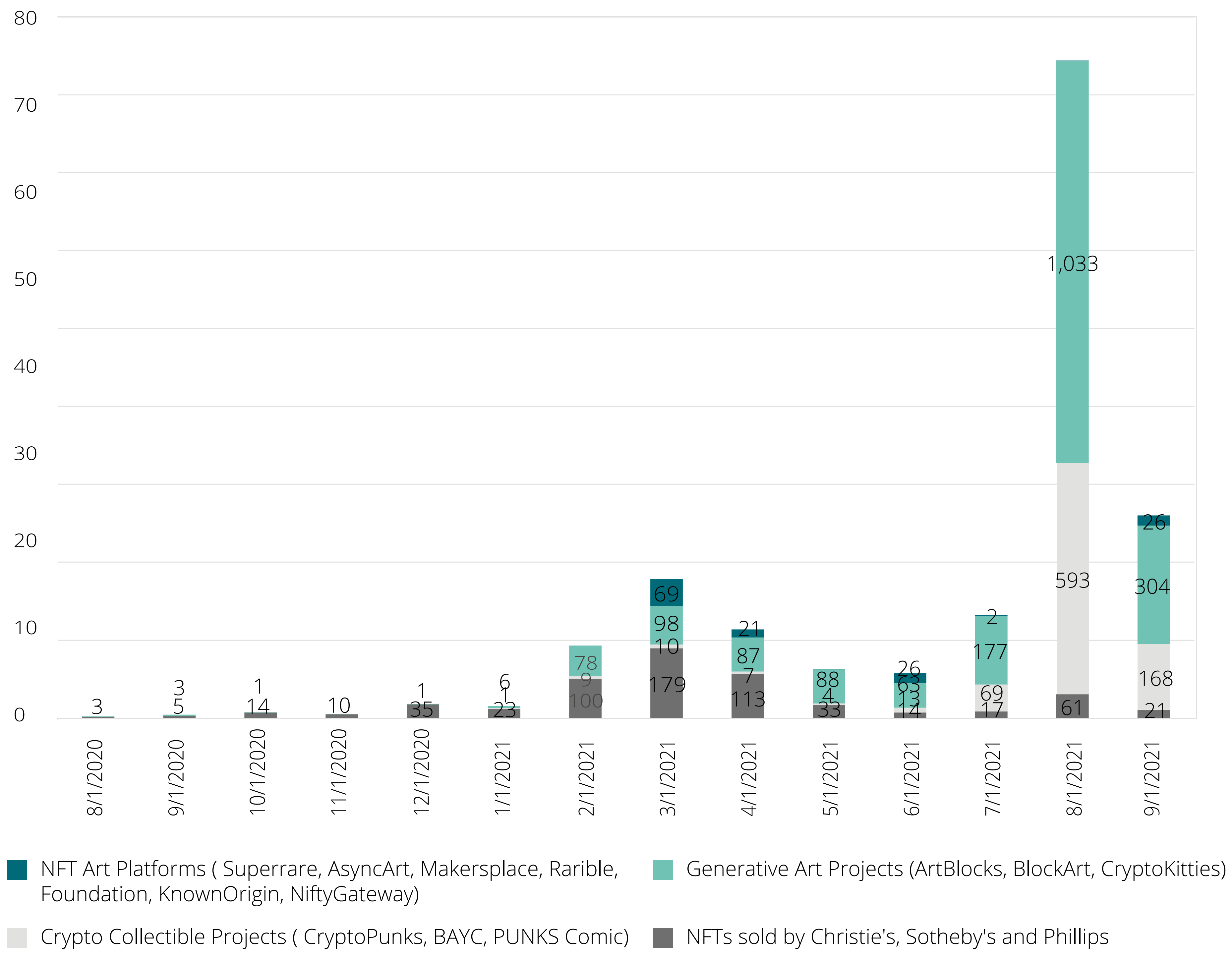
43 **Reuters**, NFT sales volume surges to $2.5 bln in 2021 first half, July 5 updated July 16, 2021
44 Hiscox Online Art Trade Report 2021 - Part 1, October 2021

Another trend related to NFTs and tokenization is the growing market around DeFi, often called "open finance". DeFi is a collective term for financial products and services that are accessible to anyone using Ethereum or another blockchain environment. It is an alternative financial system built around the crypto economy, and includes exchanges, lending and creating financial instruments such as derivatives. For a broader discussion around this topic, see the article p.269 **"Art & Blockchain: Unlocking new opportunities thanks to decentralized models.** (Section 7), as well as contributions by Look Lateral Group (p.249) and Sygnum bank (p.247) in Section 6.

These recent developments in the NFT market are likely to be a precursor for major innovations and changes to come, with implications for both the art market and the associated art and finance industry.

Figure 18. NFT art and collectibles sales (US$ million) between August 2020 and September 2021

Source: ArtTactic



Methodology

Data sources are collected from ArtTactic and Non-fungible.com and CryptoSlam. NFT sales in this analysis are based on some of the key curated NFT platforms such as; Superrare, Rarible, Nifty Gateway, MakersPlace, KnownOrigin, Foundation, BlockArt, AsyncArt as well as NFT sales through Christie's, Sotheby's and Phillips. Crypto-collectibles are based on data from sales of CryptoPunks and Bored Apes Yacht Club and PUNKS Comic. Generative art is based on sales of Cryptokitties, ArtBlocks and BlockArt.

Marcus Fox
Global Managing Director
20th/21st C. Art, Christie's

Expert voices

The 266-Year-Old Start-Up

An insider's view of the NFT boom

The art world bubbles with hyperbole. It can be hard to differentiate the truly new from something being re-packaged as such. When Christie's sold Beeple's EVERYDAYS: THE FIRST 5,000 DAYS from a $100 starting bid to a final sale price of just under US$70 million, it was clear this was the truly new emerging before everyone's eyes. If the fall of an online gavel made noise, it would have been the sound echoing around the digital world. Suddenly everyone was talking about Beeple and NFTs.

In my role I tend to work in the background, but in the flurry of media outreach, even I found myself on Canadian daytime television. Calls were coming in from a multitude of industries wanting to know how to replicate this success. In the ensuing months there has been a great deal of experimentation and education. There is a lot to unpack when combining a technological function, the existing art market, and the burgeoning market for digital art. Let's discuss some of what happened and what I've learned.

Many asked why Christie's, a 266-year-old company, got involved in something that could be considered a 'new fad.' While the auction business has been innovating over the last several years, through both intention and circumstance, the move into digital art and NFTs may have seemed an abrupt non-sequitur. When examined more closely, however, there were many leading indicators presaging this moment.

Christie's recognized early on the need to adapt and embrace like-minded community-building strategies and respond to an increasing comfort for promoting and transacting art sales online. In the same month as the soon-to-be landmark Beeple sale, Christie's had already received great feedback from being the first major house to offer an NFT at auction—a work by Robert Alice. Beeple was a long-standing practitioner in the digital art arena, with a loyal following and track record of a significant rise in market prices since October 2020. The sale of EVERYDAYS was the natural next step in our evolution.

The technology underlying NFT-based artwork provided the tool to trade digital assets with an ever-growing fanbase, but with limited attention or focus from the traditional art establishment until now. The combination of these different elements was ultimately the catalyst for our record-setting result—Christie's achieving not only the highest price ever for an NFT but the third highest price for a living artist at auction.

It is a truism that in many cases the more you learn, the more you realize how little you know. In Martin Broadwell's four level of teachings, I found myself squarely in phase two: 'Conscious Incompetence'. I came to the fast realization that there was a huge amount that I did not know. Fortunately for me, there is a vast, consistently patient and supportive community surrounding digital art. It became clear that although the sale of digital art could be conducted through Christie's channels, it really needed to be understood as a start-up. The clients were new, the currency was new, and the works being sold were new—at least to the long-standing Christie's audience.

I, along with a number of colleagues, got a crash course in ERC-721 token standard protocol, the pros and cons of different metaverses, and Metamask wallets; got to meet and work with MetaKovan, and listened and read a great deal on Clubhouse, Discord, and Twitter. Most of the legal documents surrounding a sale needed to be changed since there are no hands-on inspections, the inability to take possession eliminates shipping expenses, tax implications need to be determined, and the list goes on.

There was also the matter of cryptocurrency. The Beeple work was the first artwork to be paid-in-full in cryptocurrency by any auction house. This required Christie's to establish a secure wallet, and ensure that the requisite Know Your Client (KYC) and Anti-Money Laundering (AML) requirements of a crypto sale would be consistent with those of all other Christie's sales. It also required someone with great attention to detail to issue the invoice to the buyer. The 20-digit code to Christie's digital wallet was included on the invoice. If even one digit was mis-entered, the payment would not be received and the money would disappear forever, without opportunity for recall. Slightly terrifying!

The other thing that happens when you sell an intangible for almost US$70m is it drives headlines. The Beeple work was on the cover of most major-market newspapers in the world the day after the auction. Immediately the volume of enquiries exploded. Calls were happening in industries far beyond the traditional auction sector. Executives and IP holders were all caught trying to comprehend what happened and how best they could join in. My group established a programming and vetting committee to evaluate how the prospective leads could work with our ambitions. It felt like Christie's, and importantly, my colleagues and I were starting to become part of the community that had nurtured us in the first instance, as well as playing a role in expanding that community.

Variety and experimentation were key in determining which projects to prioritize. What can one do as a second act after the EVERYDAYS? We decided to push the idea of the intersection between the digital and physical art worlds by offering a group of Cryptopunks in our 21st C. Evening sale in May 2021 in a wry nod towards the 'historical', standard-setting NFT project conceived by Larva Labs before the NFT craze took off. The fact that this consignment came directly from the Larva Labs team, and would be presented in the context of an Evening auction in New York—the biggest platform Christie's offers—proved a winning combination with a sale price in excess of US$17 million.

On the heels of this project, we announced our collaboration with the Andy Warhol Foundation for the Visual Arts, which was quickly followed by a sale curated by noteworthy insider, Lady Phe0nix. The former aimed to find the intersection points on the once-separate Venn Diagram of the art worlds, while the latter sought to introduce a broad and heterogenous selection of artists to the wider world with a strong emphasis on the archival elements associated with the minting process. In June, coinciding with Pride Month, FEWOCiOUS disproved the myth that digital art is cold and impersonal with a series of deeply personal works on his complicated, and ultimately redemptive, path to coming out as transgender.

So, what have we learned as we close out the first six months of programming? Authenticity is key—in all respects. In a world that prides itself on decentralization, everyone has a voice. Digital replicas of physical objects hold no appeal. The digital art community, perhaps unsurprisingly, have been earlier adopters of physical works of art than the inverse. There are markets within markets depending on collecting category and price point. The prices of cryptocurrencies have a simultaneously enhancing/chilling effect on 'consumer confidence', similar to the effect of the stock market on clients invested in hedge funds.

We are still at the very beginning of this journey. The profligate spending on NFTs will face a reckoning. This is well understood in the community, yet confidence remains about the long-term prospects. New ideas of how to use NFTs across platforms are well underway, and, it's safe to say, have much room for growth, well beyond the art world. Concurrently the environmental impact of mining coins and minting tokens has moved to the fore. Many alt-chains built on Proof of Stake, or even Proof of Authority, lazy minting processes, and mining incentives offer encouraging solutions that may indicate positive change to come as the entire community rallies around creating a sustainable future for the newfound thriving marketplace.

Finally, as has occurred in many other developing markets, there is a strong need for research and education. There are new platforms constantly being deployed and new works being created, resulting in a cacophony. A market consolidation is coming. Market professionalization is coming in many forms: security, insurance, appraisals, tax regulations, display options, etc. Institutional attention with (perhaps new approaches to) connoisseurship are also coming. The community is strong, as is the realization that the more participants involved, the greater the chance for staying power. Christie's is delighted to join the ranks.

Regional trends

Wealth, economic indicators and modern and contemporary art markets

Table 6. Economic indicators

			Economic review 2020		Economic outlook 2022	
	Real GDP Growth 2020*	Real GDP Growth Trend +/-*	HNWI wealth growth 2019 to 2020**	Real GDP Growth Outlook 2022*	Economic Outlook Trend (2021 vs 2022)	Wealth Outlook 2025 (5 year growth in UHNWI population)***
Global Trend	**-3.3%**	**Negative**	**7.6%**	**4.40%**	**Positive**	**27%**
United States	-3.5%	Negative	11.3%	3.50%	Negative	24%
United Kindom	-9.9%	Negative	-3.0%	5.10%	Neutral	39%
Europe	-6.6%	Negative	2.8%	3.80%	Negative	23%
China	2.3%	Negative	11.0%	5.60%	Negative	46%
Japan	-4.8%	Negative	4.4%	2.50%	Negative	15%
Middle-East	-2.9%	Negative	6.8%	3.80%	Positive	25%
South Asia	-8.0%	Negative	5.9%	6.90%	Negative	63%
Latin America	-7.0%	Negative	-4.0%	3.10%	Negative	25%
Southeast Asia	-3.4%	Negative	5.8%	6.10%	Positive	31%
Russia	-3.1%	Negative	1.2%	3.80%	Neutral	29%
Africa		Negative	2.7%	4.00%	Positive	33%

Source: ArtTactic

* IMF World Economic Outlook, April 2021
** Source: Capgemini, World Wealth Report 2021
*** Knight Frank's The Wealth Report 2021

Table 7. Art market indicators

	Auction Market Sales 2020				Art Market Outlook 2022		
	Art Market Modern & Contemporary Auction Sales 2020 (USD million)	Market Share % in 2020	Art Market Sales Growth 2019-2020	5 Years Sales CAGR (2015-2020)	Up	Flat	Down
Global Trend	3127	100.0%	-20.9%	-4.0%	36%	43%	20%
United States	1765	56.4%	-24.1%	-4.7%	70%	25%	5%
United Kingdom	736	23.5%	-13.1%	-5.6%	42%	47%	11%
Europe	144	4.6%	-34.5%	-5.3%	45%	42%	13%
China	165	5.3%	22.5%	8.9%	56%	31%	13%
Japan	70.9	2.2%	-43.3%	-3.6%	47%	37%	16%
Middle-East	21.2	0.7%	-36.6%	-8.3%	34%	43%	23%
South Asia	76.5	2.3%	-6.6%	2.4%	6%	61%	33%
Latin America	67.7	2.0%	-1.0%	-7.8%	17%	29%	55%
Southeast Asia	12.1	0.4%	-35.5%	-30.8%	22%	60%	18%
Russia	41.8	1.3%	-38.1%	9.3%	20%	57%	23%
Africa	30.5	1.0%	-3.5%	51.7%	42%	41%	9%

Source: ArtTactic

Figure 19. United States (US$ million)

*Art market analysis is based on post-war and contemporary evening and day auctions—Sotheby's, Christie's and Phillips in New York.

Source: ArtTactic

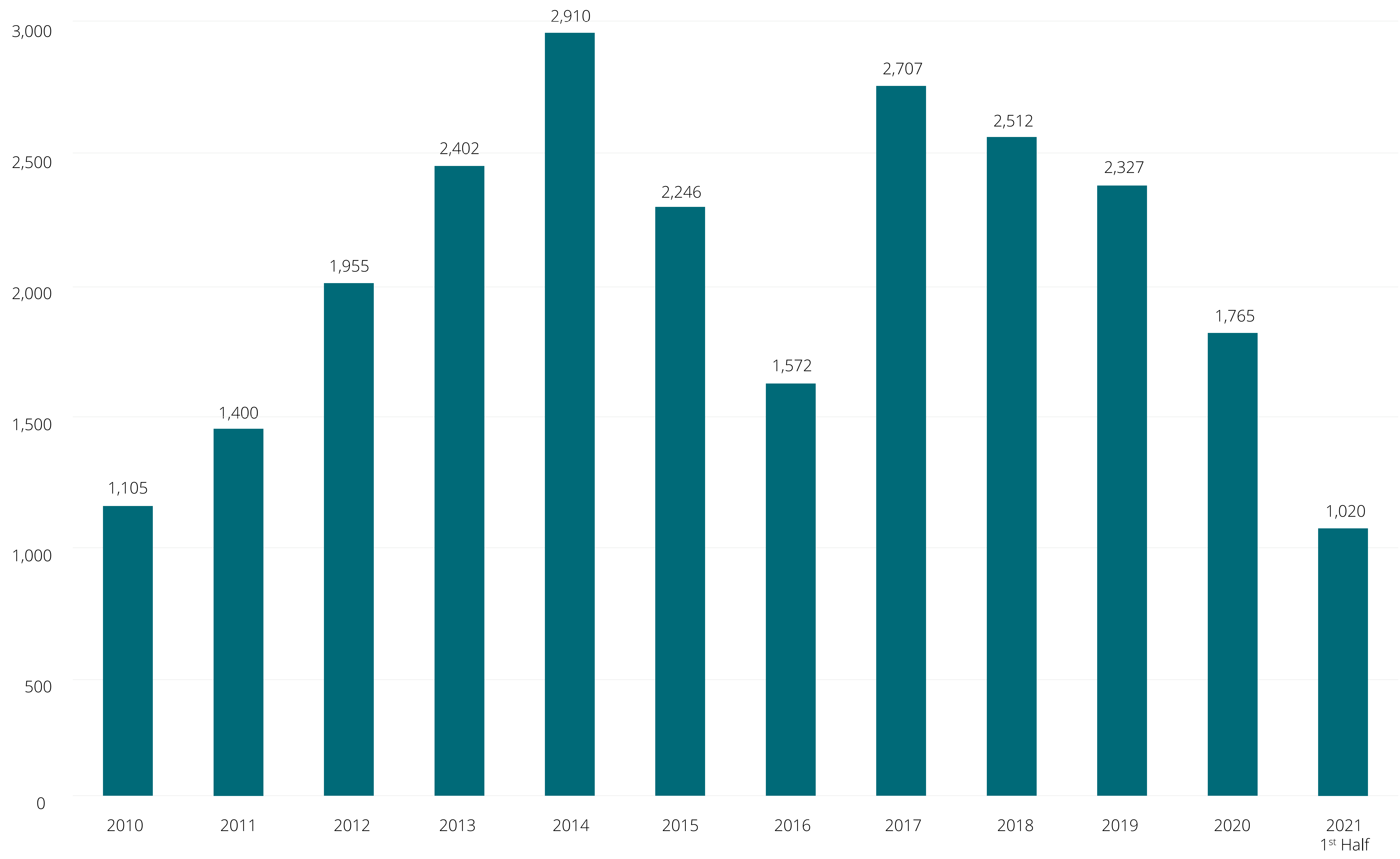


Table 8. United States

Economic and wealth indicators	Modern and contemporary art market*
HNWI wealth population (thousands) 2020	Auction sales in 2020 (US$ million)
6,575	1,765
11.3%	-24.10%
Real GDP growth 2021	Global market share
6.4%	56.50%
GDP growth outlook 2022	Art market outlook 2022
3.5%	Up:70% flat:25% down:5%
The world's largest art market experienced a fall in auction sales of 24.1% in 2020. However, strong auction results in the first half of 2021 and a positive outlook among art market experts suggest a strong recovery in 2021.	
10-year CAGR (2010-2020)	9.8%
HNWI wealth population figures are estimates from The World Wealth Report 2021 (CapGemini)	
GDP figures are from the World Economic Outlook April 2021 (IMF)	

Figure 20. United Kingdom (US$ million)

*Art market analysis is based on post-war and contemporary evening and day auctions—Sotheby's, Christie's and Phillips in London.

Source: ArtTactic

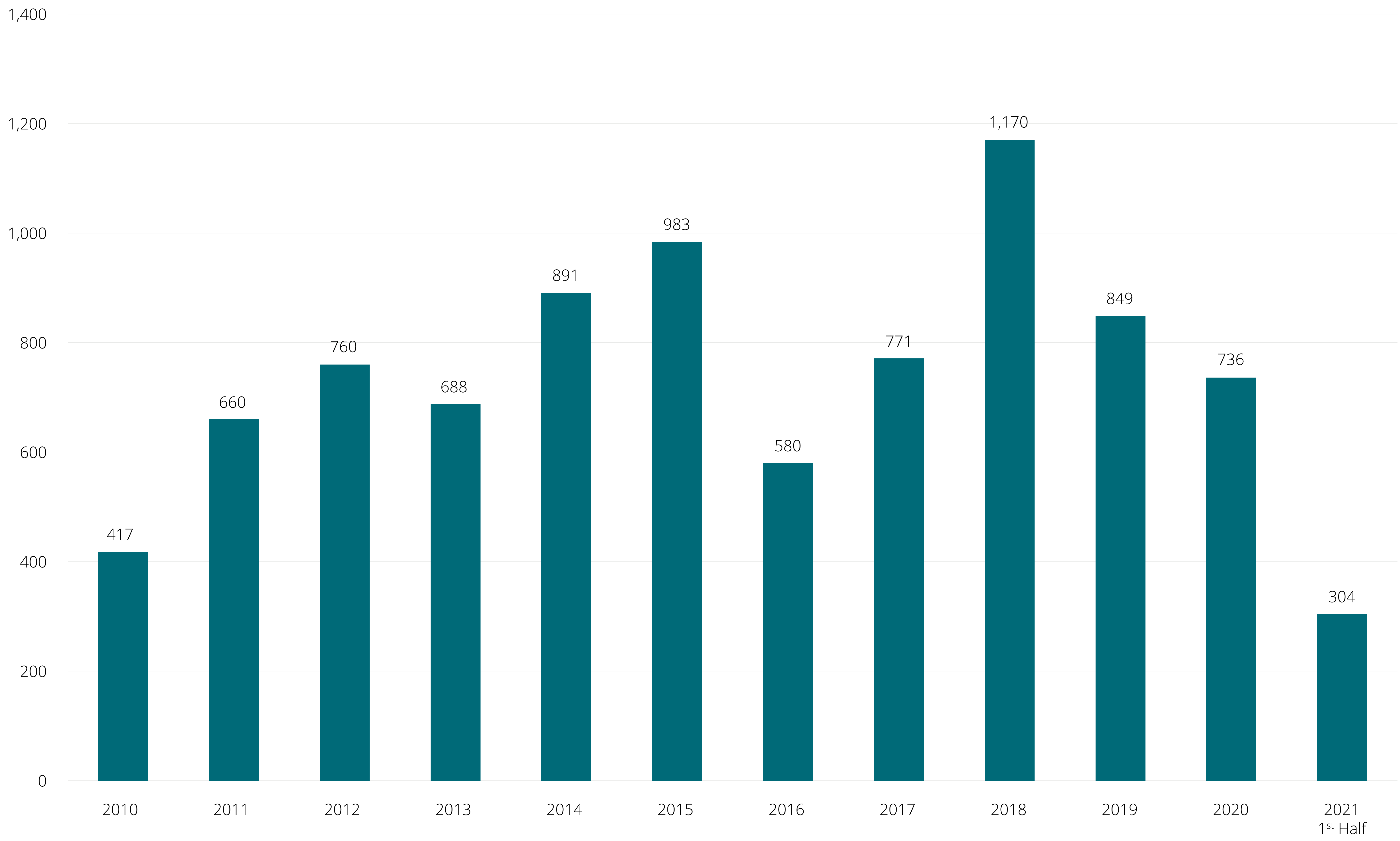


Table 9. United Kingdom

Economic and wealth indicators	Modern and contemporary art market*
HNWI wealth population (thousands) 2020	Auction sales in 2020 (US$ million)
573	736
Change in HNWI population 2019/2020	Sales growth 2019-20
-3.0%	13.10%
Real GDP growth 2021	Global market share
5.3%	23.50%
GDP growth outlook 2022	Art market outlook 2022
5.1%	Up: 42% flat: 47% down: 11%
Despite Brexit uncertainty and the impact of the pandemic, the UK art market managed to stem its losses in 2020, with a 13.1% fall in auction sales. However, modern and contemporary sales in London have not seen the same rebound as the US and European auction markets in the first half of 2021, which may be a sign that the market is shifting away from the United Kingdom in a post-Brexit world.	
10-year CAGR	5.9%
HNWI wealth population figures are estimates from The World Wealth Report 2021 (CapGemini) GDP figures are from the World Economic Outlook April 2021 (IMF)	

The advent of Brexit on 1 January 2021 triggered new challenges for the UK art market, such as a rise in red tape and delays related to the transport of artworks to and from the EU. In the following articles, on p.75 & 76, Simon Hornby, Senior Vice President, Crozier Europe, discusses the short- and potential long-term impacts of Brexit on the global art logistics industry and the UK art market as a whole. Deloitte Italy, also draws attention to the legal aspects concerning the circulation of artworks between the EU and the UK.

Figure 21. Europe (US$ million)

*Art market analysis is based on post-war and contemporary evening and day auctions—Sotheby's and Christie's in Paris, Amsterdam and Milan.

Source: ArtTactic

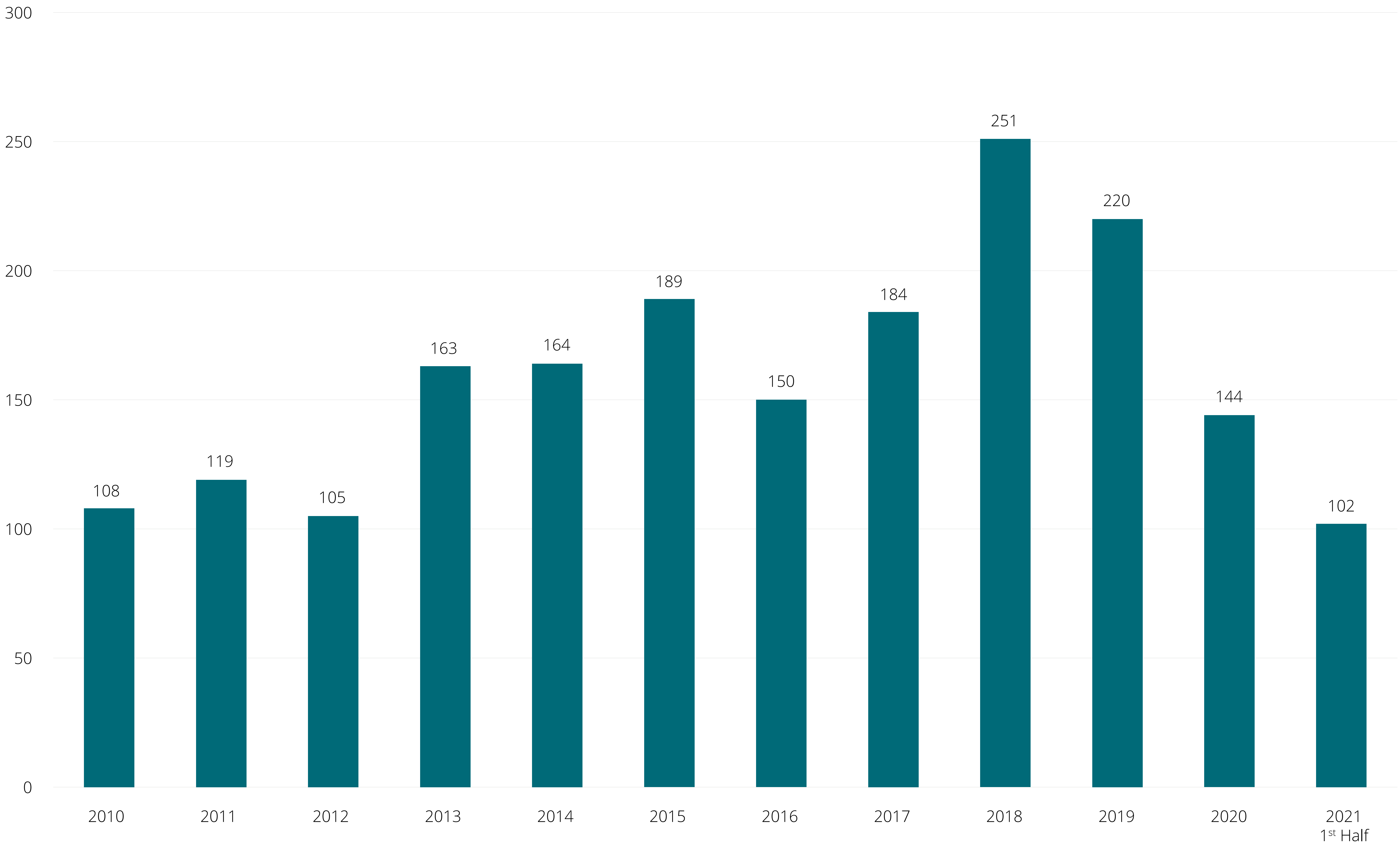


Table 10. Europe

Economic and wealth indicators	Modern and contemporary art market*
HNWI wealth population (thousands) 2020	Auction sales in 2020 (US$ million)
4827	144
Change in HNWI population 2019/2020	Sales growth 2019-20
2.8%	-34.50%
Real GDP growth 2021	Global market share
4.4%	4.60%
GDP growth outlook 2022	Art market outlook 2022
3.8%	Up: 45% flat: 42% down: 13%
The European modern and contemporary art market experienced a challenging 2020, as the auction market turned to digital and hybrid formats, with most sales conducted in New York, London and Hong Kong. However, experts remain positive about the coming 12 months, with 45% believing the European art market will rebound. Sales in the first half of 2021 show the auction market is already recouping losses incurred in 2020.	
10-year CAGR	2.9%
HNWI wealth population figures are estimates from The World Wealth Report 2021 (CapGemini) GDP figures are from the World Economic Outlook April 2021 (IMF)	

Figure 22. China (US$ million)

*Art market analysis is based on contemporary Chinese auctions - Sotheby's, Christie's, Poly Auction and China Guardian—Hong Kong and Beijing.

Source: ArtTactic

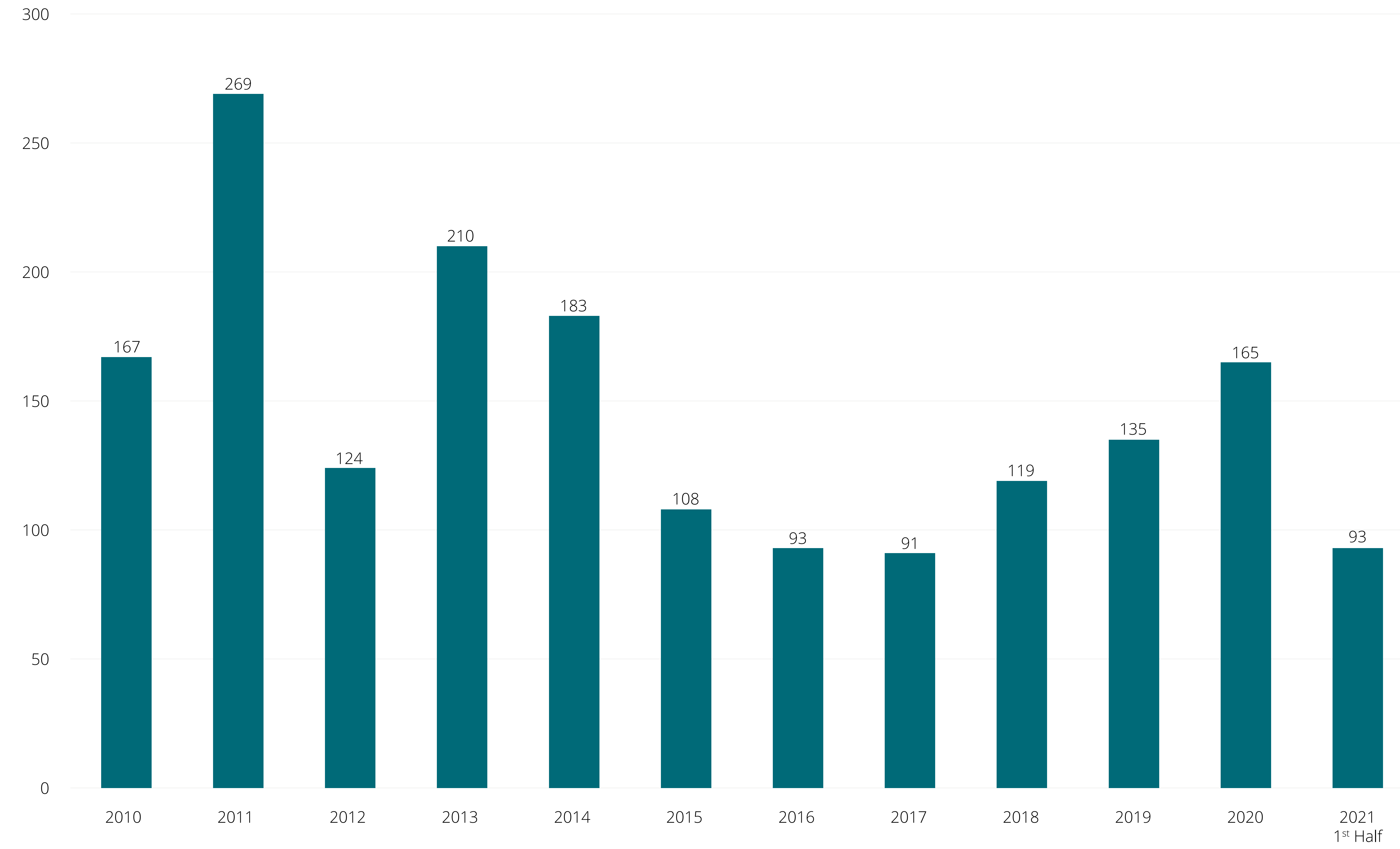


Table 11. China

Economic and wealth indicators	Modern and contemporary art market*
HNWI wealth population (thousands) 2020*	Auction sales in 2020 (US$ million)
1461	165
Change in HNWI population 2019/2020	Sales growth 2019-20
11.0%	22.50%
Real GDP growth 2021	Global market share
8.4%	5.30%
GDP growth outlook 2022	Art market outlook 2022
5.6%	Up: 56% flat: 31% down: 13%
Chinese contemporary art saw strong auction sales during 2020, despite the pandemic. The growth was particularly robust among the two Mainland Chinese auction houses, Poly and China Guardian, which saw a 44% growth in sales of Chinese contemporary art in 2020. This strong auction sales momentum has continued into the first half of 2021.	
10-year CAGR	-0.1%
HNWI wealth population figures are estimates from The World Wealth Report 2021 (CapGemini) GDP figures are from the World Economic Outlook April 2021 (IMF)	

Figure 23. Middle East (US$ million)

*Art market analysis is based on modern and contemporary auctions—Sotheby's, Christie's, Bonhams and Tehran Auction—Dubai, Doha, London and Tehran.

Source: ArtTactic

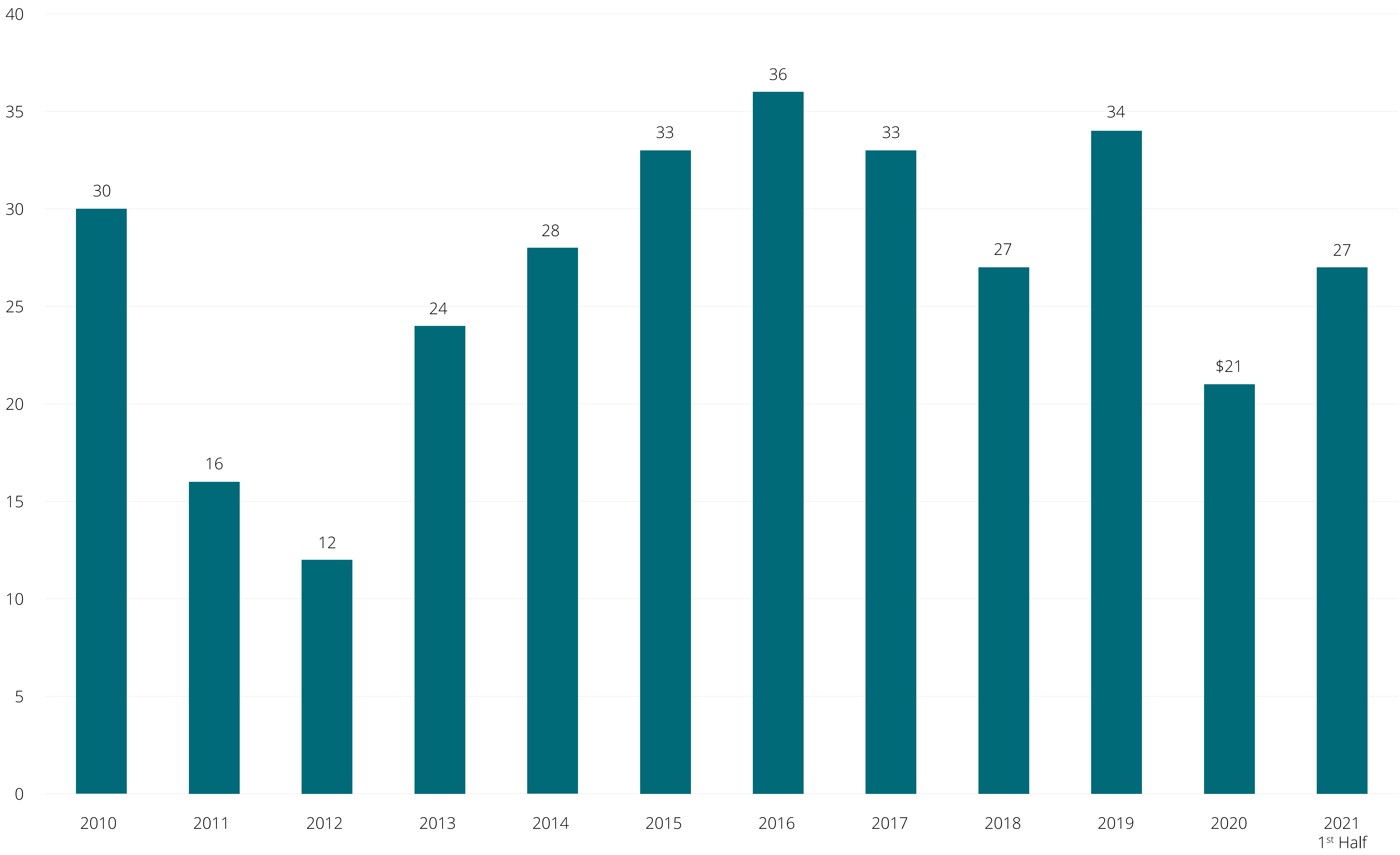


Table 12. Middle East

Economic and wealth indicators	Modern and contemporary art market*
HNWI wealth population (thousands) 2020*	Auction sales in 2020 (US$ million)
810.7	21.2
Change in HNWI population 2019/2020	Sales growth 2019-20
6.8%	-36.6
Real GDP growth 2021	Global market share
3.7%	0.70%
GDP growth outlook 2022	Art market outlook 2022
3.8%	Up:34% flat:43% down:23%
Auction sales of modern and contemporary art slowed considerably in 2020, as most auctions in the Middle East went online. However, the auction market's rebound in the first half of 2021 brings the auction market above the level of 2020. This means 2021 could potentially be a record year for Middle Eastern modern and contemporary art.	
10-year CAGR	-3.3%
HNWI wealth population figures are estimates from The World Wealth Report 2021 (CapGemini) GDP figures are from the World Economic Outlook April 2021 (IMF)	

Figure 24. South Asia (US$ million)
*The wealth population is based on India.
Source: ArtTactic

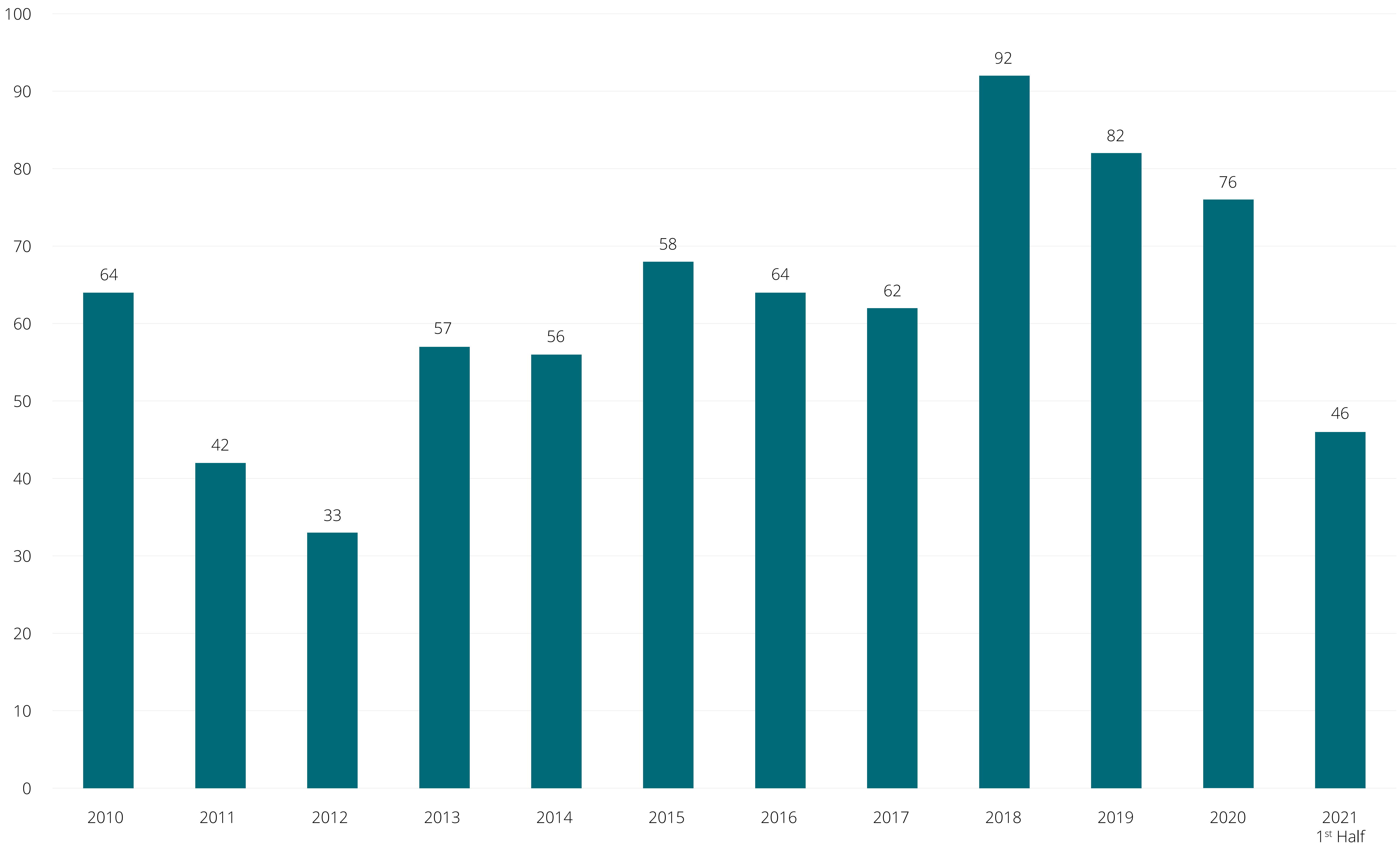


Table 13. South Asia

Economic and wealth indicators	Modern and contemporary art market*
HNWI wealth population (thousands) 2020*	Auction sales in 2020 (US$ million)
278	76.5
Change in HNWI population 2019/2020	Sales growth 2019-20
5.9%	-6.6%
Real GDP growth 2021	Global market share
12.5%	2.30%
GDP growth outlook 2022	Art market outlook 2022
6.9%	Up: 6% flat: 61% down: 33%
The South Asian modern and contemporary art market managed to weather the impact of the pandemic in 2020, with only a small decline (6.6%) in auction sales compared with 2019. However, with India being struck by a severe outbreak of COVID-19 in the first half of 2021, art market experts remain cautious about the coming 12 months.	
10-year CAGR	1.8%
HNWI wealth population figures are estimates from The World Wealth Report 2021 (CapGemini) GDP figures are from the World Economic Outlook April 2021 (IMF)	

Figure 25. South East Asia (US$ million)
*Art market analysis is based on modern and contemporary auctions—Sotheby's and Christie's—Hong Kong.
Source: ArtTactic

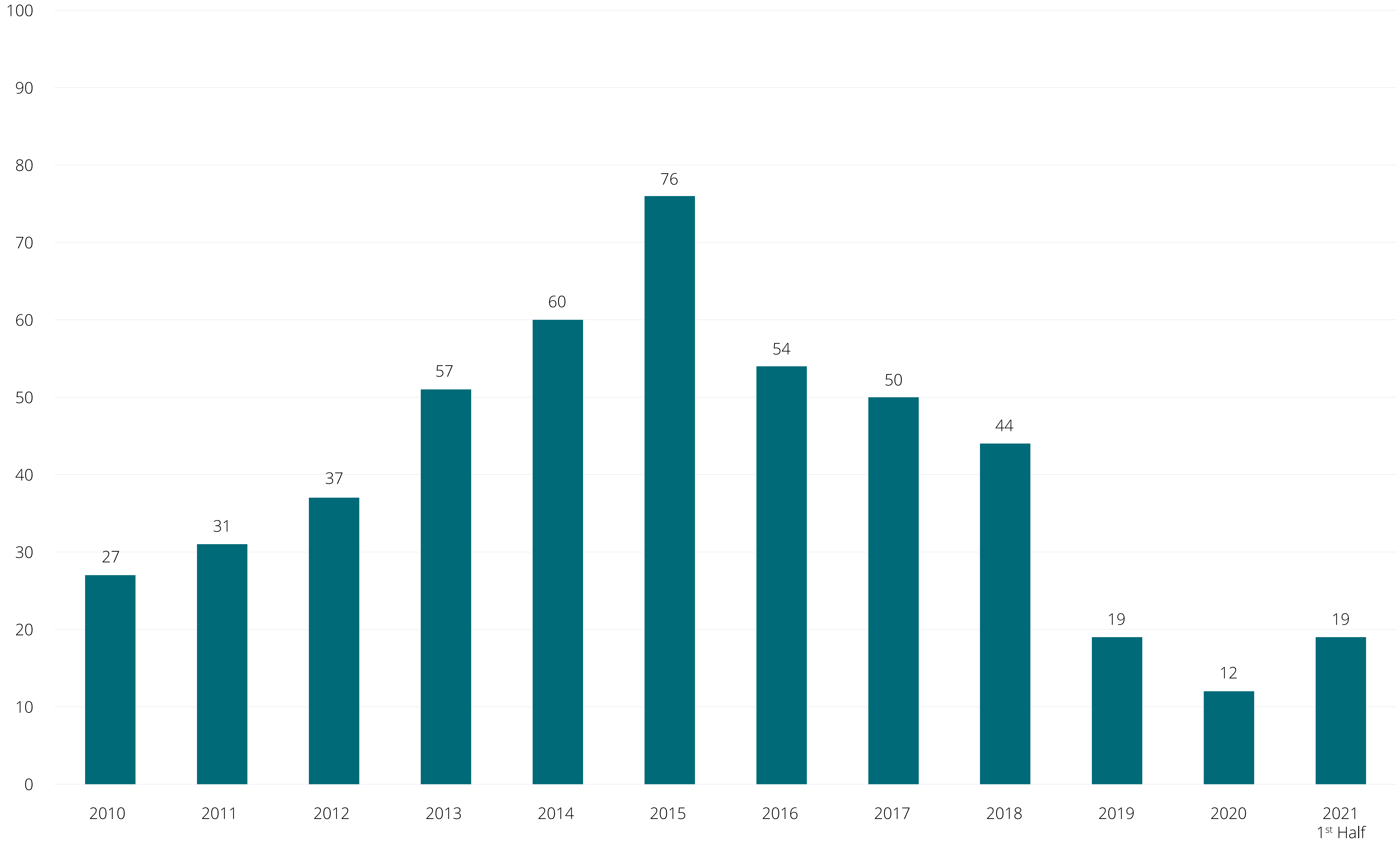


Table 14. South East Asia

Economic and wealth indicators	Modern and contemporary art market*
HNWI wealth population (thousands) 2020*	Auction sales in 2020 (US$ million)
360.4	12.1
Change in HNWI population 2019/2020	Sales growth 2019-20
5.8%	-35.5%
Real GDP growth 2021	Global market share
4.9%	0.40%
GDP growth outlook 2022	Art market outlook 2022
6.1%	Up: 22% Flat: 60% Down: 18%
Southeast Asian auction sales were down 35.5% in 2020, with more experts casting doubts about the direction of the coming 12 months. However, the first half of 2021 shows signs of a market revival, with the first six months exceeding the total sales of 2020 and 2019.	
10-year CAGR	South East Asia
HNWI wealth population figures are estimates from The World Wealth Report 2021 (CapGemini) GDP figures are from the World Economic Outlook April 2021 (IMF)	

Figure 26. Latin America (US$ million)
*Art market analysis is based on modern and contemporary auctions—Sotheby's, Christie's and Phillips—New York and London.
Source: ArtTactic

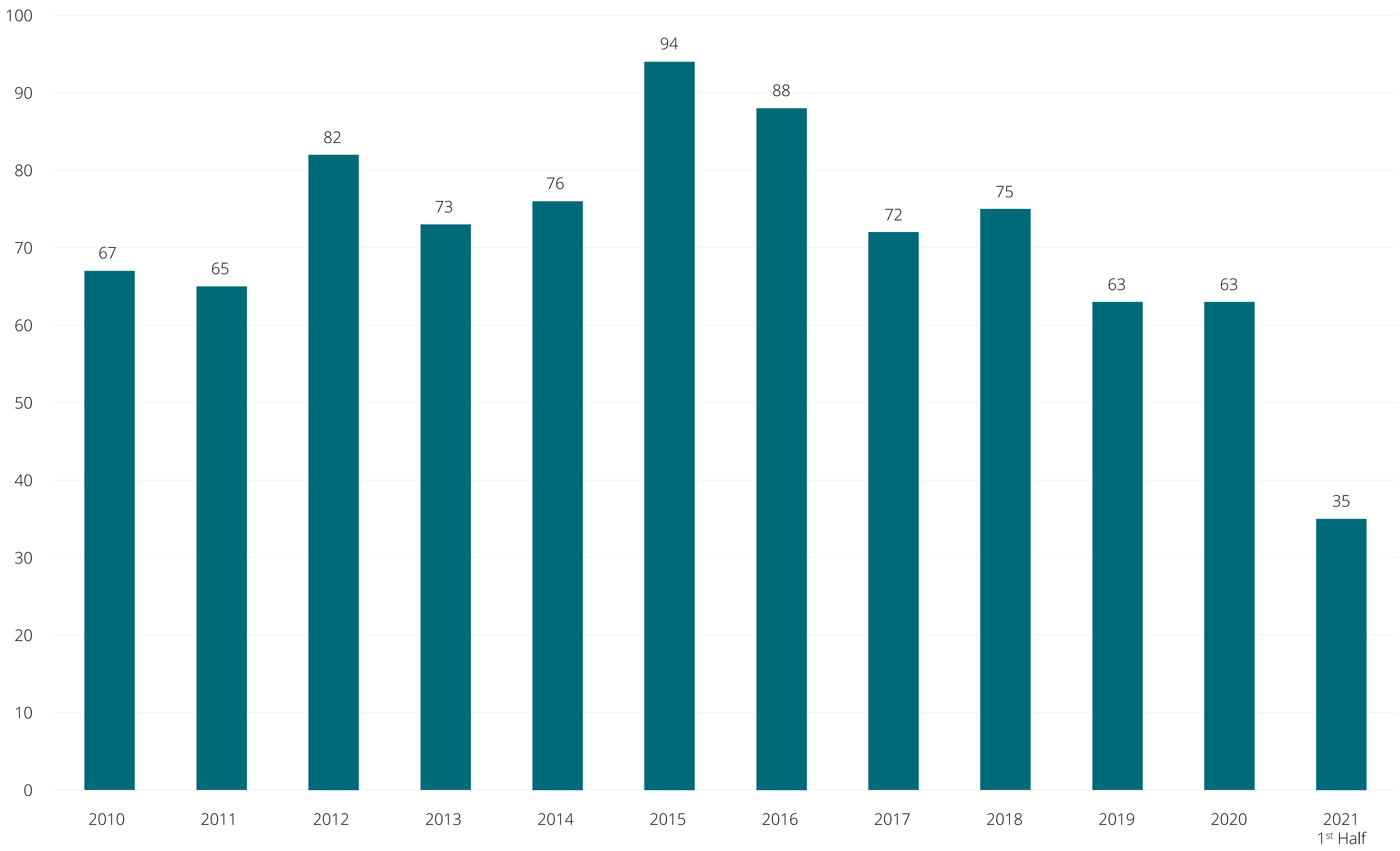


Table 15. Latin America

Economic and wealth indicators	Modern and contemporary art market*
HNWI wealth population (thousands) 2020*	Auction sales in 2020 (US$ million)
598.4	67.7
Change in HNWI population 2019/2020	Sales growth 2019-20
-4.0%	-1%
Real GDP growth 2021	Global market share
4.6%	2.00%
GDP growth outlook 2022	Art market outlook 2022
3.1%	Up: 17% flat: 29% down: 55%
Latin American auction sales weathered the pandemic well, with only a 1% decline in auction sales in 2020. Although experts remain negative regarding the market's 12-month outlook, auction sales in the first half of 2021 have set up the market to reach similar levels as in 2020 and 2021, assuming the second half of this year will be as strong as the first.	
10-year CAGR	0.6%
HNWI wealth population figures are estimates from The World Wealth Report 2021 (CapGemini) GDP figures are from the World Economic Outlook April 2021 (IMF)	

Figure 27. Russia (US$ million)

*Art market analysis is based on modern and contemporary auctions—Sotheby's, Christie's and MacDougall's—London.
Source: ArtTactic

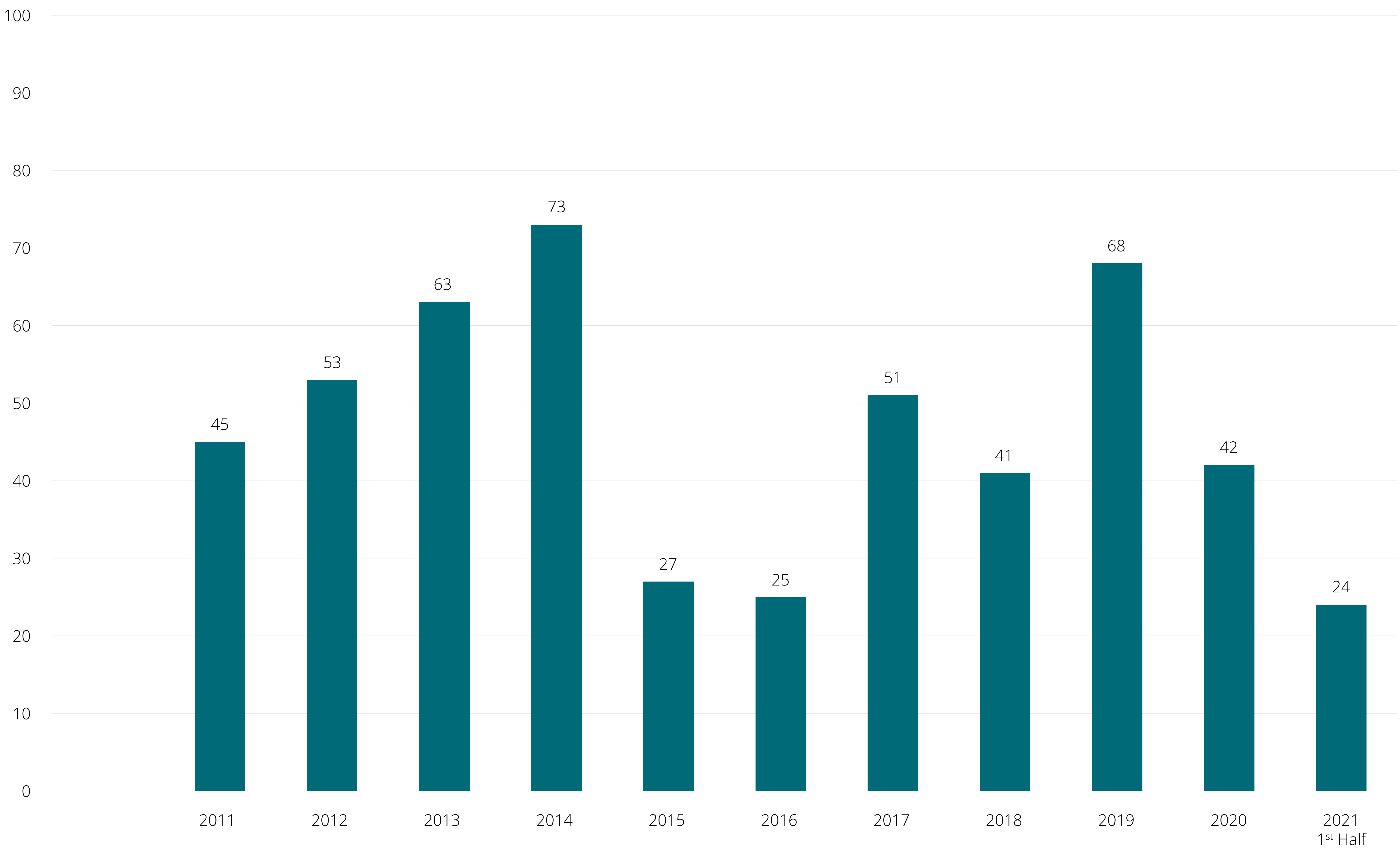


Table 16. Russia

Economic and wealth indicators	Modern and contemporary art market*
HNWI wealth population (thousands) 2020*	Auction sales in 2020 (US$ million)
218	41.1
Change in HNWI population 2019/2020	Sales growth 2019-20
1.2%	-38%
Real GDP growth 2021	Global market share
3.8%	1.30%
GDP growth outlook 2022	Art market outlook 2022
3.8%	Up: 20% flat: 57% down: 23%
While the Russian market for modern and contemporary art saw a 38% decline in auction sales during 2020, the first half of 2021 shows signs of a slow recovery. Most market experts believe the market will move sideways during the next 12 months, with 20% seeing an upside in this market.	
10-year CAGR	-8.3%
HNWI wealth population figures are estimates from The World Wealth Report 2021 (CapGemini) GDP figures are from the World Economic Outlook April 2021 (IMF)	

Figure 28. Africa (US$ million)

*Art market analysis is based on modern and contemporary auctions—Sotheby's, Christie's, Phillips, Bonhams, Piasa, Strauss and ArtHouse Nigeria.

Source: ArtTactic

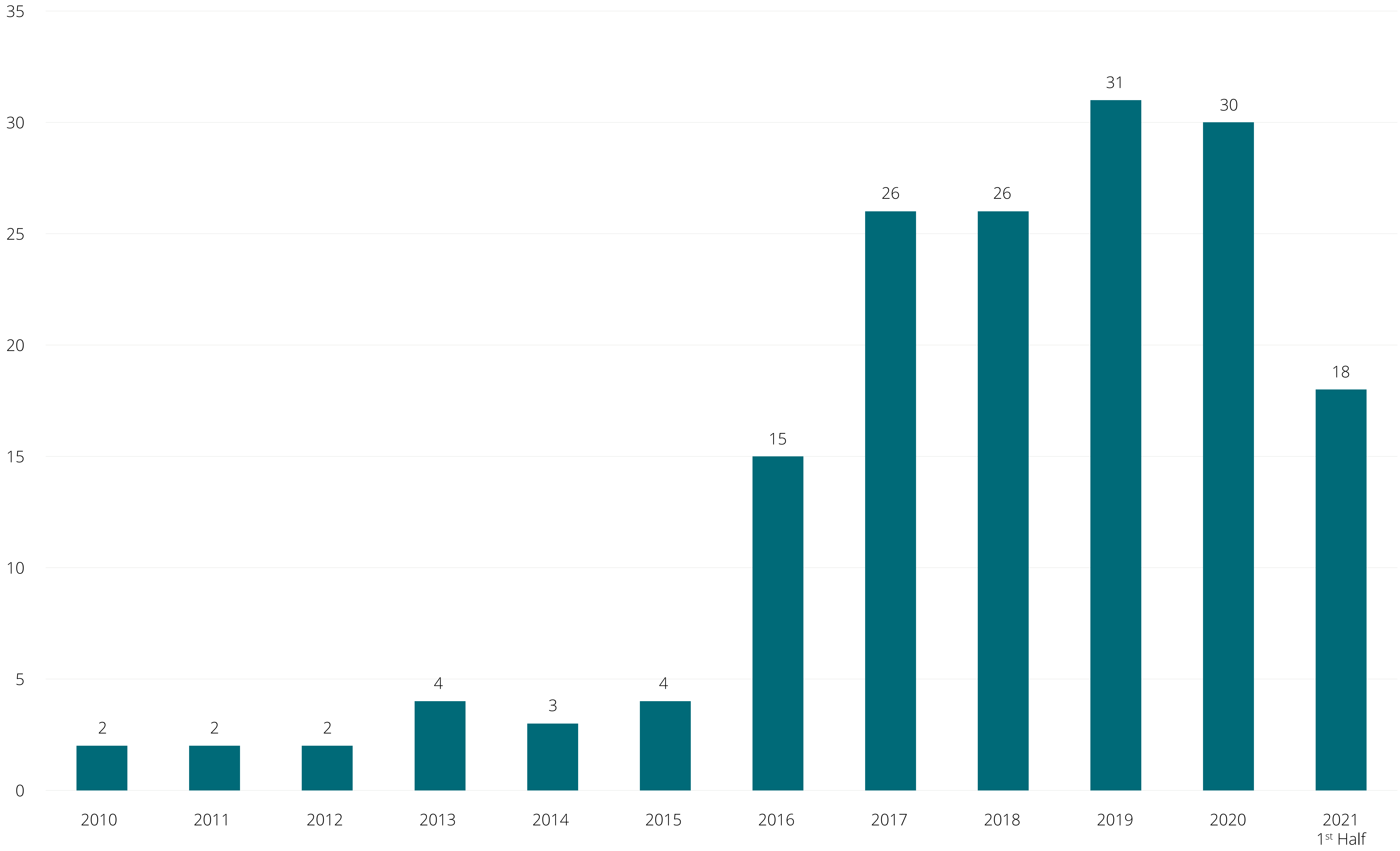


Table 17. Africa

Economic and wealth indicators	Modern and contemporary art market*
HNWI wealth population (thousands) 2020*	Auction sales in 2020 (US$ million)
181.8	30.5
Change in HNWI population 2019/2020	Sales growth 2019-20
2.70%	-2.5%
Real GDP growth 2021	Global market share
3.4%	1.00%
GDP growth outlook 2022	Art market outlook 2022
4.0%	Up: 42% flat: 47% down: 17%
The African modern and contemporary art market continued to perform well during 2020, finishing only 2.5% below the record year of 2019. Auction sales in the first half of 2021 also remain strong, with 2021 set to become a record year for the African auction market.	
10-year CAGR	22.6%
HNWI wealth population figures are estimates from The World Wealth Report 2021 (CapGemini) GDP figures are from the World Economic Outlook April 2021 (IMF)	

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Expert voices

The Brexit effect on the art market

Legal aspects concerning the circulation of artworks between the EU and the UK

The United Kingdom is a leading art market worldwide, with London holding for a long time the title of capital of the Art Market in Europe. If the pandemic has affected this market in 2020, so did Brexit, causing the rules to change and to stiffen the import and export procedures as of January 1st, 2021. How things will change in terms of numbers of sale may only be speculated on, while changes affecting the market from a legal perspective are hereby discussed.

As of Brexit day, both the EU and the United Kingdom apply the respective licensing and import-export procedures for the trade of cultural goods. Specifically, Council Regulation (EC) no 116/2009 on the export of cultural goods requires a European license to export goods outside of the EU territory, creating new paperwork for traders wishing to export artworks to the United Kingdom. Indeed, just like for any other extra-EU Country, anyone interested in exporting – any maybe sell - cultural goods from the European Union to the UK, will have to obtain such license from the relevant offices of the EU member states where the goods are lawfully and definitely resided. On the other hand, the Arts Council England will no longer issue EU export licenses and those issued before December 31st, 2020, will be valid until their expiry, no later than 12 months as of the issuance date.

It should be noted that, under the aforesaid Regulation, archeological goods are regarded as "cultural goods", whatever their value, while paintings require an export license if they are worth over €150,000. Furthermore, it is necessary to consider the restrictions and requirements set by the single Member States, which in some cases provide for stricter rules and limitations, such as those set forth by Italian Cultural Heritage Law. Indeed, for any artwork being worth more than €13,500 that needs to be exported to the UK, Italian law would require the issuance of both the EU free circulation certificate, as well as the EU export license.

Secondarily, as of January 1st, 2021, normal custom procedures apply to the import-export of artworks between the EU and the UK, like with any other Extra-UE Country. At the same time, application of VAT will definitely affect the trade with EU Member States.

Furthermore, the United Kingdom repealed Regulation (EU) 2019/880 of the European Parliament and of the Council of 17 April 2019 on the introduction and the import of cultural goods, as well. Such regulation imposes new and tighter rules on the import of goods from third Countries outside of EU. Specifically, cultural goods, which were illegally exported from a third Country to Europe, will be denied access to the EU. This regulation has, amongst other things, the objective of avoiding illicit trade to the detriment of cultural heritage as well as the funding of terrorist groups that illegally sell and export art to finance their activity. Because of the additional control procedures, the regulation has not met large enthusiasm amongst market stakeholders, also because there is no similar rule in the US, arguably the world's leading art market. The UK rejection of such regulation might "put the EU at a competitive disadvantage as trade between the UK and US will not be restricted by the measures in the same way that it will be between either of those markets and the EU".[44]

Brexit has positioned the UK as a third Country like any other with respect to the trade of artworks with European Union Member States. While it is too soon to predict how this will affect the UK art market itself, it is certainly true that the applicable legal framework will increase the amount of paperwork and make more difficult for the art market stakeholders to import and export artworks between the EU and the United Kingdom.

44 Ivan Maquisten, "In a swift post-Brexit move, UK rejects EU's strict import rules on cultural property", in "The Art Newspaper", 6 January 2021, available at https://www.theartnewspaper.com/news/uk-will-not-continue-eu-s-new-import-licensing-regulations-for-cultural-property

Simon Hornby
Senior Vice President, Crozier Europe, discusses post-Brexit experiences in the art logistics market

Expert voices

Who has fared best?

Thriving in the post-Brexit art marketplace

The impact of Brexit on the UK art storage and logistics business has, unsurprisingly, been distorted by the continuing effects of COVID-19 restrictions on most of Europe. It is likely that the true picture will only emerge in 2022—or later—depending on the effectiveness of vaccine programs across the globe and the impact on travel, art fairs, international exhibitions, and all the other components that comprise the world's art ecosystem.

What we can see is that some art market participants were better prepared for Brexit than others and many have still to fully grasp the new procedures for exports and imports involving the UK. The potential for major disruption was dissipated by most London-based shipping companies being appropriately prepared. The same cannot be said for many of the EU art specialist firms who had either decided to ignore the new order created on 1 January 2021 by the lengthy Brexit negotiations, to wait and see, or to withdraw completely from doing direct business with the UK despite London's market-leading position in Europe. For many British art transporters this has led to an increase in business—in direct road transport and customs clearance procedures—replacing some continental operators for shipments involving the UK.

The least prepared groups seem to have been smaller dealers and private collectors, who may be unaccustomed to the vagaries of customs procedures after decades of shipping property seamlessly within the bloc.

Procedures are now more complex between the EU and UK involving export and import clearances on both sides of the channel. Not only is this more time-consuming, but has also been open to interpretation as the new procedures gradually become familiar. This increase in time taken to process imports and exports has resulted in increased charges to all clients and has taken many by surprise.

We have also seen a shift in some commercial allegiances reflecting a 'flight to quality' with a re-alignment to those UK art transport companies that have demonstrable expertise in understanding and working within HMRC rules and regulations, as well as those imposed by the EU and its Member States, including tax suspension during transit and storage.

Procedures are now more complex between the EU and UK involving export and import clearances on both sides of the channel.

With Switzerland's status and relationship with the UK unchanged, we have seen traffic increasing which tends to indicate that the art hubs in Geneva and Zurich continue to enjoy their position in the market and are, perhaps, even increasing market share, despite the absence of Art Basel in 2020.

Anecdotal information indicates increases in activity in the Parisian market to avoid some of the post-Brexit friction, but is more focused on the auction market than gallery or private sales. We have also had an increase in international shipping via containers, but this is driven by the parallel agendas of carbon footprint reduction and cost containment with little or nothing to do with Brexit.

Our assessment concluded that while Brexit may have some short-term impact, the longer-term role of London as a leading art market hub is unlikely to be undermined. From a business perspective, Crozier has completed the acquisition of Martinspeed Limited in April 2021 to add to existing operations in London, Zurich and Geneva. Of more importance is the ability to build a network that can flex and adapt to changes in the global market. With a leading presence in the United States we needed to have a greater European presence to meet our client's desire for point-to-point services and a greater consistency of standards.

In many respects, the art storage and logistics industry is a decade or more behind other transport sectors in terms of technology, integrated software solutions with clients' systems, and common standards. The ability to invest in solutions that will address these needs remains the largest obstacle and cannot be overcome with an under-capitalized business model. We are therefore not alone in expecting to see a trend towards continued industry consolidation, probably at a faster pace than we have seen over the last few years, and a move towards more formal alliances in smaller markets.

The circling target of greater art market supervision is not going away with continued focus in the United States and Europe on anti-money laundering regulations being applied to those transacting in art. This will likely bring adjacent reporting and oversight, only adding to costs and causing potential complexity to comply with regulations such as the UK's Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017[45] and subsequent The Money Laundering and Terrorist Financing (Amendment) Regulations 2019[46] . Up to the last-minute, the UK government—in the form of HM Treasury—was interpreting their own regulations and announced that Artists would not be expected to register under the UK's AML law. Further

In short—more to come as this hopefully becomes clearer—one can only see a more complex environment as the UK tries to justify its post-Brexit 'freedoms'.

language in the regulations referencing 'freeports'—a term not widely used in the art market outside of much-publicized storage operations in Switzerland and Luxembourg—may be the harbinger of further regulations for Customs-bonded art storage. Given that Prime Minister Johnson has discussed the creation of freeports in the UK to stimulate regional economies for manufacturing after leaving the EU, it is hard to understand how this meshes with AML regulations designed for the art world. In short—more to come as this hopefully becomes clearer—one can only see a more complex environment as the UK tries to justify its post-Brexit 'freedoms'.

The post-Brexit art world was always going to be viewed differently by which lens you looked through. We should remember that before 2021, only 20% by value of UK art imports/exports involved EU Member States[47], so any impact on the London market should be reviewed in that context. The same report also indicated that the EU had 31% of the global art market in 2018, but without the UK this would drop to 12% of global sales.[48] So, the question may be better posed: how has the EU art market fared without the UK?

45 https://www.legislation.gov.uk/uksi/2017/692/pdfs/uksi_20170692_en.pdf
46 https://www.legislation.gov.uk/uksi/2019/1511/made/data.pdf
47 Art Basel and UBS Report: The Art Market 2020
48 idem

A look at art and collectibles at public auctions over the past 15 years

In the following article, Christine Bourron, CEO of Pi-eX Ltd, looks at the trade of collectibles at the top three auction houses over the past 15 years. What does this mean for collectors? What do the numbers tell us about the growth and crisis periods in the public auction market? And where are the new growth opportunities?

Valkyrie Octopus
©Luís Vasconcelos/Courtesy Unidade Infinita Projectos - 2015

Christine Bourron
CEO
Pi-eX Ltd

Expert voices

Growth opportunities at public auctions

Key learnings for collectors trading at auctions

From 2007 to 2021, more than US$142 billion worth of collectibles has been traded at public auctions held at Christie's, Sotheby's, and Phillips. This includes fine or decorative art, jewelry, watches, furniture, manuscripts, rugs, even sneakers, and most recently, NFTs. A monthly analysis by Pi-eX Ltd of the trade of collectibles at the top three auction houses over the past 15 years shows that the level of activity based on a 12-month rolling value has fluctuated from a low US$5.2 billion in November 2009 to a high US$13.6 billion in June 2015. As of the end of June 2021, the value of collectibles traded was US$11.3 billion.

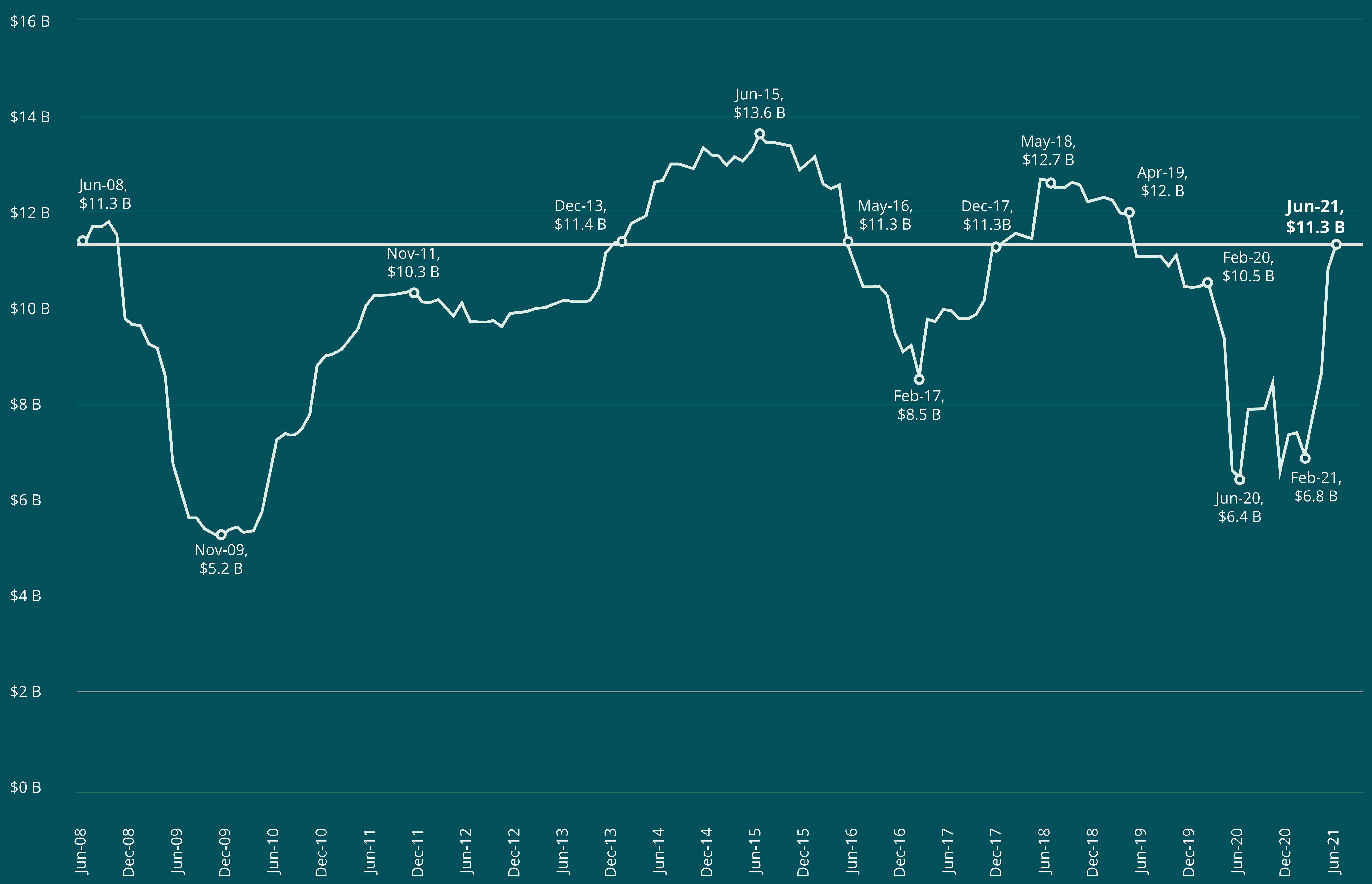
But, what does this mean for collectors? What are the numbers telling us about the growth and crisis periods in the public auction market? Where are the new growth opportunities?

This article highlights volume and value trends at public auctions over the past 15 years and identifies growing and shrinking segments by locations or types of collectibles. It derives key learnings that collectors should keep in mind when buying and selling at auctions.

As of June 2021, the level of trading on a 12-month rolling basis in US dollars at public auctions arranged by Christie's, Sotheby's and Phillips was the same as it was in June 2008. However, this overall stability does not mean that the ride has been a smooth one. Quite the contrary.

Over the past 15 years, the public auction market has experienced three serious crises: the financial crisis of 2008-2009, the crisis of 2016, and the recent COVID-19 pandemic. Less than a year ago, in June 2020, only US$6.4 billion had been traded in the previous 12 months, as auction rooms were forced to close at the start of the pandemic in March 2020. This was a sharp fall from the lofty figures of 2015.

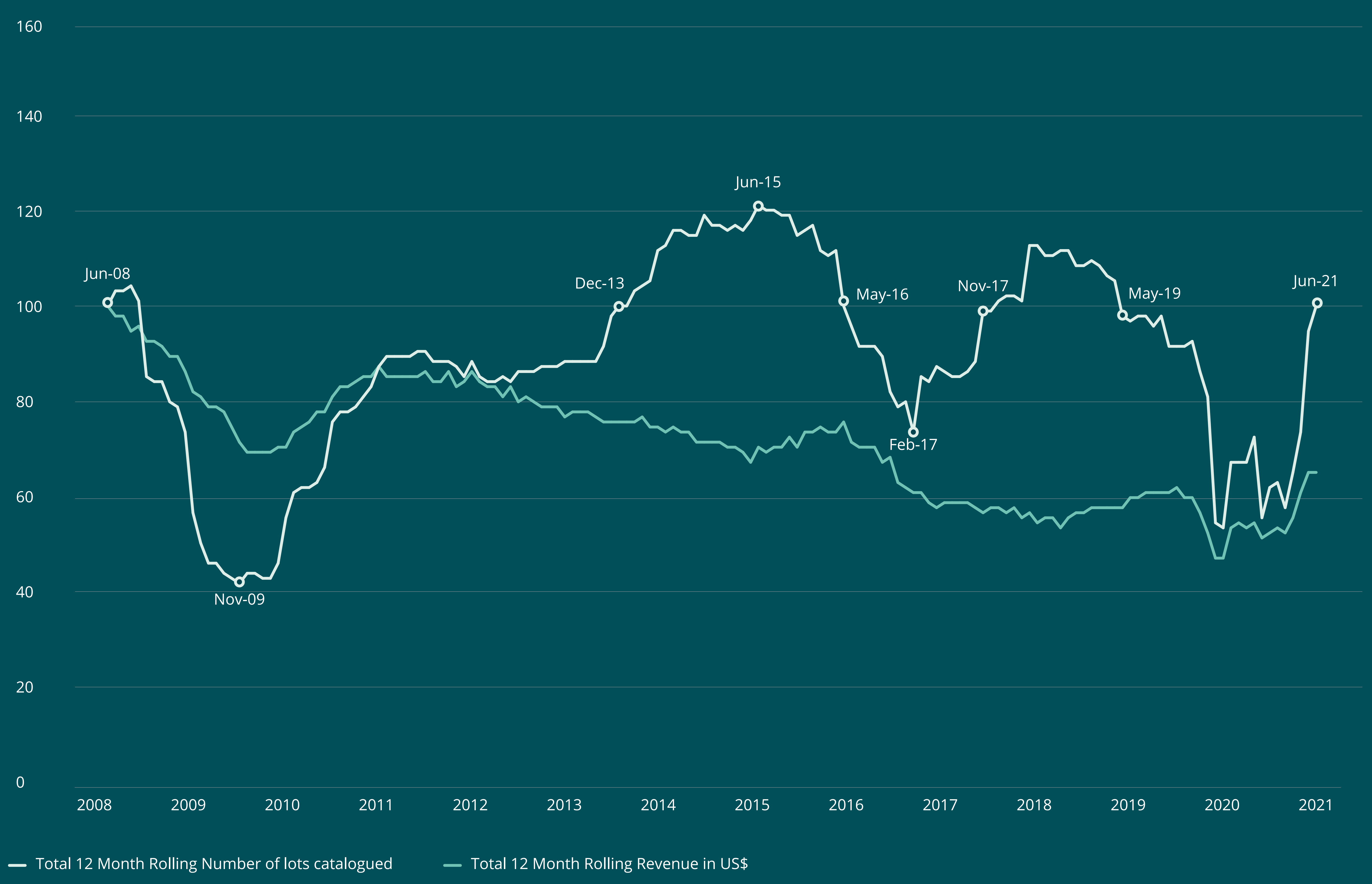
Figure 29. 12-month rolling revenue in US$ at top three auction houses, Christie's, Sotheby's, and Phillips
Source: Pi-eX Ltd proprietary database of auction results



From highs to lows, the public auction market is always on the run, in search of the next Monet or the latest innovation. The recent boom of digital art and NFTs is just a repeat of previous frenzies involving posters, Russian art, or AI works. While the overall market may seem to plateau, value never stops to migrate within the market.

Collectors should be attentive to the volatility of the public auction market
The global Pi-eX Auction Market Index (AMI) shows that the level of trading at public auctions exceeded the June 2008 level only twice in 14 years, during two short periods: December 2013 to May 2016 and December 2017 to April 2019. Any time before or after would have been a time when the market was either plummeting or recovering from a crisis.

Figure 30. Indexed value (in US$) and volume from public auctions at Christie's, Sotheby's, and Phillips worldwide (June 2008 = 100)
Source: Pi-eX Ltd proprietary database of auction results



While the total value of items traded oscillated above and below the June 2008 level, the number of lots catalogued and offered for sale at public auctions has consistently decreased from a high of over 222,000 from July 2007 to June 2008 to less than 149,000 by end of June 2021—the lowest level being reached in June 2020, with only 110,650 lots catalogued over the previous 12 months.

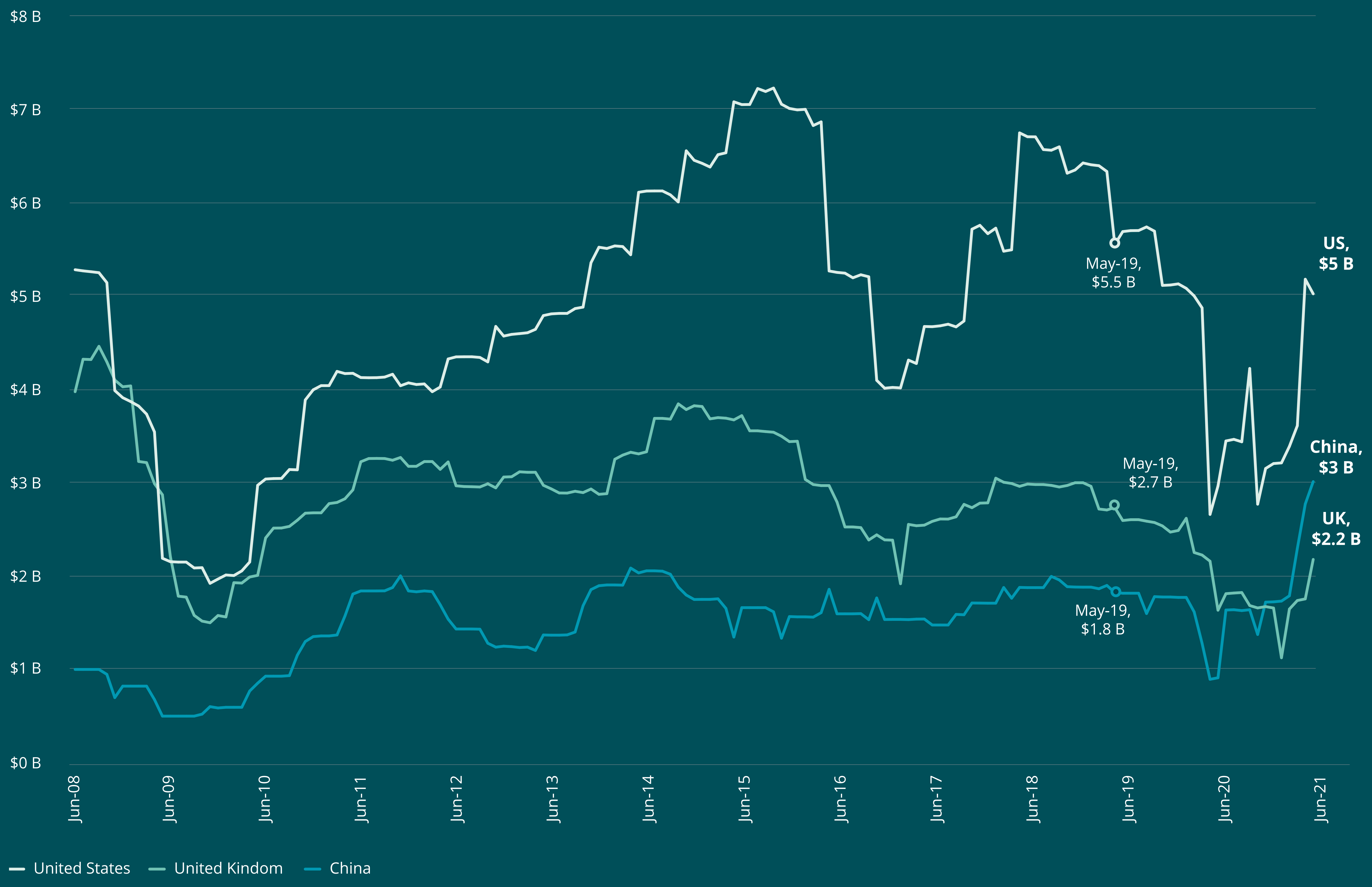
Comparing volume and value trends show how each crisis has further contributed to a reduction in the number of lots traded, resulting in a shrinking market, volume wise.

However, 2021 may break with historical trends: the broad adoption of online sales by auction houses and collectors alike may pave the way for growth—or at least a quicker rebound in the aftermath of the crisis. Indeed, as of the end of June 2021, the level of trading in volume was already higher than before the start of the COVID-19 crisis (+8%).

Diversity across regions represents opportunities for global collectors

While the overall picture shows a market shrinking in volume and at best stagnating in value, the focus in specific locations unveils a very diverse reality.

Figure 31. 12 Month Rolling Revenue (in US $) from public auctions at Christie's, Sotheby's & Phillips in the United States, United Kindom, and China
Source: Pi-eX Ltd proprietary database of auction results



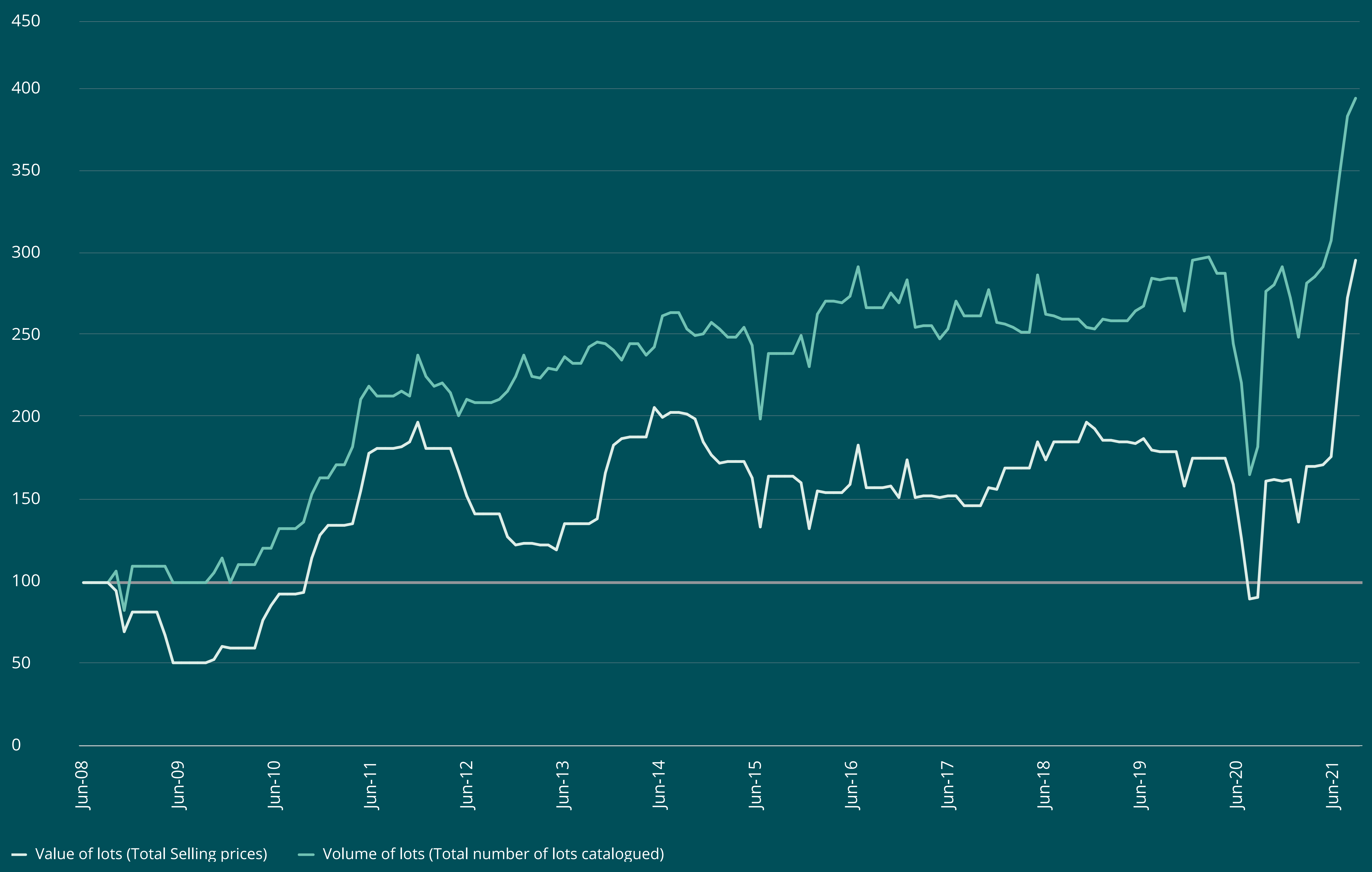
Far above all other markets, the US remains the largest market for public auctions at the top three auction houses. Reaching US$5 billion by end of June 2021, the level of trade over the past 12 months is just under its June 2008 level at US$5.2 billion.

The UK market, almost on par with the US back in 2008, fared much worse as it significantly contracted, crisis after crisis. With US$2.2 billion worth of items traded in the previous 12 months leading to June 2021, public auctions in the UK seem a mere shadow of their former selves, when they almost reached US$4 billion in June 2008. The erosion of the British pound certainly explains part of the lost value, but the foreign exchange rate is not the only cause.

During the same period, the Chinese market for the top three auction houses grew from just about US$1 billion in the 12 months preceding June 2008 to US$3 billion by end of June 2021, making China the second largest market after the US and clearly now ahead of the UK.

What opportunities does this provide for global collectors?

Figure 32. Indexed Value (in US $) and Volume from public auctions at Christie's, Sotheby's & Phillips in China (June 2008 = 100)
Source: Pi-eX Ltd proprietary database of auction results



Collectors should include China in their list of locations to trade

Compared to June 2008, the number of lots catalogued in China increased by almost 300% while the value of collectibles traded at auctions arranged by the top three auction houses in China increased by almost 200%. This shows strong demand and potential for additional growth.

Despite being hit hard by the COVID-19 crisis, with the level of trading plummeting for a few months in 2020, China has since recovered and even accelerated its growth, with strong demand and clear potential for further growth.

Collectors should expect further price volatility in the US

Over the past 15 years, the US market has seen a slow but steady erosion in the volume of lots catalogued at public auctions.

In the absence of volume growth, the rises in market value in 2014-2016 and 2018-2019 were driven by price increases mostly, which made the recovery fragile and susceptible to relapse. With the number of lots catalogued further decreasing, the value of public auctions has never returned to its 2015 level since—even when the Rockefeller private collection hit the market. Unless the recovery from the COVID-19 crisis changes the trend, collectors should expect further price volatility in the US market.

Figure 33. Indexed Value (in US $) and Volume from public auctions at Christie's, Sotheby's & Phillips in the United States (June 2008 = 100)
Source: Pi-eX Ltd proprietary database of auction results

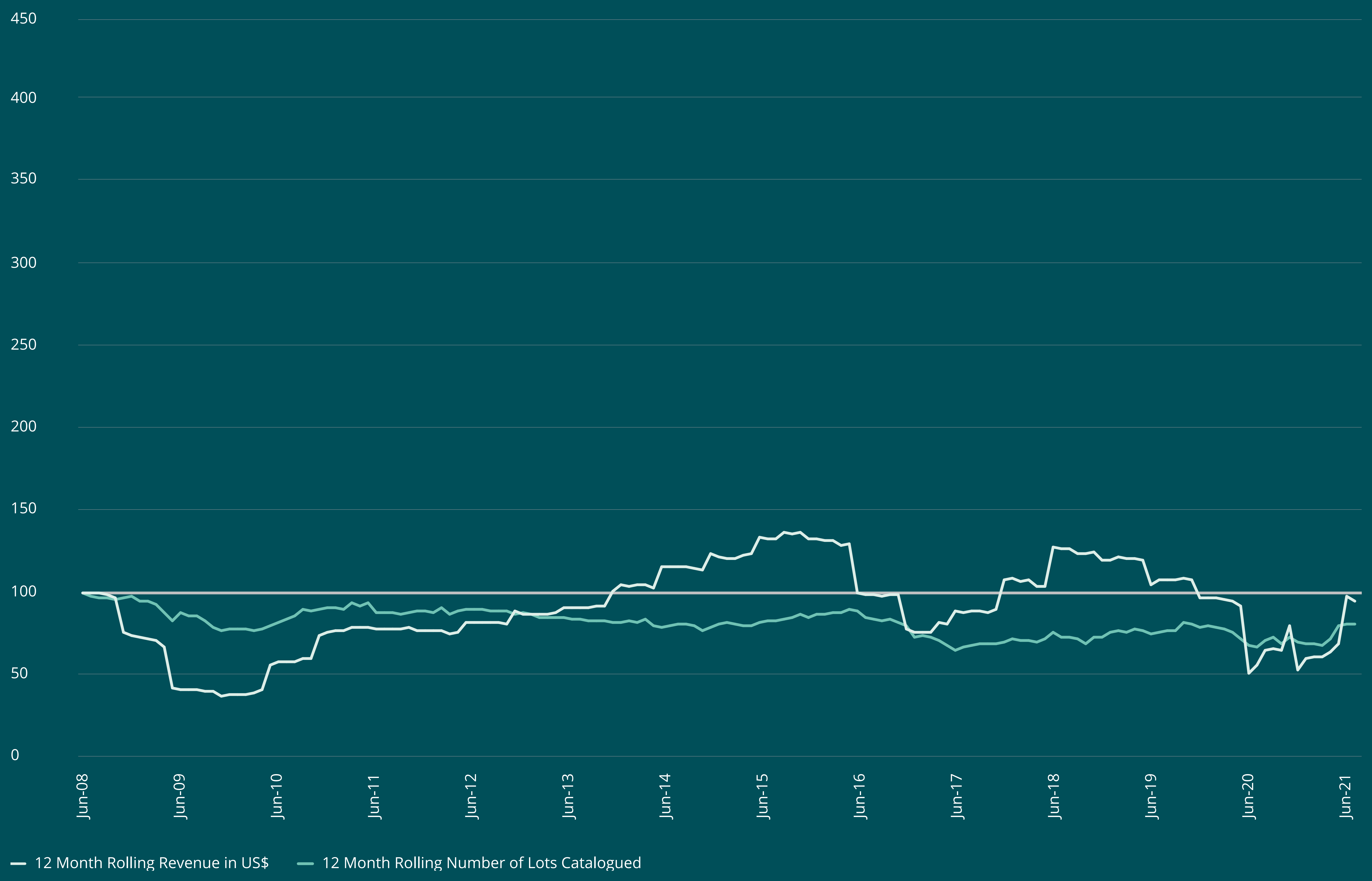
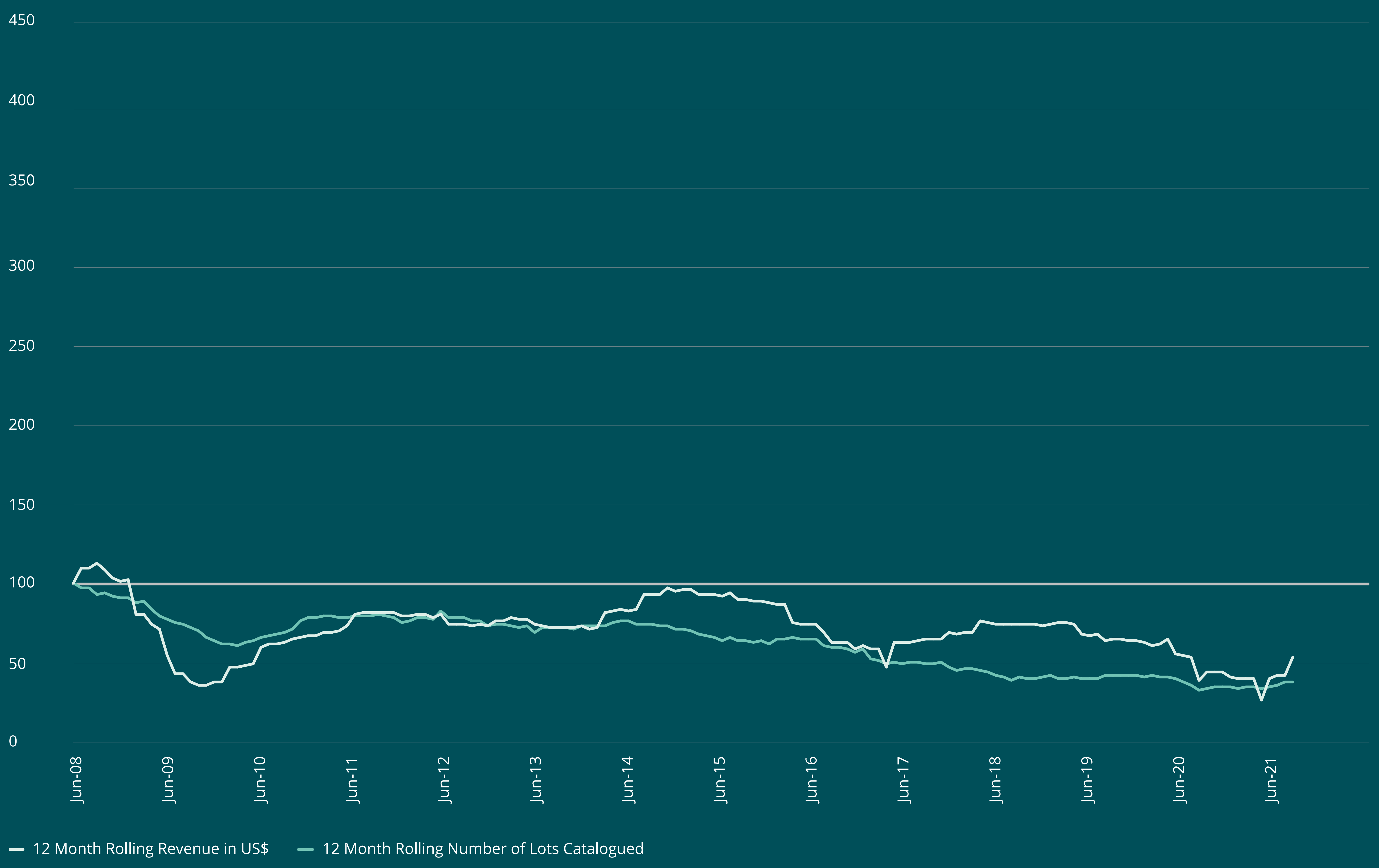


Figure 34. Indexed Value (in US $) and Volume from public auctions at Christie's, Sotheby's & Phillips in the United Kingdom (June 2008 = 100)
Source: Pi-eX Ltd proprietary database of auction results



Collectors should get ready for change in London
With both an erosion in volume and value of lots traded, London has certainly seen better days.

A much weaker British pound (£1 was almost US$2 in June 2008, but just US$1.4 in June 2021) as well as the now concrete complications of Brexit, have further harmed British trade. A true rebound has failed to materialize in the London bidding rooms at the top three auction houses in light of the COVID-19 crisis and the UK market is ripe for change.

Understanding trends across various collectible segments can also help collectors optimize value
Value created at public auctions is driven by the willingness of a few to bid on, and sometimes compete for, a particular item or lot. Different types of lots therefore command different prices.

By far, the largest segment in value at public auctions is the fine art segment which is traded via repeating sales arranged regularly at different times throughout the year. Reaching US$8.1 billion in June 2021, the trade of fine artworks represents the largest category of collectibles traded at public auctions at Christie's, Sotheby's and Phillips.

Much smaller in value, but next in size is the category of luxury items/accessories such as jewels, watches, handbags, etc. which, together, generated US$1.5 billion between July 2020 and June 2021.

Third in line is the private collection segment which gathers all sorts of items sold under the umbrella of provenance, when the auction houses consider that the provenance itself can be a source of value.

Finally last on the graph above is the decorative art segment, which gathers auctions of furniture and decorative items.

Collectors should expect new growth opportunities post COVID-19 in the fine art category
While the largest segment in size, fine art has not been the most dynamic over the past 15 years.

Figure 35. 12 Month Rolling Revenue (in US $) from public auctions at Christie's, Sotheby's & Phillips Fine art, Luxury items, private collections, decorative art
Source: Pi-eX Ltd proprietary database of auction results

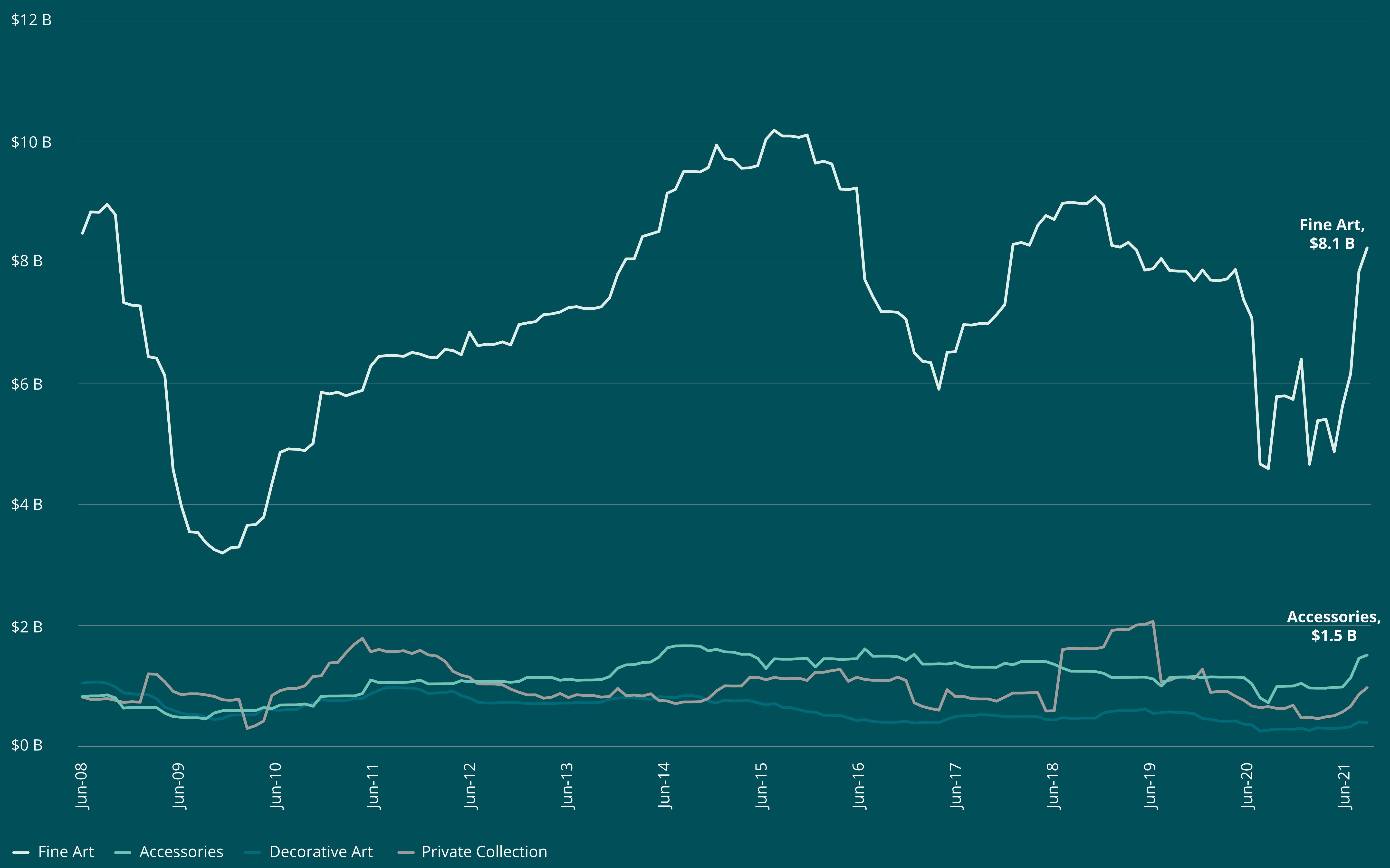
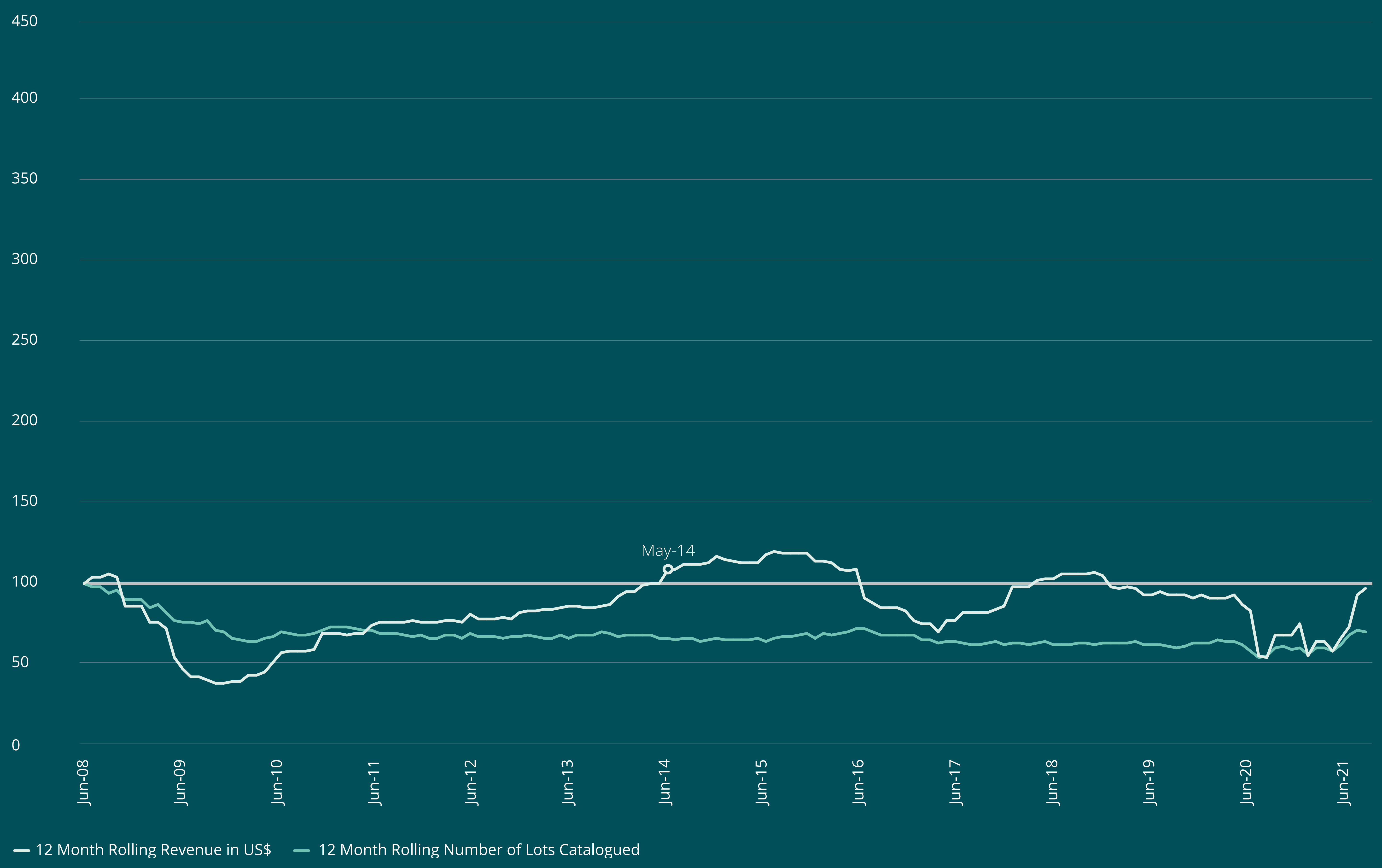


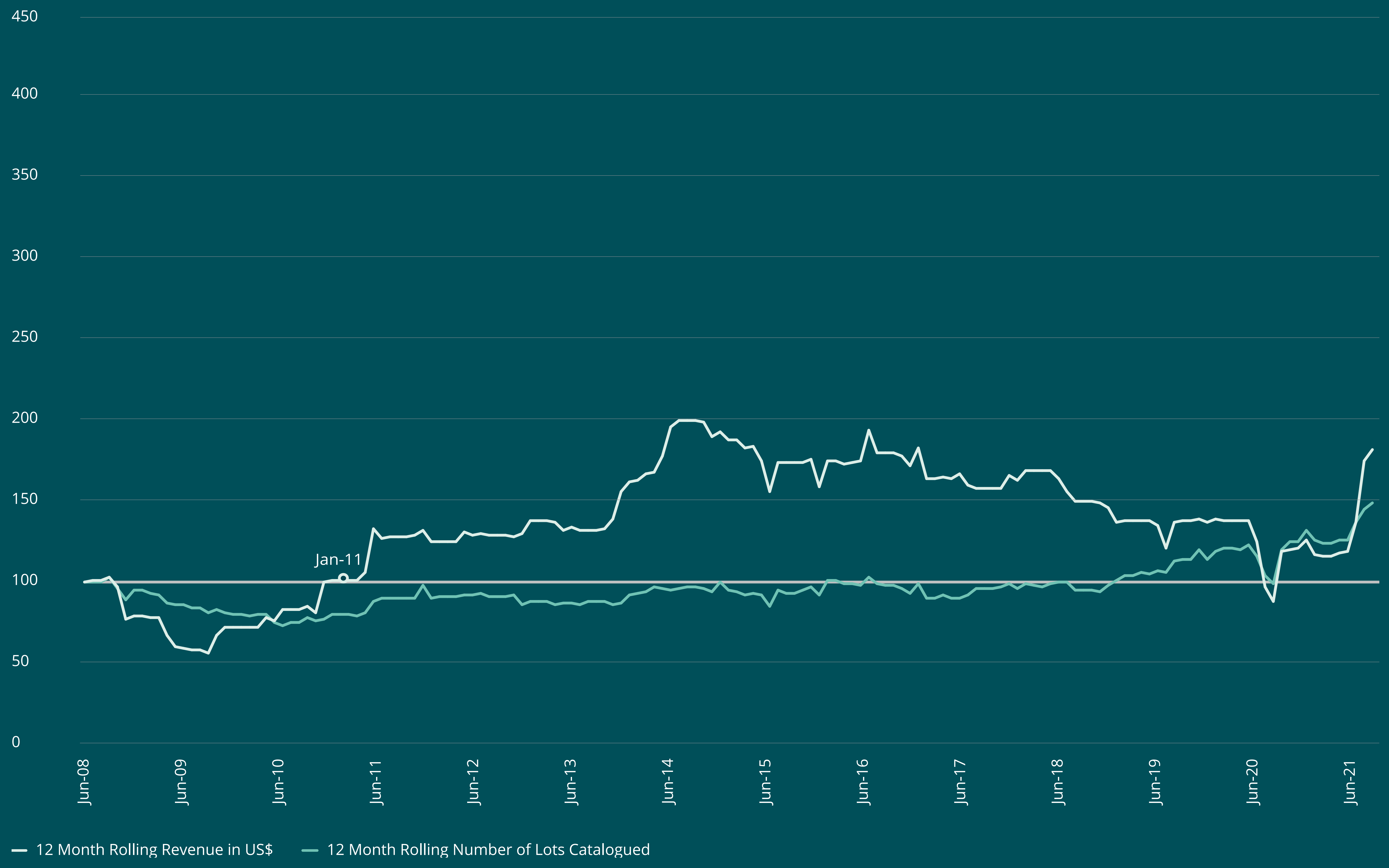
Figure 36. Indexed Value (in US $) and Volume from Fine Art public auctions at Christie's, Sotheby's & Phillips (June 2008 = 100)
Source: Pi-eX Ltd proprietary database of auction results



The welcome volume growth is clearly linked to the growth of online auctions, which have allowed the auction houses to reach a new audience.

Since 2008, the number of artworks traded has continuously decreased, first sharply from 2008 to 2010 then slowly but at a steady pace. In this context, the successive growth of the segment in 2015 and in 2018 were purely driven by price increase as the number of artworks traded showed further decline. In the aftermath of the COVID-19 crisis however, the number of artworks traded has notably increased, a trend unseen for many years. The welcome volume growth is clearly linked to the growth of online auctions, which have allowed the auction houses to reach a new audience, for which they are offering new items—whether lower price point Impressionists, Old Masters artworks, or digital art with NFTs.

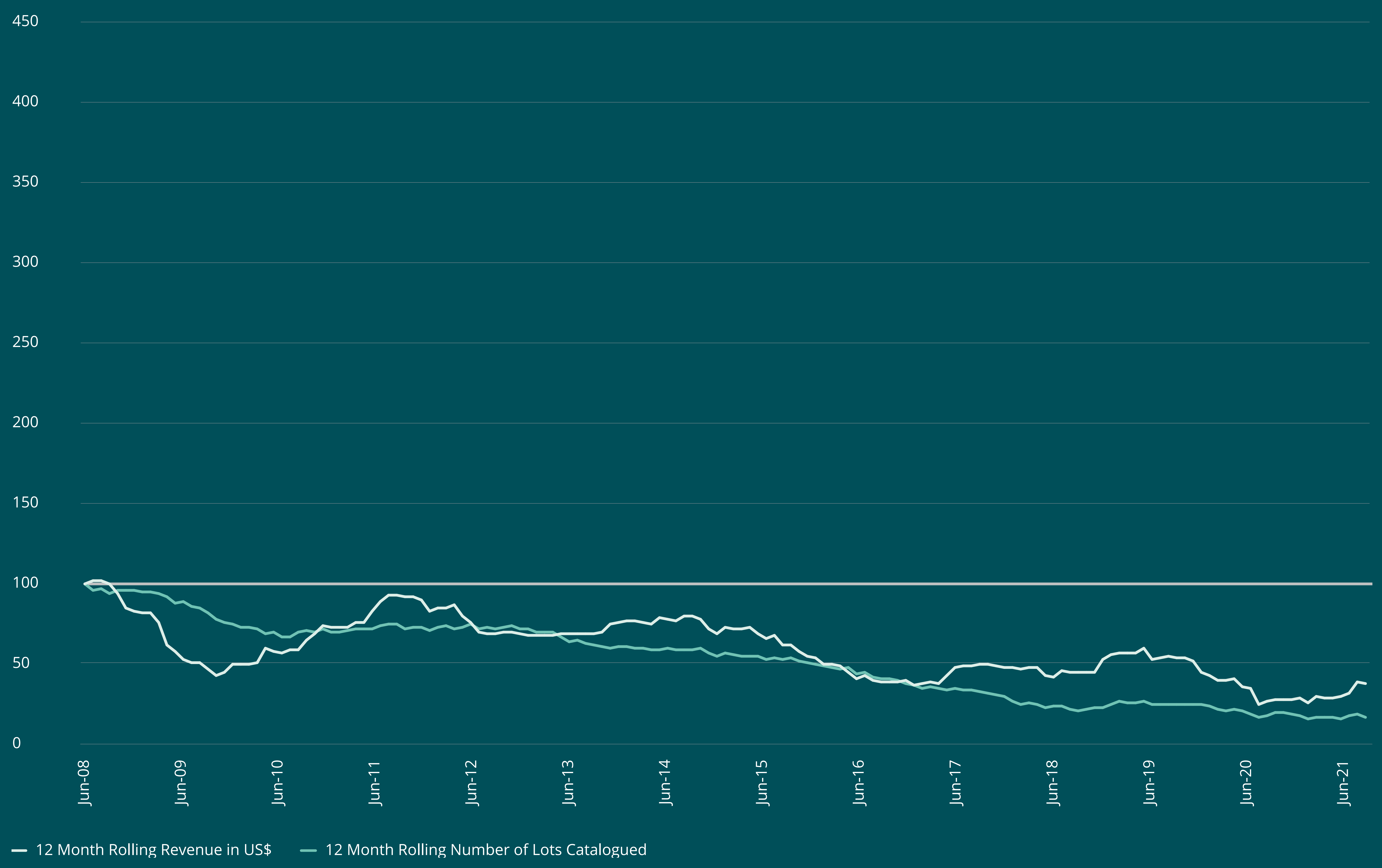
Figure 37. Indexed Value (in US $) and Volume from Luxury Items / Accessories public auctions at Christie's, Sotheby's & Phillips (June 2008 = 100)
Source: Pi-eX Ltd proprietary database of auction results



The accessories/luxury items category offers robust growth opportunities to collectors
Robust demand for luxury items has been driving the growth of the category in 2021.

In a post COVID-19 world, the number of luxury items lots offered by the auction houses has increased to meet the strong demand from buyers. As of the end of June 2021, both the volume and value of luxury items traded in auctions arranged by the top three auction houses increased by more than 30% versus their June 2019 level.

Figure 38. Indexed Value (in US $) and Volume from Decorative Art public auctions at Christie's, Sotheby's & Phillips (June 2008 = 100)
Source: Pi-eX Ltd proprietary database of auction results



Decorative art remains a challenging category for collectors

Years of shrinking volume and value in the decorative art segment has left the category as one of the least dynamic among all those traded at auction.

Despite talks of renewed interest in the decorative space, the volume of and the value commanded by these items remains low, most likely as decorative habits changed. Collectors should watch the space carefully for any potential changes.

Behind the overall picture of a volatile but stagnating market, hides multiple geographical markets and collectible segments. Value has migrated in response to collectors' changing tastes while new geopolitical realities have pushed buyers and sellers from one location and/or one segment to another. By carefully monitoring volume and value traded at auctions, collectors can identify growing markets (e.g. China and luxury items) as well as slowing markets (e.g. the UK and decorative arts) and maximize value opportunities.

By carefully monitoring volume and value traded at auctions, collectors can mazimize value opportunities.

Art and Wealth Management

02

Burlesco

Highlights

A 10-year perspective

Between December 2011 and October 2021, Deloitte Private and ArtTactic published seven Art & Finance Reports. The results of our 10-year survey analysis of different art and finance stakeholders (wealth managers, collectors and art professionals) show encouraging and upward trends regarding art's role and importance in wealth management. We have seen a consolidation of the different stakeholders' narratives and motivations for including and developing art wealth management services. Client demand for art and wealth management services has grown over the last 10 years (see figure 40 p.98). Also, wealth managers now have a clear understanding of the role of art in wealth management (see figure 39 p.97) as well as which services to offer (convergence point is at around 80%, see figure 41 p.99).

Turning point in 2016
Six years ago, we saw a significant shift in wealth managers' perception of the role and value of art and collectibles in a wealth management strategy and service offering. Whilst only 53% of wealth managers in 2014 believed art should be included as part of a wealth management service, this jumped to 78% in 2016. This marked the first time in our analysis that the wealth management industry aligned with the view of collectors and art professionals. In 2021, 85% of wealth managers said the same. **Now, the question is not so much if art should be integrated into a wealth management offering, but rather how to do it and deal with the challenges.** This interest in art and collectibles will continue as wealth managers move towards a holistic wealth management model[1].

Holistic wealth management
85% of wealth managers consider the need to develop a holistic advisory relationship with their clients as the main motivation for including art and collectibles in wealth management

Art as a capital asset
Over the last 10 years, art and collectibles have demonstrated their ability to maintain and appreciate in value, and we have seen stronger financial motivations behind art collecting. Although investment and diversification remain key drivers, the main focus in recent years has been preserving the capital allocated to art and collectible assets. The COVID-19 pandemic triggered more interest in art as a source of financial diversification among collectors; however, most wealth managers said they saw no evidence of this effect. There are signs that younger collectors are more motivated by financial considerations around art ownership compared with older art collectors.

Now, the question is not so much if art should be integrated into a wealth management offering, but rather how to do it and deal with the challenges.

Big Booby
©Bertrand Huet|Tutti/Courtesy Galerie Nathalie Obadia, Paris/Brussels

Broader spectrum of services
The spectrum of art-related wealth management services has gradually broadened over the last decade. These services fall predominantly into four categories: art and wealth protection, art and estate planning and philanthropy, art secured lending and, to a lesser extent, art investment services. Social impact investment and culture is one of the newest trends emerging in recent years, and is likely to become an integral part of an art and wealth management service offering. The share of wealth managers offering art advisory services has increased from 39% in 2011 to 78% in 2021. Collection management services have risen from 17% in 2011 to 76% in 2021, and wealth managers offering art valuation services have jumped from 39% in 2011 to 82%

1 Holistic wealth management coordinates all aspects of managing wealth

Strategic partnerships and closer relationships with art professionals

As the wealth management industry moves towards a more holistic approach regarding their service offering, over the last 10 years we have seen a strategic shift towards partnerships with external providers to deliver these services. In the context of art, a closer relationship between art professionals and wealth managers has emerged, particularly around services related to art advisory, valuation and secured lending. With 96% of art professionals stating they believe art should be part of a wealth management offering, there is a clear buy-in among this stakeholder group. Therefore, it is up to art professionals to ensure they meet the wealth management community's expectations and effectively address the challenges faced when incorporating art and collectibles into existing wealth management practices. In 2021, 69% of wealth managers said the art industry needs to modernize its business practices; art professionals must now rise to this challenge.

Adapting to changing collector needs

Collector needs and demand for art-related wealth management services have evolved over the last decade. The biggest interest is in collection management, estate planning and art investment services, as well as a growing need for art market research and information. Changes in client's behavior and motivations over the last 10 years, coupled with increasing competition in the wealth management sector, value appreciation of art and collectibles, and greater client needs for protecting and leveraging art-related wealth, have forced wealth managers to respond to new demands and develop a holistic advisory relationship with their clients.

Younger collectors are driven by a stronger emphasis on the financial aspect of art ownership, but social impact and purpose-led investment ranks on par with the emotional value of buying art

There are signs that younger collectors are more motivated by financial considerations around art ownership compared with older art collectors. In 2021, 64% of young collectors (under 35 years old) said that financial investment returns are a key motivation (compared with 30% of older collectors). At the same time, purpose and social impact investment is the highest-ranked motivation (alongside emotional value) among younger buyers at 86%, compared with 32% of older collectors. Most (93%) of collectors under 35 years old said wealth managers should incorporate art and collectibles in their service offering, compared with 74% of collectors aged above 35 years. This suggests that a new generation of wealth management clients have a strong desire to see art integrated into future wealth management strategies.

Emotional value associated with art ownership remains key for collectors

Financial motivations for buying art and collectibles are still an important part of the relationship between the wealth management sector and collectors. However, since we launched the survey in 2011, collectors' strongest motivation has consistently been the passion and emotional value associated with art ownership. It is often easy to underestimate the emotional ties that clients have to art-related wealth, but it is an important aspect for developing deeper and more sticky client relationships in an increasingly competitive wealth management industry.

Inséparables
©Unidade Infinita Projectos - 2018

The lack of regulation and transparency still dominates.

Pretty in pink
©Cortesia Museu Coleção Berardo - 2015

Obstacles to growth in the art and finance industry are slowly being addressed

Over the last 10 years, the challenges of integrating art into wealth management remain, despite seeing a slight improvement in recent years. The lack of regulation and transparency still dominates, but the share of wealth managers identifying these as key obstacles has decreased since 2017. This suggests that recent developments around anti-money laundering (AML) regulation and technology's role in increasing transparency are starting to change wealth managers' perception of these issues. Although a lack of interest or leadership does not seem to be the key issue, demonstrating the cost-benefit of including art in wealth management and a lack of internal expertise in integrating these services remain the main obstacles.

Increasing regulation in the art market could lead to a higher level of trust

With new AML regulations coming into effect this year, the broader art market was forced to comply with a new set of rules and regulations, which are likely to trigger changes in business practices. While transitioning to the new environment will be challenging for many, there is also hope that more regulation will increase the trust and credibility of the art market going forward. This should help create new opportunities for closer collaboration between art professionals and wealth managers. Although the art market has always shown a strong preference for self-regulation, for the first time almost half of collectors surveyed (46%) said they prefer more government regulation to restore trust in the market, up from 22% in 2019 and 28% in 2016.

Technology as a catalyst for future growth in art and wealth management services

The last 10 years have seen significant technological developments across all art market service areas. These range from online sales and e-commerce to advancements in digital experiences such as virtual reality (VR) and augmented reality (AR), as well as data and analytical tools to support valuation and risk monitoring. Most collectors, art professionals and wealth managers believe technology will help address issues around transparency, authenticity, provenance tracking and valuation, as well as broaden the collector base and allow new ownership models to emerge. All these factors are likely to reduce friction in today's interactions between the art market and the wealth management industry, and could open up further development and growth in art wealth management services in the future.

Although a lack of interest or leadership does not seem to be the key issue, demonstrating the cost-benefit of including art in wealth management and a lack of internal expertise in integrating these services remain the main obstacles.

Introduction

The main purpose of this section is to introduce our readers to some of the most important trends and developments emerging in the intersection between art and wealth management. Over the last 10 years, we have been monitoring the stakeholders (wealth managers, collectors and art professionals) in the Art & Finance industry, and reported on the changing role and importance of art and collectible assets within a wealth management service offering. This section of the report is structured around the following three parts:

Part 1. Wealth management trends
Here we take a closer look at some of the key factors that are shaping the global wealth management industry, from the role of technology and innovation to the need to adapt to changing client preferences and a younger client demographics.

Part 2. Wealth managers—survey findings 2021
In this part we take a 10-year retrospective view on the survey findings among wealth managers to provide a better picture of how the intersection between art and collectibles and the wealth management industry has evolved since 2011. We also specifically look at wealth managers' motivations for including art into their service offering, as well as what art related services are being offered. Current challenges and future areas of focus, are also discussed in this section. The section includes the following article. **Broadening horizons and pursuing new revenues—art advisory is no longer limited to the ultra-high net worth**, Eugénie Dumont, Art Collections Manager, Banque Degroof Petercam

Part 3. Collectors and art professionals—motivations and behavior
This section concentrates on art market stakeholders (art professionals and collectors) and their motivations and demand for art related wealth management services. As in part 2, we also look at how this has changed over the last decade, and what role they see wealth managers having when it comes protecting, enhancing and leveraging art and collectible wealth.

Over the last 10 years, we have been monitoring the stakeholders (wealth managers, collectors and art professionals) in the Art & Finance industry, and reported on the changing role and importance of art and collectible assets within a wealth management service offering.

Carnaby
©Unidade Infinita Projectos - 2011

The rise of digital assets and cryptocurrencies presents both opportunities and risks, as well as a changing competitive landscape from other financial services firms as well as non-traditional players.

Tea for Two
©Unidade Infinita Projectos - 2015

Part 1. Wealth management trends

Macro-trends

A post-pandemic world introduces new challenges and opportunities for the wealth management industry
The COVID-19 pandemic has plunged the world into uncharted territory. After months of lockdowns, social restrictions and economic hardship, individuals and businesses are gradually adapting to a new normal. But what does this new normal mean for the wealth management industry?

Innovation and transformation needed as the wealth industry undergoes a seismic shift
According to a recent report by CapGemini[2], seismic shifts in the macroeconomic, technological, and social landscape are accelerating transformation in the wealth management industry. The rise of digital assets and cryptocurrencies presents both opportunities and risks, as well as a changing competitive landscape from other financial services firms as well as non-traditional players. The client base is also evolving to include a greater presence of younger and tech-savvy individuals, and non-traditional families. To stay relevant, these shifts require wealth managers to follow a new competitive game plan with a greater focus on innovation. According to Oliver Wyman[3], the pivot from investments to holistic advice will become a "must have" rather than a "nice to have".

Adapting to clients' changing preferences
While the continued growth in wealth and changing client preferences are creating new opportunities for wealth managers, it also means they must look at the market through a new lens and reset their priorities to reflect evolving client needs and behaviors.

With lower margins and near-zero interest rates, growing regulatory requirements leading to rising compliance costs and profit margin pressure and the current pandemic crisis, wealth managers actors should strongly consider changing their traditional business models and adapting to current demand to reverse the profitability curve.

One way is by developing a holistic approach to enhance benefits for customers. Sophisticated investors value holistic advice—it is more modern, resolves multiple objectives into different investment strategies (from cash flow needs to wealth transition), and is flexible enough to meet their clients' needs.

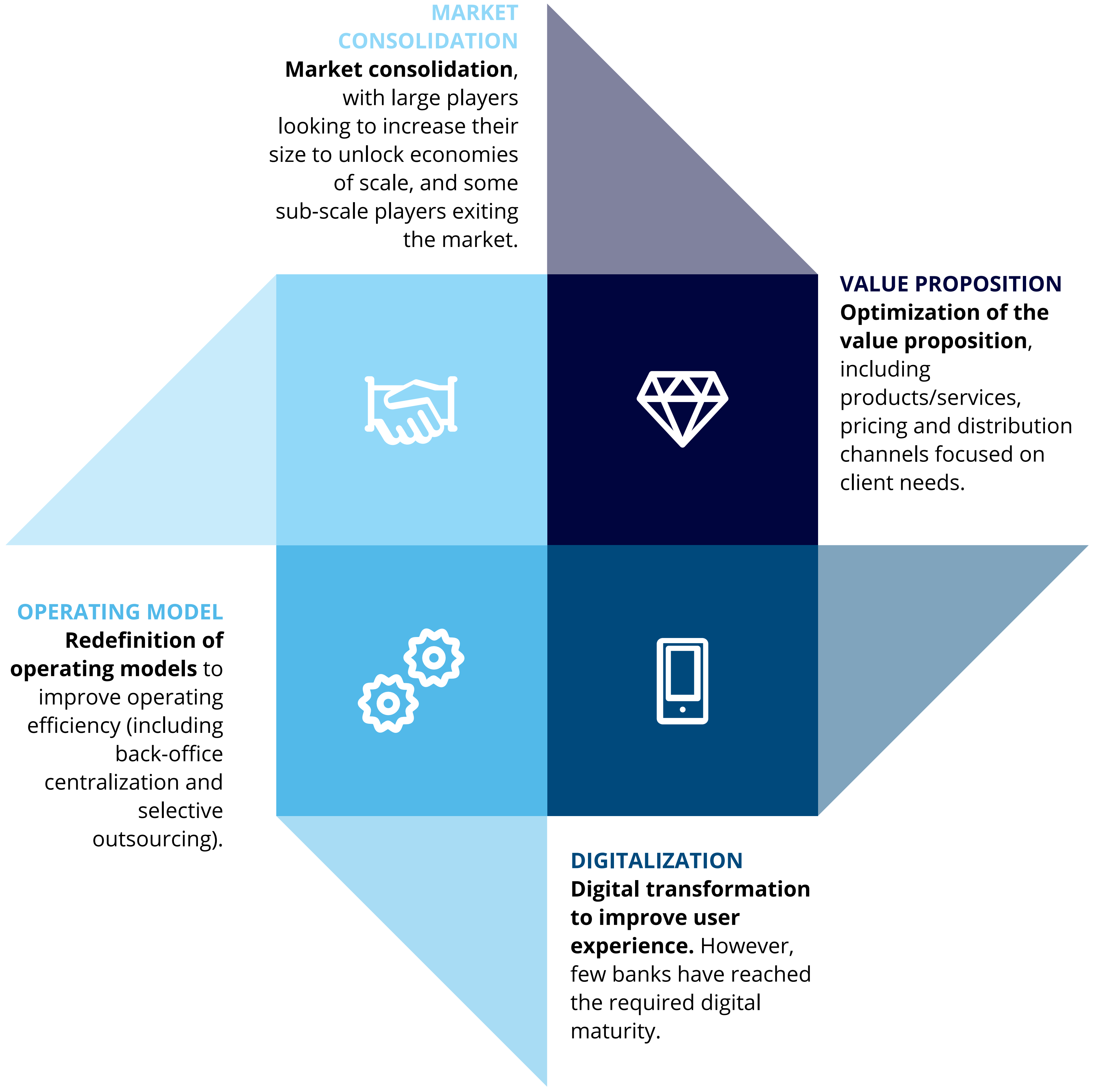
To set themselves up for future success, wealth managers will also need to invest in an adequate IT infrastructure. Several actors are seeking collaborations with FinTechs to differentiate themselves, develop new products and services and enhance their operational efficiency through digitalization with a particular focal point on how technology can become a catalyst and enabler for building and strengthening client relationships. These include a broader range of tailored services by working with external partners and using digital tools effectively to replace and complement traditional face-to-face services, an important aspect for the younger generation.

2 Source: Cap Gemini, 'World Wealth Report 2021', p.5
3 Source : Oliver Wyman, 'Wealth Management - 10 Ideas for 2021', https://www.oliverwyman.com/our-expertise/insights/2020/dec/wealth-management-10-ideas-for-2021.html

Nénuphar
©Joana Vasconcelos - 2010

Another focus point is modernizing the client relationship. Front-office staff must adapt the way they interact with clients. Digital channels, a clever use of analytics, and full personalization of service offerings will enable organizations to unlock additional revenue potential. Wealth managers must elevate the client journey by providing deeper and richer insights with more holistic, tailored and meaningful experiences and services. The focus on "purpose" related services is growing in importance, as clients want to address issues around sustainability and social impact.

Investor demand has shifted towards more sustainable investment strategies that are focused on environmental, social and governance (ESG) goals. The advent of a global climate crisis and the disproportionate impact of COVID-19 on developing nations are likely to further increase this demand. These issues are particularly relevant to the younger generation. According to research[4] from The Economist Intelligence Unit (EIU), commissioned by RBC Wealth Management, 76% of younger generations in the United Kingdom say it is increasingly important to consider ESG factors when investing, compared with 37% of older generations.



Overview of strategic initiatives

Source: Deloitte Luxembourg

4 'The shifting landscape of global wealth' written by The Economist Intelligence Unit Limited 2019. https://www.rbcwealthmanagement.com/global/en/research-insights/the-shifting-landscape-of-global-wealth/detail/

Part 2. Wealth managers—survey findings 2021

A. Art as part of a wealth management offering—10 year perspective

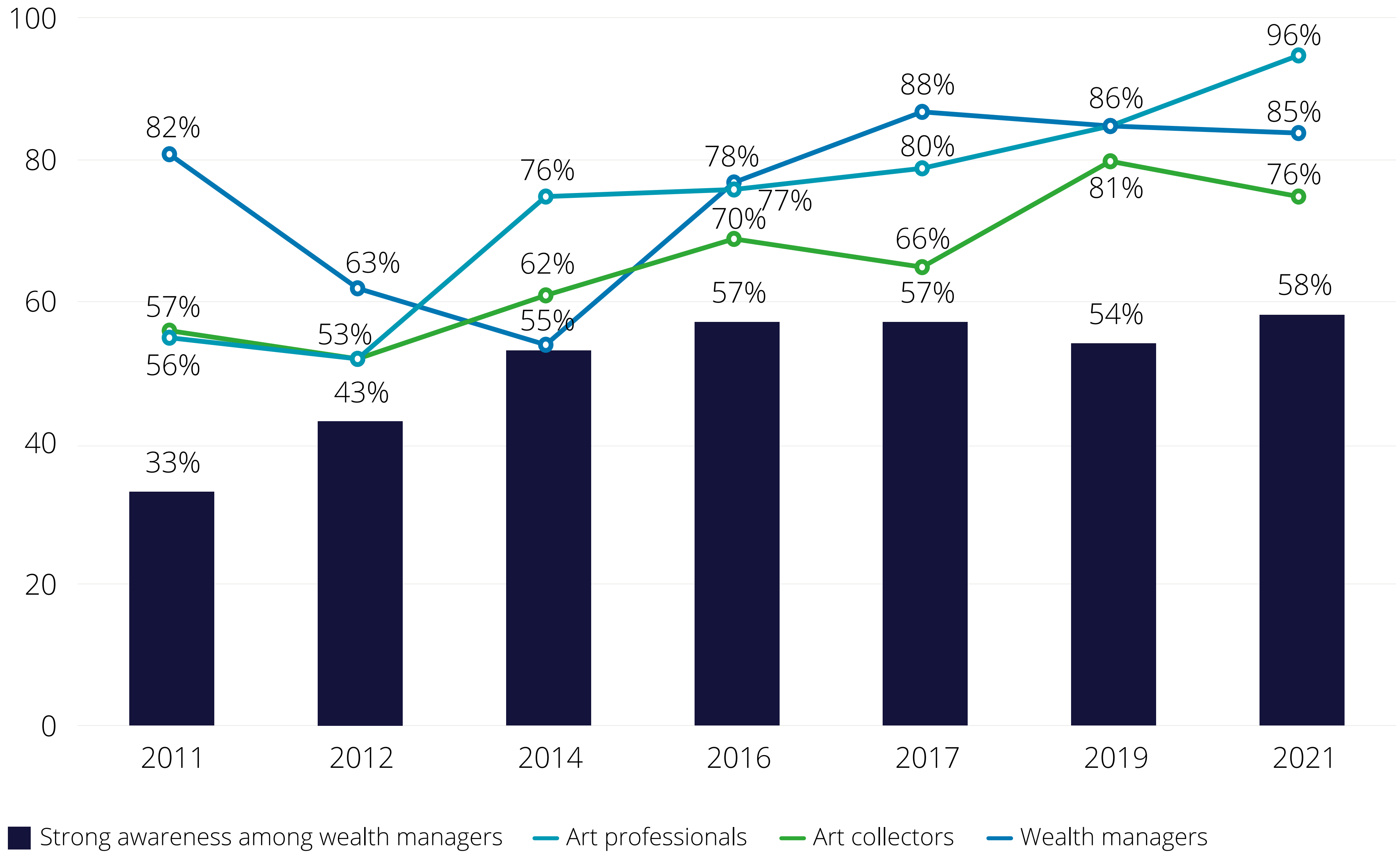
Ten years have passed since Deloitte Private & ArtTactic launched its first Art & Finance Report in December 2011[5]. Since the inaugural report, the stakeholder survey sample has grown year on year, with increasing global participation from wealth managers. We have built a decade of data and market research around various aspects of art in the context of wealth management, including regulation, technology and issues facing the next generation. On this 10th anniversary, it is time to reflect on some of the key changes and developments over the last decade, and show how far the art and finance industry has come.

The role of art in wealth management is now a well-understood concept: the vast majority (85%) of wealth managers believe there is a strong argument for including art and collectibles in their wealth management service offering, even if they are yet to do so (compared with 86% in 2019).

Table 18. Survey sample 2011–2021

Sample	2011	2012	2014	2016	2017	2019	2021
Private banks	19	30	35	53	69	54	59
Family offices	0	0	14	14	27	25	21
Art collectors	48	81	90	94	107	105	115
Art professionals	140	112	122	126	155	138	182
Art secured lenders							11

Figure 39. Do you think that art and collectibles should be part of a wealth management offering?
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021



The role of art in wealth management is now a well-understood concept
The vast majority (85%) of wealth managers believe there is a strong argument for including art and collectibles in their wealth management service offering, even if they are yet to do so (compared with 86% in 2019).

In 2016, we saw a turning point among
Wealth managers and their perception of the value that services around art and collectibles can bring to wealth managers and their clients. More than three-quarters of wealth managers agreed, up from 53% in 2014. This was the first time in our analysis that the wealth management industry aligned with collectors and art professionals about the importance of including art in their wealth management strategy and offering. Today, the question is not if art should be integrated into wealth management services dedicated to high net worth individuals (HNWIs), but rather how to do it.

5 Previous editions of the Art & Finance report are available at www.deloitte-artandfinance.com

Wealth managers are increasingly aware of art market trends and developments around art as an asset class
58% of wealth managers said they had a strong awareness of recent developments around art as an asset class, the highest proportion since the survey was launched, and up from 33% of wealth managers in 2011.

Art professionals see art as an integral part of wealth management
95% of art professionals view art as a viable asset class, and would like to see it become a part of standard wealth management practice. This represents the highest proportion since the survey began, and up from 56% in 2011.

Collectors continue to want wealth managers to incorporate art in their service offering
More than three-quarters (76%) of collectors would like wealth managers to incorporate art in their service offering. This is down from 81% in 2019, but up from 57% in 2011.

85% of wealth managers consider the need to develop a holistic advisory relationship with their clients (to look at all the assets of their clients) as the main motivation for including art and collectibles in wealth management.

Figure 40. 10-year perspective (wealth managers): what do you consider to be the strongest arguments for including art and collectibles in wealth management?

Over the last 10 years, beyond being an emotional asset, the financial consideration of art collecting has become more important and art is increasingly positioned **as a capital asset.** Art and collectibles have demonstrated an ability to both maintain and appreciate in value, and we have seen stronger financial motivations behind art collecting. Although investment and yield-seeking motivations remain key drivers, the main focus in recent years has been around the preservation of the capital allocated to art and collectible assets. Art and collectible wealth has become an integral part of the relationship between wealth managers and their clients.

Changes in clients' behavior and motivations over the last 10 years, coupled with increasing competition in the wealth management sector, have forced wealth managers to respond to new demands regarding art and collectible wealth and develop a holistic advisory relationship. One of the strongest drivers behind this response is the ongoing low-interest-rate environment, forcing investors to look for new investment opportunities. Whilst only 28% of wealth managers said this was the main argument for including art in wealth management in 2011, this increased to 46% in 2021, and has remained relatively constant since 2016, when 49% said the same.

Figure 41. Wealth managers
10-Year Perspective: Which of the following services do you offer?
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021

With more clients incorporating art and collectibles into their overall portfolio of wealth, combined with the increasing value of art, 59% of wealth managers in 2021 stated they have seen greater demand for wealth management services aimed at protecting, enhancing and monetizing the value of art, up from 28% in 2011 and 40% in 2016. Wealth managers are also experiencing strong client pressure, with 48% saying their clients were increasingly demanding art-related services this year, up from only 11% in 2011 and 34% in 2019.

Wealth managers have developed a more holistic art service offering over the last 10 years

Whilst art and client entertainment was the most common approach to servicing art-related needs in 2011, the spectrum of art-related wealth management services has gradually broadened over the last 10 years, with a convergence point of around 80% for all services except investment. These services are predominantly in art and wealth protection, art and estate planning and philanthropy, art secured lending and, to a lesser extent, in art investment services. These categories correspond to the report's structure, and we refer to Sections 3, 5 and 6 for a more in-depth analysis of these services and latest trends.

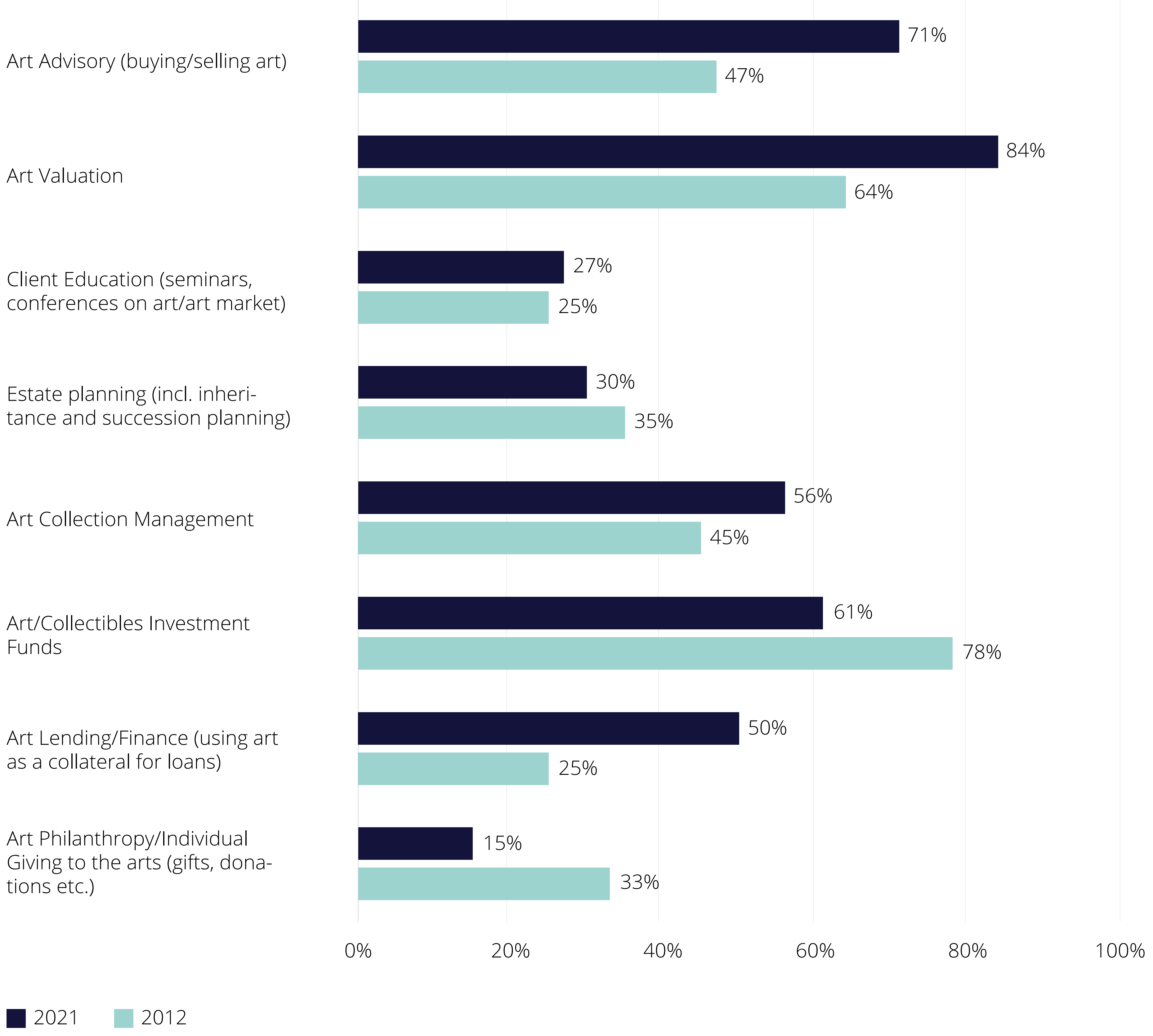
Over the last decade, these service areas have seen a significant increase in adoption among wealth managers with an established art service offering[6]. Regarding art and wealth protection, the share of wealth managers offering art advisory services has increased from 39% in 2011 to 78% in 2021. Collection management services grew from 17% in 2011 to 76% in 2021, and art valuation services rose from 39% in 2011 to 82% in 2021.

Art and estate planning services have also grown in recent years, with 82% of wealth managers offering this service in 2021 compared with 40% in 2011. Related to estate planning, a further 76% of wealth managers said they offered art philanthropy services, up from 40% in 2011. This signals the important role that art-related wealth is playing in the global generational wealth transfer currently taking place.

With the increasing focus on the financial aspects of art and collectibles, we have also seen a positive trend around art secured lending and art investment-related services. Wealth managers offering art secured lending services have increased from 21% in 2011 to 76% in 2021. Although the art investment fund market has remained relatively static in recent years, surprisingly in 2021, 62% of wealth managers said they offered their clients the opportunity to invest in art through these investment products, up from 11% in 2011. Section 7 covers in more depth the range of new art investment services that are emerging, which could mean this area is ripe for further growth in the years to come.

6 68% of wealth managers surveyed stated that they offer art-related weatlh management services (see p.92)

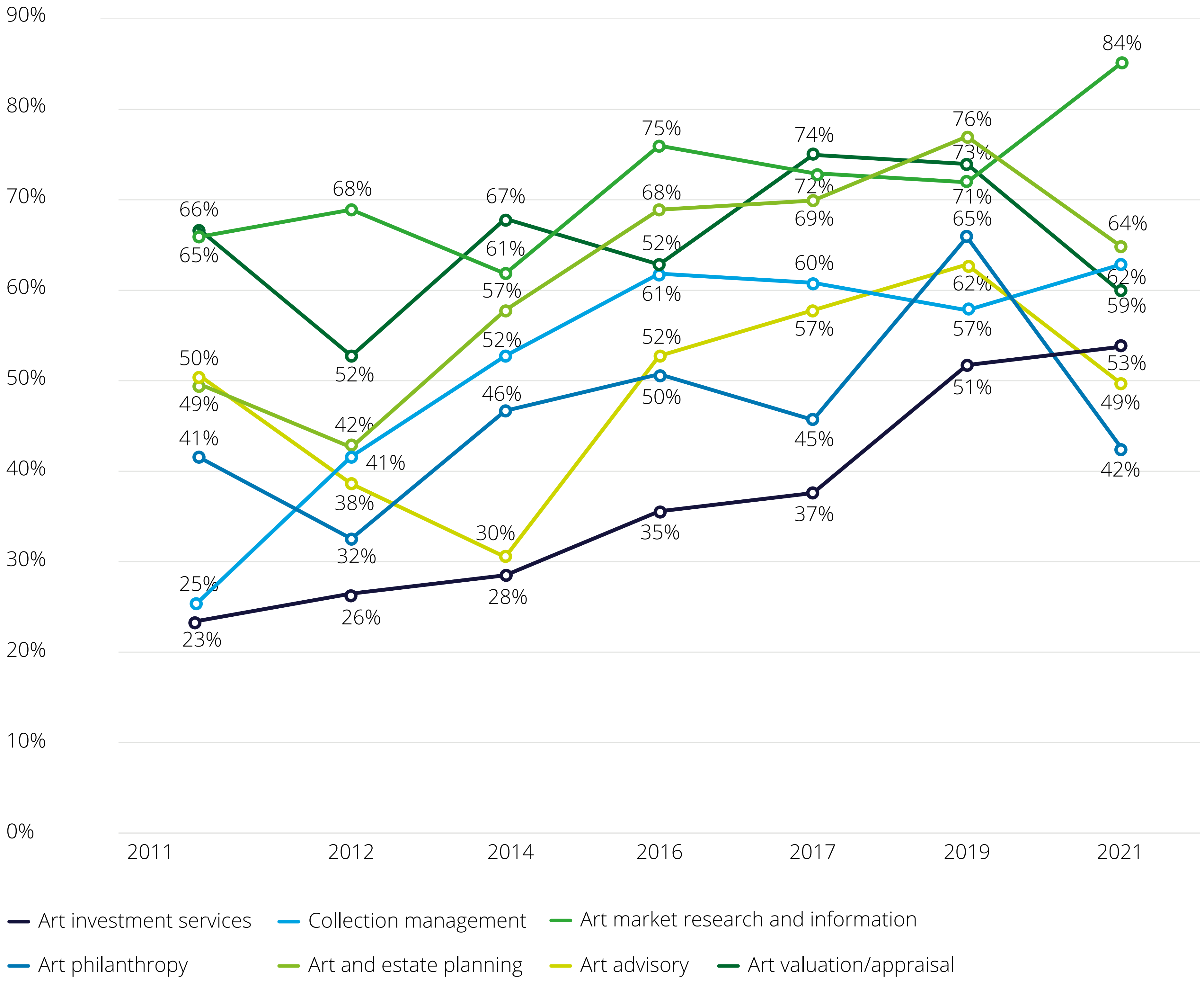
Figure 42. Wealth managers
What art services are delivered by a third party?
Based on % wealth managers with an existing art wealth service offering (2012 vs 2021)
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021



Precious
©Unidade Infinita Projectos - 2018

As the wealth management industry moves towards a more holistic service offering, over the past 10 years we have seen a strategic shift towards partnerships with external providers to deliver these services. In the context of art, a closer relationship between art professionals and wealth managers has emerged, particularly around services related to art advisory, art valuation and art secured lending.

Figure 43. Collectors: Which of the art wealth management services are most relevant to you?
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021



Collector demand for art-related services has changed in areas around investment and collection management

Collector needs and demand for art-related wealth management services have also evolved over the last 10 years. The biggest interest is in the areas of art investment services, collection management, art advisory, estate planning and art philanthropy services, as well as a growing need for art market research and information. In 2021, more than half of collectors (53%) said art investment services were among the most relevant products that wealth managers could offer, up from 23% of collectors who said the same in 2011.

With collectors accumulating more art and collectible wealth, the need for services to protect and monitor these assets has grown, as well as the demand for collection management services among collectors. In 2021, 62% of collectors said they considered this service to be the most relevant, up from only 25% who said the same in 2011. This corresponds with recent report findings that more collectors (76% in 2021) would like to see wealth managers incorporate art-related wealth in their service offering (see figure 56 on p.117).

In recent years, we have also seen a stronger desire among collectors for art market research and information—in 2021, 84% of art collectors felt it was a service that wealth managers should offer, up from 65% in 2011.

In 2021, 62% of collectors said they considered collection management to be the most relevant up from only 25% who said the same in 2011.

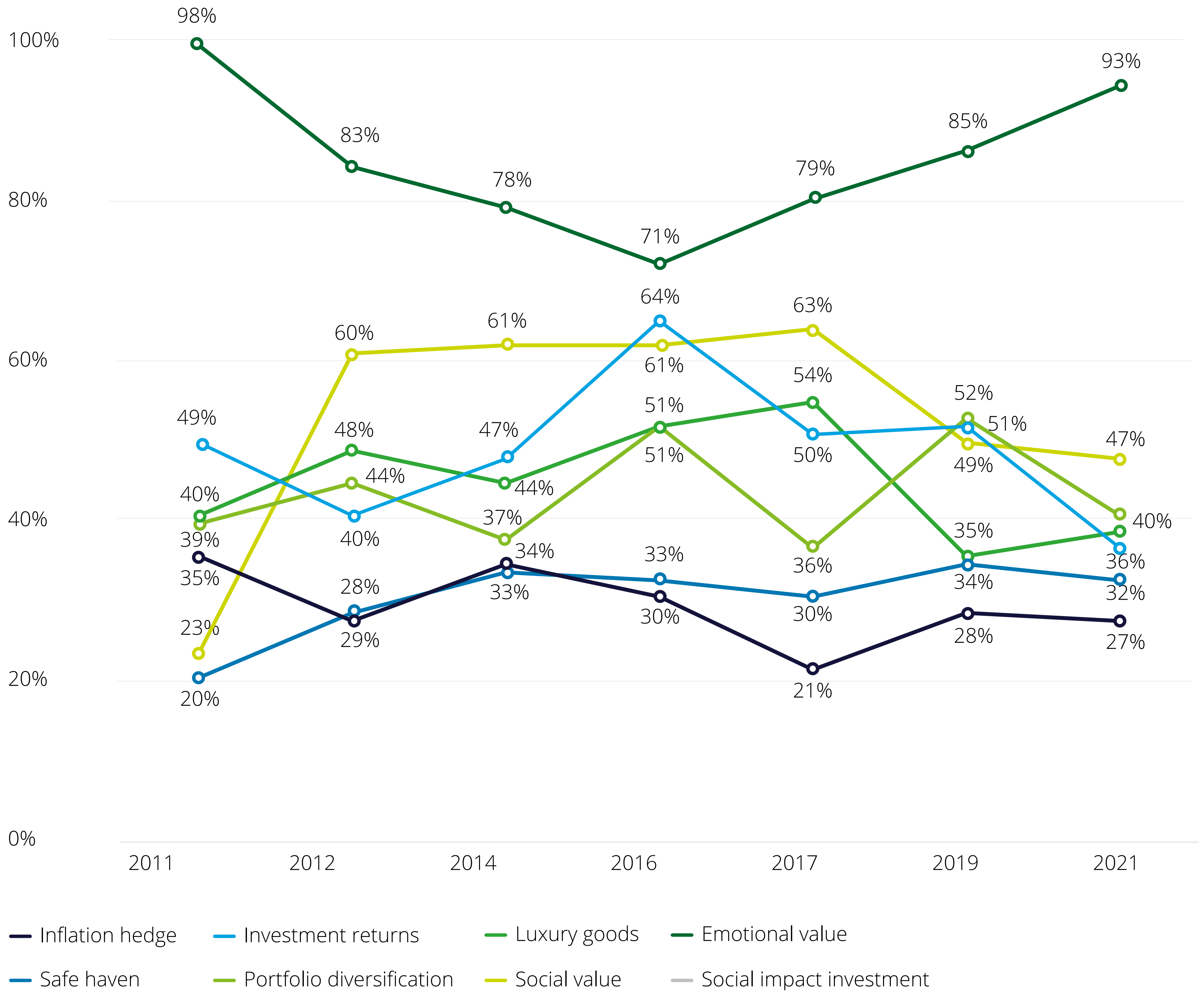
Silver Spider
©Luís Vasconcelos/Courtesy Unidade Infinita Projectos - 2015

Emotional value of art ownership takes center stage

The passion and emotional value associated with art have been collectors' strongest motivations since we launched the survey in 2011, but financial motivations have remained a stable feature since 2011, albeit at a lower level. As in previous years, we would argue that is exactly the reason why wealth managers should engage with this asset class, by offering services catering to both the strong emotional value associated with art ownership as well as the increasing financial value that has built over the last two decades. Wealth managers are well-placed to manage, enhance and protect these assets, as well as creating a stronger, more holistic relationship with their clients, which 85% of wealth managers cited as the primary reason for including art in their wealth management offering .

Figure 44. Collectors: Which of the following motivations are most important in buying art?

Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021



Brancura
©Unidade Infinita Projectos - 2019

Key challenges

Why are wealth managers struggling to incorporate art and collectibles in their services?
Over the last 10 years, we have noticed a slight improvement regarding the challenges faced by wealth managers in offering art-related services. The lack of regulation and transparency remains a key hurdle, although the share of wealth managers who said these were key obstacles has fallen since 2017. This suggests that recent developments around AML regulation and the role of technology are starting to change wealth managers' perceptions around these issues. Challenges that have become more of a concern are demonstrating the cost/benefit of including art in wealth management, as well as the lack of internal expertise to embed these services into existing offerings. A lack of interest or leadership does not seem to be an issue when integrating art in wealth management.

Lack of regulation remains a concern
Despite the recent introduction of new AML legislation in Europe and the United States, 61% of wealth managers are still concerned about the lack of regulation in the art market, identifying it as a main obstacle in offering art-related services and products. This is slightly higher than 58% in 2019 but an improvement from both 2011 (72%) and 2014 (83%). This could suggest that more regulation may be required to allow the wealth management industry to fully embrace art as a viable asset class. We explore the main threats and elements of mistrust more closely in section 8 (p.279). What is evident, is that art market stakeholders must continue to build trust among the wealth management community to drive future growth[7].

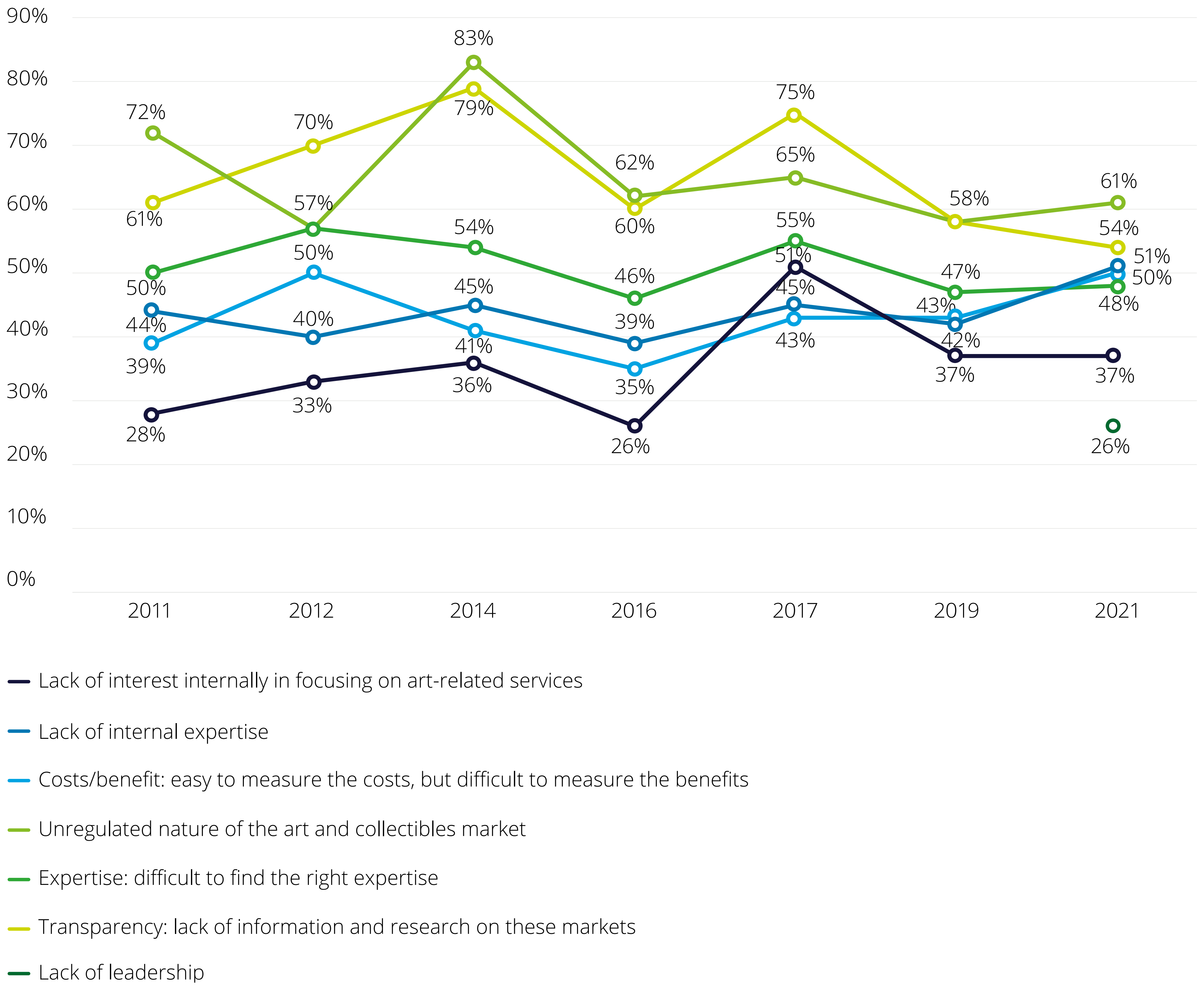
Low transparency
In 2021, 54% of wealth managers state that low transparency and a lack of information and research on the art market are key challenges in offering these services, compared with 58% in 2019 and a peak of 79% in 2014. This slight improvement could hint that the art world's recent move online, offering more price transparency and easier access to information, has increased the market's transparency during the pandemic.

Lack of internal expertise and interest
51% of wealth managers said that a lack of internal expertise was a key challenge when developing art-related service offerings, up from 43% in 2019 and 44% in 2011. Almost half (48%) of wealth managers also struggled to find the right expertise, compared with 47% in 2019 and 50% in 2011. This year 26% of wealth managers cited the lack of leadership within the organization as a key hurdle, and 37% said that lack of internal interest was a key challenge.

New initiatives could address the lack of internal expertise in the wealth management sector, such as professional online networks and marketplaces for art professionals. These networks could help connecting verified talents from the global art market with wealth managers.

Hard to measure the benefits
Half of wealth managers said it was difficult to measure the exact benefits of art-related services and their impact on their bottom line. This was up from 43% in 2019 and 39% in 2011, showing that wealth managers struggle to find tangible links between these services and the ultimate client and business benefits. However, despite this, the increasing adoption of art and collectible services by wealth managers suggests their value lies in allowing firms to differentiate themselves on the market and retain clients in an increasingly competitive landscape.

Figure 45. 10-year perspective: wealth managers: what do you see as the biggest challenge in offering art-related services/products?
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021



7 Source: Deloitte Insight, The link between trust and economic prosperity by Ira Kalish, Michael Wolf, Jonathan Holdowsky. The positive relationship between trust and the macroeconomy is well known. Trust is like an interdependent web that connects all actors in an economy and influences how they work together to drive growth

B. Wealth managers: 2019 versus 2021 comparison

B.1. Motivations and rationale

Changing attitudes among wealth managers in 2021

Since the pre-pandemic findings of our last survey in 2019, we have seen several shifts in wealth managers' perceptions of the role of art and collectibles in wealth management. This year's survey findings show a positive change in wealth managers' attitudes towards the importance of art and collectibles within a holistic wealth management offering.

Figure 46. Wealth Managers: What do you consider the strongest arguments for including art and collectibles in wealth management?

Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021

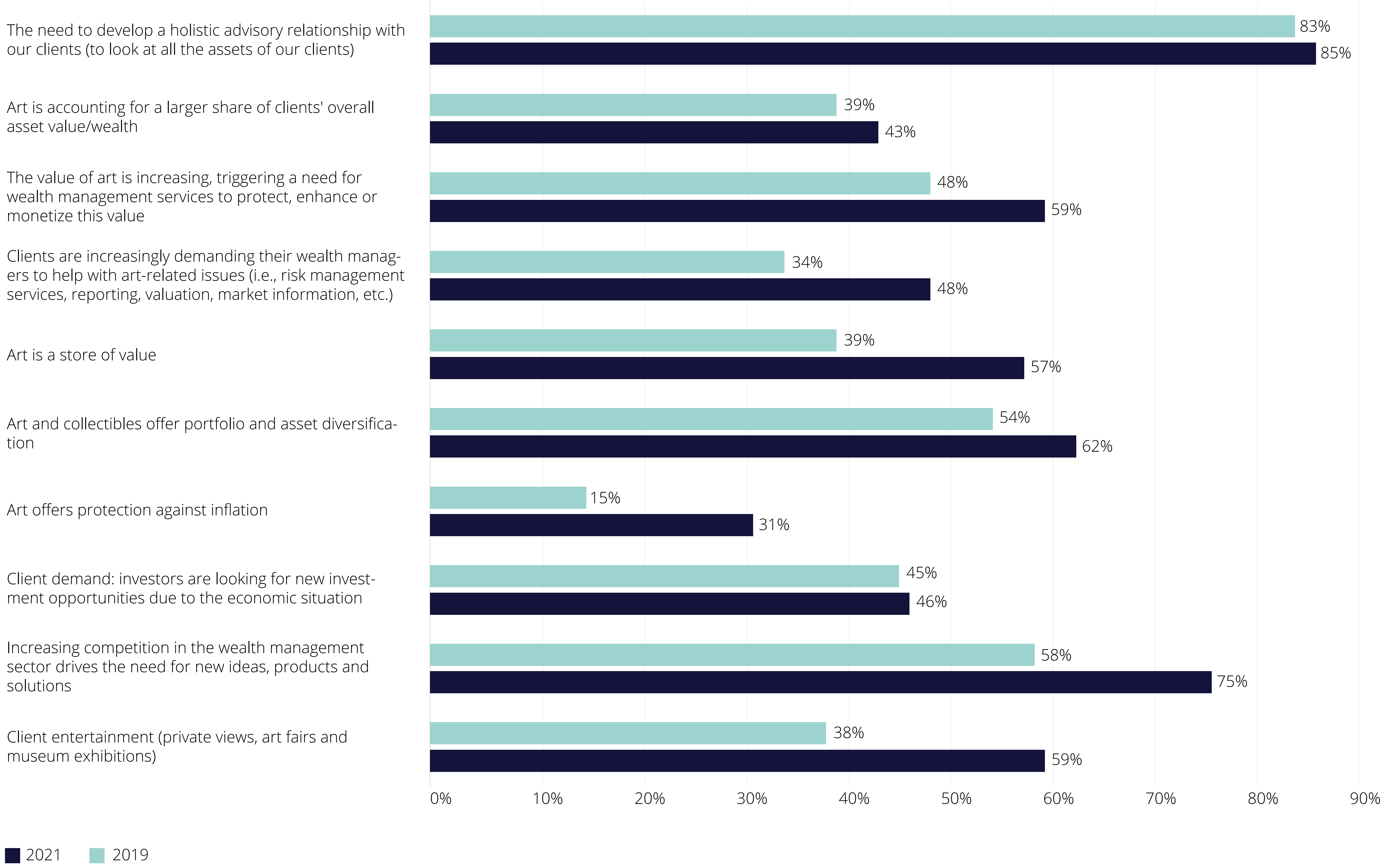
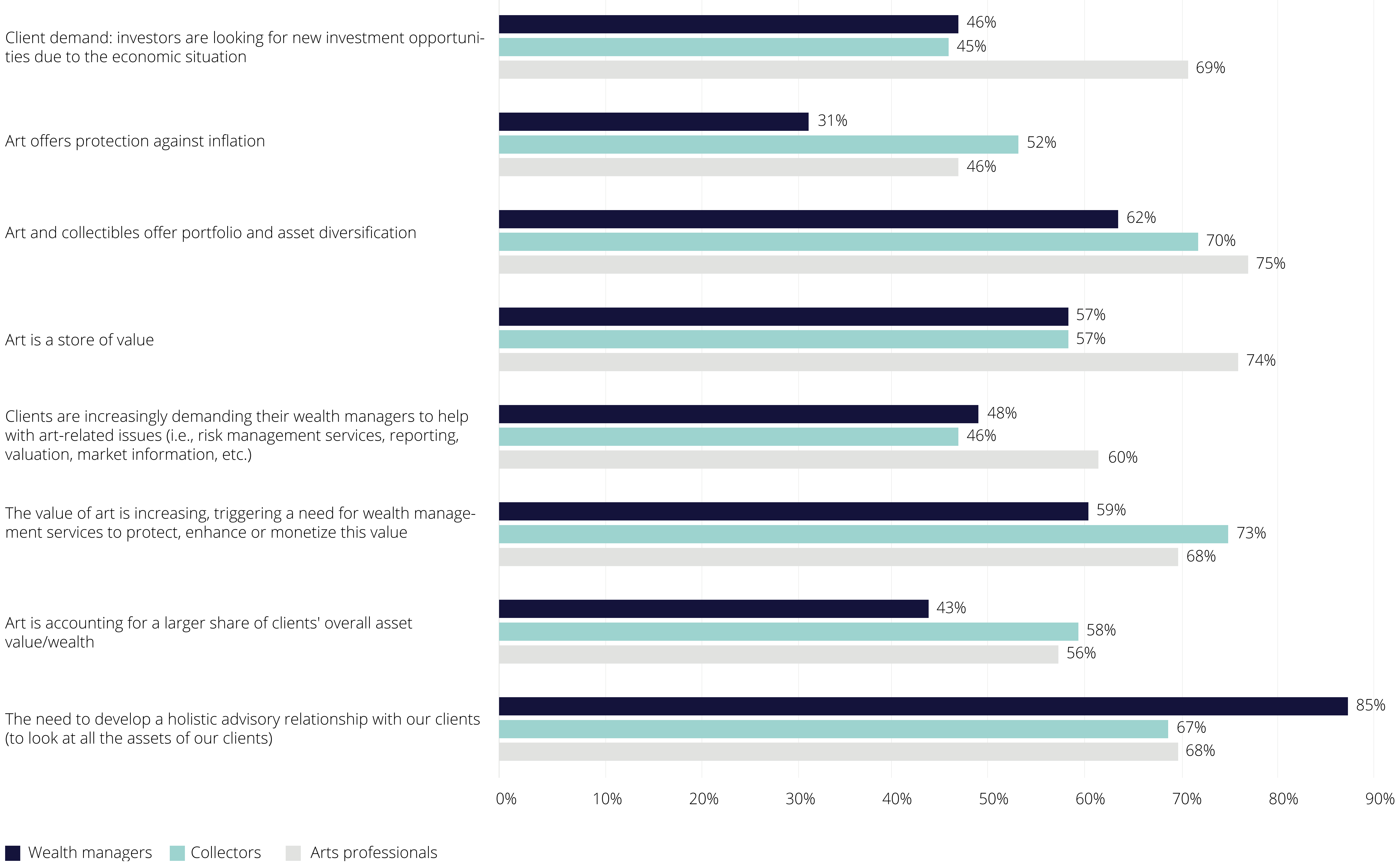


Figure 47. Stakeholder comparison: what do you consider to be the strongest arguments for including art and collectibles in wealth management?
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021



The move towards a holistic wealth management model is driving interest in art and collectibles
85% of wealth managers said the need to develop a holistic advisory relationship with their clients is the dominant reason for embedding art and collectibles in the service offering, up from 83% in 2019. This year 67% of collectors and 68% of art professionals saw this as a strong motivation for wealth managers to incorporate art and collectibles.

Art as a store of value
The art market's strong performance and resilience over the last 24 months, including the hardship caused by the pandemic, has changed wealth managers' perception of art as an asset class. More than half (57%) of wealth managers see art as a store of value, up from 39% in 2019. This is in line with collectors, with 57% saying this was a strong motivation, while a significantly higher share of art professionals (74%) agreed, up from 69% in 2019. This could signal that art market professionals are increasingly viewing art as a financial asset and not only a collectible.

Higher art values trigger the need for financial services
This year, 59% of wealth managers said higher asset values of art and collectibles have triggered a renewed look at wealth management services aimed at protecting, enhancing or monetizing the value of art. This was significantly higher among collectors (73%) and art professionals (68%), which suggests a growing client demand for wealth management services related to art in order to manage the financial value associated with art and collectibles.

Art and collectibles account for a significant part of overall wealth
Related to the previous point about art asset inflation, our findings in Section 1, shows that art and collectibles account for an estimated 5% of collectors' financial wealth, or an estimated $1,481 billion in 2020. This year 58% of collectors and 56% of art professionals said this is the main reason why wealth managers should incorporate art in the service offering. Awareness of this trend seems to be growing among wealth managers, with 43% saying this is a key motivation for wealth managers to offer these services, against 39% who said the same in 2019.

Fear of inflation

To address the economic shock triggered by the COVID-19 crisis, central banks expanded their quantitative easing (QE) programs to support their economies and the functioning of global financial markets in 2020[8]. Inflation figures in many global economies are climbing. Rising goods prices were one of the major reasons that US core customer price index (CPI) inflation jumped to 3.8% year-on-year in May 2021, the highest since the early 1990s. The focus on alternative, hard-asset investments as an inflation hedge is likely to intensify over the coming 12 months. This year 31% of wealth managers see art and collectibles as potential protection against inflation, up from 15% in 2019. Due to fear of higher inflation, the role that art could play as an inflation hedge is becoming increasingly important among collectors (52%) and art professionals (46%), potentially meaning that collectors are increasingly regarding the art market as a safe haven against the growing risk of inflation.

Portfolio diversification

This year 62% of wealth managers view art and collectibles as viable assets for portfolio diversification, up from 54% in 2019. The art market's resilience during the COVID-19 pandemic seems to have convinced more wealth managers in 2021 of the benefit of art and its low correlation to other asset classes (see artnet article p.225). Portfolio diversification is also high on the agenda for collectors (70%) and art professionals (75%) who view art and collectibles as an asset diversification tool.

Competition in the wealth management industry

Increasing global competition requires new strategies to retain and recruit new clients. An expanded service offering that includes art and collectibles is one of the key drivers to remaining competitive, with 75% of wealth managers identifying this in 2021, up from 58% in 2019.

Client pressure is increasing

As the art market grows and more clients acquire art, there is a burgeoning demand for wealth managers to help with art-related issues (i.e., risk management services, reporting, art secured lending, valuation, market information, education, etc.). In 2021, 48% of wealth managers said client pressure was a compelling reason for including art and collectibles in their service offering, against 34% in 2019. This was higher among art professionals, where 60% said they believed their clients were looking for wealth management services for their art-related wealth. More than half (54%) of art collectors said this was a strong reason for wealth managers to adopt and expand their service offering to include art.

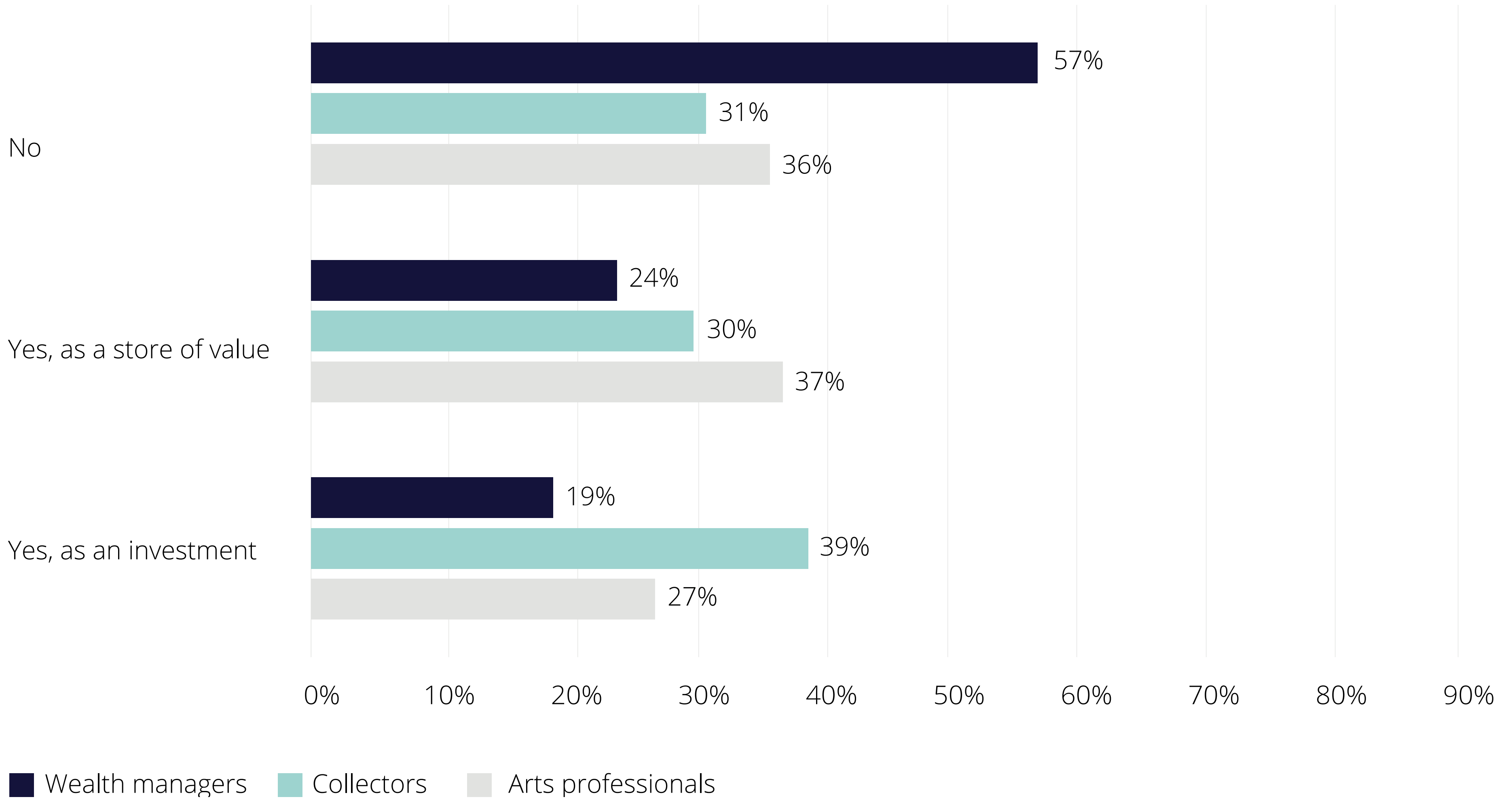
Social value and client engagement matters

Since the outbreak of the COVID-19 pandemic, wealth managers have lost their traditional face-to-face contact with clients. This year's findings suggest wealth managers increasingly see art as an entertainment and client engagement tool, as the world gradually opens up. More than half (59%) of wealth managers said that client entertainment (private views, art fairs, and museum exhibitions) were important motivations for including art in their service offering, up from 38% in 2019.

The COVID-19 pandemic triggered more interest in art as a source of financial diversification, while most wealth managers said they saw no evidence of this effect

In 2021, 19% of wealth managers said that the COVID-19 pandemic had triggered an increasing interest in art as an investment, with 24% of wealth managers saying they had experienced higher demand for art as a store of value. However, most wealth managers (57%) said they saw no evidence of the pandemic affecting demand for art as an asset class. This differs significantly from our survey of art collectors and art professionals, where around one-third had seen a positive impact on interest during the pandemic. This year 39% of collectors and 27% of art professionals said the COVID-19 pandemic had triggered an increasing interest in art as an investment, with 30% of collectors and 39% of art professionals seeing stronger interest in art as a store of value. This demonstrates the role of asset/wealth protection that art and collectibles can play in periods of uncertainty. A minority of collectors (31%) said that the pandemic had no impact on demand for art as an asset class, with 36% of art professionals saying the same.

Figure 48. During the COVID-19 pandemic, have you seen an increasing interest in art and collectible assets as an investment or store of value?
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021

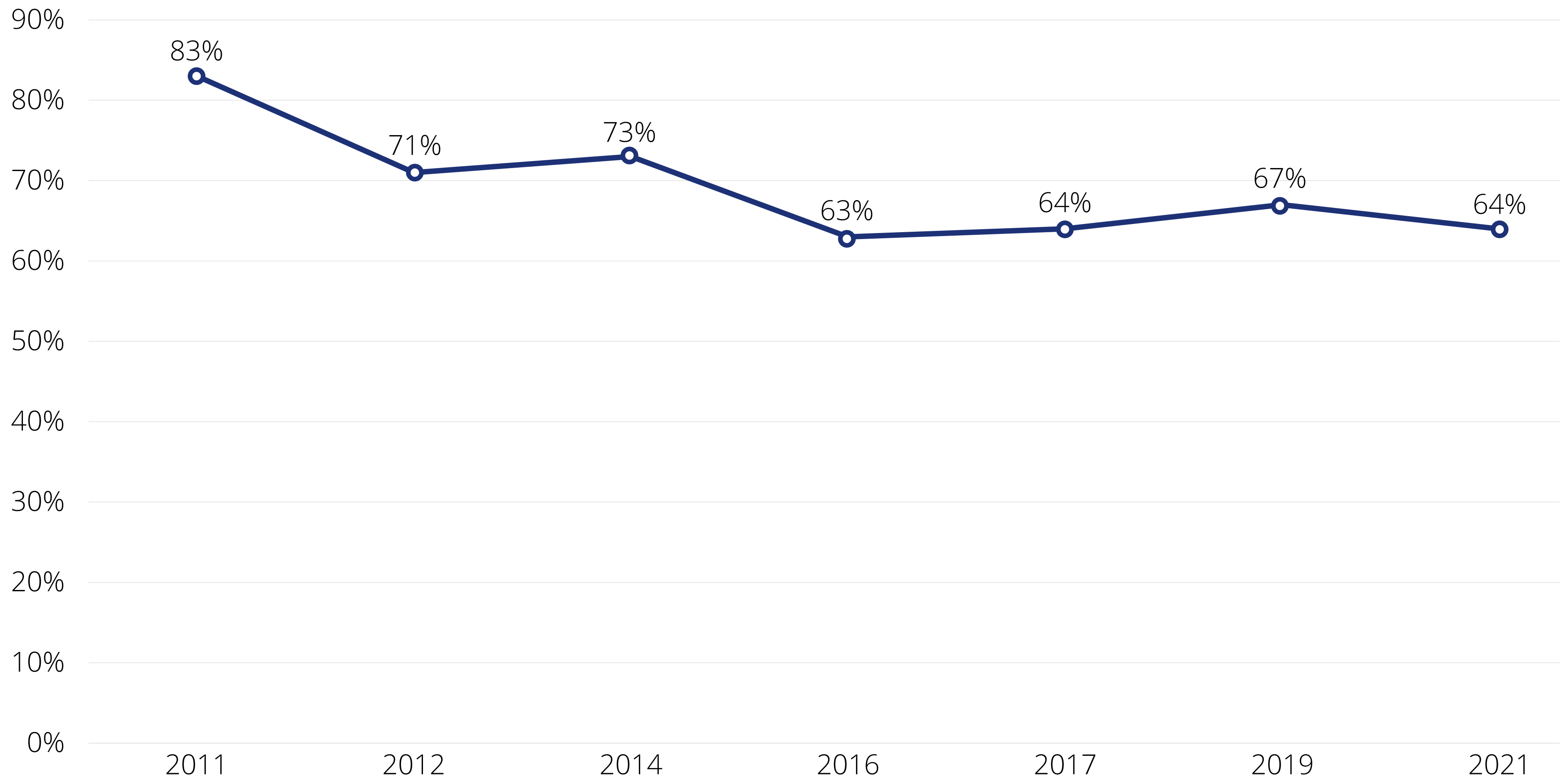


8 Source: https://www.atlanticcouncil.org/

B.2 Art-related services offered by the wealth management industry

What art-related services do wealth managers currently offer?
Of the wealth managers surveyed, 64% have integrated art into their wealth management service offering. This share has remained consistent over the last four editions of the Art & Finance report, even with the rising number of wealth managers participating in the survey each year. Although there is still work to be done to encourage more wealth managers to incorporate art in their wealth management practices, the findings suggest that the market and audience are growing. Eugénie Dumont, Art Collections Manager at Banque Degroof Petercam shares her approach on Art advisory in her contribution on p.115.

Figure 49. Percentage of wealth managers with art integrated into their wealth management services offering
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021



Sacré Coeur
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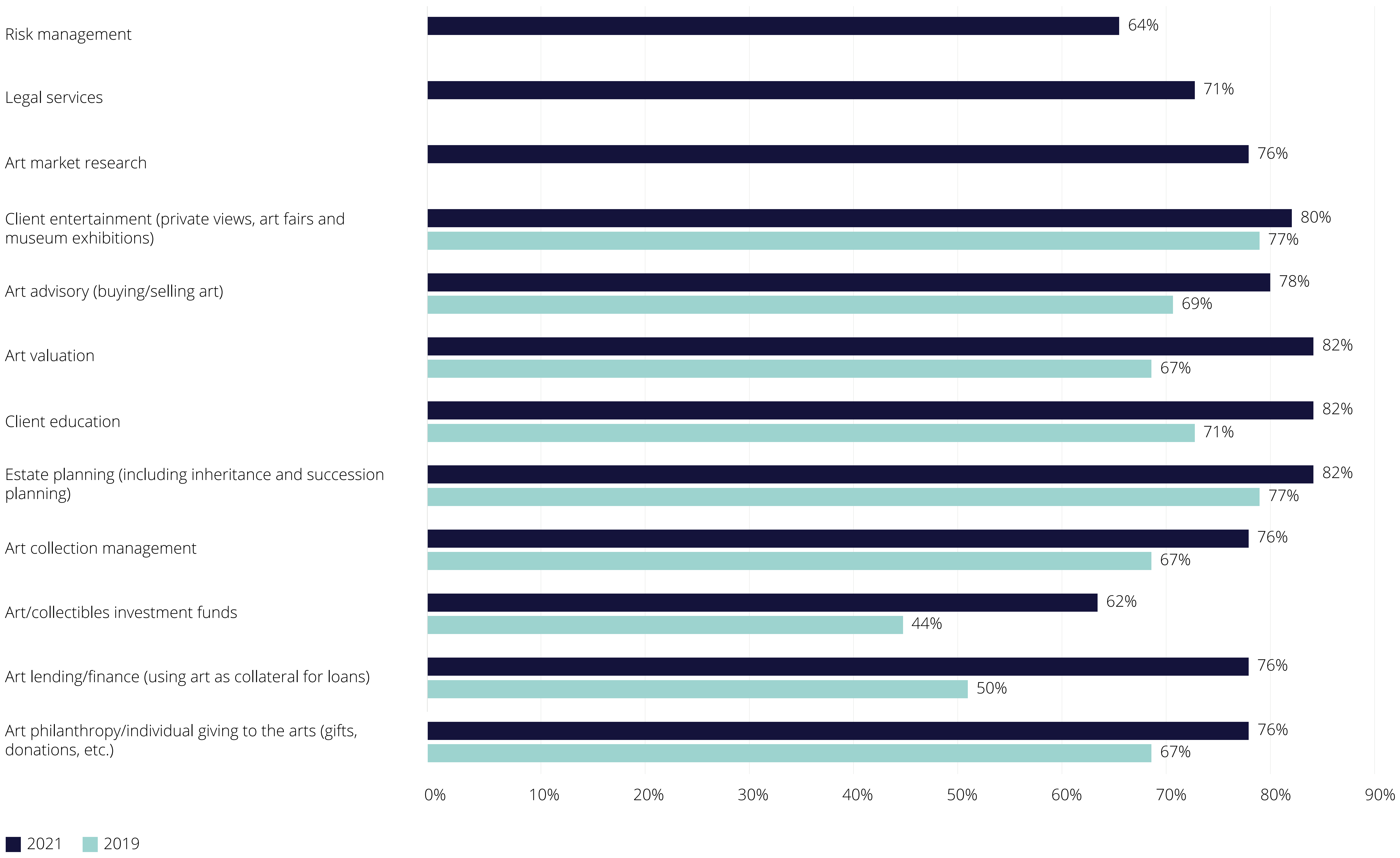
Figure 50. Wealth Managers: Which of the art related services do you offer?
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021



Note : Risk management, legal services and art market research have been added in the survey this year

What art-related services do you offer?
In this year's survey, the art-related services offered by wealth managers have increased across the board. This suggests a further move towards a more holistic approach to art wealth management, focusing on aspects around protection, accumulation and transfer as well as turning art-related wealth into a working asset (art secured lending). For the first time in the last 10 years, it looks like we have reached a point of no return, and the focus going forward will be on increasing the sophistication of the art wealth management services offered.

For the first time in the last 10 years, it looks like we have reached a point of no return.

In terms of the future, 59% of wealth managers said art estate planning will be part of their main focus over the coming 12 months.

Blup
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Estate planning and philanthropy ranks even higher than 2019 on the list of art-related services, as wealth managers start preparing for the global wealth transfer
This year 82% of wealth managers with an established art service offering said they offered clients estate planning services related to art, up from 77% in 2019. Most (76%) of these wealth managers offered services around art philanthropy and individual giving (setting up foundations, arranging gifts and donations) compared with 67% in 2019. Of these wealth managers, 70% said they offered estate planning services in-house, down from 88% in 2019, suggesting they are increasingly seeking outside expertise to help with the often complex environment of art-related wealth. In terms of the future, 59% of wealth managers said art estate planning will be part of their main focus over the coming 12 months, the highest priority this year but down from 65% in 2019. The slightly lower percentage could signal that some managers have already invested in this area and are shifting their attention elsewhere. In terms of art philanthropy, 47% of wealth managers identified this as an area of investment and focus in the coming year (the third-highest priority service), compared with 51% in 2019.

Art valuation has become an integral part of art wealth service offering
82% of wealth managers with an established art service provision said they offered services around art valuation, up from 67% in 2019. For most (84%) this service is provided by third parties, which suggests that the dialogue and collaboration between traditional art valuation professionals and the wealth management industry have grown over the last two years. This highlights the trends and priorities outlined in previous editions of the Art & Finance report, which called attention to the need for art market professionals and the wealth management industry to be more closely aligned. This now seems to be happening, paving the way for better integration of art-related skills and financial expertise necessary to grow the overall market. It also confirms the recognition of the increasing wealth and monetary value allocated to art and collectibles, as well as the need for proper monitoring.

Client education is taking center stage
82% of wealth managers that already provide art-related services said they offer client education around art-related issues, compared with 71% in 2019. As wealth managers increasingly embrace art and collectibles in their service offerings, they invest more effort in educating their clients about their services and how they can play an active role in helping their clients. Seventy-three percent of wealth managers said these services were organized in-house, the same as in 2019. While 50% of private banks and 47% of family offices said client education would be a priority area in the coming 12 months.

Client entertainment is important as the world comes out of the pandemic
After almost months of lockdowns and social restrictions on gatherings, most people are longing to return to some kind of normality. Most (80%) of the wealth managers that already provide art-related services said they offered client entertainment, up from 77% in 2019. Of the private banks surveyed, 63% said they would prioritize client entertainment in the next 12 months, compared with 47% in 2019. This signals that wealth managers are keen to establish face-to-face relationships with their clients after a prolonged period of remote and virtual contact. Over the next 12 months, 58% of wealth managers said they would focus on art entertainment as a way to reconnect and find new modes of engagement with their clients.

Art advisory services see an uptick this year

78% of wealth managers that already provide art wealth management services said they offered art advisory services to their clients, compared with 69% in 2019. These services were predominantly delivered through external advisors, with 71% of wealth managers saying they use a third-party expert. As previously mentioned, regarding valuation services, the wealth management industry and art professionals seemed to have found a common collaborative ground to service clients' needs in the past two years. The increasing level of regulation, such as the new AML legislation for the art market, could boost levels of trust in the market and among its professionals, further opening opportunities between the art and the wealth management industry. As a high number of wealth managers already offer art advisory services to their clients, only 27% said this will be an area of focus over the coming year, compared with 33% in 2019. According to Banque Degroof Petercam (see p.115), art advisory is no longer limited to ultra-high net worth individuals (UHNWIs).

More focus on art collection management

76% of wealth managers that already provide art-related services said they offered art collection management services, compared with 67% in 2019. More than half (56%) said this service was provided by a third-party company, compared with 60% in 2019. This could mean that wealth managers are keen to internalize the collection management

Goutte
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76% of wealth managers with an established art service offering said they provided art secured lending services to their clients, compared with 50% in 2019. Half of these wealth managers said this service was offered in-house, while 50% was provided through third parties.

system with their own reporting systems, creating an in-house service going forward. Over the next year, 86% of family offices (but only 22% of private banks) said this will be an area of focus. It is clear that family offices are increasingly looking for better ways to manage their clients' collections and embed this as part of their overall wealth reporting service offering.

Art secured lending gains traction

76% of wealth managers with an established art service offering said they provided art secured lending services to their clients, compared with 50% in 2019. Half of these wealth managers said this service was offered in-house, while 50% was provided through third parties. The uptick in the number of wealth managers providing financing solutions around art corresponds with the growth in the art secured lending market seen over the last year (See art secured lending section 5). Over the next 12 months, 29% of wealth managers said this will be an area of focus, compared with 26% in 2019.

Art investment services are becoming more important as clients are looking to diversify

62% of wealth managers with an existing art-related service offering said they provided a range of art investment services, up from 44% in 2019 and the highest percentage since 2014. The majority (61%) delivered this service through an external provider. This suggests a growing interest in art as an investment, and mimics the renewed interest around art investment funds, fractional ownership, non-fungible tokens (NFTs) and tokenization. Over the coming 12 months, 18% of wealth managers said they will focus on this area, compared with only 4% in 2019. See Section 6 for more information.

Art market research finds an important role

76% of wealth managers with an established art service offering said they provided art research related services to their clients, suggesting that wealth managers are increasingly leveraging their role as a neutral party in the art market to help inform and educate their clients. This research and information is predominantly provided by third parties (65%), and suggests a closer collaboration between existing art market data and research providers and the wealth management industry. This collaboration is likely to increase the trust in and demand for art market data and information going forward. This is particularly vital as only 18% of wealth managers express a high level of trust in art market data this year, compared with 16% in 2019.

Legal services

This is the first year we have included legal services in our survey. Of the wealth managers that already provide art-related services, 71% said they provided their clients with legal advice and assistance. Although 44% said they provided these services in-house, 56% relied on external expertise. This is already an important service, because as the value of art increases, more art is used as collateral for loans, and tax issues from cross-border transactions are becoming commonplace.

Risk management

64% of wealth managers with an established art service offering said they provided services around risk management and art, with 69% of these services provided by third parties. Risk management services would include know your customer (KYC) and AML, risk of counterparty/payment, liquidity risk, valuation risk, shipment, insurance and legal risks.

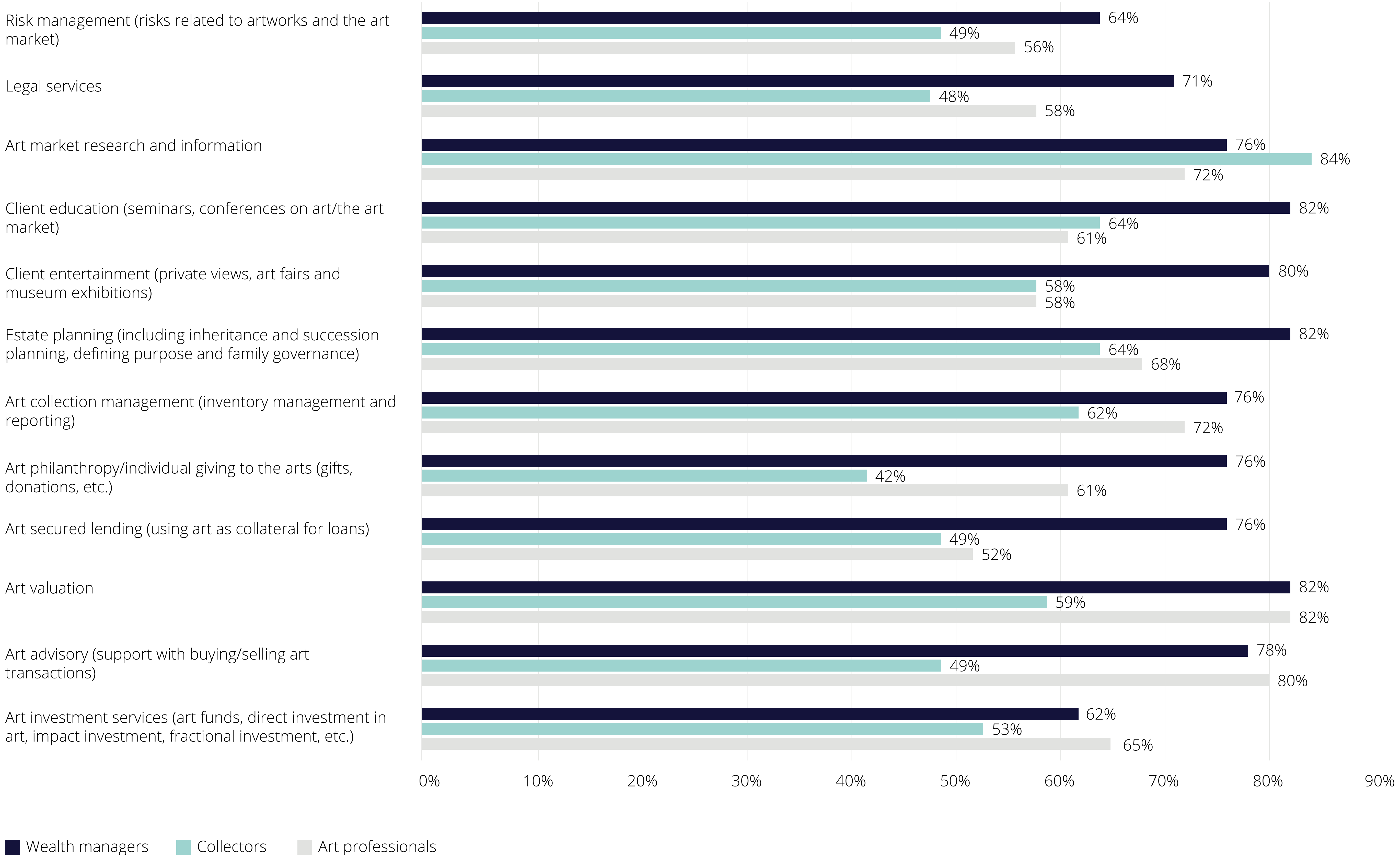
Gap analysis:

Art professionals and wealth managers are strongly aligned, with art professionals welcoming the development of art wealth management services and the increasing collaboration with wealth managers.

Collectors, on the other hand, are looking for quality and unbiased information from their trusted advisors to make informed decisions. While emotion is an important motivation for collecting, a collection management strategy and proper due-diligence processes are also required when collectors acquire art. We see a real opportunity for wealth managers to connect with their clients on these factors, by being an independent source of information and expertise. This also offers wealth managers an ideal entry point to integrate art into their wealth management offerings. Future collaborations with the growing number of ArtTech companies could be a way to initiate this process.

Figure 51. Gap Analysis: Which services are most relevant to collectors and art professionals vs what wealth managers are currently offering?

Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021



Wealth managers: which services will you focus on in the next 12 months?

A stable Art & Finance future indicator over the last 7 years suggests a certain maturity around art and wealth management services, particularly for the more traditional services such as estate planning and philanthropy. It is interesting to note the renewed interest in art investment services after eight years of decline. Art secured lending remains an area of focus and development.

Figure 52. Wealth Managers: Which services will you focus on in the next 12 months?

Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021

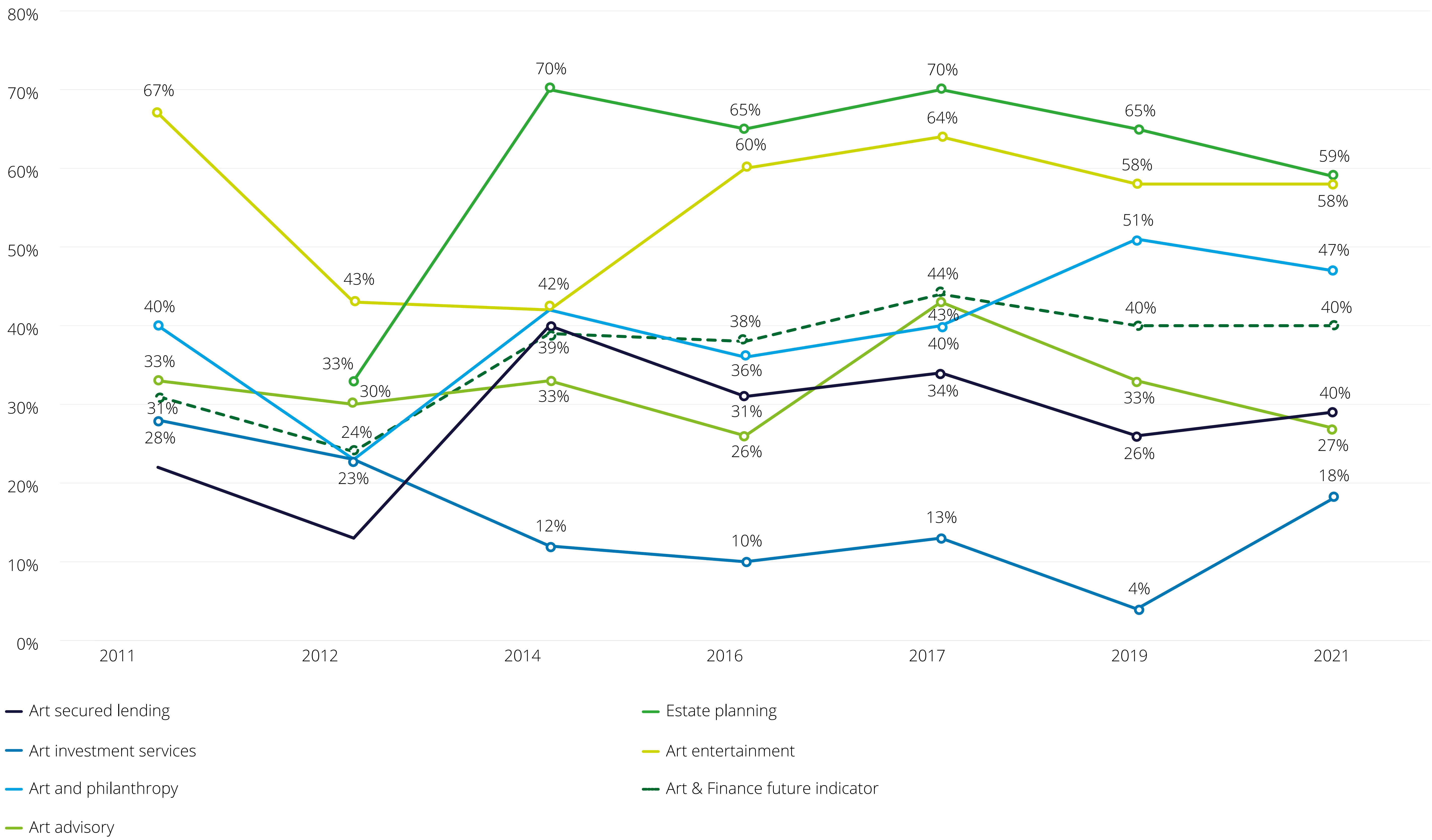
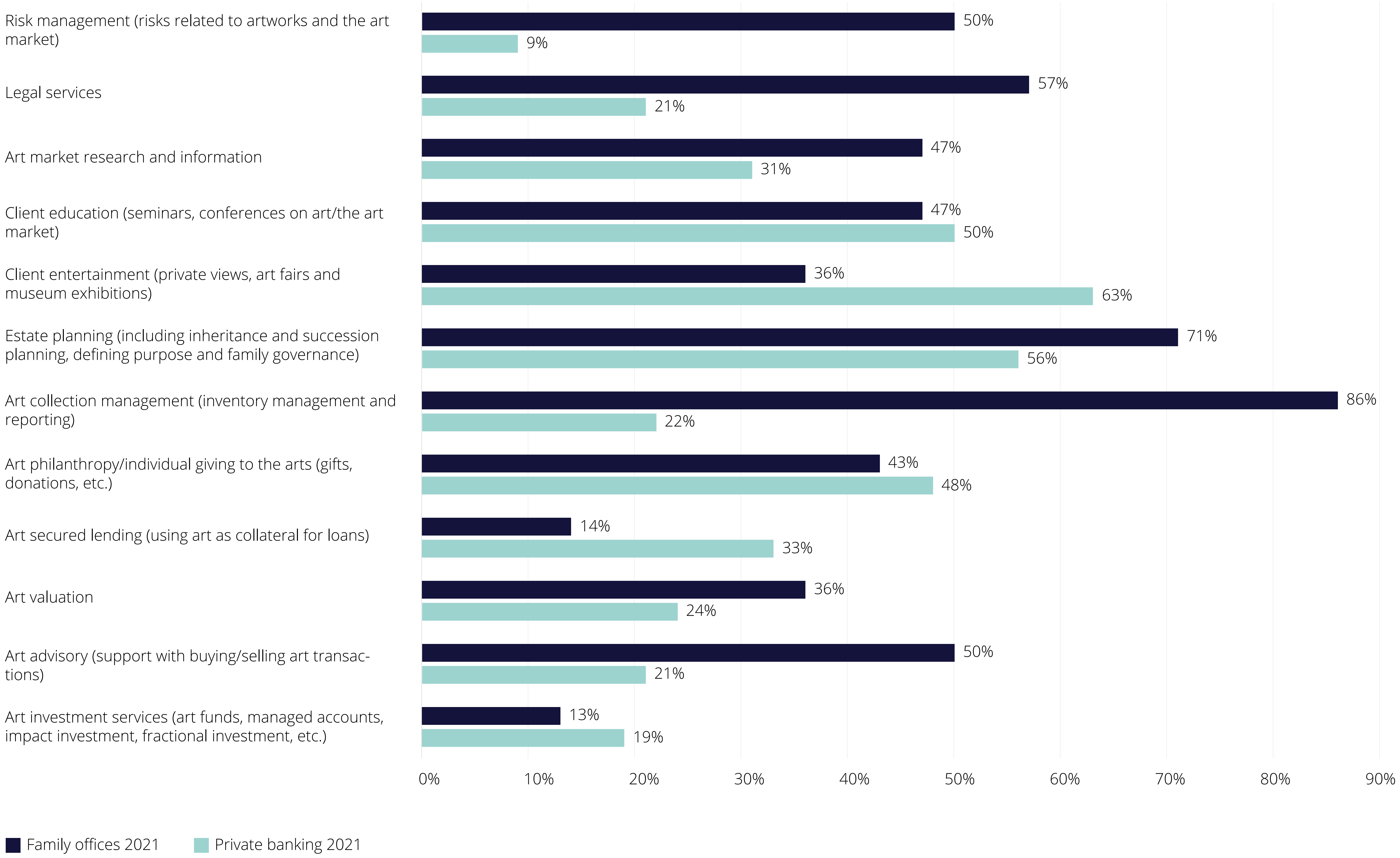


Figure 53. Private banks vs. family offices: which services will you focus on in the next 12 months?
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021



Private banks versus family offices[9]: which services will you focus on in the next 12 months?
There are distinct differences in the priorities and focus of private banks and family offices when it comes to art and wealth management[10].

Family offices are investing more in art-related services
In this year's survey, 64% of wealth managers, 61% of private banks and 75% of family offices said they offered art-related services as part of their service offering. This is compared with the 67% of wealth managers, 72% of private banks and 55% of family offices in 2019. It is interesting to note that family offices seem to have stepped up their efforts in servicing art-related wealth since our last survey in 2019, corresponding to the growing focus on art and collectibles as part of a holistic wealth management strategy.

9 The graph shows a breakdown of priorities based on two samples 1) private banks and 2) family offices. The results will be different from the aggregate category of wealth managers, which is a weighted average of both private banks and family offices
10 There are limitations in these interpretations due to the survey covering more banks than family offices and more US banks than US family offices

Family offices direct their focus on holistic service offerings around art wealth management

86% of family offices said that art collection management (inventory management and reporting) will be a high priority area in the short term, compared with only 22% of private banks. Regarding their investment priorities for the coming 12 months, 71% of family offices cited estate planning and 57% cited legal services related to art. Half of the family offices surveyed identified risk management, while only 9% of private banks saw this as a priority. Forty-seven percent of family offices said they will increase their focus on art market research and information, compared with 31% of private banks. This suggests that a closer alignment between art market research and data providers and the family offices industry could prove fruitful.

Private banks direct their attention to client engagement

Whilst family offices are bolstering their efforts around specific services aimed at managing collections or collectible wealth, private banks indicate they will concentrate their short-term efforts on client engagement. Of the private banks surveyed, 63% said that art entertainment (private views, exhibitions and art fairs) will be their focus over the coming months as the art world opens up. Half of private banks said they would also dedicate more efforts to client education, such as seminars and conferences related to issues in the art market. Estate planning (56%) and philanthropy (48%) also remain high on the agenda. One-third of private banks also expect to be more active in the art secured lending area, compared with only 14% of family offices.

Despite a holistic approach being one of the main drivers for including art as part of wealth management services, the offering remains traditional, with only a few private banks (22%) considering offering collection management and reporting services in the future. The question is, will this change with the development of new collection management platforms and the possibility of having security tokens backed by art objects, which we discuss further in Sections 6 & 7? Offering collection management and reporting services could allow wealth managers to be more proactive in their service offering and integrate the estimated US$1.4 trillion of wealth held in art and collectibles by UHNWIs in wealth management.

True Faith
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Eugénie Dumont
Art Collections Manager
Degroof Petercam

Expert voices

Broadening horizons and pursuing new revenues

Art advisory is no longer limited to the ultra-high net worth

In recent years, the art advisory field has grown within the banking sector in response to clients' desire to expand asset allocations beyond traditional portfolio management.

In light of the significant increase in value for a large number of post-War and contemporary artists, Art as an asset class has undoubtedly seduced a broader public in a more global market, with NextGen collectors setting the pace towards new trends.

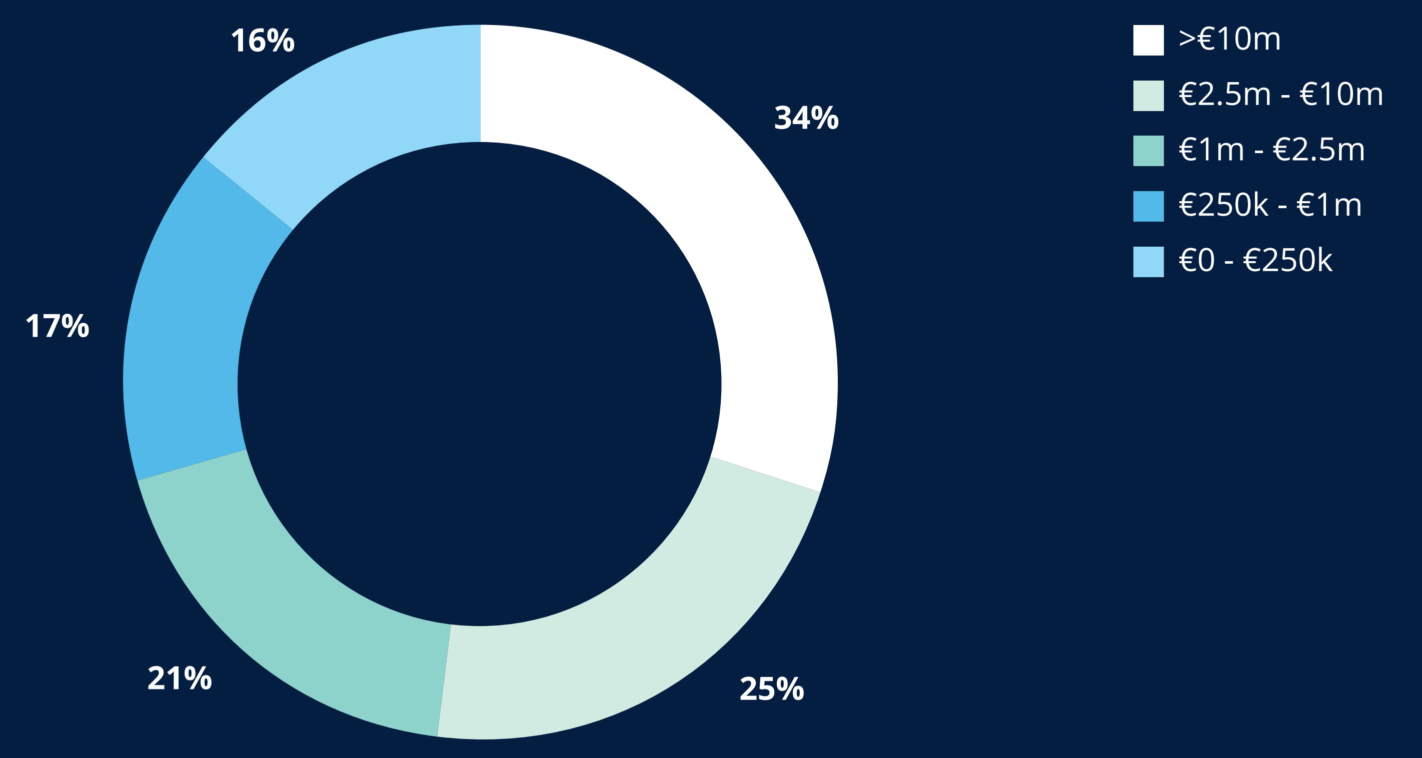
So, how have banks positioned themselves within the art advisory sector, and how are they adapting to the increasing demand from a wider target segment?

Art advisory is no longer limited to ultra-high net worth individuals

Art advisory and collection management services are usually targeted at ultra-high net worth individuals (UHNWI). This trend is based on the principle that UHNWI is more likely to own art and collectibles through inherited collections or diversify their wealth with the perspective of financial returns and tax incentives. They represent the segment with the strongest demand for such an offering, with a third of UHNWI clients showing interest in art-related services. However, there has been growing interest from other segments which have not traditionally stood out. In the past 12 months, almost half of art collection management requests originated from the mid-market segments, with a quarter of them expressing an interest in art.

Interestingly though, the requested services among the various segments differ significantly. UHNWI tends to request estate planning, inventory services, and appraisals services, in line with the likelihood of bigger existing collections and the upcoming transfer of wealth to the next generation. Conversely, the mid-market segments seek transaction advisory, with a keen interest in building

Figure 54. % interested in art



a collection and diversifying their wealth, targeting contemporary and emerging art. Their social aspirations translate into distinct motivating factors when acquiring art, focusing on cultural support and social impact rather than aesthetics and potential returns. Additionally, it is interesting to notice the ad-hoc nature of UHNWI requests compared to a long-term management approach sought after by the other segments. This permanence also aligns with the rise of more holistic wealth management, including art.

Many wealth management institutions offer internal estate planning capabilities combined with outsourced art-related services that are sufficient for ad-hoc requests. However, a client-centric approach requires a shift of focus to a more comprehensive understanding of the clients' needs and a more emotionally driven management of their wealth. It becomes increasingly relevant to build in-house expertise and reduce the third-party expert reliance to foster the next generation of wealthy individuals. Stirring away from the intermittent requests and aiming at long-term management of passion investments, it is time for wealth managers to consider deploying full-fledged advisory and collection management services. All with dedicated in-house expertise, as is already the case for other services supporting core management activities.

From indirect to direct revenues; a virtual win-win for art and wealth management

Wealthy individuals' interest in art usually begins with a need for a more personal relationship with their wealth manager, likely due to a rise in social and cultural awareness. They do not simply look at the return on investments any longer; they seek to align their wealth manager's values with their own. In that respect, client centricity has become a distinguishing factor against the competition.

Artistic and cultural corporate engagement usually comes as a steppingstone towards more established art advisory services. Our competitors have developed an art offering, starting with philanthropy, education, and entertainment through sponsorships and corporate collections. Larger institutions can then develop these further with appropriate collection management, advisory, and financing services.

Nonetheless, these activities rarely generate direct revenues unless in-house expertise includes additional services such as valuations, inventories, or financing, which require tremendous investments and resources to achieve.

The recent developments observed in tokenization and blockchain technology may bridge the gap for wealth managers. Partially solving the transparency and liquidity issues, the tokenization (or securitization) of either real or virtual artworks turns these from non-bankable to bankable assets. Former art funds can now find a more adapted and open-ended structure to be traded freely on the market. The increased liquidity that arises will also lower the risk level of this alternative asset class, encouraging activities such as art financing. Additionally, it will improve data availability and will better support traditional appraisals carried out by specialists thanks to the rise of artificial intelligence. This same concept can therefore allow wealth managers to address the needs of other segments that previously did not have access to these services. They can also incorporate these non-bankable assets into their client's portfolios, enabling new recurring management fees and, therefore, direct revenues.

Art related services development stages

Indirect Revenue → **Direct Revenue**

Artistic and Cultural Corporate Engagement				Art Advisory and Collection Management			
Sponsorship	Philanthropic	Corporate Collection	Exhibitions	Outsourced Advisory services	Insourced Advisory services	Art Financing	Securitization & Active Asset Management

Conclusion

Turning away from intermittent requests and aiming instead for long-term management of passion investments, it is now time for wealth managers to consider deploying of full-fledged advisory and collection management services. Dedicated in-house expertise will reinforce client centricity and address the needs of a broader target segment and the next generation of wealthy individuals. Banks and wealth managers can then leverage internal capabilities, blockchain technology, and tokenization to incorporate (so far) non-bankable assets, such as art and collectibles, in their portfolio management and generate new direct revenue streams.

Part 3. Collectors and art professionals—motivations and behavior

Survey findings 2021

Figure 55. Does your clients have significant art collections? (% saying yes)
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021

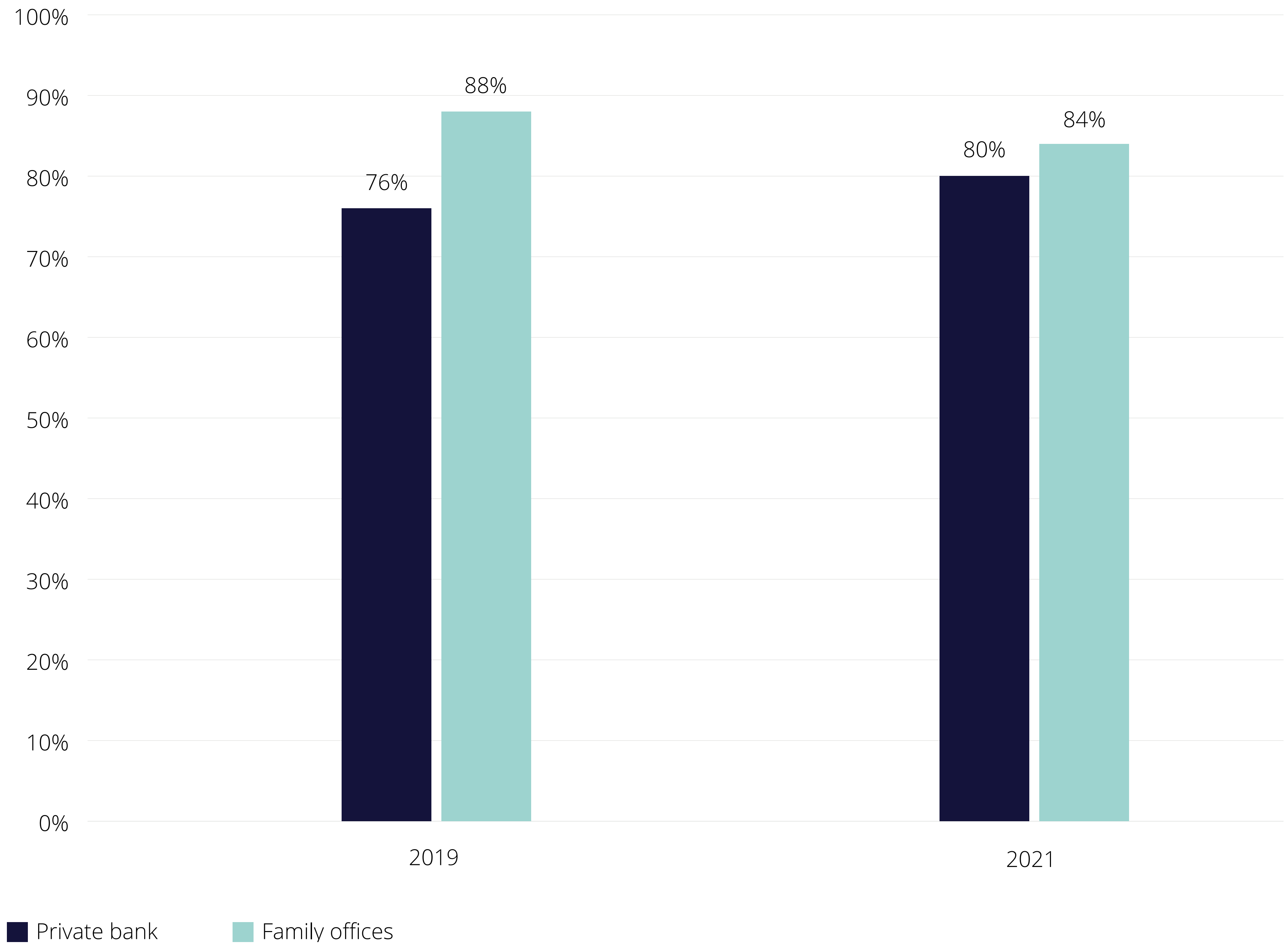
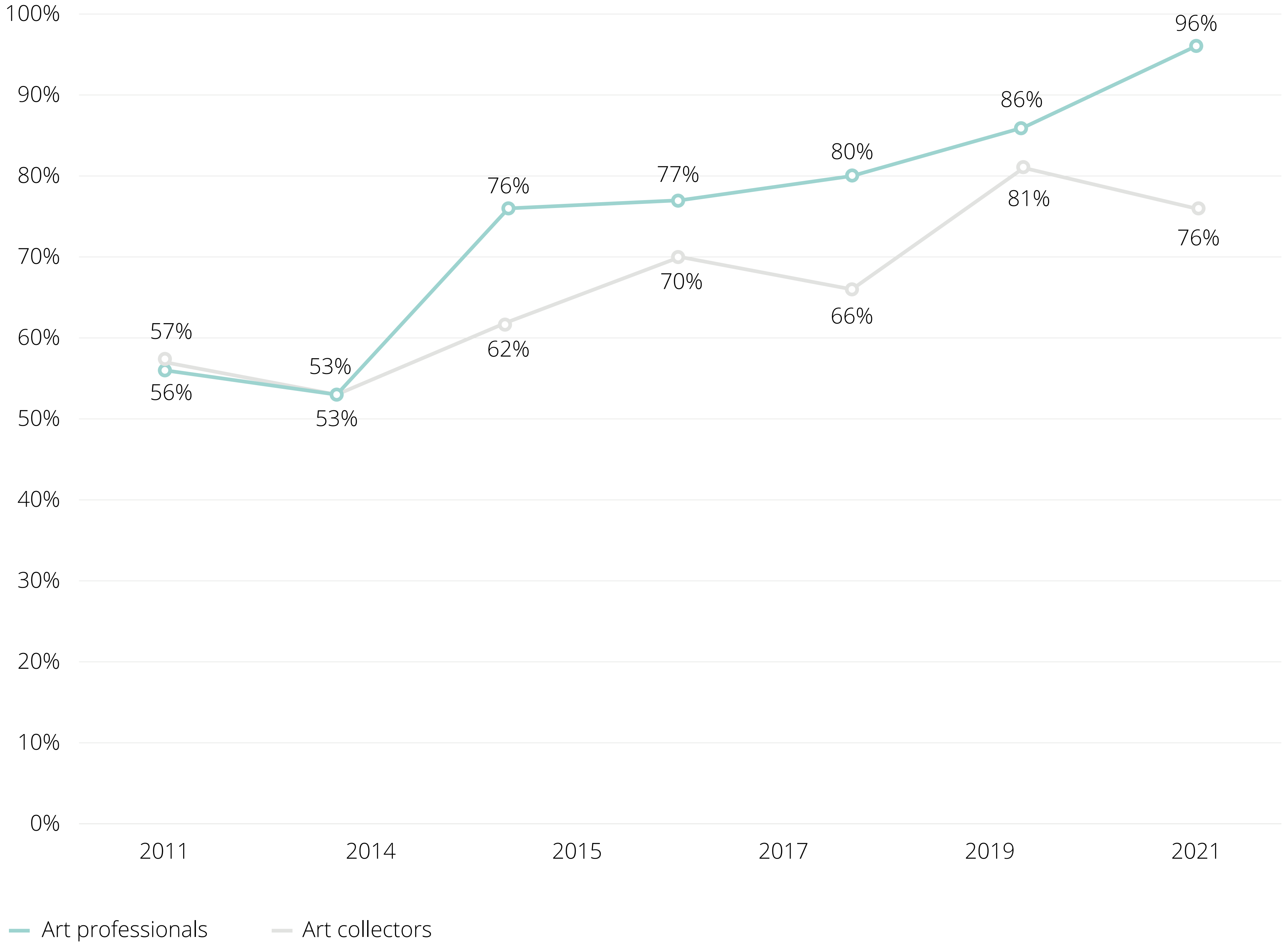


Figure 56. 10-Year Perspective: Do you think that art and collectible should be part of a wealth management offering?
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021



This year, 81% of wealth managers, 80% of private banks and 84% of family offices surveyed said they had—or believed they had—clients with significant art collections. These results are similar to 2019's findings.

The demand for art wealth management services has remained high among collectors and art professionals for many years. This year, 76% of collectors said they would like wealth managers to incorporate art and collectibles into their service offering, down from 81% in 2019. It is clear that most collectors see art and collectibles as assets that should be part of an overall wealth management service offering, and that wealth managers need to respond to this demand. It is positive to see that, this year, the wealth management industry seems to have risen to this challenge. There is an overall increase across all art-related services offered by wealth managers, evidence of the growing focus and dedication being paid to this emerging asset class.

It is also interesting to note that 96% of art professionals said they believe art should be part of a wealth management offering, up from 86% in 2019. This signals art professionals' strong desire to build closer relationships with the wealth management industry. However, 69% of wealth managers said the art industry needs to modernize its business practices. This signals there is significant room for improvement among art professionals to ensure they meet the expectations of the wealth management industry.

Collector motivations:

Figure 57. Emotion vs Investment: Why do your buy art? (art collectors)
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021

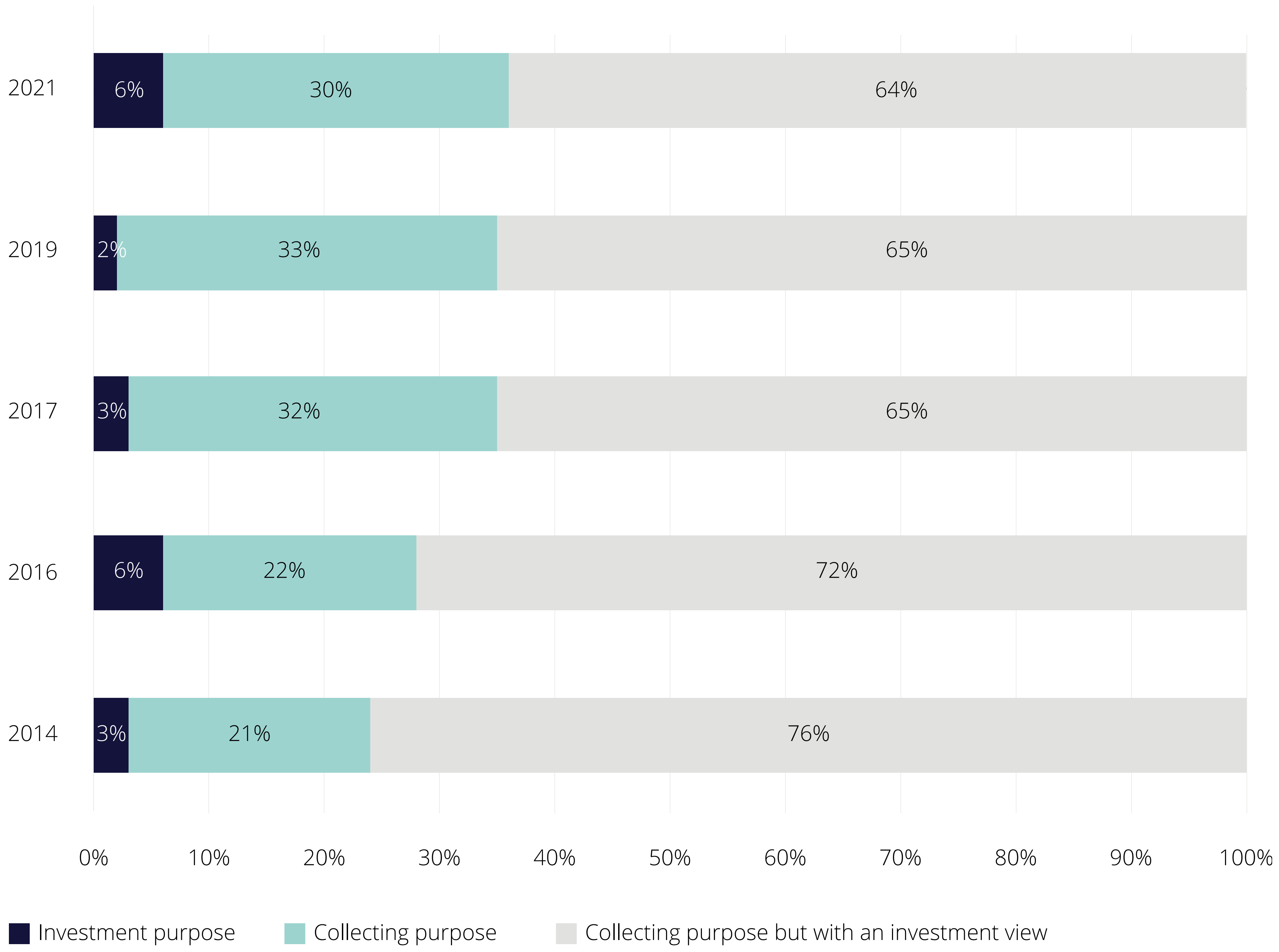
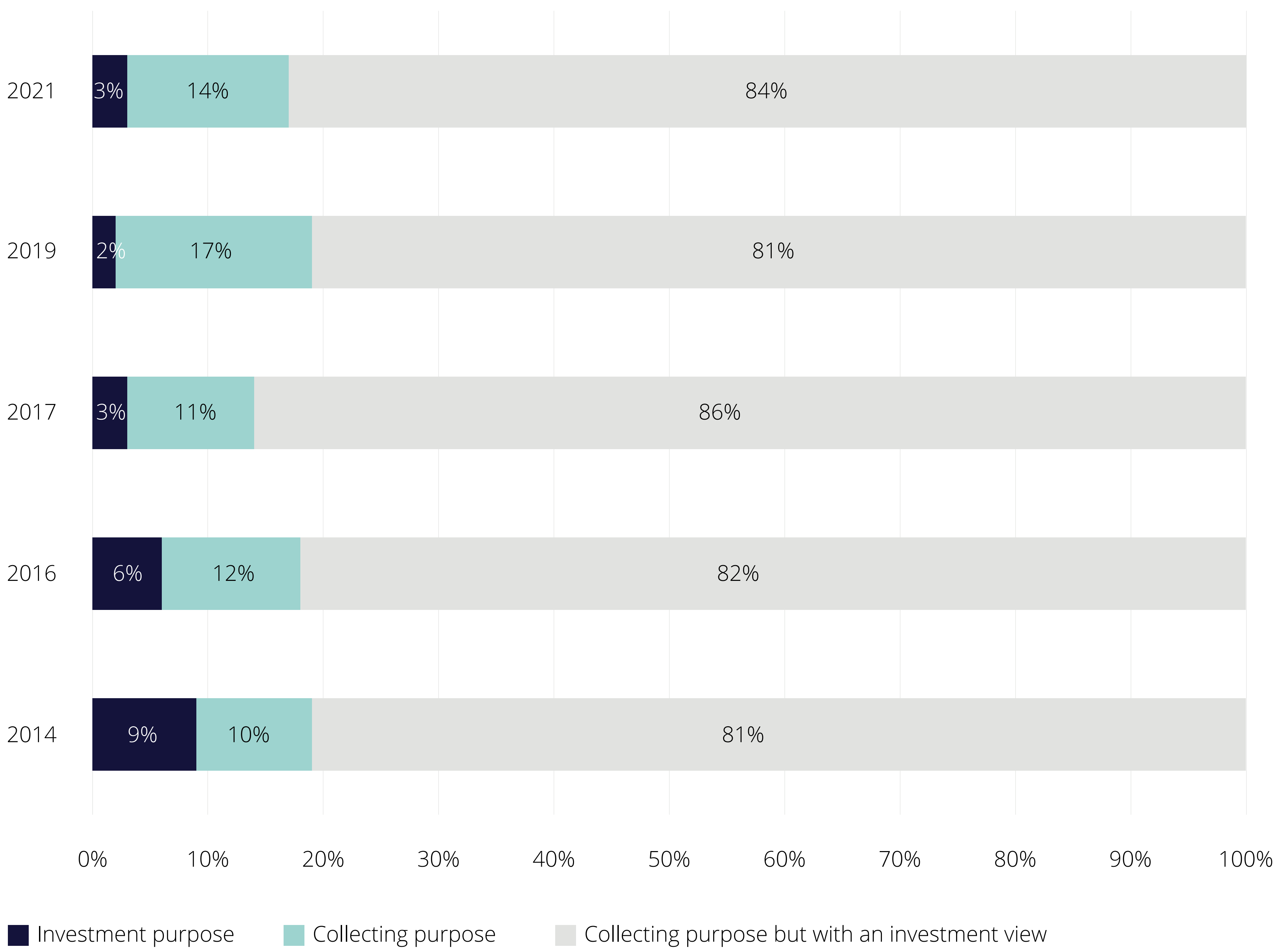


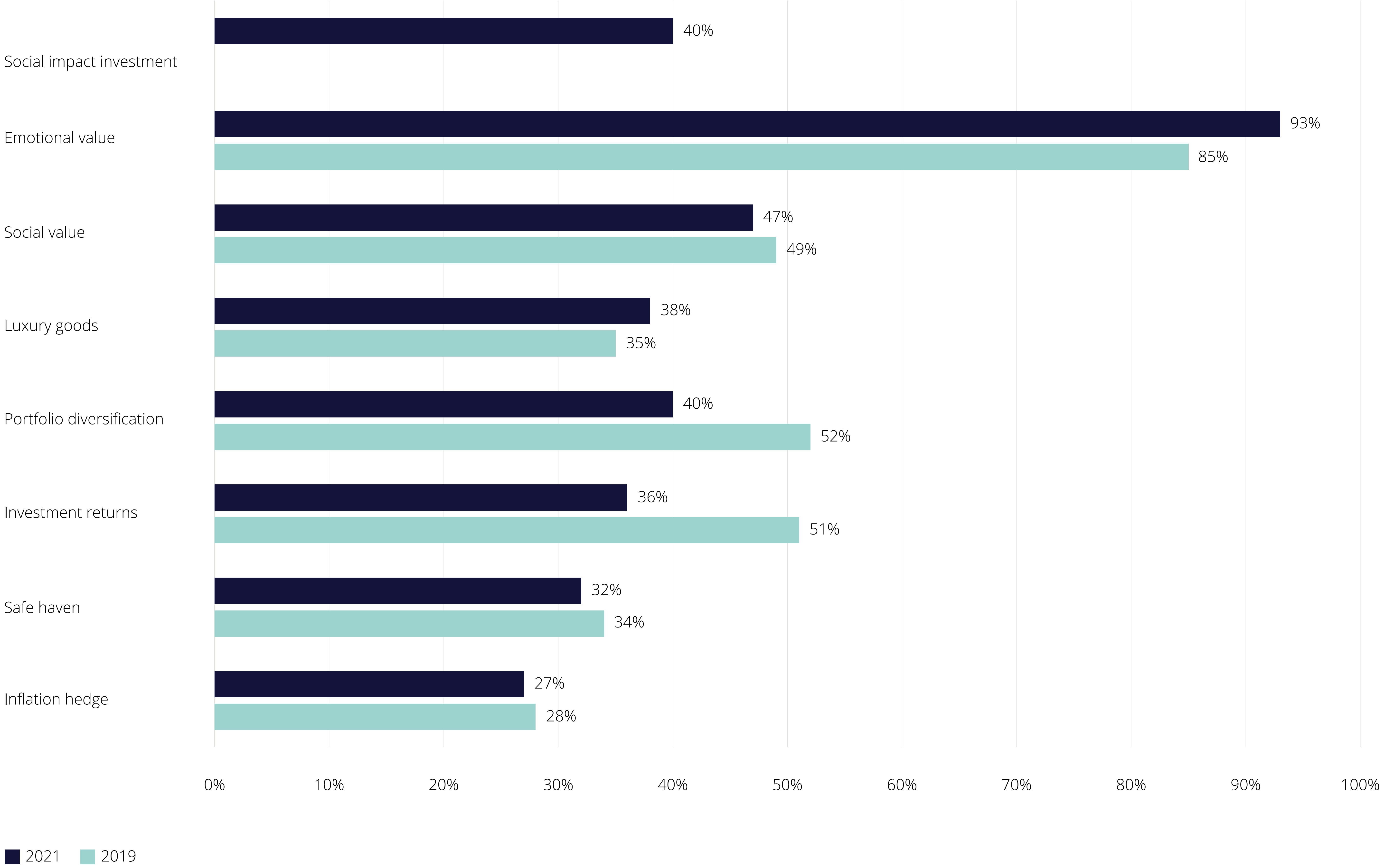
Figure 58. Emotion vs Investment: Why do your buy art? (art professionals)
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021



Passion versus investment

64% of collectors said they bought art to collect but also with a view to invest, while 30% said they bought art as a pure passion, similar to our previous report findings. When asking what is the main reason for buying art, 86% of art professionals said they believe their clients buy art for passion and also to invest, while only 14% believe collectors buy purely for passion. Only 6% of art professionals believe their clients buy art solely for investment purposes, corresponding to only 6% of collectors who said they buy art for investment. Although only very few collectors classify themselves as investors, it is worth noting the seemingly growing demand for art investment services among non-collectors of art, which is evident in the market's fractional ownership of art and the growing interest in NFTs and tokenization this year (see Section 6 for more information around art investment trends). These new trends could soon trigger a new set of wealth management services around alternative forms of art investment, as 33% of wealth managers said they are interested in fractional ownership and 28% said they would be looking at NFTs in this year's survey (see figure 99 on p. 239).

Figure 59. Collectors: Which of the following motivations are most important in buying art?
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021



Emotional value of art ownership takes center stage
This year, 93% of collectors said they buy art primarily for emotional reasons, compared with 85% in 2019.

Social value is important in a post-COVID-19 world
47% of collectors said the social value associated with art ownership was an important motivation, compared with 49% in 2019. After a year of social restrictions, canceled art fairs and art exhibitions, collectors around the world are longing to re-engage with the global art scene. While it may take a different shape than in the past, the social aspect of owning art and the feeling of being part of a global community continues to play a key role. This year, wealth managers said they would focus more on art entertainment as social restrictions are lifted, and this is likely to play an important role in re-engaging with their client base this year.

Investment returns, store of value and portfolio diversification
Although the financial aspects of art ownership are secondary, there is clear evidence that investment returns, diversification, and art as a store of value still carry significant importance. Of the collectors surveyed, 36% said they bought art for investment returns (down from 51% in 2019), 40% said they saw art as an asset diversification tool (compared with 52% in 2019) and 32% said they considered art a "safe haven" or a store of value (compared with 34% in 2019). With the prospect of higher inflation on the horizon, 27% of collectors see art as an inflation hedge, compared with 28% in 2019. Recent findings from the Art Basel and UBS art market report 2021[11] show that most collectors rated financial motivations for collecting as important, a higher percentage this year compared with previous years. Using art to diversify wealth portfolios was ranked as the highest financial motivation among collectors, with financial motivations (such as investment) regarded as important among three-quarters or more of millennial collectors. Our survey shows similar trends, with 64% of collectors under 35 years old saying that investment returns and portfolio diversification were key motivations for buying art, compared with 30% of collectors over 35 years old.

Social impact investment
This year we added a new motivation to our survey, focusing on social impact investment as a key driver for buying and investing in art. Overall, 40% of collectors said this was one of their primary motivations, rising to 86% for collectors under the age of 35. This could signal that investors are looking beyond financial returns when buying or investing in art, and are increasingly looking at the social impact that these investments can generate. This new finding supports the need to explore the development of social impact investment products for the art and cultural sector. (See Section 4 in this report.)

> ...investors are looking beyond financial returns when buying or investing in art, and are increasingly looking at the social impact that these investments can generate.

Magic Mint Tetris
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11 Art Basel & UBS Report, 'The Art Market 2021', p.320-321

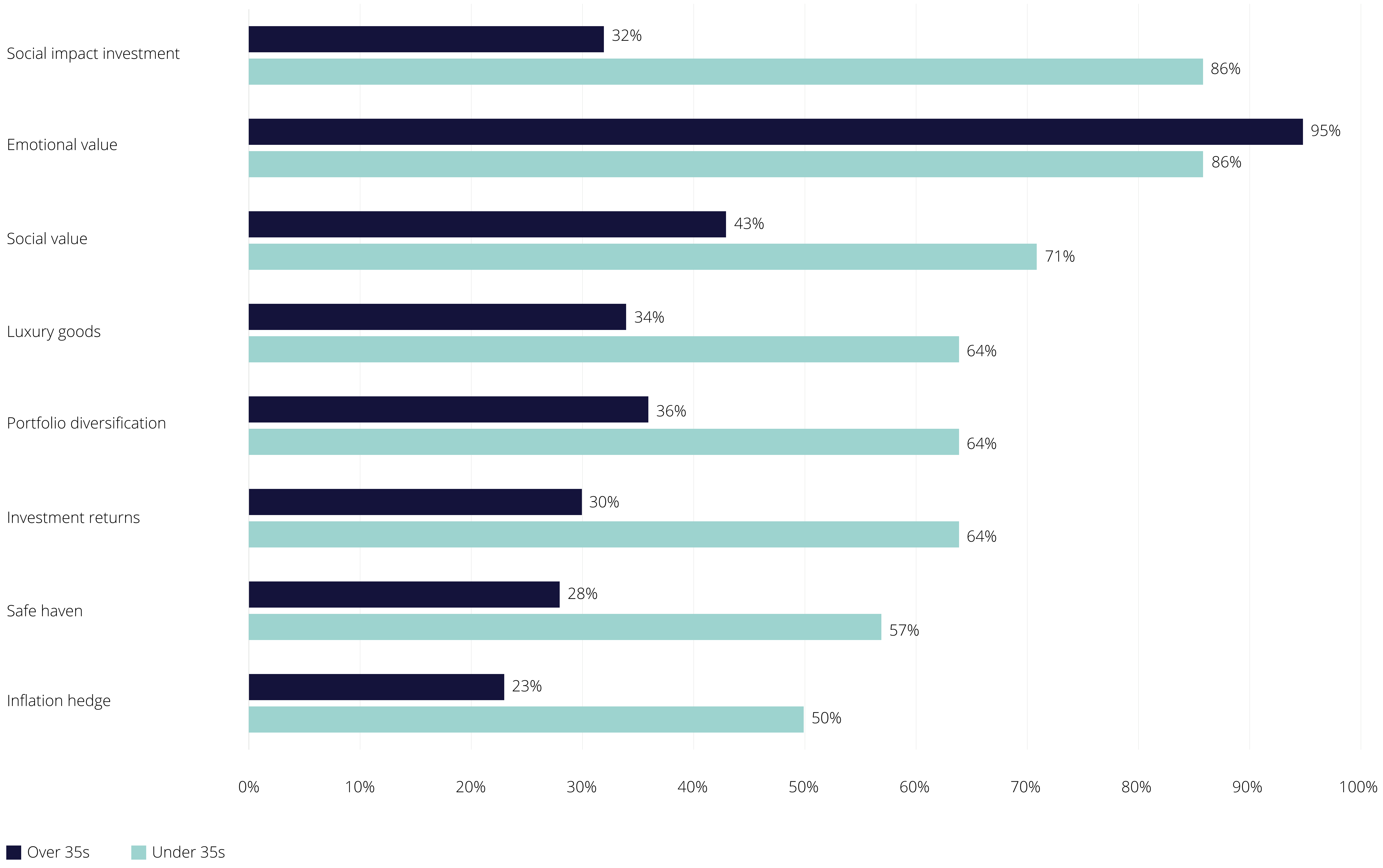
NextGen collectors—a different perspective[12]

In this edition, we decided to start tracking the motivations of NextGen collectors aged 35 and under compared with older collectors. It is important for wealth managers to better understand NextGen collectors and their motivations to differentiate and tailor their value proposition to younger demographics.

Please note that our analysis at this stage relies on a smaller number of younger collectors and should be interpreted as indicative. We have supported our findings with external research where relevant.

Motivations

Figure 60. NextGen: What are the most important motivations when buying art?
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021



12 See also NextGen collectors—a different perspective in Sections 6 and 7, p.221 and p.252.

Millennial buyers are increasingly viewing art through a prism of social and investment values.

Pintura Louis XIII
©Unidade Infinita Projectos - 2017

Young art collectors see art as a natural part of a wealth management service offering, as more of their overall wealth is invested in art

93% of collectors under 35 years old said wealth managers should incorporate art and collectibles in their service offering, compared with 74% of collectors aged above 35 years. This suggests that a future generation of wealth management clients have a strong desire to see art integrated into wealth management offerings. The vast majority (85%) of collectors under 35 said art accounted for a larger part of their overall wealth, and that the increasing value of art triggered the need for wealth management services to protect, enhance and leverage the value of art. These findings resonate with results published in the latest UBS and Art Basel Art Market Report 2021[13], which found that some collectors had a relatively high proportion of their overall portfolios of wealth invested in art—61% reported an allocation of over 10%, with wealth measured by including real estate and private business assets. A few collectors (28%) also reported that over 30% of their wealth portfolio was accounted for by their art collections, with younger collectors tending to have a higher share allocated. Thirty percent of millennial collectors had more than 30% of their wealth held in art, which was double the level of some of their older counterparts such as baby boomers. The report cites lifecycle factors and the build-up of other assets over time as potential reasons for this difference, but overall it shows art's significant position in some young collectors' wealth portfolios.

Social impact and purpose-led investment ranks on par with the emotional value of buying art

Purpose-led and social impact investment is the highest-ranked motivation among younger buyers, with 86% compared with 32% of older collectors. This motivation among younger collectors, which goes beyond purely personal consumption and enjoyment, is reflected in other studies of millennial and younger generations. The Hiscox Online Art Trade Report 2020[14] found that social impact and patronage was ranked as the second-highest motivation for buying art (behind passion and emotional value), with 76% of millennial collectors agreeing. This implies that millennial buyers are increasingly viewing art through a prism of social and investment values.

Younger collectors are driven by a stronger emphasis on the financial aspect of art ownership

There are signs that younger collectors are more motivated by financial considerations around art ownership compared with older art collectors. Almost two-thirds (64%) of collectors under 35 years old said financial investment returns are a key motivation, compared with 30% of collectors over 35 years old. Sixty-four percent saw portfolio diversification as a key component of art ownership, compared with 36% of older collectors, and 57% saw art investment as a safe haven in times of uncertainty, whilst only 28% of older collectors said the same. Half of younger collectors also viewed art as an inflation hedge, compared with 23% of older collectors. These findings resonate with a recent study by Artsy, which found that investment was a higher driver among NextGen collectors—58% said it was one of their top reasons for collecting.[15]

13 Art Basel & UBS Report, 'The Art Market 2021', p.290
14 Source: Hiscox Online Art Trade Report 2020, p.9
15 Source: Artsy - Art Collecting 2021, p.33

Art & Wealth Protection, Estate Planning and Philanthropy

03

Coeur De Paris
©Joséphine Brueder/Ville de Paris - 2018

Highlights

Global wealth transfer
The world is on the cusp of an unprecedented transfer of wealth. Over the next decade, it is estimated that US$15 trillion[1] of wealth will be transferred to millennials and Generation Z. Aside from the wealth planning implications, this substantial shift also raises important questions around art-related wealth and the next generation of art owners' tastes and priorities.

Art-related wealth requires stewardship
The preservation of artwork through wealth planning transcends tax and legal considerations. Collectors frequently rely on trustees for a broad range of stewardship services, including the professional handling of collections, procuring insurance, and arranging storage and security.

Strong demand for research and information
This year, 84% of collectors identified art market research and information as the most relevant art wealth management service, up from 71% in 2019. This trend particularly resonated with the vast majority (92%) of younger collectors. This signals a strong appetite for research that is validated and supported by private banks and family offices. Through collaboration with data providers, software developers and market researchers, wealth managers can seize this opportunity to develop a new range of art-related services around research and information, especially for younger demographics.

Collection management and wealth reporting
A significant majority (62%) of collectors cited collection management services as the second most relevant service that wealth managers could offer, compared with 57% in 2019. This indicates a strong desire by collectors for their trusted advisors to consider art and collectibles as an asset class in its own right. The majority of collectors and wealth managers believe that art and other collectibles should be part of wealth reporting. Collection management and reporting can also help wealth managers gain a better understanding and visibility of their clients' art-related wealth, allowing them to proactively create a broader and holistic client engagement.

Technology and new collection management tools
Digital transformation and the rise of the online art market have catalyzed the transformation of existing practices around art collection management. We will likely see further collaboration and partnerships between technology platforms and the wealth management industry going forward.

Estate planning and art collections
This year, only 43% of wealth managers said their clients' estate plans sufficiently addressed their art collection (a steep decline compared with 67% in 2019). Regarding family offices, 67% said their clients had sufficiently addressed their art collection in their estate plans. However, only 37% of private banks said the same, suggesting that wealth managers' knowledge about their clients' art-related wealth remains low among private banks. This presents an opportunity for banks to proactively identify and initiate discussions with their clients regarding their art collections.

Sr. Vinho
©Ana Isabel Miguel - 2010

1 Source: IQ-E, 'The Great Global Wealth Transfer', July 2020. Whitepaper. P.2

It is worth noting that the younger collectors surveyed placed more importance on art and philanthropy services.

Long-term estate planning around art is in its infancy

Very few (12%) of the collectors surveyed said they had formalized their estate documents with their estate planning advisors. A further 51% said they were considering this but had not yet started the process. With a significant wealth transfer expected between generations over the coming decade, wealth managers need to engage with their clients on this subject.

Lack of dialogue with heirs

Of the collectors who plan to leave their collection to their family, only 31% had specifically discussed the artworks they will bequeath and provided the means to care for the art. While 57% of collectors said they had not yet discussed this with their heirs but intend to do so. Few (11%) said they had not discussed it and would leave this to their spouse or executor to deal with. These findings suggest a need for more engagement and dialogue around estate planning, while underscoring the importance of implementing a proper family governance structure around art-related wealth to ensure a smooth transition between generations.

Art and philanthropy

Of the collectors surveyed, 42% said the most relevant service that wealth managers could offer was regarding art and philanthropy, compared with 65% in 2019. This sharp drop may be due to the pandemic triggering a desire to support more "urgent" philanthropic needs such as health, poverty, inequality and education, relegating culture as a secondary priority in the current environment. However, it is worth noting that the younger collectors surveyed placed more importance on art and philanthropy services, with 69% saying this was the most relevant service that a wealth manager could offer. This suggests that cultural institutions need to rethink their reliance on traditional donations and individual-giving strategies and move towards a more purpose-led and impact-oriented giving and investment strategy, particularly as they become reliant on younger demographics.

Cactus
©Unidade Infinita Projectos - 2002

Introduction

With an estimated USD1.48 trillion of ultra-high net worth individuals' (UHNWIs) wealth in art and collectibles (see Section 1), the protection and management of art-related wealth have grown in importance in recent years, while the demand for art-related wealth management services has also risen across all generations of clients. In this section, we look specifically at services related to collection management and trends emerging around art and estate planning and philanthropy.

this section is divided in 2 parts

Part 1: Art and wealth protection

Part 2: Art and estate planning and philanthropy

We are delighted to feature a series of global

expert contributions providing insights into new

developments and trends, such as:

1. **Art within wealth—a retrospective and look ahead**
2. **New Humanism and Art Insurance—how digitization shifts the focus of art insurance towards customers and their quality of life**
3. **The art and science of managing collectibles and luxury assets—key considerations for family offices**
4. **Philanthropy and the arts: what role can contemporary wealth management play?**
5. **A Token Gesture: can Philanthropy Benefit from the Growth of Blockchain Technology?**
6. **Philanthropy & Art – An Introduction to Income and Estate Tax Implications**

To provide context on this important topic, Suzanne Gyorgy and Dominic Picarda at Citi Private Bank share both a historical and forward-looking view of the role and importance of art and wealth management services during the lifecycle of an art collection.

Sr. Vinho
Ana Isabel Miguel - 2010

Suzanne Gyorgy
Managing Director and Head of Art Advisory and Finance
Citi Private Bank

Dominic Picarda
CFA, Head of Content Strategy
Citi Private Bank

Expert voices

Art within wealth

A retrospective and look ahead

Throughout history, many of the world's wealthiest individuals and families have collected great works of art. They have done so primarily for reasons of pleasure. Identifying, acquiring, and then displaying artworks can create enormous personal satisfaction. Likewise, shared passion for art among collectors from around the world also creates new friendships and ties that transcend geographies.

For over forty years, Citi Private Bank has advised wealthy individuals and families about their art collections. As the market has evolved through the concept of lending against artworks, we have continued to play an active role in the art finance sector. From this vantage point, we examine the needs of today's art collecting clients and consider potential developments for the future.

Advisory services then and now

While collecting art can bring various rewards—emotional and otherwise—it also poses challenges. This is true both for experienced and potential collectors. For aspiring collectors, knowing where to begin is far from easy. Without a carefully defined vision and an acquisition strategy to implement it, suboptimal outcomes are highly likely. Even for seasoned collectors, the task of staying abreast of developments and opportunities can be daunting.

As true as that is today, it was even more so a generation or two ago. In the pre-digital age, intelligence about art fairs and auctions was readily available only to the initiated. Wealthy collectors and would-be collectors based in countries outside the then much smaller international art circuit were at a particular disadvantage. It was in response to such challenges that Citi became the first financial institution to establish its art advisory service in 1979, offering wealthy individuals and families art expertise they could not readily obtain elsewhere. The founding art specialists helped inform prospective collectors about the world they wished to enter. They analyzed the state of the market and the latest trends, highlighting acquisition opportunities for seasoned collectors and newcomers alike. As well as insights, they provided access, connecting clients to auctions, galleries, and their peers.

Much has changed since the late '70s. The world of art has undergone a great opening up. However, challenges around access and advice persist, albeit in rather different ways. A dearth of information has become a deluge. Not only have art fairs proliferated, but can often now be accessed virtually from anywhere. The art advisors of today are thus no longer a source of scarce information in a closed environment—instead, they help make sense of constant activity across a vast landscape.

Of course, the advice that collectors require has always gone beyond market trends. In relation to specific acquisitions and sales, they also seek guidance upon authenticity, condition, provenance, and pricing. And whereas Citi's original advisory service had a small group of two in-house art specialists, its latter-day incarnation has various experts with specialisms including Modern and Contemporary art, Latin American art, Chinese ceramics and antiquities, and 19th century and Impressionist art.

The growth of art finance

As early clients began to amass collections of art, a further opportunity emerged. Collectors wanted to be able to raise cash by borrowing against these valuable assets, just as they could already do with their real estate and financial holdings. Strong growth in art prices in the late 1970s and for much of the 1980s reinforced the appeal of this.

Against the backdrop of today's thriving art lending market, it is easy to forget how radical an innovation art finance was. At that time, discussing art and finance together was considered distasteful in art circles. But while discretion was paramount, at least one famous example of an early art loan remains widely known.

The iconic artists Christo and Jeanne-Claude were best known for their spectacular, but temporary public exhibitions, such as a giant curtain hung between two mountains. While these installations were free for everyone, the costs of the creative process were enormous. The artists helped to meet them by selling their smaller works, but often found themselves selling hurriedly at large discounts to raise cash in the final stages of each public project.

While art lending was and remains a service for collectors, Citi agreed to arrange a line of credit for Christo and Jeanne-Claude. The facility was secured against the artists' collection of their own works. During each project, they were therefore able to draw down on their credit line and then service it by selling off works later on, at favorable times of their choosing.

Today, art finance is an established source of liquidity for many collectors worldwide. Collectors can seek liquidity from their holdings of internationally marketable paintings, sculptures, drawings, and photographs of high quality and value. They typically use the funds raised to acquire further artworks, make financial investments, or for many other purposes.

Wealth planning

For many wealthy individuals, their art collections represent a significant element of their wealth. As such, they need to consider not only how to develop their collections, but also how to structure their ownership. By having a robust wealth plan, collectors can help protect their treasured assets during their lifetimes and beyond. Appropriate structuring can enable artwork to be passed efficiently to beneficiaries, without going through probate or having to be sold to meet estate taxes.

However, the preservation of artwork via wealth planning extends beyond tax and legal considerations. Collectors frequently rely on trustees to help provide stewardship more generally. This includes such things as the professional handling of a collection, procuring insurance, and arranging storage and security.

Philanthropy in art

Collecting art is often a means for wealthy individuals and families to give back to society and perpetuate their legacies. They typically do so by lending or indeed gifting their artworks for the appreciation of the public. Such philanthropic generosity can in turn promote understanding of the cultural heritage associated with the art.

While the motivations for and benefits of donating art are straightforward enough, the process involved is often less so. In the US, for example, collectors are sometimes surprised by the related rules. IRS regulations around art donations vary according to whether the donor is also the artwork's creator, whether the donation is made to a private nonoperating foundation, and whether a nonprofit's use of the artwork relates to its charitable mission.

Likewise, donations can encounter unexpected hurdles with recipients. For example, many major museums may not wish to accept an individual piece of a collection, unless it fills a gap in their permanent collection. They may also be less inclined to accept a proposed gift of an entire collection and so perhaps less notable art institutions may have more flexibility and space when it comes to receiving donations of artwork.

Potential donors therefore need to prepare carefully. Donations are best planned in consultation with a collector's legal counsel, tax professionals, and art advisors. This group of experts can be helpful in negotiating and documenting the transaction to ensure there are clear, enforceable terms. But while the regulations vary and compliance can be onerous, a gift of artwork can be priceless for many nonprofits.

However, the preservation of artwork via wealth planning extends beyond tax and legal considerations. Collectors frequently rely on trustees to help provide stewardship more generally.

The future

The world is in the early stages of an unprecedented transfer of wealth. Over the next two decades or so, tens of trillions of dollars of wealth is set to pass from the baby boomer generation to their successors. Aside from the wealth planning implications, this substantial shift also raises important questions about the tastes and priorities of the next generation of art owners.

Few assets are more personal than art collections. Tastes between generations very often differ, which is partly reflected in the demand for various genres over time. The heirs of collectors typically share their parents' passion for art, but have their own distinct preferences.

We observe various potentially significant shifts in relation to the next generation of art collectors. They are much likelier to seek inspiration about trends and possible acquisitions from social networks. They are also more disposed to purchase artworks—even high value pieces—via digital means. The latter trend has been accelerated by the pandemic, during which leading auction houses held successful online sales.

In the same way, tomorrow's collectors seem likelier to engage with digital artworks. Many of the next generation have grown up using digital technologies and are especially open to innovations such as cryptocurrencies, blockchain, and non-fungible tokens (NFTs). The role of art advisor to wealthy individuals and families thus looks set to encompass pixels and a Smart Contract Address as well as paintings, sculpture, drawings, and photographs.

Part 1. Art and wealth protection

Collection management is an all-embracing term for the different aspects of art and collectibles caretaking. A good collection management strategy is the foundation of a quality collection, ensuring its cultural, historic and financial value is preserved. It involves practical aspects such as art advisory services related to buying and selling, valuation, legal matters, insurance, conservation, exhibition loans and shipping and storage. But it also increasingly requires wealth management services around ownership structures, tax planning, legacy and estate planning, as well as philanthropy.

A recent study by Marsh[2] found that, since 2008, the number of families and individuals collecting art as an investment has grown. As values have increased significantly over time, so has the importance of preserving the value of art and other collectibles by ensuring the appropriate security, climate control, and maintenance—such as conservation and restoration—as well as insurance against theft and damage.

Although collection management is nothing new, we have seen significant technological developments in recent years, boosting efficiency while streamlining and integrating fragmented services in one place. This has helped usher the many analog aspects of the art market into the 21st century. Digitalization and the rise of the online art market have catalyzed the transformation of existing practices around art collection management.

Technology-driven collection management tools, including Lobus, Artory, Arternal, ArtLogic, ArtBase, Arteia, ArtBinder, amongst others, are paving the way for collectors and art professionals to store and share data more transparently and efficiently, maximize efficiency, and leverage this data to polish their operations. This is essential for the modernization of the art market, which 69% of wealth managers said was necessary to align the art and collectibles world closer to the wealth management industry.

We will likely see further collaboration and partnerships between technology platforms and the wealth management industry going forward. Of the collectors surveyed, 79% said they wish to have their art-related wealth incorporated in existing wealth reporting, providing them with a holistic view of their overall wealth. Wealth managers are keenly aware of this client demand, with 73% saying their clients expected them to provide this service this year (compared with 67% in 2019).

We have already begun to see consolidations and partnerships between art professionals and technology platforms, combining different services or expanding their offering to become an integrated service provider. Examples of this trend include Artory and the Winston Art Group; Artory and Tagsmart; artnet AG and Artfacts.net; Arte Generali and Wondeur.ai; Crozier Fine Arts and Arius Technology; Art Rights and FERCAM Fine Art, amongst others. These developments could help forge a closer relationship between art professionals and the wealth management community.

In the following article p.130, Giovanni Liverani, CEO of Generali Deutschland, shares his views of how technology is transforming Arte Generali's role of protecting their clients' art assets, from the payment of claims to protection, prevention, assistance, and partnership with clients.

Related to the topic of Art and wealth protection, see also articles in section 8 pg 308 **Mitigating bankruptcy risk to artwork consignments in the United States**, Megan Noh, Partner - Co-chair, Art Law, PRYORCASHMAN LLP and pg 311 **Collection management platforms: legal issues concerning the digitalization of art collections and the use of new technologies**, Ida Palombella, Partner; Federica Caretta, Director, Valentina Favero, Manager, Deloitte Italy.

A good collection management strategy is the foundation of a quality collection, ensuring its cultural, historic and financial value is preserved.

Gateway
©Image by Allan Pollok-Morris_Courtesy Jupiter Artland - 2019

2 Marsh, Family office Benchmarking Study 2021 p.17

Giovanni Liverani
CEO, Generali Deutschland AG
Group Management Committee, Assicurazioni Generali SpA
Global sponsor, ARTE Generali

Expert voices

New humanism and art insurance

How digitization shifts the focus of insurance in general, and art insurance in particular, towards human beings and their quality of life

When we hear about new technologies revolutionizing old industries, we tend to think of car manufacturers and travel agencies. But insurance is also affected by this revolution. In fact, there has never been such a powerful shock to the insurance industry. This shock certainly presents its challenges, but simultaneously it opens up promising avenues for a better customer experience. Using the examples of Generali Deutschland—the company I lead—and of art insurance—one of the insurance segments showing the highest potential—I would like to walk you through this true "Copernican Leap".

All industries are undergoing transformation due to digitization and connectivity: the COVID-19 pandemic accelerated this process dramatically. A recent study[3] revealed that the number of remote workers in the US will increase by 87% compared with pre-pandemic levels.

The insurance business is no exception. Due to the implementation of new technologies, insurance is experiencing a paradigm shift, as it transitions from a mere service that reimburses claims, to an all-encompassing one that protects, prevents, assists, and partners-up with customers.

A few examples here could be useful. At Generali Deutschland, we pioneered a scheme whereby term-life and health insurance subscribers get rewarded for adopting healthier lifestyles, that we track even by using new technologies. As members accomplish certain goals, we offer them benefits in the form of, for example, coupons for online purchases and/or discounts on the premium paid. We also launched an app that, thanks to AI, allows users to self-monitor their most important vital signs, such as blood oxygen saturation and their heart rate, through nothing else but their smartphone's camera. We are also testing a robot that reduces the risk of accidental falls by training vulnerable people, such as the elderly.

This transformation affects art insurance too.

To understand how, we should simplify and distinguish art buyers into two main categories: those who buy art for its emotional value and those who do it for its investment potential.

When art is an emotional purchase, it has a profound meaning for the owner, who is ready to put extra effort in protecting, enjoying, and sharing an artwork. The reimbursement of claims is therefore the core—but not sole—element of a comprehensive solution that offers all the services in which an art lover is truly interested, such as qualified advice and consultancy before the purchase, safety measures, transportation, restoration, and storage.

3 Business Wire, "Upwork Study Finds 22% of American Workforce Will Be Remote by 2025," December 15, 2020.

Clearly, even in art insurance, reimbursing claims is no longer enough. Be it for the love of art or for investing, art owners demand services that go beyond a swift and fair payment. The sorts of innovation that have emerged in recent years allow us to meet this demand effectively and efficiently.

When art is mostly an investment, the owner wants to protect and also maximize its value. In this case, art is an asset class and the approach to owning it is akin to asset management. Here again, insurance—according to its traditional definition—is the core, but not sole component of a solution that protects the value of the asset from adverse circumstances and contributes to boost it, for instance by providing the collector with useful and granular data on the performance of a specific artist.

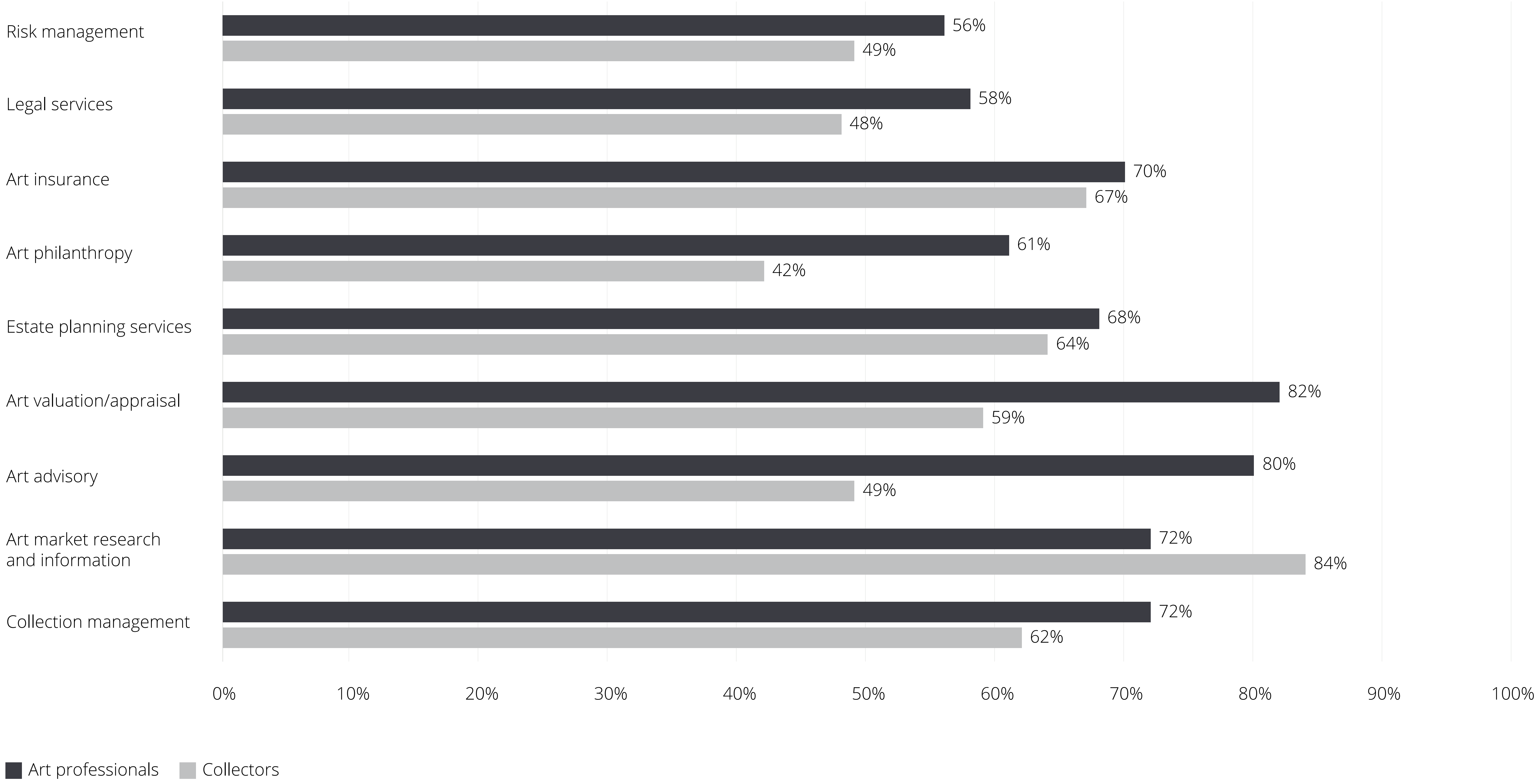
Clearly, even in art insurance, reimbursing claims is no longer enough. Be it for the love of art or for investing, art owners demand services that go beyond a swift and fair payment. The sorts of innovation that have emerged in recent years allow us to meet this demand effectively and efficiently. ARTE Generali, the business unit we launched at the end of 2019, has developed the technology and the digital ecosystem to meet the needs of all art owners, to make their life easier, and to contribute to the much-needed evolution of the fine art insurance segment.

Broadly speaking, by adopting digitization and connectivity, insurers are now able to do things that were unthinkable just a few decades ago. These include making extremely precise risk assessments, ensuring round-the-clock and remote assistance to clients, and personalizing solutions on the basis of a client's lifestyle. Something spectacular is happening in insurance: for the first time ever, the client and his or her life quality are truly at the center of our business model, ushering in what I can only describe as a "new humanism in insurance".

- Insurance is experiencing a paradigm shift fueled by new technologies;
- Payment of claims is no longer enough, as clients demand protection, prevention, assistance, and partnership;
- Art insurance is no exception. Whether the client is an art lover or an art investor, art insurance requires a holistic approach; and
- This new approach puts the human being and his or her life quality at the center of the insurance business model, ushering in a "new humanism in insurance".

Survey findings 2021: collectors and art professionals

Figure 61. Art & Wealth Protection: Which of the art wealth management services most relevant?
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021



30 Anos do 25 de Abril
©Unidade Infinita Projectos - 2004

Figure 62. Collectors: Which of the art wealth management services most relevant to you?
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021

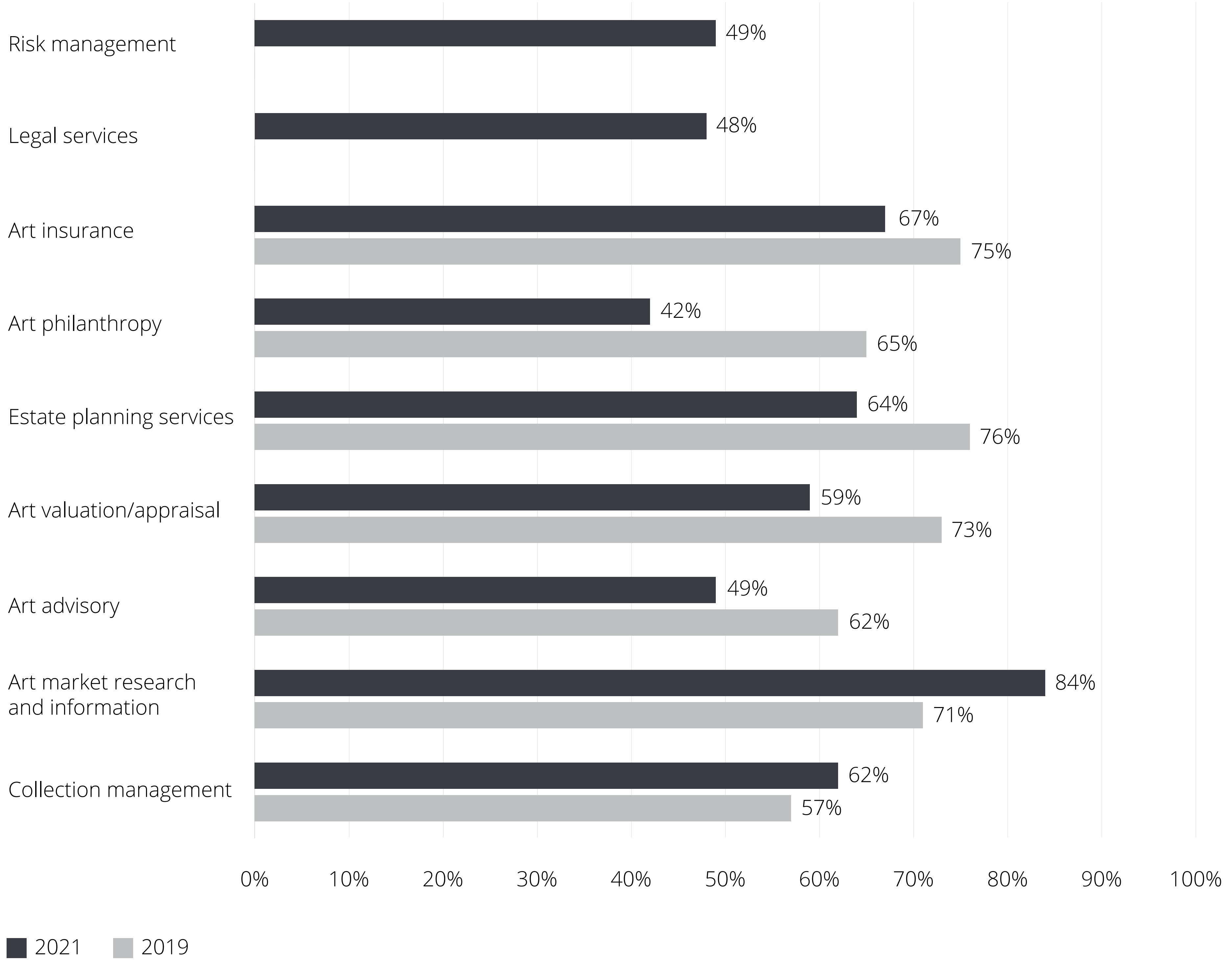
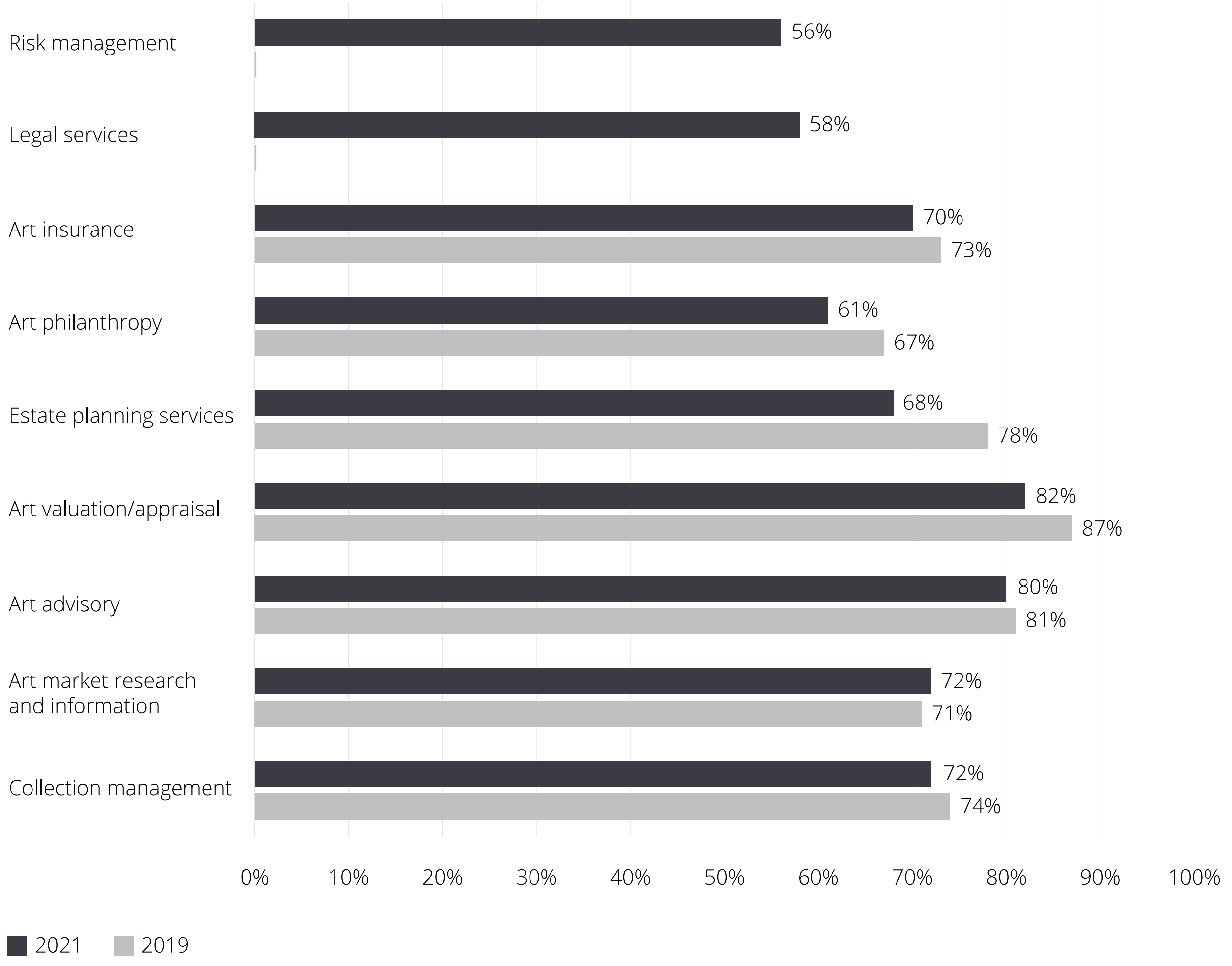


Figure 63. Art professionals: Which of the art wealth management services most relevant?
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021



Coeur de Paris
Joséphine Brueder/Ville de Paris - 2018

Research and information

84% of collectors identified art market research and information as their most relevant art wealth management service, up from 71% in 2019. Most (72%) of art professionals also said this was the most relevant service to their clients, compared with 71% in 2019. This could indicate a keen demand for research that is validated and supported by private banks or family offices, likely due to collectors' lack of trust in art market data—73% expressed a moderate to a low level of trust. By collaborating with data providers, software developers and market researchers, wealth managers could develop the market for art-related research and information. There are opportunities for data providers to develop appropriate services for the wealth management sector, with 76% of wealth managers with an existing art-related offering saying they provided art research-related services to their clients.

Collection management and wealth reporting

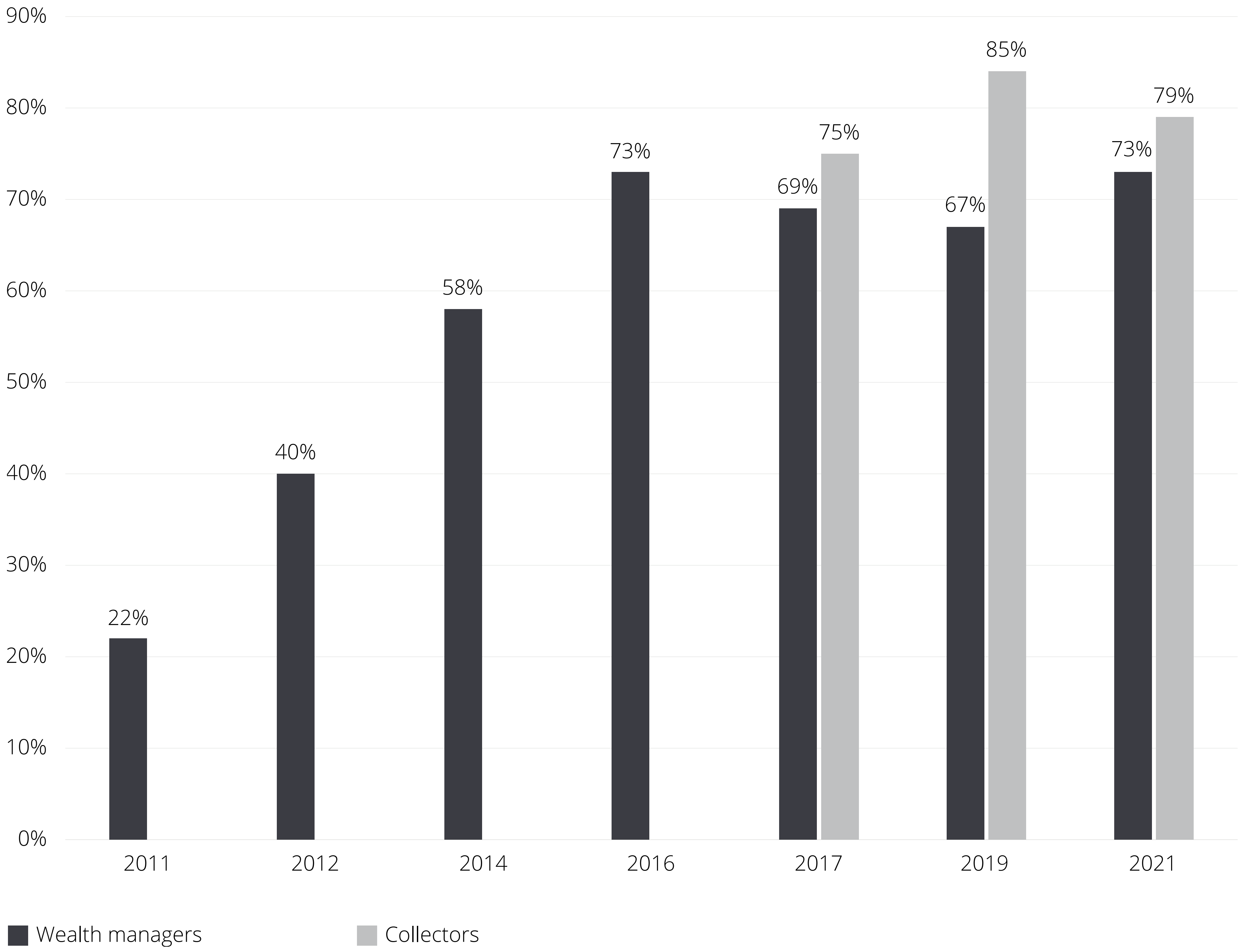
62% of collectors indicated that collection management was the second most relevant service that wealth managers could offer, compared with 57% in 2019, and 72% of art professionals said the same, compared with 74% in 2019. The majority of collectors and wealth managers believe that art and other collectibles should be part of wealth reporting to provide a consolidated view of clients' wealth and have a better view of their overall exposure. Of the collectors surveyed, 79% said they are interested in this service compared with 84% in 2019, and 73% of wealth managers said their clients expected them to provide this service, compared with 67% in 2019. These findings indicate that collectors are eager for their trusted advisors to consider art and collectibles as an asset class in its own right. The increasing interest in collection management services among wealth managers is also a testimony to this emerging trend; however, it is still to be put into practice.

Collection management and reporting can help wealth managers gain a better understanding and visibility of their clients' art-related wealth, allowing them to proactively create a broader and holistic client engagement.

In the article on p.257, Deloitte UK shares insights into how wealth managers can create a professional and transparent framework around the management of art and collectibles. This involves inventory management, facilitating discussions between family members to set strategic objectives, assessing risks based on these objectives, and implementing plans to mitigate these risks.

Figure 64. Wealth Managers & Collectors: Should art and other collectible assets be consolidated into overall client wealth reporting? (% of colletors saying yes, and % of wealth managers who said their clients expect them to)

Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021



Art valuation

59% of collectors believe that art valuation would be a relevant service for wealth managers to offer, compared with 73% in 2019. However, this belief was significantly higher among art professionals, where 82% said this was the most important service for their clients, compared with 87% in 2019. Of the wealth managers with an existing art and collectibles offering, 82% said they provided services around art valuation, up from 67% in 2019. Most (84%) wealth managers said this service was provided by external, third-party providers, demonstrating once again the increasing engagement between the wealth management industry and art market professionals.

Art advisory

This year, 49% of collectors feel that art advisory would be a relevant service for wealth managers to offer, compared with 62% in 2019. This was significantly higher among art professionals, where 80% believed this was the most important service for their clients, compared with 81% in 2019. Of the wealth managers with an existing art-related offering, 78% said they provided art advisory services to their clients, compared with 69% in 2019, and 27% said this is an area they would further develop over the coming 12 months.

Art insurance

67% of collectors said that art insurance-related services are the most relevant that wealth managers can offer, compared with 75% in 2019, and 70% of art professionals agreed, compared with 73% in 2019.

Legal services

48% of collectors said legal art-related services are the most relevant that wealth managers can offer, with 58% of art professionals saying the same. Of the wealth managers with an existing art-related offering, 71% said they provided their clients with legal advice and assistance.

Risk management

49% of collectors said that risk management would be the most relevant service that wealth managers could offer, with 56% of art professionals saying the same. 64% of wealth managers with an existing art-related offering said they provided services around risk management and art.

Pop Galo
Luís Vasconcelos/Courtesy Unidade Infinita Projectos - 2016

NextGen collectors—a different perspective

Market research and information remain key for millennial collectors

92% of younger collectors (under 35 years old) said art market information and research was the most relevant service that wealth managers could offer, compared with 82% of older collectors. This corresponds with 92% of younger collectors saying education was an important service, compared with 58% of older collectors. This suggests that younger collectors could be looking to wealth managers for guidance and support in their collecting endeavors.

Strong demand for collection management and advisory services among younger collectors

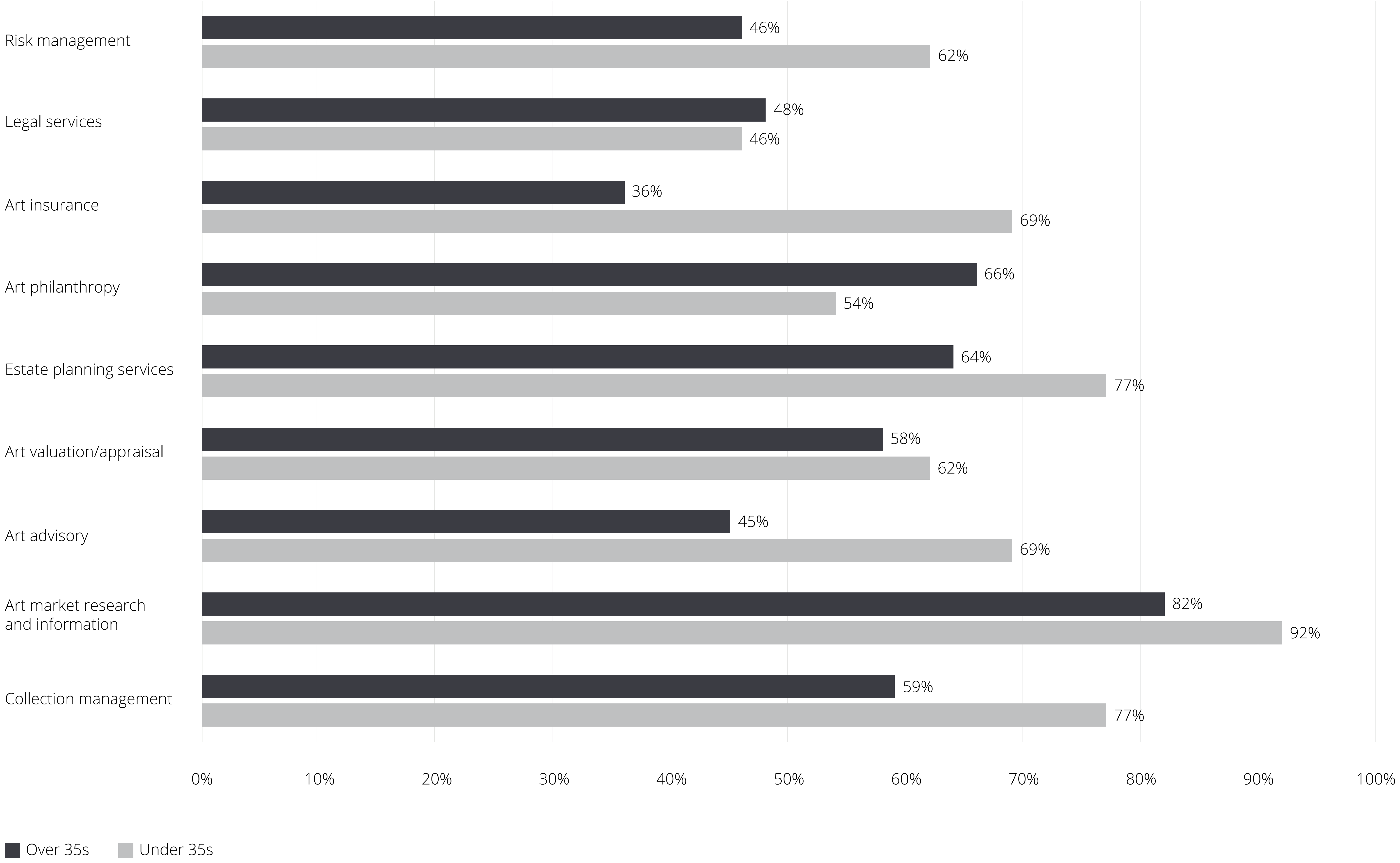
77% of younger collectors said that art collection management services were highly relevant to them, compared with 59% of older collectors, followed by 69% of younger collectors who said art advisory services were important, compared with 45% of older collectors.

Risk management services deemed more important for younger collectors

Continuing the trend of younger collectors demonstrating a stronger financial motivation behind the ownership of art, 62% said that art risk management services should be part of a wealth management service offering, compared with 46% of older collectors.

Figure 65. NextGen: Which of the art wealth management services most relevant to you?

Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021



Jutta Tornivaara
Director
Deloitte UK

Expert voices

The art and science of managing collectibles and luxury assets

Key considerations for family offices

Managing an art collection professionally is an exceptionally complex task. From dealing with the challenges of a less than transparent market such as establishing and assessing provenance, verifying authenticity and performing an accurate valuation, to arranging appropriate storage and transportation, insurance and ongoing care – specialist knowledge is required at every step.

For family offices, managing an art collection comes with additional challenges and idiosyncrasies that are very different to a professional investor, gallery or museum. Some family art collections are exceptionally vast and complex. They often grew organically over a number of years and multiple generations representing a crucial part of the family legacy with respective emotional value attached to them.

Some family offices are also responsible for managing a portfolio of other high value assets such as jewelry, fine wine, and classic or rare cars. These assets are often kept in family residences across various jurisdictions, including private yachts, and move between them regularly.

This can present challenges for family offices, particularly those that are leaner in their operations. Often within a family office, a small group of in-house employees alongside third-party specialists are responsible for all aspects of private asset management which can lead to key-man risk and sometimes blurred reporting lines. Limited real-time information about the assets managed, multiple systems to update and often a lack of guidance from the family about their objectives with respect to these assets are day-to-day realities for some family offices.

In this article we draw upon our experience of working with a range of family offices across multiple geographies and provide some key considerations for those seeking to professionalize how they hold and manage art or other investments of passion made by the families they serve.

Key considerations for family offices

Create and maintain a single source of truth
A critical first step towards professionalizing the management of collectibles and luxury items is to conduct a stock-take and create a comprehensive single catalogue of all relevant assets (or update an existing one). The asset catalogue should include all relevant details to support not only day-to-day management but also strategic decision-making and planning for life events (e.g. succession, trust distributions, tax filings). Typically, the inventory should include the following as a minimum:

- Type of object
- Creator or originator
- Name or title
- Inventory identification number
- Purchase price and date
- Most recent valuation and date
- Location
- Condition
- Legal owner (e.g. family member, relevant company or trust)

Assigning a unique asset identification number to each object is key to avoiding duplication and makes it easier to identify and monitor assets as they move between locations.

A process should also be established to review and update the catalogue on an ongoing basis. It is generally preferred that the central catalogue should be updated by a dedicated employee on the basis of periodic reports (usually monthly) from a responsible team member at each location. If the assets are kept in multiple locations, the reporting procedures should be consistent across all of them when the assets are bought, sold or otherwise leave the location. Robust processes should be established to track assets at all times (particularly high-value items) with clear responsibilities assigned to specific members of the family office team. The asset catalogue and tracking procedures should also include the items in off-site storage and safety deposit vaults. Depending on the complexity of the family office and the portfolio of assets, the catalogue can be maintained simply in spreadsheets, with a potential overlay of analytics to assist in reporting. Alternatively, IT systems could be utilized to mitigate risks of version control issues and enforce segregation of duties in the preparation and review of the catalogue.

Assigning a unique asset identification number to each object is key to avoiding duplication and makes it easier to identify and monitor assets as they move between locations.

The family office should consider performing a regular stock-take and have procedures in place outlining how it should be performed e.g. market value threshold for the assets to be included, the properties and rooms (or parts of properties) which are included or excluded from the stock-take. More frequent checks may be advisable with respect to high-value assets.

Family offices are increasingly using independent third parties to perform an "audit" of their physical assets, especially for high-value items and where the assets are spread across a large number of locations.

Set direction of travel
One of the most important reasons why families set up family offices is protection of their assets. And nowhere is this more pertinent than with respect to the family's cherished art and other private assets which they often want to preserve for future generations. However, neither protection nor day-to-day administration of such assets can be done efficiently without clear direction of travel set by the family.

The family should define the vision for the key parts of their collection and private assets as well as strategic and near-term objectives. Whether the goal is to sell-down, gift to a gallery or a charity, open a private museum or continue to grow the collection; the family office team requires clarity from the family to be able to serve them in a risk-controlled and efficient way. Other issues for the family to think through include:

- deciding on an appropriate ownership structure;
- analyzing cashflow requirements of their private assets (e.g. new acquisitions and ongoing costs) and what these would mean for the family's other shared assets and, if relevant, for the family members' personal funds;
- agreeing on the family members' rights and obligations related to the enjoyment these assets and
- how strategic decisions with respect to them will be made.

Alignment between family members on these critical points is essential as persistent unresolved family conflicts could jeopardize even the most comprehensive plans. Building alignment can be challenging as the family grows through generations, and it is only natural that each new generation would want to bring their own vision and perspectives to the table. The families that create and preserve multi-generational art and other collections share many similarities in terms of how they make decisions and maintain alignment which include:

- making an effort to have an open and constructive dialogue;
- allowing the upcoming family leaders to set their own objectives while being guided by the vision defined by the preceding generation;
- focusing on consensus and shared family values;
- maintaining a learning mindset with the view to enhancing the collection and finding innovative ways to govern and manage it through the years.

Perform a risk assessment
Maintaining a risk register is considered the gold standard of corporate governance and many family offices are adopting it with respect to the operating businesses and investments they manage for the family as well as the risks faced by family members. In our experience, due to the complex and sensitive nature of some of the collectibles and luxury items, including assets into the family office's risk assessment could be beneficial.

A risk assessment for such assets would typically involve analyzing, evaluating and reporting on misappropriation of and damage to assets, insurance, reputation risk, fraud and other financial crime, tax and legal risks. It is key to maintain an up-to-date and comprehensive inventory of all relevant assets for the risk assessment exercise to be meaningful. The strategy set by the family will inform the analysis of relevant risks and mitigation plans.

Manage third party risks
Family offices often rely on a large number of third parties in the management of art, collectibles and other luxury assets. These may include galleries, auction houses, brokers, valuation specialists, insurance providers, maintenance, security and transportation specialists; all of which introduce risk into the family office and its operations. Despite such relationships often being formed on a recommendation and lasting for many years, family offices should perform suitable due diligence, and put in place an ongoing monitoring program.

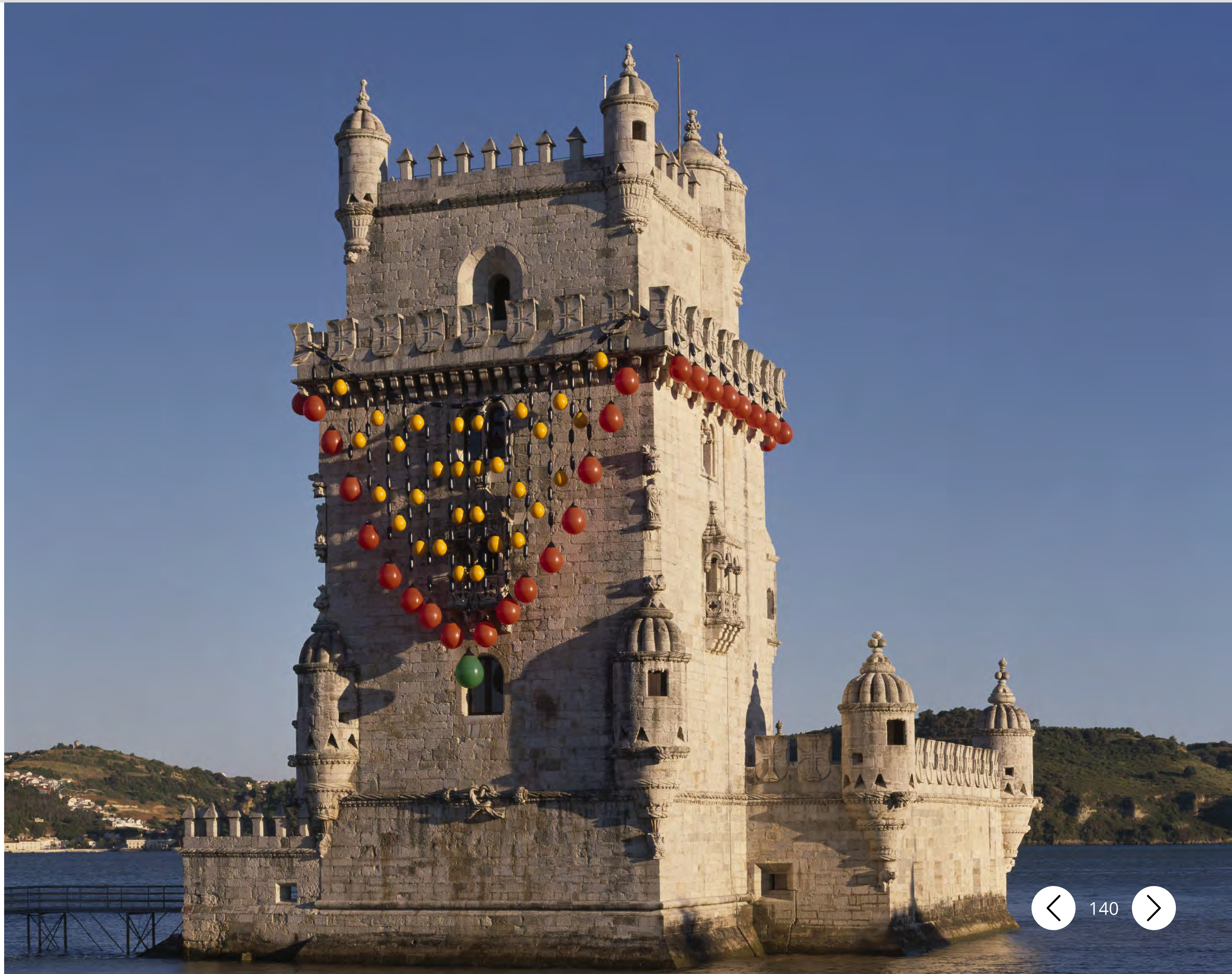
Key issues to watch out for may include reputation of third party organizations (background checks on key employees are advisable), resilience and crisis management protocols in place (e.g. what actions they will take to prevent internal fraud or if they are subject to a cyber-attack), and conflicts of interest. The family office should identify a preferred suppliers list for each service they use and cascade it down to the relevant property / locations' managers.

In the still opaque market of art, collectibles and luxury items, the challenges faced by family offices that manage these assets are vast and often complex. But adopting a strategic and structured approach can help position the family office as an effective guardian of some of the family's most treasured assets.

If you are a family office seeking to professionalize the management of collectibles and luxury assets, following the following three simple steps provide a good starting point:

1. Create or update a single and comprehensive inventory of the family's collectibles and luxury assets;
2. Facilitate on-going discussion between family members to define the vision for the collection and to set and evaluate strategic objectives; and
3. On an ongoing basis, assess risks based on the agreed strategic objectives and put plans in place to mitigate those – including all key service providers in this assessment.

The strategy set by the family will inform the analysis of relevant risks and mitigation plans.



Part 2. Art and estate planning and philanthropy

Introduction

While every industry has undergone dramatic changes over the past 18 months, the wealth sector has witnessed a major shift in generational wealth transfer. The threat of the COVID-19 pandemic has forced older generations to speed up their plans to transfer their wealth to younger generations. According to a recent article in Campden FB[4], the top priorities for UHNW families will be the protection and preservation of wealth, both for current and future generations.

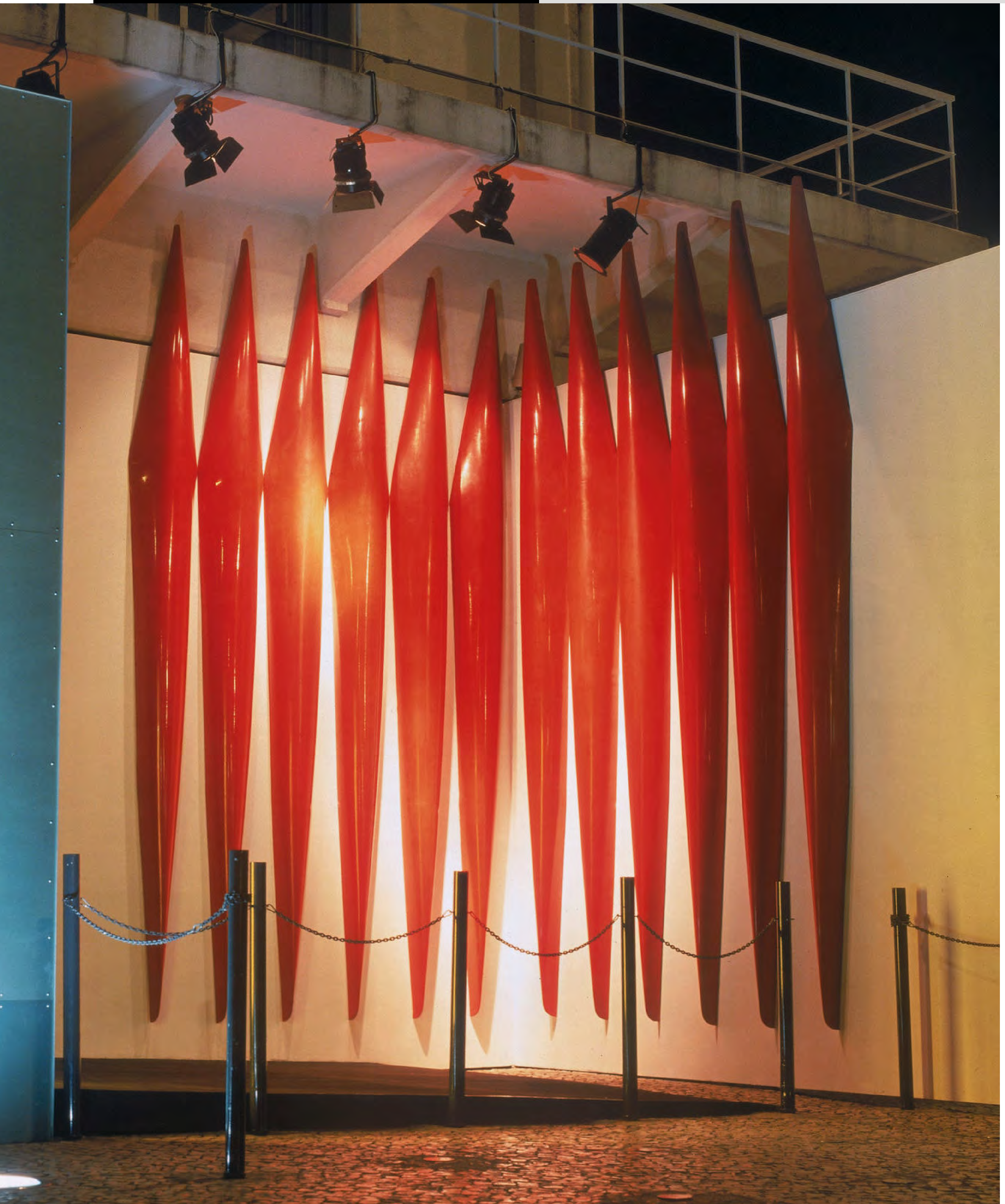
According to a July 2020 whitepaper by IQ-EQ[5], the next 10 years will trigger a US$15 trillion transfer of wealth to millennials and Gen Z. For UHNWIs with more than a US$100 million net worth, 62% are over the age of 75, highlighting the urgency of this transition. Before the pandemic, the wealth transfer for this generation was expected to begin in the next five years; however, the impact of COVID-19 on older generations has accelerated this timeline.

A similar level of urgency is also likely regarding art-related wealth among older generations of collectors, potentially triggering an increased focus on art and estate planning and philanthropy in the wealth management sector over the next decade. However, our findings show that, while art and estate planning has become one of the key services provided by wealth managers, there is still a significant gap in their awareness and understanding of clients' art and collectible assets.

This could indicate that the wealth management industry is not sufficiently prepared to address the challenges and issues regarding wealth transfer, particularly relating to art and collectibles wealth. The recent urgency around estate planning issues and wealth transfer highlights the importance of wealth managers initiating discussions with their clients about their art-related assets, and could present new opportunities to service the complex needs of their global client base.

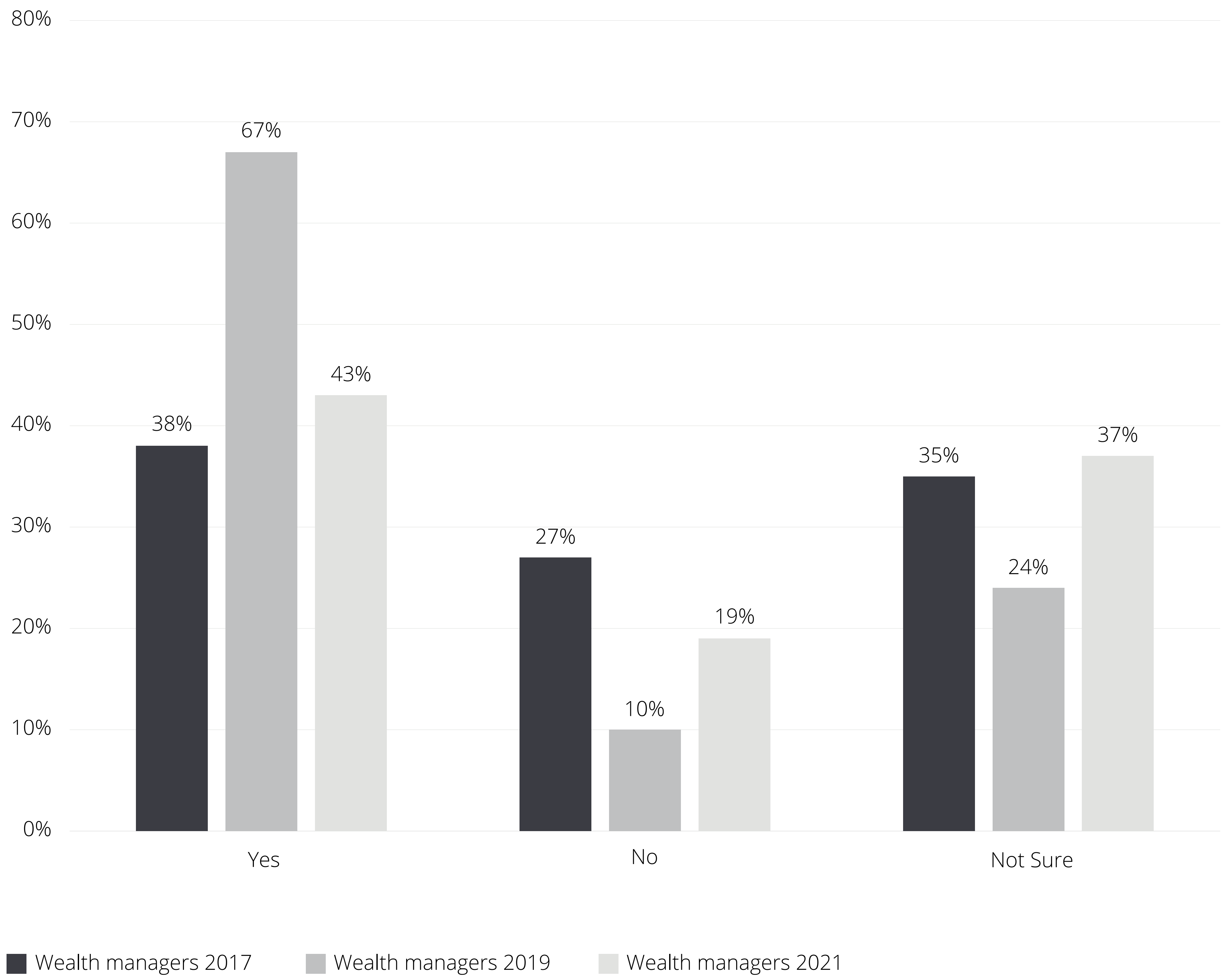
A Jóia do Tejo
©DMF, Lisboa/© Unidade Infinita Projectos - 2008

4 https://www.campdenfb.com/article/preparing-generational-wealth-transfer-post-covid-19
5 Source: White Paper – The Great Global Wealth Transfer, July 2020 – IQ-EQ



A. Art & Estate Planning
Survey findings 2021: wealth managers

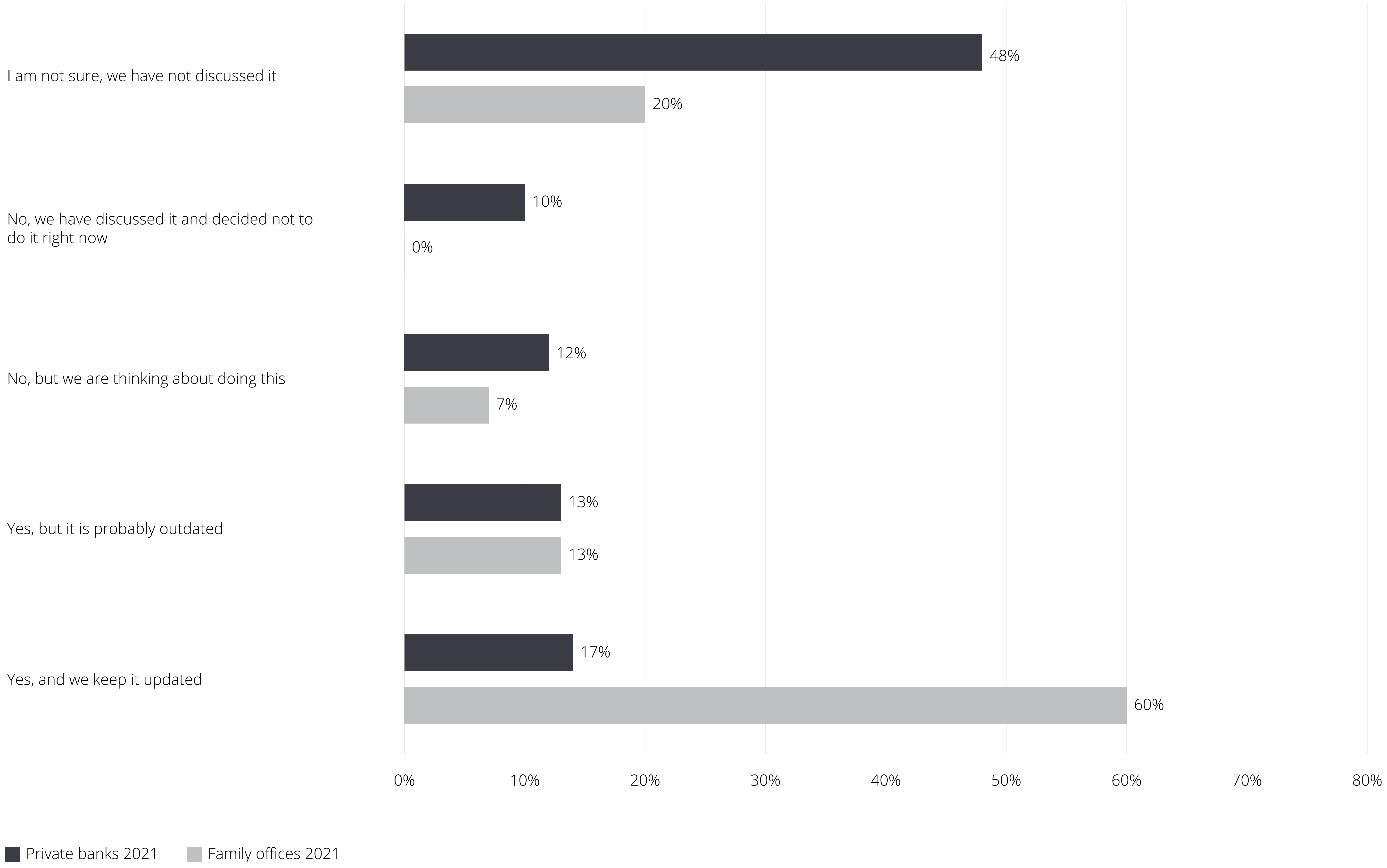
Figure 66. My clients have estate plans that sufficiently address their art collection
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021



12K1, 2001
©Luís Vasconcelos/Courtesy Unidade Infinita Projectos - 2001

Estate planning and art collections
This year, only 43% of wealth managers said their clients' estate plans sufficiently addressed their art collection, a steep decline compared with 67% in 2019. Regarding family offices, 67% said their clients had sufficiently addressed their art collection in their estate plans. However, only 37% of private banks said the same, while 44% said they did not know. This suggests that wealth managers' knowledge about their clients' art-related wealth remains low among private banks, presenting them an opportunity to proactively identify and initiate discussions with their clients regarding their art collection.

Figure 67. My clients maintain an inventory of their collection that at a minimum identifies each piece, its present location and its approximate value so that we could help to administer the estate without the collector's input
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021



Of the private banks surveyed, 48% said they did not know how their clients managed their collections, including what kind of collection management system they used and the information they stored. Only 20% of family offices said they were unaware, and 60% said their clients maintain a collection inventory that the family office is responsible for keeping up to date, compared with only 17% of private banks who said the same.

Vitrine
©Ana Paula Carvalho - 2008

Survey findings 2021: collectors and art professionals

Collectors survey—estate planning

Art and estate planning

64% of collectors said art and estate planning was the most relevant service that wealth managers could offer, compared with 76% in 2019. Most (68%) of art professionals said the same, compared with 78% in 2019. Of the wealth managers with an existing art-related offering, 82% said they provided clients estate planning services related to art, up from 77% in 2019.

Long-term estate planning around art is in its infancy

Only a few (12%) of the collectors surveyed said they had formalized their estate documents with their estate planning advisors. A further 51% said they were considering this, but had not yet begun. With significant wealth expected to be transferred between generations over the coming decade, wealth managers should engage with their clients on this subject.

68. Collectors: Do you have a long-term plan for your collection?
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021

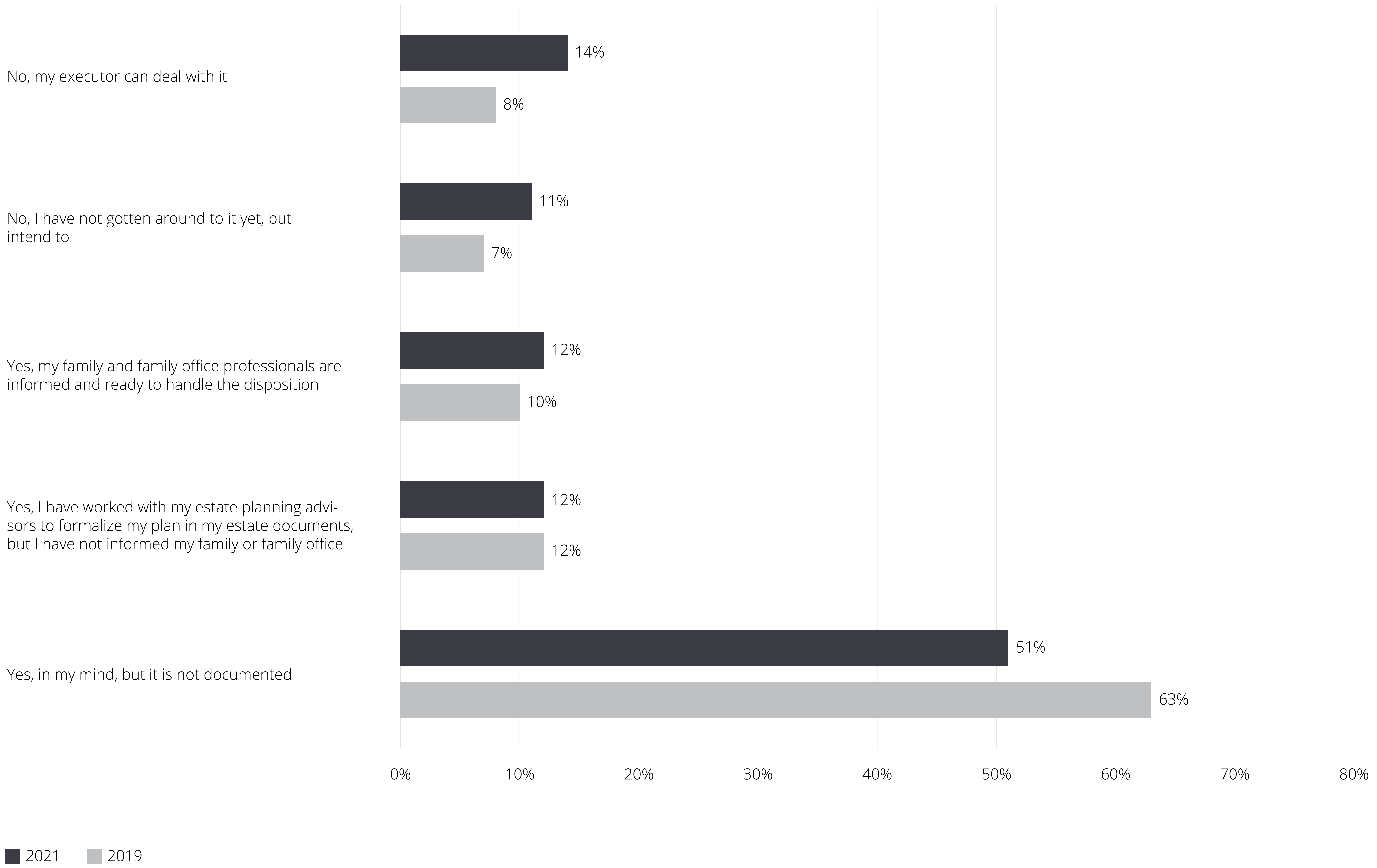
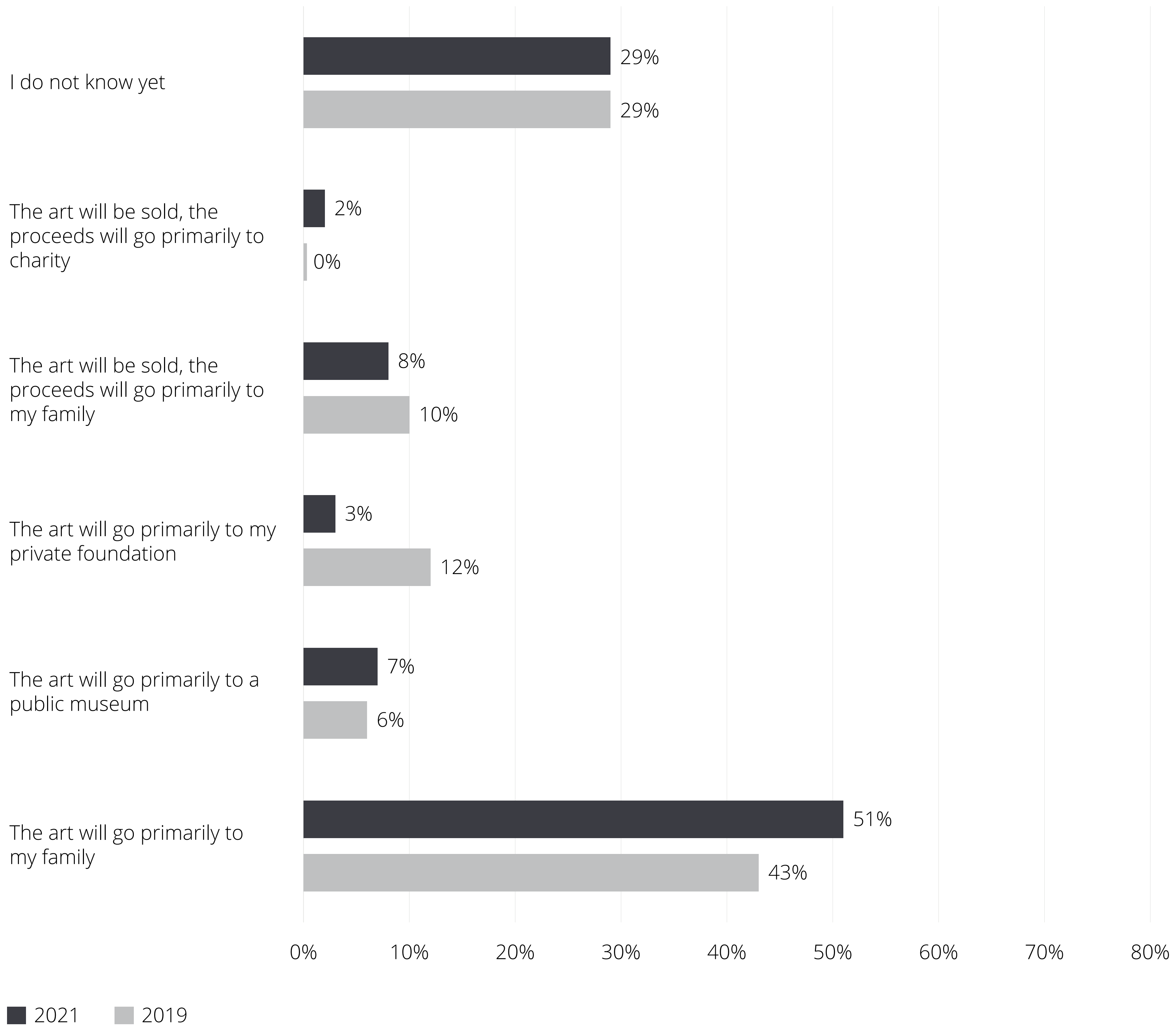


Figure 69. Collectors: what type of arrangements have you made in your estate plan for your art collection?
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021

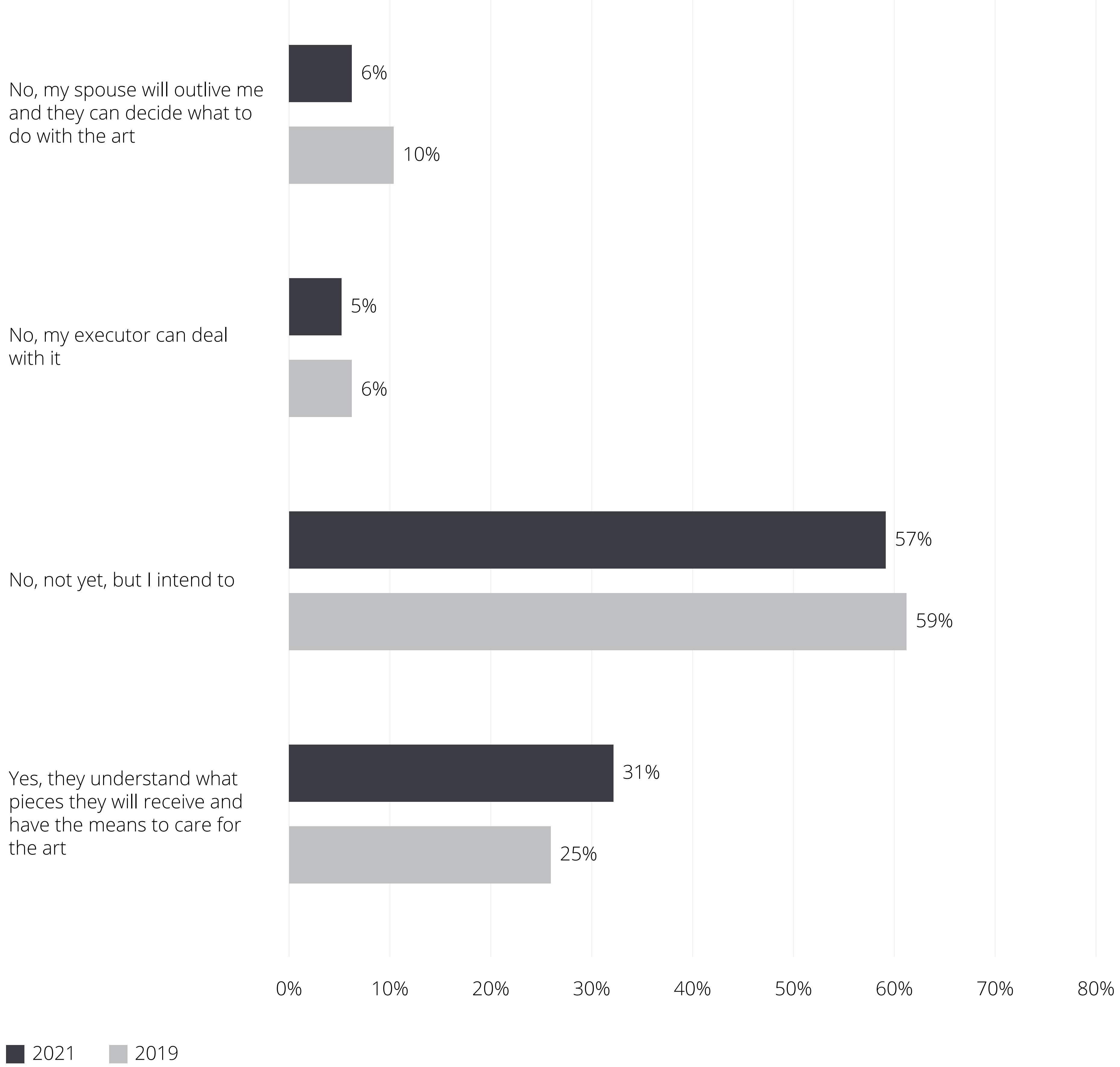


What will happen to art collections?

51% of art collectors said their collection would primarily go to their family, up from 43% in 2019; 7% said they would donate their collection (or parts of it) to a museum; and 3% said it would go to their private foundation, a sharp drop compared with 12% in 2019. Very few (10%) of collectors said the art will be sold, with 8% saying the proceeds would go to family and 2% to charity. Nearly a third (29%) of collectors said they were unsure about the arrangements they will make in the future regarding their collection.

Miss Jasmine

Figure 70. Collectors: if you intend to leave some or all of your collection to your heirs, have you discussed it with them?
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021



Lack of dialogue with heirs

Or collectors who plan to leave their collection to their family, only 31% had specifically discussed the artworks they will bequeath and provided the means to care for the art. While 57% of collectors said they had not yet discussed this with their heirs but intended to do so. Few (11%) said they had not discussed it and would leave this to their spouse or executor to deal with. These findings suggest a growing need for more engagement and discussions around estate planning, while underscoring the importance of implementing a proper family governance structure around art-related wealth to ensure a smooth transition between generations.

Nearly a third (29%) of collectors said they were unsure about the arrangements they will make in the future regarding their collection.

Steak 'n Shake
©Unidade Infinita Projectos - 2016

Philanthropists' priorities have changed during the pandemic, with funding channeled towards causes that address the more acute needs triggered by the crisis.

B. Art and philanthropy

Integrating philanthropy into wealth management is a growing trend seen around the world. Wealth advisors who do it well will reap the benefits of deeper client relationships and long-term client retention, while helping their clients positively impact the world.

As global wealth has risen during the pandemic, so has the level of inequality. COVID-19 is not an equal opportunity virus—it has disproportionately affected our society and industries. Inequality is now responsible for many of the world's challenges, ranging from health, climate change, income and poverty, education and migration.

This has heightened the focus on private philanthropy in recent years, with initiatives like The Giving Pledge, announced by Warren Buffett, Bill Gates and Melinda French Gates in 2010 and now boasting 216 signatories from 24 countries[6]. The Giving Pledge is a global, multi-generational commitment by the world's wealthiest individuals and couples to create a greater culture of giving to help tackle society's most pressing problems.

There are signs that these initiatives are increasing individual giving—data from the United States shows that individual giving has grown from US$246.73 billion in 2010 to US$324.1 billion in 2020[7], representing a 31.3% increase in this period.

However, individual philanthropic giving to arts and culture in the United States has grown at a slower rate of 22.7%, from an annual US$15.87 billion[8] in 2010 to US$19.47 billion in 2020. This demonstrates the tough competition faced by arts and cultural organizations to attract private funds to the sector and the need for them to act, which is discussed in the article p.171 from Adrian Ellis in Section 4.

The COVID-19 pandemic has intensified this challenge, with art and cultural organizations experiencing the strongest decline of 7.5% in philanthropic funding, compared with an increase of 11.3% in 2019. Philanthropists' priorities have changed during the pandemic, with funding channeled towards causes that address the more acute needs triggered by the crisis. While this may be a short-lived trend, the art and cultural sector risks being left behind if it does not demonstrate its value and impact on our society better.

Bernadine Bröcker Wieder, Co-Founder and CEO, Vastari in her article p.150 looks at the utilization of tokenized assets on the blockchain for fundraising and donations to support art organizations.

Micaela Saviano, Partner and Jared Lowe, Senior Manager at Deloitte Private USA discuss tax implications & philanthropy in the US in their article p.152: Philanthropy & Art – An Introduction to Income and Estate Tax Implications

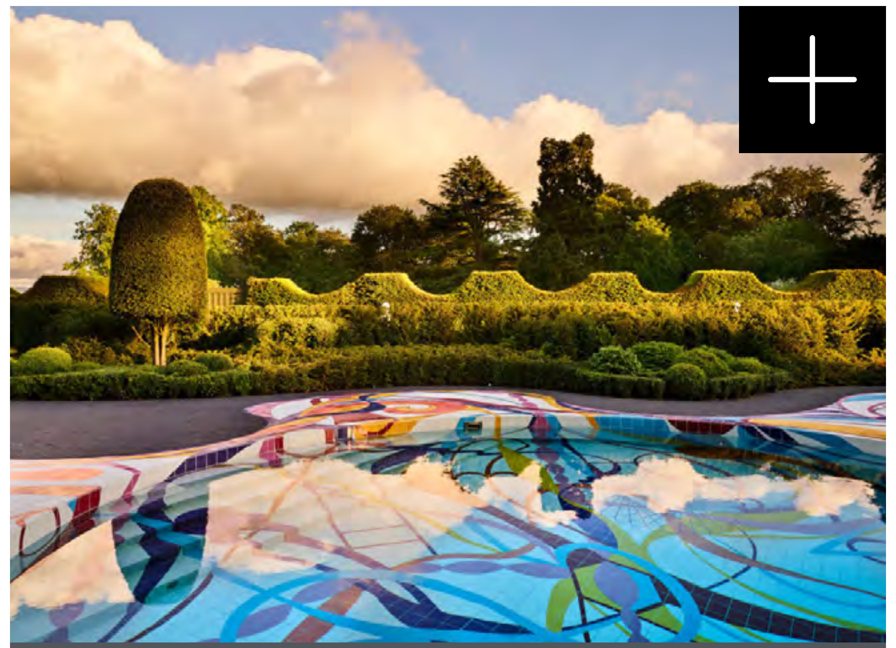
Foundations and supporting the arts

According to the most recent report of Giving USA, US foundations contributed US$88.55 billion[9] to charitable giving in 2020, 19% of the total charitable giving. Another report by Foundation Grants to Arts and Culture in 2018 stated that 9% of US foundation giving went to arts and culture—69% of this came from independent foundations, followed by 24% by community foundations, while corporate foundations accounted for roughly 5% of donated US dollars to the arts.

Another report from 2018, The Global Philanthropy Report supported by UBS[10], found that 18% of the 30,000 foundations surveyed focused at least some of their resources on arts and culture. This was the fourth priority after education (35%), human services and social welfare (21%), and health (20%).

Foundations are also increasingly employing a range of social investment strategies to maximize their impact; as a result, there is a growing interest in evaluating and measuring program outcomes. The subject of social investment in art and culture is further developed in Section 4.

6 The Giving Pledge, Press Release, December 21, 2020
7 Giving USA – The Annual Report on Philanthropy for the year 2020
8 Giving USA – The Annual Report on Philanthropy for the year 2020 (these figures are adjusted for inflation)
9 Giving USA – The Annual Report on Philanthropy for the year 2020
10 Paula D. Johnson, Harvard Kennedy School, the Hauser Institute for Civil Society at the center for public leadership, Global Philanthropy Report, Perspectives on the global foundation sector, with generous support from UBS, 2018

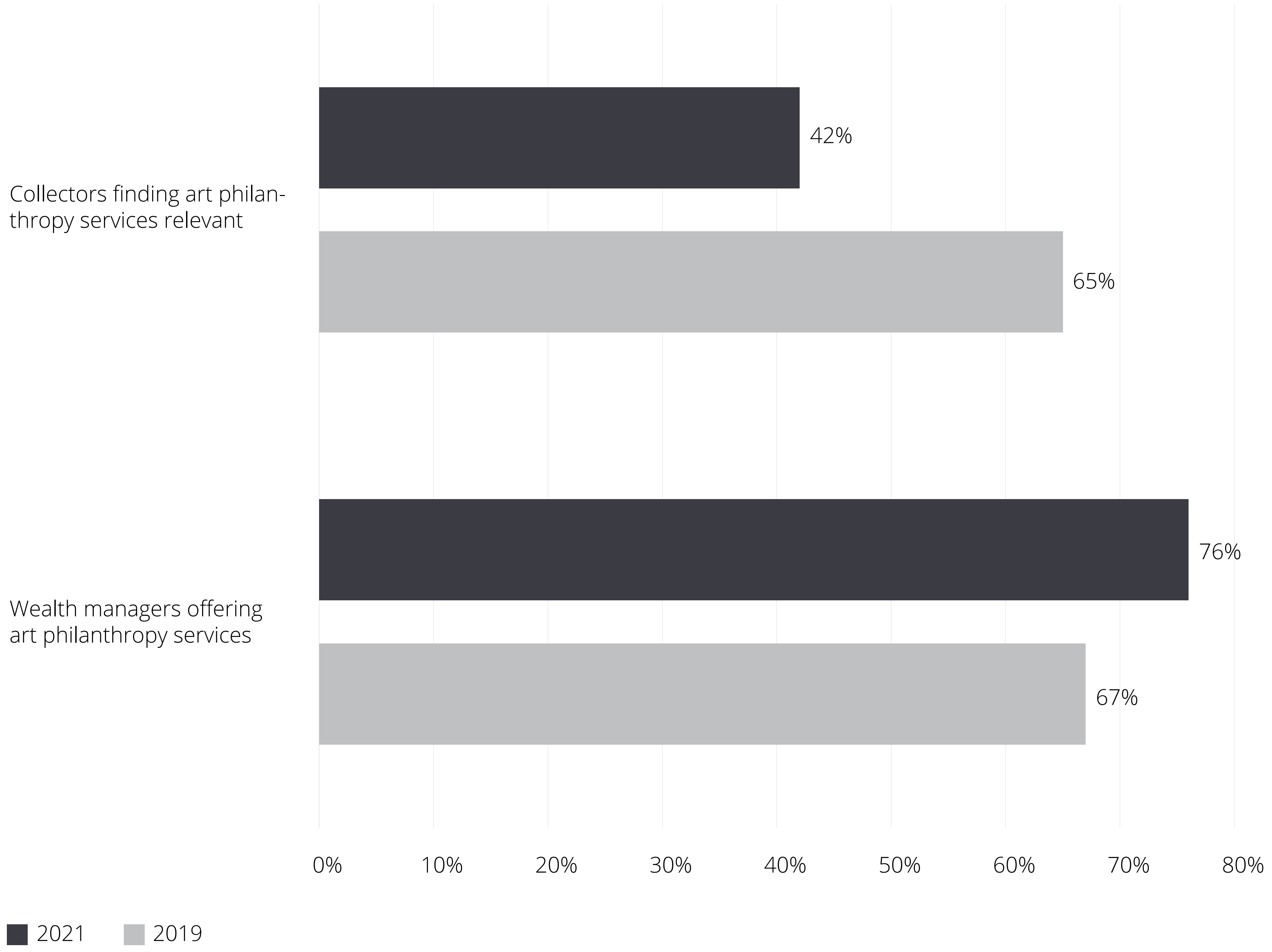


Cultural institutions need to rethink their reliance on traditional donations and individual-giving strategies and move towards a more purpose-led and impact-oriented giving and investment strategy.

Gateway
©Image by Allan Pollok-Morris_Courtesy Jupiter Artland - 2019

Survey findings 2021: collectors and art professionals

Figure 71. How relevant are art philanthropy services for collectors vs what wealth managers are currently offering?
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021



Art and philanthropy
42% of collectors said that art and philanthropy was the most relevant service that wealth managers could offer, compared with 65% in 2019. Most (61%) of art professionals said the same, compared with 67% in 2019. A significant majority (76%) of wealth managers said they offered services around art philanthropy and individual giving, including setting up foundations, arranging gifts and donations, compared with 67% in 2019. This sharp drop may be due to the pandemic triggering the desire to support more “urgent” philanthropic needs such as health, poverty, inequality and education, relegating culture as a secondary priority in the current crisis. However, it is worth noting that the younger collectors surveyed placed more importance on art and philanthropy services, with 69% saying this was the most relevant service that a wealth manager could offer. This is aligned with this younger age group’s focus on purpose and social impact investment, one of the highest-ranked motivations among younger buyers (86%) compared with just 32% of older collectors.

This suggests that cultural institutions need to rethink their reliance on traditional donations and individual-giving strategies and move towards a more purpose-led and impact-oriented giving and investment strategy, particularly as they become reliant on younger demographics. Section 4 looks at this in more detail.

In the article below, Laurent Issaurat, head of Art Banking Services at Société Générale Private Banking, discusses the role of wealth management in supporting their clients’ art and philanthropy needs and activities.

Laurent Issaurat
Head of Art Banking Services
Societe Generale Private Banking

Expert voices

Philanthropy and the arts

What role can contemporary wealth management play?

For centuries, benefactors have naturally gravitated towards culture and the arts. Nowadays, this patronage is growing in value worldwide, with over US$1,481 billion[11] in collectibles (primarily art) held by ultra-high-net-worth individuals, and US$1.5 trillion[12] in financial assets entrusted to private foundations.

When love for the arts and a generous intention come together, what role can private banking's wealth management play in giving their clients the professional support they need to make their plans a reality? This article breaks down this role into three steps.

Step 1: weigh up the (many) options
When it comes to art and philanthropy, the options are almost endless. Some initiatives are easy to put in place and are not capital-intensive. They mainly involve giving financial support to organizations, such as museums, cultural centers or associations operating in the fields of arts and culture. These organizations can be public or private, and cover a gamut of art forms, from the most ancient to the most avant-garde and contemporary.

The level of financial support is also flexible, with participation entry thresholds often starting at EUR100 or less—and from there, the sky is the limit for "major patrons". The privileges that come with this support—invitations to events, access to the directors and curators of institutions, having the patron's name inscribed on the tableaux *d'honneur*—mostly depends on the pledged amount.

Irrespective of the beneficiary organization's size and profile, patronage programs are an easy entryway into the world of art and philanthropy, alongside a thrilling social experience. It is also the preferred form of patronage for collectors, 80% of whom support museums and non-commercial cultural organizations regularly[13].

Therefore, these programs offer newcomers an ideal place to start. From there, these new patrons can contribute further time and financial resources through personal initiatives that are independent of existing structures. This also offers a myriad of possibilities.

11 Art and Finance Report, Deloitte & ArtTactic, 2021, p.39
12 Paula D. Johnson, Global Philanthropy Report, Harvard Kennedy School, 2019, p.10
13 Anders Peterson, TEFAF rt Patronage in the 21st Century, ArtTactic, 2020, p.7

For example, patrons can provide financial support to emerging artists by buying their artwork, or through networking, in the way of centuries-old traditional patronages practiced by the like of Francis I of France, or the Medici. In addition to supporting specific artists directly, patrons can set up structured and recurring initiatives, of which art prizes, grants, artist residencies and art festivals are some of the more popular. These initiatives require much more time and resources, of which by far the most complex and demanding is creating a private museum.

Step 2: sketch out and clarify a project
Once a favorite format has been determined, it is time to analyze the project's context, resources and objectives. Patrons should pay close consideration to their family ties; someone without an heir who wishes to support a museum is in a different position to someone who would consider involving their children in a long-haul project. In some other cases, benefactors will own a company that they wish to associate with the project.

Criteria such as the time horizon, the recurring or one-off nature of the initiative, and the amount of resources allocated to the project are decisive. Support can also vary significantly, ranging from gifts in kind (of an artwork or an entire collection), a monetary donation, or volunteering skills and time. The latter is a form of support that younger generations of philanthropists seem to particularly enjoy.

In addition to resources, the future patron needs to consider their preferred areas of interest. For example, the type of artist (contemporary, emerging, or more established); specific periods in art history; regions of the world; and art forms and formats (painting, video, photography, sculpture, drawing, digital art, street art, etc.).

In some cases, the patron's philanthropic interest extends beyond the art world to other areas, such as health or education. This can translate into initiatives where art—and sometimes even artists themselves—get engaged in programs that aim to provide help to specific communities; for example, people in hospitals, prisons, or areas with limited or no access to culture. Here, the benefactor's end goals and philosophy play a decisive role.

Another point to keep in mind is that some projects are purely altruistic—for example, donating artwork to a museum without asking for anything in return—while others have another purpose altogether, such as creating an artist's residency to build a personal collection from the resulting artworks. Regarding "venture philanthropy"[14], a fairly recent concept, acts of generosity are combined with strict management of how resources are used, so these need to be taken into account.

Step 3: put the project in motion
Now that the project is better defined, it can be implemented. This means addressing its legal, fiscal and financial structure, which may require specialist expertise. In some cases, the financial aspect is easy enough to understand—especially if it involves a one-off commitment of resources. However, this can prove more complex for long-term projects.

For example, creating a private museum requires not only substantial initial capital investment, but also the ability to finance the long-term running costs, which often tend to be underestimated. Therefore, it may be worth considering other options, such as opening a virtual museum rather than a bricks-and-mortar institution.

Naturally, the legal and financial structure will also depend on the patron's country of tax residency and where the project is located. Some parts of the world are more generous towards philanthropists than others, and provide tax incentives that vary significantly from one place to another. On top of a robust financial, legal and fiscal structure, bringing a philanthropic art project to life will also benefit from an in-depth understanding of the art world and its largely unwritten rules.

Take the case of an art prize. To truly benefit artists and the art ecosystem, this award must win the respect of most institutions, dealers, critics and collectors. This means establishing a credible selection process, and putting together a robust jury comprised of esteemed art world professionals and/or collectors.

More generally, continued cooperation and trust with artists, public and private institutions, patrons, collectors, and market intermediaries can open the door to unexpected developments and opportunities. In some instances, an initiative can go beyond its local or national framework by joining global programs, such as the United Nations' goal to protect the world's culture and natural heritage[15]. This approach can transform a philanthropist's project into a universal and long-term endeavor, and encourage international collaboration.

In conclusion,there are three takeaways. First, combining an interest in the arts with a generous intention opens up a vast and exciting world of possibilities. It can be useful to start small, for example, by supporting artists, museums or associations before moving onto more complex projects. This allows the philanthropist to build up practical experience and familiarize themselves with the art ecosystem.

Secondly, it is important to clearly outline the project before setting up the legal and fiscal structure.

And thirdly, a successful project that is both sustainable and ethical will have been defined in the most informed and knowledgeable way possible.

In all these matters—and given their growing financial importance—private bankers and wealth managers can be of invaluable assistance.

14 A new kind of philanthropy that involves applying the principles of capital venture to philanthropic pursuits
15 *Goal 11.4 of the United Nations Sustainable Development Goals*

Bernadine Bröcker Wieder
Co-Founder and CEO
Vastari

Expert voices

A token gesture

Can philanthropy benefit from the growth of blockchain technology?

The coin offerings in 2017 and the sale of non-fungible tokens (NFTs) in 2021 demonstrated that crypto-assets can generate a large amount of funds. After the devastating financial impact of the global pandemic on arts organizations and producers, many were inspired to think that some of this capital may be diverted to arts philanthropy, rather than commercial art practice. There are three main ways that the blockchain has interacted with art philanthropy thus far.

Digital art or assets sold for charity
Both on and offline charity auctions are a popular way for philanthropic organizations to raise funds for good causes, with artists often donating work, or offering it at a very low price. The week after Beeple sold his famous "Everydays: The First 5,000 Days" at Christie's, he announced that he would be auctioning a work to help tackle the climate impact of cryptocurrency (Forbes, 15 March 2021), whilst at the Proof of Sovereignty: A Curated NFT Sale by Lady Phe0nix on 25 May 2021, two lots—offered by Gucci and Jenny Holzer —donated proceeds to charity, to Unicef USA and NiaTero/Save the Children, respectively. (Christies, 25 May 2021).

Platforms are now being developed to specifically cater for charitable NFTs, operating on a range of protocols from Binance (NFT for Good and Cointribute) to Ethereum (Cryptograph and Aniseed). This technology, alongside further initiatives and planned launches, encourages the industry to grow.

Selling NFTs for profit still incurs tax liabilities and, as the audits of blockchain trails improve, more shady sources of funds may yet be uncovered (CNBC, 4 November 2020). From this writer's perspective it appears possible that a portion of sales of crypto-assets for charity may have been offered to avoid the tax liability of for-profit sales—an option open until the industry achieves some sort of maturity. However, charitable token sales can also improve once the beneficiaries better understand how to interact with purchasers of crypto-assets and the development of wallet functionalities continues.

Donations of cryptocurrency and crypto-assets
Alongside raising funds with blockchain tokens, arts organizations and charities may increasingly see donors wishing to provide support via crypto-assets. Some examples exist that also demonstrate the problems with such philanthropic activities.

The founder of the Ethereum Foundation, Vitalik Buterin, made headlines in May 2021 when he announced that he would donate over US$1 billion worth of cryptocurrency to India's COVID-19 Relief Fund set up by Shandeep Nailwal, an Indian cryptocurrency entrepreneur who founded Polygon, a layer two protocol on Ethereum. Buteriks' donation of 500 ETH and 50 trillion Shiba Inu meme coins was praised in the media (Quartz India, 16 May 2021). But there was a catch to this donation valuation: Vitalik donated 5% of the total Shiba Inu coin in circulation, a move which caused the price of the currency to fall by 50% (Timesnow News, 4 June 2021). This complicated the perceived value of the donation versus the actual value the charity could then claim. How might, for example, this relate to tax relief for crypto-asset donations to art museums?

Most museums interviewed for this article were not interested in owning or operating a crypto wallet, nor had they accepted any donations in cryptocurrencies or cryptoassets. But in June 2021, the ICA Miami was the first museum to break ranks and go on record to accept a gift of NFTs from a collector, "CryptoPunk #5293" (Coindesk, 9 July 2021). Alex Gartenfeld, the museum's director, stated that the museum's team and donors are working at the "cutting edge of intellectual discourse, more than just collecting". This acquisition required answers to many different questions than usual, particularly around security risks and the valuation for insurance. At the time of writing, Gartenfeld admitted that it would be several months before the acquisition was properly processed into the collection, and that his team was handling this internally, while speaking to colleagues at other museums who had previously acquired works utilizing blockchain technology. Gartenfeld felt that once the work had a place in the collection, it "basically no longer has a price," removing a significant amount of the risk with the wider cryptocurrency world. (Interview, 16 July 2021)

Creating crypto-collectibles to raise funds for arts institutions

A nascent area for museums and collections is the concept of creating (or minting as the industry likes to call it) limited edition collectibles inspired by the collection or activities of the museum. Intellectually and legally, these crypto-collectibles can be structured in a variety of ways, from creating highly limited or unique editions of famous works (as done by the Uffizi Gallery in Florence, the Galleria dell'Accademia in Venice, and the Hermitage in St Petersburg) or minting larger editions related to exhibitions (as done by the Whitworth in Manchester in collaboration with Vastari Labs and the British Museum in collaboration with La Collection).

However, further writing and research is required to clarify the ownership and copyright of the assets being minted, their relationship to the original artwork, and to the governance of the institution. Indeed, lawyers and technologists at the Art Identification Standard Association have been debating the legal frameworks of art crypto-collectibles. To date, however, very few scholarly articles have been written about the subject, and museums' stances on the metaverse or digital twins remains ambiguous. Scholars, such as PhD candidate Frances Liddell from the University of Manchester, are reporting real-time on museum NFTs (Cultural Practice 16 March 2021). Similarly, curators, including Dr. Tina Rivers Ryan from the Albright Knox Museum, critically placed contemporary crypto-art into context (ArtForum, May 2021). Despite these early efforts, it appears that much greater information, use cases and research is still required to clarify what these philanthropic fundraising crypto-collectibles mean for the institution in the long term.

To conclude, utilizing tokenized assets on the blockchain for fundraising and donations could undoubtedly provide some much-needed income for a sector that has suffered over the past two years—and reduced government funding over decades. However, most examples are still too new and the exploration of, and writing around, the sector not yet developed enough for final conclusions to be drawn. The full story of crypto-philanthropy remains to be written, but in the meantime one should look for guidance from those most active in the sector.

This complicated the perceived value of the donation versus the actual value the charity could then claim. How might, for example, this relate to tax relief for crypto-asset donations to art museums?

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Expert voices

Philanthropy & Art

Not as simple as it first appears

Philanthropy, income tax planning, and estate tax planning are often on the minds of collectors and their advisors, but perhaps more now than ever as the US waits to see if relevant tax legislation is passed. This article will provide a high-level overview of the potential tax benefits and considerations of charitable giving for US income tax and US estate tax purposes for collectors and investors[16] using fine art and collectible assets.

Charitable Income Tax Deduction

US taxpayers may generally be allowed a fair market value ("FMV") charitable deduction for income tax purposes for art and collectible assets gifted to charity, which have been held for more than one year[17]. Note that the FMV charitable deduction is limited to donations to certain domestic organizations which will use the donation within the US. For collectors willing to donate their appreciated art, this has two potential tax benefits, in addition to any other non-tax personal or societal benefits. As with all qualifying charitable contributions, the first is that the deduction will potentially offset other taxable income (subject to the applicable adjusted gross income limitation), dollar for dollar, in the year of contribution. The second potential tax benefit to the owner of the fine art or collectible, is not recognizing taxable gain on the appreciated asset if it were sold instead of donated. Example 1 below shows the incremental benefit of donating an appreciated asset in-kind, rather than selling an asset and donating the proceeds.

16 Artists who own self-created artwork will have different tax results of donating inventory property. This article does not address the considerations for artists
17 See Treas. Reg. Section 1.170A-1(c). Note that art assets with a holding period of less than one year will be treated as ordinary income property, with a charitable deduction limited to the tax basis

Table 19.

	Scenario #1 No contribution	Scenario #2 Cash Contribution of Asset Proceeds from sale	Scenario #3 Contribution in-kind
Interest Income	$ 1,000,000	$ 1,000,000	$ 1,000,000
Gain on Sale	$ -	$ 200,000	$ -
Charitable Deduction	$ -	$ 300,000	$ 300,000
Net Taxable Income	$ 1,000,000	$ 900,000	$ 700,000
Income Tax	$ 370,000	$ 333,000	$ 259,000
Tax Benefit of Deduction	$ -	$ 37,000	$ 111,000
Assumptions: Tax rate - 37%+,[1] Asset FMV - $300,000, Tax Basis - $100,000, Net Gain - $200,000.			

1 Artists who own self-created artwork will have different tax results of donating inventory property. This article does not address the considerations for artists.

Table 20.

		Public Charity	Private Operating Foundation	Private Foundation
Short-term capital gain property	Deduction amount	Tax Basis	$Tax Basis	Tax Basis
	Applicable Limit	60% AGI	60% AGI	20% AGI
Long-term capital gain property with related use by charity	Deduction amount	FMV	FMV	Tax Basis
	Applicable Limit	30% AGI	30% AGI	20% AGI
Long-term capital gain property without related use by charity	Deduction amount	Tax Basis	Tax Basis	Tax Basis
	Applicable Limit	60% AGI	60% AGI	20% AGI

However, there are some important limitations:

First, the fair market value deduction is limited to art gifted to public 501(c)(3) charities, or private operating foundations[18] that use the art for its exempt purpose[19]. The charitable deduction for art not used for the exempt purpose of the organization, is limited to the donor's tax basis. Likewise, the income tax deduction for charitable contributions to a private foundation that is not a private operating foundation is limited to tax basis[20].

Second, the overall donation is limited to a percentage of the taxpayer's Adjusted Gross Income ("AGI"). The applicable percentage limitation depends on the holding period of the asset, the type of charity the art is donated to (a public charity, a private foundation, etc.) and whether the charity used the asset in a manner related to its exempt purpose[21].

A museum displaying the donated art in a public gallery would be considered use of the artwork in a manner related to the exempt purpose of the museum. However, this does not mean that only art museums qualify; many other charities can use fine art in an exempt purpose. Keep in mind that if the charity intends to sell the donated art, even if the proceeds will be used for its exempt purpose (i.e. purchasing another piece of art), the sale does not qualify as "related use" of the donated art, which is required for purposes of donor receiving a FMV deduction.

Next, the contribution cannot be of a partial interest . The donor may not retain a substantial interest in the property to qualify for a charitable deduction. An example is if a donor owned both the painting and copyright, and retained the copyright, while donating the painting, it would preclude the income tax charitable deduction because an interest in the painting was retained (the copyright). This limitation may be of more interest as the market demand for non-traditional assets, such as Non-Fungible Tokens ("NFT"), has grown.

Although partial interests are not deductible, fractional interest donations can be obtained. Donors may make a donation of a fractional interest in a piece of artwork if the full amount of the artwork is contributed by the earlier of 10 years or date of the donor's death. Additionally, the fair market value of the artwork is established at the date of the first donation and applies to all later fractional interest donations, regardless of whether the fair market value appreciates in subsequent years. The charitable organization must also possess the artwork for its relative annual ownership (e.g. days in the year times ownership percentage). For these reasons, donors may be hesitant to make fractional interest donations. But, it can be a useful mechanism to "time" charitable deductions against a donor's taxable income to enhance the value of the full deduction over several tax years if there would otherwise be AGI limitations or tax rate considerations.

Finally, the determination of fair market value requires the taxpayer to obtain, and often attach to the tax return, a qualified appraisal which meets the strict requirements under IRC Section 170(f)(11). Even with a qualified appraisal, taxpayers should be aware that the IRS may review and adjust the value of the donation under audit. In fact, the IRS maintains in-house appraisers and an external body of industry specialists - the Art Advisory Panel - which serve as an independent panel to review appraisals submitted by the IRS.

18 See IRC Section 170(b)(1)(F) for definitions of the types of foundations which qualify
19 IRC Section 170(e)(1)(B)
20 IRC Section 170(e)(1)
21 IRC Section 170(f)(3)

Planning to Use the Charitable Deduction:

Beyond the limitations and considerations discussed above, taxpayers and their advisors should consider the character of income being offset by the charitable deduction. With the highest current marginal tax rate of 37%, and the long-term capital gain and qualified dividend rate at 20%, taxpayers might look to make charitable contributions in years in which they have higher than normal ordinary income due to increased interest, wage, or operating income from flowthrough businesses to use the charitable deduction against that "higher-tax-rate" income. Taxpayers may want to consider modeling, and perhaps multi-year modeling, particularly if tax legislation is passed.

Charitable Estate Tax Deduction

Assets passed to charity at death qualify for a fair market value charitable deduction which may reduce the taxable estate[22]. The value of the deduction is the value of the asset includable in the taxable estate. Similar to an income tax deduction, an appraisal is necessary to support the fair market value of the artwork in the estate. In both cases, the value may be questioned by the IRS under audit.

Unlike the income tax charitable deduction, which is limited to US charities, generally speaking, the estate tax charitable deduction is not limited to transfers to domestic organizations or trustees for use within the US. Also, unlike the income tax charitable deduction which limits donations to private foundations to a tax basis deduction, charitable bequests at death made to a private foundation may provide for a full fair market value donation to the estate. However, planned bequests to a private foundation should be reviewed with care if the long-term intent is to sell the art from the private foundation. Private foundations are subject to onerous excise taxes which can be triggered with transactions with persons "related" to the estate, which may extend beyond family members.

Executing charitable gifts during lifetime or bequests at death take careful legal drafting and likely some negotiations with the charitable organization. Because of the significant tax benefits alone, taxpayers may want to seek specialized advisors as they work on tax and legal planning for their collectible assets.

Estate Tax – A brief overview

When considering using charitable giving as an estate planning tool, it is important to generally understand who is subject to US estate tax and what assets are subject to the estate tax.

The US taxes US citizens and US residents who have established domicile in the US (collectively "US domicilliaries") on their personal balance sheet at the date of death. The estate tax rate is assessed at 40% of the taxable estate, which includes worldwide assets. Current law provides an applicable exclusion amount (AEA), otherwise known as the "lifetime exemption," of $11.7M (as of 2021) for US domicilliaries. As a result, US domicilliaries incur estate tax once their taxable estate, including prior taxable gifts, exceeds $11.7M.

Non-US-domilliaries may also be subject to US estate taxation if they own property in the US, including real estate, tangible property, and stock of US corporations. However, they do not qualify for the $11.7M applicable exclusion amount and receive a much smaller exemption amount of $60,000. Some countries and the US have established gift and estate treaties in place which may reduce a taxpayer's US tax exposure.

It is worth noting that an exception exists for art work owned by a nonresident alien located within the US on their date of death if the art work is: 1) imported solely for public exhibition, 2) on loan to a nonprofit public gallery or museum, and 3) on exhibition or en-route to or from an exhibition.

Although an expanded gift and estate planning discussion it is beyond the scope of this article, because of potentially significant US estate tax and possibly state estate and inheritance taxes, many taxpayers proactively transfer art assets to their family or to trusts during their lifetime. Lifetime gift planning transfers ownership of the assets to grow in value outside the taxable estate. However, because of the tangible nature of art assets, special care should be taken to avoid any retained use or enjoyment of the gifted assets in accordance with Section 2036[23]. If considering any charitable or estate planning with art assets, it is important to discuss such plans with trusted advisors before any action is taken to understand the potential income and estate implications as well as to avoid any unexpected tax consequences.

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22 IRC 2055
23 IRC Section 2036

Culture & Social Impact Investment and Sustainability

04

Piano Dentelle #3
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Highlights

Culture, social impact investment and sustainability exist at the intersection between philanthropy and investment.
This is a relatively new domain for the art wealth management industry, providing wealth managers with a new client service focusing on social impact and purpose-led investment in the art and culture sector.

Investors see social investments as an opportunity, but art and culture still lag behind
A recent report by Oliver Wyman and Morgan Stanley[1] projects that high net worth (HNW) and ultra-high net worth (UHNW) sustainable investments will grow by 18% per year to reach a total of US$9 trillion by 2024. It can be challenging to provide evidence and arguments for why the art and cultural sectors are eligible for impact investing in the first place. According to a Global Impact Investing Network (GIIN) survey in 2020[2], 9% of respondents said they had directly invested in art and culture, but this only accounted for 0.1% of the sample assets under management (AUM).

Sustainable impact investment in the arts could become an attractive investment model
In this year's survey, 28% of collectors and 31% of art professionals identified sustainable impact investment in the arts as the most attractive investment model. This was significantly higher among the younger demographic (under 35 years old), where 50% said socially responsible investment products in culture would be the most interesting to them. This implies that wealth managers that expand their sustainable investment offerings are well-positioned to grow the highly attractive younger client segment in the future.

Art as a catalyst for social change and community cohesion
The power of the arts drives large-scale social change and helps tackle some of our biggest global challenges. Many artists address social issues in their work and make publicly accessible art, which can help improve the quality of life in surrounding neighborhoods and strengthen communities.

The cultural and creative sectors (CCS) constitute a key growth driver in many countries
While often perceived to be of little relevance to the overall economy, economic data shows that the CCS are a key growth driver in many countries and represent some of the fastest-growing sectors in the world's economy. They also play a role in spurring creativity and innovation, critical factors for adapting to the COVID-19 pandemic. The United Nations (UN) has declared 2021 as the International Year of Creative Economy for Sustainable Development.

A Ilha dos Amores
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Culture, social impact investment and sustainability exist at the intersection between philanthropy and investment. This is a relatively new area for the art wealth management industry, providing wealth managers with a new client service that focuses on social impact and purpose-led investment in the art and culture sector.

1 Morgan Stanley and Oliver Wyman, 'Global Wealth Management Report 2020', p.25
2 Global Impact Investing Network (GIIN) Research Institute, 'Annual Impact Investor Survey 2020', p.33

The international community has also recognized culture's role as a driver of sustainable development
The Agenda for Sustainable Development, which was unanimously adopted by UN Member States in September 2015, comprises 17 sustainable development goals (SDGs) and 169 specific targets, and includes several explicit references to cultural topics[3]. Cultural organizations represent a key driver for social change towards sustainable development, providing a platform for public debate and education.

The cultural and creative sectors suffer from a lack of funding, a situation exacerbated by the pandemic. The COVID-19 crisis has created an acute need for the CCS to find and explore new alternative sources of revenue and partnerships and to reconsider many of their traditional funding models. If culture is set to play an important role in society and sustainable development, there is an opportunity to find better ways and models for connecting impact investors with the CCS' financing needs.

Creative and cultural organizations need to improve the ways they analyze their performance and impact
This is particularly important in this post-pandemic period, since many art and culture organizations are struggling to stay afloat. Measuring impact can enhance their transparency towards stakeholders, strengthen their relationships with society, and potentially attract new supporters and donors.

New technologies can also support impact investment in creative and cultural organizations
Blockchain and tokenization are already being harnessed to generate new revenue streams. While the recent technological advancement in artificial intelligence (AI) and network theory now allows us to analyze how cities and their networks of tens of thousands of museums, non-profit organizations and commercial galleries help spur and nurture creativity in the field of contemporary visual art.

There are signs the impact investment market is gradually opening up for the art and culture sector
New initiatives have been launched, such as "Creativity, Culture, and Capital: Impact investing in the global creative economy (CCC)", a partnership between Fundación Compromiso, Upstart Co-Lab (United States), and Nesta Arts & Culture Finance (United Kingdom), that aims to attract impact capital and investment to the creative economy.

Art and culture in a smart city strategy
Culture and impact investment could be influenced by the role culture can play in a smart city strategy. There is an increasing realization that urban smart cities must combine both technology and culture, because improving quality of life does not only require technology; it is also a question of connecting and inspiring people.

With the growing recognition that CCS can support cities to be "smarter", more sustainable investment products may develop
Culture impact bonds may become a reality in the future, helping develop a new generation of smart cities. These would successfully integrate culture and creativity within an inclusive and sustainable urban growth strategy, whereby repayment of investments in culture and creativity would be subject to social and not simply financial impact.

Macedónia
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3 In particular, SDG 11 aims to ensure that the cities of tomorrow are "inclusive, safe, resilient and sustainable" and target 11.4 focuses on protecting and safeguarding "the world's cultural and natural heritage". Moreover, the Agenda aims to ensure "inclusive and equitable quality education and promote lifelong learning opportunities for all", highlighting the importance of culture for sustainable development

Introduction

Culture, social impact investment and sustainability exist at the intersection between philanthropy and investment. This is a relatively new area for the art wealth management industry, providing wealth managers with a new client service that focuses on social impact and purpose-led investment in the art and culture sector. This approach is part of the global trend around sustainable finance.

The intersection between culture and social impact and sustainability was a topic we first introduced in our Art & Finance Report 2019 and during the Deloitte Art & Finance conference in 2020. In this section, we explore some of the links between art and finance and the CCS and the role they play in sustainable development. We also explore the role of culture and creativity in a smart city strategy, and how this could boost the development of sustainable investment products dedicated to the CCS.

Another important development is this year's UN initiative, which dedicates a whole year to the creative economy and its critical role in promoting sustainable development[4], especially in a post-coronavirus world. In November 2020, the UN adopted resolution A/RES/74/198, declaring 2021 the "International Year of Creative Economy for Sustainable Development". Tabled by Indonesia, it was backed by 81 countries, a ringing endorsement of an often misunderstood and misrepresented section of the global economy.

Sustainable finance

Responsible investment

Mainly focused on screening and excluding investments in certain countries, companies or sectors.

ESG integration

Mitigating risks by integrating ESG factors into the decision process, to identify issues and engage with the company to make changes.

Impact investing

Investments to primarily achieve specific and positive social or environmental benefits while also delivering a financial return.

From minimizing negative impact...

... to integrating Environmental,Social and Governance factors in financial investment decisions...

... and maximizing positive impact

Source : Deloitte Luxembourg

Arthur
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4 UNCTAD, 'Creative economy in the sun', 13 January 2021 - https://unctad.org/news/creative-economy-have-its-year-sun-2021

In Indonesia, which brought the resolution to the UN General Assembly, the creative economy contributes 7.4% to the nations' GDP.

Thalie
©Bertrand Huet|Tutti/Courtesy Galerie Nathalie Obadia, Paris/ Brussels - 2008

The resolution recognizes the creative economy's potential to support developing and transitioning economies to diversify production and exports and deliver sustainable development inclusively and equitably.

On 30 July 2021, **the Ministers of Culture of the G20 group of the world's largest economies agreed for the first time in history on a G20 Declaration on Culture that firmly positions culture as a major engine for sustainable socio-economic recovery in the wake of the COVID-19 pandemic[5].** It includes five key priorities: the protection of cultural heritage; culture and climate change; culture and education; cultural and creative industries; and culture in the digital transformation.

So, what is the creative economy?
The creative economy covers the knowledge-based economic activities of the "creative industries", which include advertising, architecture, arts and crafts, design, fashion, film, video, photography, music, performing arts, publishing, research and development, software, computer games, electronic publishing and TV/ radio. The creative economy accounts for about 3% of global GDP, according to a 2015 study by professional services firm EY[6]. But its true worth arguably increases when cultural value is added to its commercial gains.

In Indonesia, which brought the resolution to the UN General Assembly, the creative economy contributes 7.4%[7] to the nations' GDP. It also employs 14.3% of its workforce, from craft to gaming, fashion to furniture. In the United Kingdom, creative industries made a record-breaking contribution to the economy in 2017, supplying GBP101.5 billion to the country's coffers, and has grown at nearly twice the economy's rate since 2010.

These are monetary examples of the creative economy's wider impact. It is proving to be a powerful emerging economic sector, strengthened by digitalization and a surge in services. Its contribution is expected to grow, and if key trends can be harnessed, we may be living in a more creative world in the future.

The aim of this section is to explore the impact of investment in the CCS and to support a broader engagement on this budding topic.

This section has three parts:

Part 1: Global shifts in sustainable investment trends

Part 2: CCS and sustainable impact investment

Part 3: Reinventing smart cities through culture

Where do we stand in terms of sustainable investment offerings for the CCS today? And could this be an area of expansion for wealth management? These topics are addressed in more detail in this section and by the articles from Blue Rider Group at Morgan Stanley & Niki Charitable Art Foundation, Therme Group, Deloitte Italy, Deloitte Russia, Wondeur.ai, AEA Consulting, Foundation Compromiso & Alterna, IULM University and the European Commission.

In the following article, Deloitte Russia discusses how a company can be sustainable and presents a short overview of the social impact and sustainability of corporate art collections in Russia.

"Corporate collecting is one of the most interesting ways that businesses and art can interact. Businesses can harness art as a marketing and branding tool to shape the messages they want to send to society. Art can be used to create shared values for employees and the organization. It is undeniable that art has become an integral part of the working environment and is often covered by corporate ESG strategies."

5 UNESCO webpage, G20 agrees first declaration on culture (unesco.org). Last consulted 3rd August 2021
6 EY, 'Cultural times - The first global map of cultural and creative industries', December 2015
7 UNCTAD, 'Creative economy in the sun', 13 January 2021 - https://unctad.org/news/creative-economy-have-its-year-sun-2021

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Expert voices

Corporate art collection as a contribution to the society

By way of opening

What does it take for a company to be sustainable, not just today, but in the future, too? Our article provides a short overview of corporate art collections in Russia from the perspective of their social impact and contribution to corporate sustainability.

The international community has recognized the role of culture as a driver of sustainable development. The United Nations declared the year 2021 the International Year of Creative Economy for Sustainable Development. According to UNESCO's research, in the developed countries, the share of creative industries can account for up to nine percent of the GDP, while the sector employs 30 million people worldwide. Strengthening the economy through the creation of intangible assets has become a worldwide practice. Involvement of creative industries into the economy can improve quality of life, create new jobs, engage new generations in the creative process, boost tourism, as well as improve country's reputation abroad. This can be achieved via a combination of state, corporate, and private initiatives.

Art could be classified as the most intangible part of the creative industry that has a spillover effect to the entire society.

Over the last years, the idea of sustainable growth has come to the forefront of many business strategies. The ESG (environmental, social, and governance) drivers, such as diversity, equality, and inclusion, human rights management, and environmental performance act as intangible assets of companies. In the business community, art is not always associated with sustainability, but, as we would like to discuss in this article, it could and should be.

As the humanity met the coronavirus pandemic, the relationship between the sustainability agenda and the art world attracted a growing interest. Rethinking the traditional values has been a common side effect of the pandemic and it further demonstrates how art can be an organic part of sustainable growth in a world of rapid change.

Starting from the Salon des Refusés (1863), art has held the privilege to speak in a voice of its own, delivering a message that trespasses the purely aesthetic boundaries. Today, we believe, is the right time for art to become a part of corporate strategy and vision.

This article focuses on the impact corporate art collecting can make on the society and sustainable development.

Art investment as an ESG investment
Small businesses and large corporations alike are investing into collections of fine art: this is a tradition dating centuries back. Many collections were started based on the patron's tastes and passions (like those of the Medicis, Rockefellers, etc.). Later on, the trend towards responsible consumption encouraged companies to act as caretakers, rather than owners, of their cultural heritage and showcase what treasures were amassed.

In the past, corporate art collection was seen as a status symbol, a PR tool, and an investment instrument in one. Nowadays, companies use art collections to achieve their sustainability goals, to shape and reflect their brand image, and to create a certain business personality. What is even more important, art is an international language. Both clients and partners will understand the message transmitted through the contemporary art, so the artworks related to the nature and society will support the ESG strategy in a perfect way.

As highlighted by Loa Haagen Pictet, Chairman of The International Association of Corporate Collections of Contemporary Art (IACCCA), Head of Art, Pictet Group, Chief Curator of Collection Pictet it is believed that artwork in the workplace inspires creativity and provides intellectual stimuli for the employees. "As the employers are hoping to cater to younger recruits, the focus is increasingly on a millennial-friendly ethos of social responsibility", says Ms. Haagen Pictet. "In a world where intangibles, including message of the company and the social impact, play significant role both in internal processes, such as talent management, and in fostering an indirect bond between the business and external stakeholders. A certain competitive edge can be gained by using art as a tool to shape powerful messages about business values and social responsibility issues. Art gives holistic thinking for a corporation to reach out not only to employees and colleagues, but also to the civil society."

This opinion is supported by Marina Sitnina, Executive Vice President of Gazprombank, General Director of Art Finance: "Just like any collecting, corporate collections say a lot about the collector, serving as an expression of corporate identity and as a certain message to the society as a whole. According to Ms. Sitnina, a collection can become a kind of a mediator between a specific person and the art world as a whole, encouraging others to see more, understand, be interested, in other words—continue self-development."

Global corporations spend huge budgets to identify the trends and manage business risks, while artists aim to predict the future. In the early 1960s, when the ESG values were not yet recognized by businesses and there were no sustainability reports for investors, the contemporary art with its statements around ecology and peace on Earth helped the society look deeper into the meaning and the context and explore the world around.

Today, most major businesses are mature, focusing on long-term planning and sustainable development priorities. Art can help build something truly worthwhile in the long run. A message conveyed through art could last forever, as people will see it in a museum in 10 or 100 years. If a company sets up a corporate collection of contemporary art, it speaks volumes of the company's forward-looking aspirations, readiness to meet the challenges of the time, and confidence in the future, notes Ms. Sitnina.

Elena Tolchennikova, a shareholder of JART, a major Russian art gallery, notes that many companies in their newly born art collections focus on younger artists, as their works better reflect the current times.

Russian view
Russia has a rich cultural heritage. We are proud of our world-class museums, famous artists, and unique history. At the same time, Russia is not represented in the leading international art market reports, does not appear on the map of contemporary art; Russian artists do not win awards at international art exhibitions. How to combine Russia's heritage, its modern ambitions, and the current situation in the domestic art industry?

We conducted a brief research based on the publicly available data to look at how 50 major Russian companies (the Forbes Top 50 list) engage with art.

Elena Tolchennikova, a shareholder of JART, a major Russian art gallery, notes that many companies in their newly born art collections focus on younger artists, as their works better reflect the current times.

We found that:

- One company from the list has a corporate art collection exhibited in Russian museums. The collection reflects the company's business profile and is maintained as a part of the company's heritage.
- Two companies support the contemporary art through organizing residences for artists and art competitions.
- Most companies on the list do not have a direct art message; however, they support art and culture as a part of the social policy, sponsoring major Russian museums, local culture centers, or biennales of contemporary art, and implementing other initiatives.

Russian businesses follow the international trends, but their involvement with art is yet to become systematic.

The corporate collection can support a company's ESG goals and priorities – it could be a collection of young artists, regional art, or artworks where the climate and environmental agenda defines the key message.

For example, Gazprombank is collecting contemporary Russian art, from the 1990s to the present. It aims to put together a collection reflecting the recent stage in the development of our society, its artistic and intellectual environment. As noted by Ms. Sitnina, "collecting contemporary art, contributing to the creation of a heritage for the future is a corporate decision arising from the bank's social mission and directly related to the support that the bank provides to the development of culture and the enhancement of heritage in this area."

Supporting the ecosystem

Including art into the corporate ESG strategies also shapes the wealth management industry in the long term. Many services were developed to enable the growth of the art ecosystem. Even during the ongoing pandemic, when the entire art world is at a halt, banks have continued to collect, lend, and exhibit art and have sustained their arts programmes.

There are several questions to answer before starting a corporate art collection.

- How to collect?

Most corporate collections today are professionally run. When forming a corporate art collection, the responsibility extends beyond a single individual. While the management board can spell out the key message, it is up to the curators to put together a collection that will last in time and help build bridges: between the company and its employees, clients, and the local community.

- What is the purpose of the collection?

Every business that runs a corporate collection of art has to make that decision. From what we can see, such collections are rarely about the money. Companies aim to use art as a tool to define their brand and send social messages as opposed to prioritizing asset-value growth.

- How to demonstrate the collection?

With anti-COVID-19 restrictions in place, virtual formats come to the fore, such as exhibiting the collection online, participating in virtual art events, and gaining visibility on the social networks. Technologies came to rescue during lockdowns to bring the audience closer to the artists. Deloitte CIS Art & Finance team invited peers and clients on virtual tours to Russian artists' workshops, giving a sneak peek of the art world without having to leave home.

On a parting note

Corporate collecting is one of the most interesting formats where businesses and art can interact. Businesses can utilize art as a marketing and branding tool to shape the messages they want to send to the society. Art can be used to create shared values for the employees and the organization. It is undeniable that art has become an integral part of the working environment and is often covered by the corporate ESG strategies.

As noted by Ivan Kukhnin, Sustainability Services leader and a partner for Deloitte CIS, "We have seen a rapidly growing interest in the ESG agenda among Russian businesses over the last few years. We feel that ESG is becoming a strong driver of transformation, including the slow changes in the mindset of corporates and society. Looking into the future, we believe that the business community will need additional ways to communicate and structure their ESG messages and art will play a big role in that."

However, to achieve sustainable growth of the art market in Russia, it is necessary for companies to continue supporting the local art ecosystems and bring the domestic creative industries to the international professional standard.

Deloitte Russia Art and Finance team would like to thank contributors to this article: Loa Haagen Pictet, Chairman of The International Association of Corporate Collections of Contemporary Art, Head of Art, Pictet Group, Chief Curator of Collection Pictet, Marina Sitnina, Executive Vice President of Gazprombank, General Director of Art Finance, and Elena Tolchennikova, a shareholder of JART gallery, Ivan Kukhnin, Sustainability Services leader and a partner for Deloitte CIS.

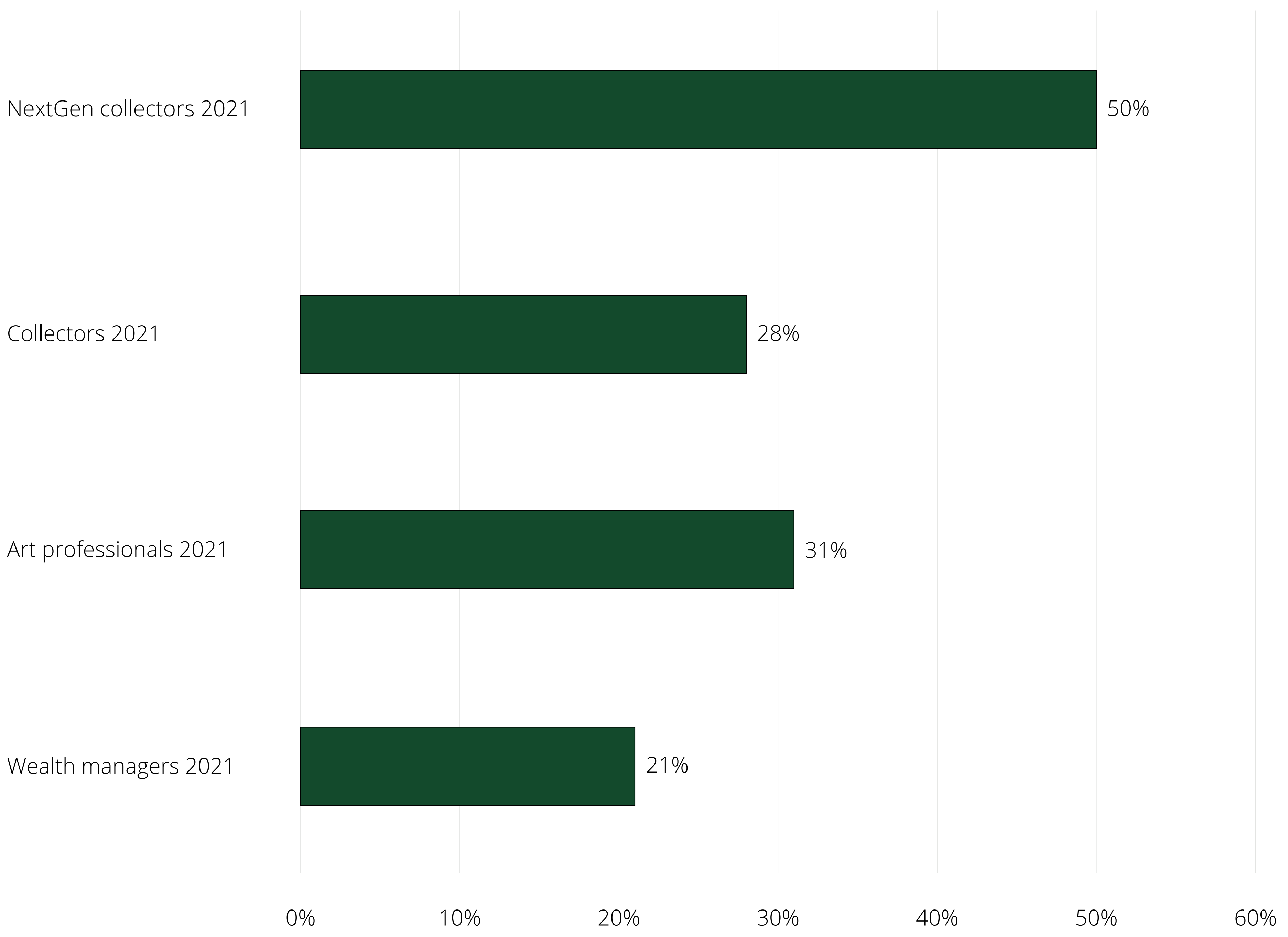
Part 1. Global shifts in sustainable investment trends

In the aftermath of the COVID-19 crisis, investors will increasingly consider environmental, social and governance (ESG) factors to mend the divisions created by the pandemic and address the shortcomings of our economies and social systems. There are many indicators that investors see social investments as an opportunity.

A recent report by Oliver Wyman and Morgan Stanley[8] projects that HNW and UHNW sustainable investments will grow by 18% per year to reach a total of US$9 trillion by 2024. In a June 2020 report[9], GIIN estimated the market size of the sustainability investment industry to be US$715 billion and growing rapidly, driven by investors determined to generate ESG impacts alongside financial returns.

The UBS June 2021 Investor Watch[10] report shows that—for now— investors are focused on something deeper: a search for meaning and purpose, alongside a desire to contribute more to the world around them.

Figure 72. Demand for social impact investment products in culture
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021



This trend is likely to keep growing as investors, predominantly younger demographics, are increasingly engaged with systemic issues like climate change and wealth inequality. In this year's survey, 28% of collectors and 31% of art professionals said sustainable impact investment in the arts is the most attractive investment model. However, this was significantly higher among younger demographics (under 35 years), where 50% said socially responsible investment products in culture would be the most interesting to them. This implies wealth managers that expand their sustainable investment offerings are well-positioned to grow the highly attractive younger client segment in the future.

On p.64, a discussion with Anna Raginskaya, Financial Advisor, Blue Rider Group at Morgan Stanley and Bloum Cardenas, Trustee, Niki Charitable Art Foundation illustrates how art and culture can benefit from the sustainable investment drive.

"Impact investing is an important concept for the arts community in general because the power of the arts drives large-scale social change and helps address some of our most important global challenges. Many artists address societal issues in their work and make publicly accessible art, which can help improve the quality of life in surrounding neighborhoods and strengthen communities."

On p.167, Therme Art, the cultural incubator of Therme Group, shares its social impact investment engagement with culture, stresses the urgent need to reimagine our cities across social, economic and environmental dimensions, and explores the role that culture plays in this.

8 Source Morgan Stanley and Oliver Wyman, 'Global Wealth Management Report 2020', p.25
9 Global Impact Investing Network (GIIN) Research Institute, 2020 Annual Impact Investor Survey, June 2020
10 UBS Investor Watch, The new valuables, Global insights: What's on investors' minds, June 2021

Anna Raginskaya
Financial Advisor, Blue Rider Group at Morgan Stanley

Bloum Cardenas
Bloum Cardenas with her grandmother, Niki de Saint Phalle. Photograph courtesy of Laurent Condominas

Expert voices

Impact investment

How art and culture can benefit from the drive towards more sustainable investment

The worlds of arts, culture, and finance collide every day in the decisions that arts organizations, particularly those with endowments, make as investors. These decisions can have major impact. In 2020, flows into US sustainable funds totaled US$51.1 billion—roughly equal to the cumulative flows of the previous decade—as concerns about social unrest, inequality, and climate change gripped investors in the wake of COVID-19.

The **Deloitte Art & Finance team** sat down with **Anna Raginskaya** of the Blue Rider Group at Morgan Stanley and **Bloum Cardenas** of the Niki Charitable Art Foundation to explore how Niki de Saint Phalle's artistic legacy, as well as her environmental and social values, are reflected in the Foundation's investment decisions. Our conversation explored the latest trends in impact investing, and what this investment approach can mean for the art community broadly.

Can you explain the term "impact investing" and how environmental and societal concerns factor into your work?
Anna Raginskaya (AR): Impact investing is a broad term that covers any form of investment that considers financial returns and impact objectives in tandem. Impact objectives vary widely, and may include supporting arts and culture, combating climate change, improving lives for low income populations, and promoting gender and racial equity.

Environmental, Social, and Governance (ESG) criteria refer to a variety of measures related to how a company conducts business beyond revenues and costs. These measures are increasingly being shared with the public, as investors consider ESG metrics a factor in identifying the companies in which they will—and will not—invest. Many investors are engaging proactively to push companies to be more sustainable and improve their ESG scores.

The Blue Rider Group is a boutique advisory within Morgan Stanley that works with non-profit organizations, foundations, and families, with a special focus on the cultural community. We leverage an open-architecture investment platform to construct customized portfolios for clients, and are committed to sustainable and impact investing by actively incorporating ESG strategies.

Nearly all of the Blue Rider Group's clients engage in some form of sustainable or impact investing. This is especially true of our philanthropic clients, who consider this investment approach to be an important tool to activate the "other" 95% of their assets—beyond the 5% they spend annually for charitable purposes—in support of their mission. In addition to addressing our clients' financial needs, we facilitate introductions between philanthropists and non-profits, raise awareness about organizations, and help support projects that strengthen the cultural community.

Why is impact investing an important concept for the arts community in general?
AR: We believe in the power of the arts to drive large-scale social change and help address some of our most important global challenges. Many artists address societal issues in their work, and make publicly accessible art, which can help improve the quality of life in surrounding neighborhoods and strengthen communities.

Our clients realize that their investment choices and support for arts and culture can have similar long-term impacts. Therefore, sustainable and impact investment approaches feel symbiotic for our mission-driven clients in the cultural community.

Why is impact investing important to the Niki Charitable Art Foundation?
Bloum Cardenas (BC): The Niki Charitable Art Foundation was created by my grandmother, Niki de Saint Phalle, and became officially active upon her death in 2002. The foundation maintains over 1,000 works and 5,000 graphic works of art by Niki, as well as her archives, intellectual property, and droit moral or moral rights, which are recognized in most European and Latin American nations, and protect artists from unwanted use, modification, or distortion of their work that may adversely affect their reputation.

Throughout her life, Niki invested in what she believed in passionately—mostly in building her art, but later also in science (because of her own health issues), AIDS research, etc. She was a great supporter and believer in science and scientists. She participated in multiple clinical trials, and also invested in a number of developing pharmaceuticals.

Her recent exhibition at MoMA PS1, *Structures for Life*, curated by Ruba Katrib, explored the many ways she defied artistic conventions, from her interdisciplinary approach to her engagement with these pressing social issues.

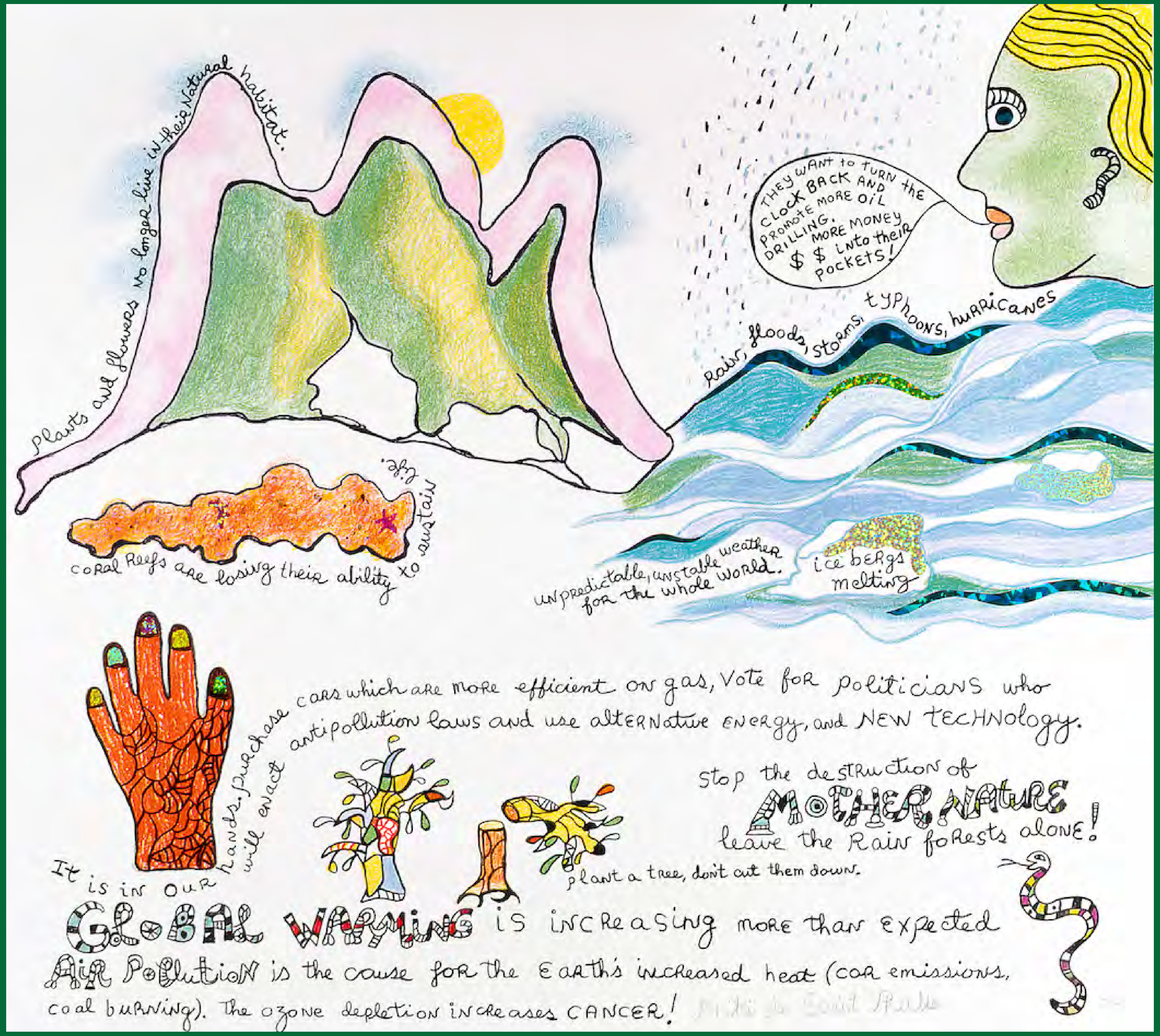
Niki provided written guidelines to help guide the Foundation's work, and the Foundation's engagement with impact investing is something that we see as a continuation of our exercise of her moral rights. We have sought out investments that are consistent with the impact objectives she pursued in her lifetime—opportunities that are environmentally sustainable, and promote gender equity and racial diversity. We are mindful that often good intentions have unexpected consequences, and are thankful to have a team helping us navigate these investments and our efforts to be a positive force.

What kinds of investment products are available to pursue impact goals related to supporting the arts community?
AR: The impact investment industry has evolved tremendously over the last decade. Today, there are many sustainable investment vehicles, across most major asset classes, which are accessible to investors of all sizes.

Our clients tend to employ some combination of three main approaches to pursue impact:

- **ESG integration**, the most common approach, which involves proactive investment in funds which select companies with the best practices on ESG compared to their peers, and prioritizes funds that take an active role with the management teams of companies in which they are invested to effect change.
- **Thematic investing**, a more solutions-focused approach that is most directly impactful, for example, providing access to capital, affordable housing, and community services for low-income populations.
- **Restriction screening**, which seeks to minimize or avoid investment in companies and sectors that are harmful. For example, many of our clients try to avoid exposure to the private prison industry.

Our clients realize that their investment choices and support for arts and culture can have similar long-term impacts. Therefore, sustainable and impact investment approaches feel symbiotic for our mission-driven clients in the cultural community.



Niki de Saint Phalle. Global Warming, 2001

With regard to arts and culture specifically, our clients currently access relevant investments through a fund which finances affordable housing projects for artists and cultural workers. We are seeing demand in the market for more tailored funds in this space—2021 is the UN Year of the Creative Economy, and we hope this also drives more development of relevant investment products.

Describe some impact investments made by the Niki Charitable Art Foundation.
BC: The fund Anna mentioned gives us exposure to a number of affordable housing projects across the US which are designed specifically for artists, with live/work set-ups, workshops and exhibition spaces. We really see this kind of investment as core to our mission and ethos. We are invested in a property like this in Southern California, not too far away from San Diego, where Niki lived for the last decade of her life, and a city that still hosts many of her public sculptures. The property is 100% affordable, and features an on-site non-profit gallery that lets resident artists show and sell their work.

More broadly, we are invested in a fund that finances essential environmental, social, and economic development projects, something we think Niki would have felt strongly about. We proactively tilt towards issuers that score high on gender diversity, looking at factors such as women in leadership positions, accommodations for working moms, workplace health and safety, and whether or not the company is a signatory of the Women's Empowerment Principles. We also look for investments that align with values of social justice: improvement in the lives of those in historically marginalized communities, and increased economic opportunity for people of color. In line with Niki's wishes, our portfolio excludes the tobacco, alcohol and firearm industries.

Is there a trade-off between "impact" and financial performance? How have ESG investment products performed over the last year?
AR: This is one of the great misconceptions about impact investing. Morgan Stanley recently published a report that looked at the performance of ESG funds vs. their traditional peers in 2020. It found that US sustainable equity funds outperformed their traditional peers by 4.3% **in 2020** (and looking back over a 30 year period, we see consistent performance of sustainable funds in line with, or better than their peers).

This isn't surprising; a company's awareness of ESG issues can be an important form of risk-management and also opportunity. Some of the companies that were most resilient to COVID-related stress, for example, had made significant progress particularly on the "S" or social piece of this equation—they built a flexible, resilient, and diverse workforce that was able to adapt quickly to the challenges presented by the pandemic. The difficult events of the past year underscored the importance of sustainability concerns for companies and strengthened the rationale for sustainable investing.

For mission—driven investors, this is really promising—investing in companies that are aligned with their values can also be very good for their bottom line.

What importance does the Niki Charitable Art Foundation believe that this kind of investment plays, not just in relation to its own endowment, but broadly?
BC: Ultimately, it is about alignment: feeling like the Foundation is operating, holistically, in a manner that's aligned with our mission and values and what Niki would have wanted. We would love to share our work with others in the hope that other foundations and arts organizations may take our lead. We are grateful to be leveraging our power to make the world a better place, not only by sharing Niki's work and philosophy with the public, but also through our choices as investors.

Mikolaj Sekutowicz
CEO, Co-Founder and Curator,
Therme Art

Ilaria Peloso
Collections and Development Manager,
Therme Art

Elena Fadeeva
Cultural Development and Partnerships Manager,
Therme Art

Case study

From wellbeing to long-lasting cultural legacy

Therme art's social impact investment

In recent years, the relationship between sustainability, arts, and culture has attracted growing interest.[11] This trend has fostered the launch of an increasing number of initiatives and research activities that aim at providing the multiple actors involved—civil society, governments, non-governmental organizations, private businesses, and investors—with innovative and dedicated solutions for the implementation of more effective and inclusive strategies to the preservation and valorization of culture[12].

In the midst of our ever-evolving social and ecological landscapes, artistic thought and production can provide the experimental ground to develop more sustainable and equitable solutions[13].

In this case study, we will illustrate how Therme Art is engaging with art and culture to create social impact and how it is responding to the trends of democratization and digitalization currently overriding the art market.

Case study: Therme Art
Therme Art is the cultural incubator of Therme Group. Responsible for outreach to creative communities, it curates forums and panel discussions on culture, science, and society. The incubator also works with internationally renowned artists and architects, as well as emerging talents, to commission and develop site-specific artistic projects that challenge the limitations of conventional exhibition spaces and redefine contemporary art viewing. Therme Art provides the resources, means, and expertise required to fulfil the visions of artists that often cannot be realized in galleries or museums, regardless of their complexity regarding production processes, installation, and long-term maintenance.

Therme Group designs, constructs, and operates the world's most technologically advanced and sustainable water-based wellness facilities. In addition to delivering landmark entertainment and wellbeing destinations, Therme integrates culture, nature, water, and technology to create natural urban oases that benefit the mental and physical health of all who visit.

Cultural expansion
The main motivation behind every project within the wide network of Therme Group is rooted in attaining social and environmental wellbeing through art and culture. The strategy underlying this approach, from a financial perspective, lies in its value as a long-term investment that defeats the ephemerality through the establishment of long-lasting legacies. This tenet is the core principle behind Therme Group's most recent cultural expansion projects.

11 EIF, Market Analysis of Cultural and Creative Sectors in Europe: A sector to invest in, 2019, p. 32
12 Deloitte Luxembourg and ArtTactic, Art&Finance Report, 2019, p. 115
13 Arts Council England, The Value Of Arts And Culture To People And Society: An Evidence Review, 2014, p. 25

In 2019, through the flying drone sculpture Franchise Freedom by Drift, Therme Art co-initiated—for the first time in art history—the creation of a joint-venture artwork. Through this cooperation between Drift, Pace Gallery, and Therme, Franchise Freedom has its own legal and economic entity to support the operation, exhibition, and promotion of the work. This case, where a company has been created around a single artwork, has brought a fresh economic model to the market.

In March 2021, Therme Art announced its strategic investment in Superblue. A groundbreaking initiative launched by Marc Glimcher and Mollie Dent-Brocklehurst, Superblue creates art centers capable of hosting large-scale experiential art exhibitions. Therme Group joined the founding partner Emerson Collective—Laurene Powell Jobs' organization that is committed to building a just and equitable world—as a pari-passu investor and resource to Superblue, adding to the unparalleled expertise in art, technology, business, and social impact reflected across Superblue's leadership team and partners.

Having launched its first public center in Miami in the spring of 2021, with installations by Es Devlin, teamLab, and James Turrell, Superblue is pioneering a new model for audiences to engage with the work of leading experiential artists outside of the traditional frameworks of museums, commercial galleries, and temporary art events. Featuring long-term installations, Superblue experiences are specifically conceived for the presentation of large-scale immersive works, where the barrier between viewer and artwork diminishes as visitors become active parts within the art itself. There are plans to reproduce this model in metropoles worldwide.

Ticketed art experiences represent a new source of income for artists, who so far have been relying on collectors mainly as financial sources. Superblue pays each artist an upfront fee to create an immersive work, as well as a royalty from gross ticket sales throughout its run. Since every Superblue artist receives funding directly from the general public, the relationship becomes more lucrative the more popular an installation becomes, aiming to emulate mass-culture businesses such as Hollywood, the pop music industry, and book publishing[14].

Experiential art has already proven to attract the interest of investors, collectors, and, most importantly, the general public. Its impact, scale, and accessibility have created a more democratic way of interacting with art, popularizing it among wider audiences[15]. This concept fully reflects Therme Art's mission—to step beyond traditional art market frameworks and bring art to our urban environments in new, innovative formats. Curated experiences are considered essential catalysts of wellbeing, as these generate an even stronger impact when shared with others.

In the words of Therme Art's Co-founder and CEO, Mikolaj Sekutowicz: "Therme Art was founded to put culture at the very heart of Therme Group's new urban development strategy. There is an urgent need to reimagine our cities across social, economic, and environmental dimensions; and culture is a key factor in this equation. Within the art community, Superblue empowers the most creative people in our society to realize ground-breaking projects that reflect the much-needed shift from an economy based solely on transactions, to an economy of cultural experiences that foster mental and physical wellbeing."

Democratization of the art market

Over the course of the last 20 years, the digital revolution has initiated a process of democratization and popularization of culture[16]. Today, those manifestations are on one side the creation of popular experiential art centers, and on the other, the creation of a huge community of micro-investors, collectors, and buyers emerging from the crypto world[17].

In response to this trend and as a by-product of the solid network of art market experts from associated business branches advising it, Therme Art has developed an impact-oriented strategy for art investment. The commissioning, planning, development, and realization of long-term, multi-media installations, often created by collectives of visual artists, sound designers, and creatives, is a complex process that requires adequate organizational and financial structures. In order to meet the above mentioned needs, Therme Art has created an independent corporate structure in Luxembourg, tailored to financing, managing, and operating intellectual property-related commissions and productions worldwide. This corporate structure allows long-term investments to flow into income-generating cultural assets that have been undervalued and underrepresented within the art market.

14 Artnet.com, "Why the Pandemic Will Actually Strengthen the Art Experience Economy—and the Old-Fashioned Gallery Business,Too", 12 April, 2021
15 The Economist, "Beyond the frame - A change in how people consume contemporary art is under way", 17 April, 2021
16 Marios Samdanis, "The impact of new technology on art", In J. Hackforth-Jones I. Robertson (Eds.) Art Business Today: 20 Key Topics, (London: Lund Humphries, 2016), pp. 164-172
17 ArtTactic, NFT Market Report, 2021, p.7

The trend towards perceiving art as an investment and real asset class can already be considered an established one on the market, and Therme Art believes that investment in the cultural sector steps beyond the financial framework. Recent trends towards democratization of the market are close to Therme's holistic vision and approach to wellbeing. Its success at addressing new audiences through the investment in Superblue, was the main inspiration for launching a new project, which would research non-fungible tokens (NFTs) and address them in Therme Art's value proposition.

Therme Art is working with the most avant-garde branches of the market to establish its new, for-profit venture, focusing on engaging new audiences, digitalization, and sustainability. Similar to ticketed art experiences, NFTs democratize the art market by opening a completely fresh, intriguing sector. NFT drops and platforms have not yet become an alternative to the traditional art market channels represented by galleries and auctions houses, however they have highlighted a community of people interested in collecting, as well as a community of digital artists. Despite the fact that the NFT market is still unregulated and volatile, the technology behind it can offer art buyers and sellers enormous benefits in terms of security, individuality, traceability, and undisputed ownership records of digital artworks, which can be easily bought in the primary and traded in the secondary markets[18].

Throughout history, technological developments have introduced new ways in which people can experience art. Being spoiled by phones and computer screens, people yearn for real-life visceral experiences[19]. This is the reason why Therme Art, in partnership with leading technology providers, blockchain experts, and institutions, is creating the first infrastructure to allow artists to design complex productions bridging all of the existing media—from painting, sculpture, video, and photography, to AR and VR and multi-sensorial experiences, and holograms. Furthermore, NFTs provide increased user and market accessibility, and thereby additional sources of income for artists, thus bringing more sustainability and balance into the existing artistic ecosystem. Whilst creating a sustainable market for digital assets, Therme Art also addresses the securing, guaranteeing, and insuring requirements necessary to make NFTs bankable assets. Technology is a key driving force behind the human evolution and Therme is aiming to connect the latest technological developments with art and artists in order to create unique experiences accessible to everyone.

Inspired by the revolutionary ideas behind the Bauhaus movement, which centered on art and design to transform all aspects of everyday life, Therme Art strives to create more sustainable environments where culture is in constant dialogue with other disciplines, creating symbiotic forms that meet the technological, social, ecological, and market demands of our times. In this endeavor, Therme Art is guided by the diverse knowledge and advice of artists, environmentalists, data experts, architects, technologists, scientists, and urban planners, and most by the communities which are directly affected by this effort. Therme believes that only through collaboration and continuous intellectual exchange can a world that is founded on human and environmental wellbeing emerge. In its restless creativity and curiosity, art can help show us the way.

18 ArtTactic, NFT Market Report, 2021, p.17
19 The New York Times, "Up to My Eyeballs in Art at Superblue", March 18, 2021

Part 2. CCS and sustainable impact investment

Despite the increasing debate about the CCS' importance, they are still lacking adequate attention from policymakers, financiers and other economic actors as they are often perceived as having little relevance to the overall economy. Despite this widespread misconception, CCS are a key growth driver in many countries and represent some of the fastest-growing sectors in the world's economy. However, the CCS' value not only lies in their direct economic impact but also in their role in spurring creativity and innovation, critical factors for adapting to the COVID-19 pandemic.

Despite this, the CCS still lack sufficient funding, which has been exacerbated by the pandemic. The following UNESCO reports have provided evidence of this situation:

- The June 2021 UNESCO report[20] "Cultural and Creative Industries in the Face of COVID-19: an Economic Impact Outlook" illustrates that the CCS have fared consistently worse than national economies overall. It is estimated their gross value added contracted by US$750 billion in 2020. Also, job losses in this field are conservatively estimated to be 10 million worldwide, a rapid drop that could profoundly affect the livelihoods of creative workers, especially freelancers who are experiencing higher levels of income loss and unemployment.
- UNESCO's second report[21] on the impact of COVID-19 on museums in April 2021 "Museums around the world in the face of COVID-19" sounds the alarm on the lack of public support for museums during this time—50% of respondents noted a significant reduction in public subsidies, in some cases as high as 40%—and stresses that, without urgent action, the place of museums in national cultural policies may be jeopardized.

In this context, Adrian Ellis, Director, AEA Consulting and Chair, Global Cultural Districts Network, discusses the need to explore new business models in the non-profit cultural sector on p.171.

Magnifico
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20 Unesco, 'Cultural and Creative Industries in the Face of COVID-19: An Economic Impact Outlook', June 2021
21 Unesco, 'Museums around the world in the face of COVID-19', April 2021

Adrian Ellis
Director, AEA Consulting and Chair, Global Cultural Districts Network

Expert voices

So much talk, so little action...

Business model innovation in the non-profit cultural sector

Whenever the cultural sector - museums, performing arts centers, concert halls, orchestras, theatre companies and the like - experiences financial difficulties, there is usually talk about the need for new business models. This is prompted both by the reality that new sources of income are needed if the sector is to continue in its old ways , and by the laxative effect that the rhetoric of financial reinvention can have on philanthropic and government funders that are otherwise leery about 'doubling down' on commitments to troubled assets. Supporting 'new business models' offers them the possibility of an exit strategy, of generating wider 'lessons for the sector', and of branding that associates their financial support with innovative thinking.

But new business models—transformational ways of arranging assets to generate new sources of income, to increase significantly existing ones, or to transform the cost base of an organization—are relatively rare in the non-profit cultural sector. This article explores why and suggests some ways forward.

Some Impediments To Business Model Innovation

The most obvious reason for a lack of business innovation in the cultural sector is that failure tends to be punished – in terms of reputation, career advancement, etc. – more vigorously and publicly than success is rewarded, and this asymmetry builds in a systemic bias toward the status quo. The structures of non-profits—unwieldy non-executive boards, restrictive regulatory frameworks that are the corollary of their tax privileges, adverse tax implications for 'unrelated business income', and pay structures that cannot easily accommodate financial incentives—all push in the same fiscally conservative direction.

A second reason is that cultural institutions rarely have the financial stamina to build reserves of risk capital for business development in the same way that they more commonly do for artistic development. Their balance sheets are unable to support investment without 'betting the house'. But any potential initiative that requires them to secure third-party funding tends to be seen internally as 'crowding out' potential funding for other purposes regarded as less speculative and more urgent. Risk capital for business development therefore needs to be very obviously *only* available for that purpose, which is why funders interested in encouraging innovation often create clearly earmarked sources of funding that are not fungible.

A third contributory factor is the priority that has been afforded to capital projects over the past few decades. This has left the sector with a high fixed cost base, in both real estate and often unionized labor, at a time when many other sectors, from publishing to taxi-cabs to music production, have pushed an agenda of technologically-driven disintermediation and sought to enjoy the nimbleness that comes with low overheads. We, meanwhile, tend to see an expanded fixed cost base as synonymous with growth—and growth as synonymous with impact.

Finally, of course, cultural executives are often conservative by both instinct and training—much of the sector's *raison d'etre* is, after all, to conserve tangible and intangible cultural assets. This fosters a particular cast of mind and disposition that is suspicious of gratuitous change.

For these reasons, cultural organizations' responses to severe financial challenges often tend to be political in nature—i.e. focusing on lobbying for resources to support the *status quo*—rather than *economic*—i.e. seeking to reengineer the business model to accommodate changed conditions. Where an organization is too big or too important to fail, this is a wholly rational strategy. Countless memoirs of arts leader's recount with satisfaction how they have lobbied governments and courted donors; while for the same reason numerous advocacy reports attempt to map the instrumental benefits of the arts on health and wellbeing, social cohesion, and the night-time economy.

However, there are grounds for thinking that political responses may have diminishing returns. The universe of politically under-written cultural institutions is shrinking as they experience multiple legitimacy crises around restitution, diversity, challenged funding sources, employment and investment strategies, and as alternative calls on philanthropic and public resources mount. At the same time, the overall financial demands of the sector have grown with its physical expansion[22].

Much organized philanthropy is moving away from the support of cultural organizations outside the context of their contribution to addressing specific social issues. US foundations have adopted the term "legacy institutions" to describe cultural organizations that represent historic commitments in their funding portfolios rather than current priorities. And while individual giving is larger than foundation support in the US, the latter is resonant in terms of thought leadership and influence. Emergency public sector support for cultural organizations—especially in the EU—has been generous during the pandemic, but this resurrection of counter-cyclical neo-Keynesian economic policy will inevitably be reigned back. Emergency funding is a stock not a flow.

The cultural sector is therefore emerging from COVID-19 with lots of talk of the need for new business models, but less action. The digital pivot is a good example. Cut off from live audiences during the height of the pandemic, arts organizations moved content online to retain—and expand—their contact with audiences. The results have been remarkable, and it probably represents a lasting adjustment to the programming agendas of many institutions. But digital capture and distribution require new investment in skills and equipment and almost none of this artistic and technical innovation has been matched by a supporting business model—the content is mostly free and, where not, income streams are generally anemic. The model is programmatically exciting and financially unsustainable.

And some reasons why they are needed

All this suggests a sector that may not be ideally positioned for the changes in the wider operating environment that it is facing. These are formidable. The West has entered a potentially extended period of rapid, discontinuous and unpredictable change with a now well-rehearsed catalogue of drivers, most of which are resistant to technocratic solutions. These include:

- Rolling low-level pandemics and their fallout for international travel, public expenditure priorities, and patterns of social behavior;
- The accelerating impact of the climate crisis on supply chains, migration patterns, civil unrest, and therefore funding priorities;
- Increased political volatility as the consensus that representative democracy is a morally and functionally superior model of governance erodes, in the process deepening divisions around the appropriate place of social and racial equity on civic and cultural agendas[23];
- Technologically-fueled changes to the labor market and leisure time (e.g. the impact of AI on automation, the impact of digital commerce on the high street and the town square etc.); and
- The impact of social media attention—and especially 'digital swarming'—on inter alia the perceived legitimacy of board members' sources of wealth, sponsors' relationship to extractive industries, and the appropriate composition of institutional endowments and the subsequent chilling of the appetite for board service and financial support from historically significant sources.

Each of these has a clear potential impact on the business model of cultural organizations[24]. A shorthand term for all this turbulence, coined by the US Army War College in the 1980s, is VUCA—Volatility, Uncertainty, Complexity, and Ambiguity. And the consensus is that the appropriate strategic response to a VUCA environment is to foster optionality, resilience, and an agile-responsive organizational culture. If you don't know what is coming around the corner, then you want to be able to keep your options open, with a business model and an organizational culture that helps ride out the next bout of turbulence rather than one inflexibly molded to the current environment.

22 See Adrian Ellis 'The Long Boom' Deloitte Art & Finance Report, 2019

23 For the culture sector this – the erosion of the liberal democratic consensus – has in turn eroded the 'arms-length' relationship between cultural organizations and governments in many countries including Britain and illiberal democracies like Poland and Hungary. Museums for example have been drawn into highly charged political debates about the appropriate breadth of historic narratives. See for example Alex Barker and Peter Foster 'The War on Woke ' The Financial Times 1 June 2021 https://www.ft.com/content/7c9c06ae-574b-43b6-88d6-7d07b6368a08

24 For more on these possibilities see Wallace Foundation and AEA Consulting 'Navigating Uncertain Times: A Scenario Planning Toolkit for the Arts & Culture Sector' October 2020 https://www.wallacefoundation.org/news-and-media/press-releases/pages/wallace-aea-consulting-navigating-uncertainties-caused-by-covid-19-planning-toolkit-press-release.aspx

From diagnosis to prognosis to prescription
A default prognosis would suggest a period of retrenchment in the face of challenges that the sector is not well-equipped to handle, with programmatic vigor sapped by the high fixed cost base that we have created for ourselves. This would be accompanied by reluctant consolidation, an increasingly strident 'political' response to financial challenges, and with artistic and operational innovation mostly bubbling up outside the administrative apparatus of established, but overburdened institutions - period of Schumpeterian creative destruction but one played out in slow motion because the absence of an integrated capital market allows inefficiencies to remain for prolonged periods. Some closures can reasonably be anticipated, but more common will be institutions of which the agendas subtly shift from their stated mission, grounded in the public good, to one of organizational survival. We already see this in the field of opera, where smaller, lighter companies dominate the creative agenda and traditional behemoths struggle to keep the show on the road.

This scenario would be a profound loss to society and economy, and an authentic exploration of new business models that are mission-congruent *and* that significantly increase new sources of income or radically cut costs is needed. But this first requires a prescription that addresses the *organizational* obstacles before identifying candidate business model options[25].

This scenario would be a profound loss to society and economy, and an authentic exploration of new business models that are mission-congruent and that significantly increase new sources of income or radically cut costs is needed.

Stakeholders—boards and funders—need to address explicitly the incentives to innovation and support informed risk-taking and its occasional failure; performance assessment needs to be more mature and objective and to reflect progress toward compelling strategic goals; arms-length enterprise subsidiaries with greater entrepreneurial freedoms should be the norm; and the unthinking linking of physical expansion to increased impact should be challenged.

The usual context in which future options are explored—and capital projects dreamt up—is that of ritualistic 'strategic planning'. This needs a radical rethink. Strategic planning in nonprofit cultural organizations tends to afford little opportunity for substantive reexamination because it is designed to produce 'outward facing' rhetorical documents, heavy with spin and virtue signaling. The plans are intrinsically 'political' in the sense described above. And they emphasize concrete – sometimes literally so – ambitions that can have simple eye-catching metrics attached to them. Lighter touch planning processes with greater analytical rigor and focus on organizational adaption to changed operating environments are badly needed. And increased reliance on earned income also begins to free organizations from coercive philanthropy in which funders' strategic objectives trump the organization's own.

And the models themselves? Cultural institutions can and do have transformative impact on local and regional economies—the rationale for much recent investment. But these benefits are externalities that the generating institutions are unable to capture. Countless new arts buildings for example have made many adjacent property developers wealthier, but this is not incorporated into their business model as the capital gains cannot be captured. If one is looking for new sources of funding, then there are devices outside the cultural sector that have been developed to capture these externalities—tax credits, landbanks, special assessment districts. They require collaboration between the public and private sector and need to be baked into strategies early, but they do offer a plethora of possibilities[26].

With respect to earned income, it is obvious that the conventional sources of earned income – admission charges, food and beverage, inhouse retail - are unlikely to have the growth potential to transform the business model. They are also, critically, not best viewed from a purely commercial perspective as there is a mission-related component to their pricing and management, relating to broadening access and enhancing the visitor experience.

The most promising areas for significant earned income are therefore in partnerships where the brand and expertise of a cultural institution is focused on a specific asset—e.g. art hotels, branded online retail, consultancy—and pursued in a framework that separates it from the core business. It may be argued that the skills required for increasing earned income in adjacent areas are difficult to secure and harness and distant from the core skills of a museum. But then, thirty years ago, one could have said the same of fundraising.

25 Mission congruence would exclude for example museums quietly selling items from their accessioned collection to meet operational needs, which US museums are under the current dispensation from their industry body AAMD
26 For an extended analysis of the tools available for value capture see Kiley Arroyo, 'Capturing Value and Preserving Identity' Global Cultural Districts Network 2020 from https://gcdn.net/wp-content/uploads/2020/10/GCDN-Capturing-Value-and-Preserving-Identity-2020-Report-Executive-Summary-Table.pdf

The COVID-19 pandemic has created an acute need for the CCS to explore new alternative sources of revenue and partnerships and to reconsider many of their traditional funding models. If culture is set to play an important role in society and sustainable development, there is an opportunity to find better ways and models for connecting impact investors with the CCS' financing needs.

It can be challenging to provide evidence and arguments for why the art and cultural sectors should be eligible for impact investing in the first place. According to a GIIN impact investor survey in 2020[27], 9% of respondents said they had directly invested in art and culture, but this only accounted for 0.1% of the sample AUM.

Culture plays an important role in society and sustainable development. Creative and cultural organizations need to **improve the ways they analyze their performance and impact.** This is particularly important in this post-pandemic period, since many art and culture organizations are struggling to stay afloat. **Measuring and reporting impact can enhance their transparency towards stakeholders, strengthen their relationships with society,** and potentially attract new supporters and donors.

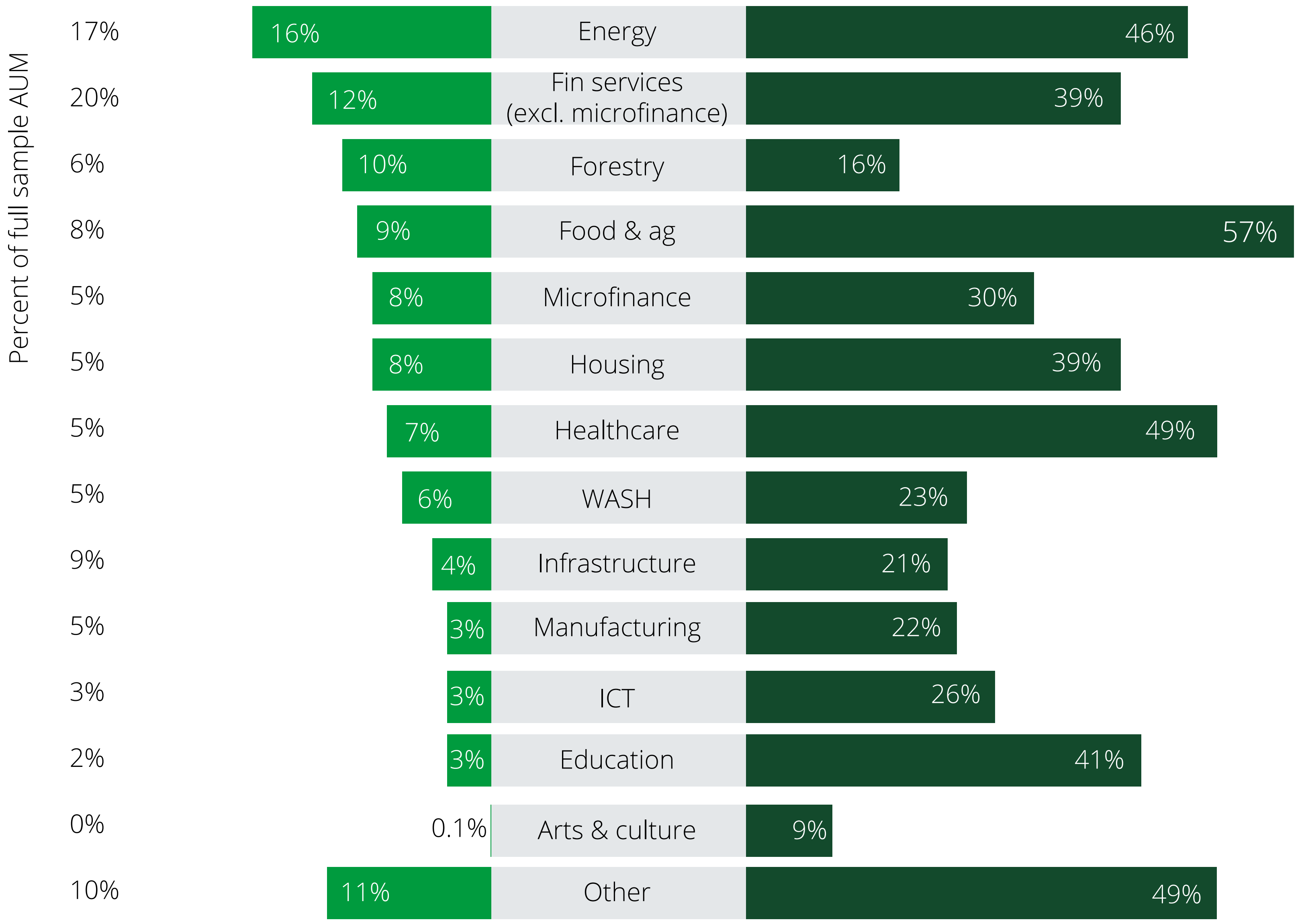
In its contribution on p.178, Deloitte Italy discusses how creative and cultural organizations can improve the methodologies they use to analyze their performance and impact, proving their accountability to relevant stakeholders.

New technologies can also support impact investment in creative and cultural organizations. Blockchain and tokenization are already being harnessed to generate new revenue streams (see also Sections 6 and 7). While the recent technological advancement in AI and network theory now allows us to analyze how cities and their networks of tens of thousands of museums, non-profit organizations and commercial galleries help spur and nurture creativity in the field of contemporary visual art. The article from Wondeur, The cultural power of cities in a global cultural market; on p.186 presents this approach and the related results for the first time.

So, can we develop financial products that aim to support the CCS? Is there a future for socially responsible investments in culture? There are signs that the impact investment market is gradually opening up for the art and culture sector. One recent initiative "Creativity, Culture, and Capital: Impact investing in the global creative economy (CCC)", a partnership between Fundación Compromiso, Upstart Co-Lab (United States), and Nesta Arts & Culture Finance (United Kingdom), aims to connect impact capital and investment to the creative economy. The following article talks more about this initiative, as well as the Cromatica initiative in Latin America.

Figure 73. Left side - cent of AUM excluding outliers; n = 289; AUM = US$221 billion. Right side - cent of respondents with any allocation to each sector; n = 294; respondents may allocate to multiple sectors.

Source: GIIN, 2020 Annual Impact Investor Survey



Note: 'Other' includes investments that did not align to these sector categories such as real estate, tourism, community development, retail, and sector agnostic investments.

27 Global Impact Investing Network (GIIN) Research Institute, 2020 Annual Impact Investor Survey, June 2020, p.33

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Case study

Art and culture in Latin America

An opportunity for impact investing

Inequality is a historical and structural characteristic of the Latin American and Caribbean societies, and it conspires against development and the exercise of rights and democratic governance. There is 1) inequality of economic means: access to and use of income, assets, and expenditure; 2) inequality of capabilities: acquisition of skills, knowledge, and abilities; 3) inequality of opportunities: access to social, economic, or political positions; 4) inequality of recognition: visibility and affirmation of individual and collective identities; and 5) gender parity despite recent progress in promoting gender equality.

Nonetheless, these are promising times for anyone in the creative economy in Latin America. The creative economy is a set of activities that, when interlinked, enable ideas to be transformed into goods and services based on, or connected to creativity and culture, with the potential to address inequality in a systematic way[28]. While much of the rest of the economy appears becalmed, creativity is continuing to experience a heady mix of dynamic growth and a proliferation of new business models, as well as stunning new technologies that are making culture even more intense and engaging[29]. Latin America is no stranger to this trend—several countries in Latin America have identified creativity as a strategic industry for economic development, with prominent cities earning a spot in UNESCO's Creative Cities Network (UCCN). Historically, the creative industries have been dominated by Argentina, Brazil, Colombia, and Mexico, though other countries such as Chile have recently begun expanding their creative products. Buenos Aires' creative sector represents more than 8.6% of the city's GDP and 9.1% of the city's workforce, while in Colombia, the creative economy accounts for 3.4% of the country's GDP. President Ivan Duque's administration has passed several laws aimed at strengthening the creative economy, such as the Orange Law and the 2018 Finance Bill, emphasizing pre-existing laws with the same objective. Mexico is the top exporter of creative assets in Latin America and the Caribbean, with its audiovisual industry in Mexico City generating almost US$15 billion. The Brazilian creative economy employs over 11 million people and is estimated to account for over 10 percent of GDP[30]. Data shows that where creativity and culture are recognized as contributing to dialogue and understanding between peoples, as empowering people to take ownership of their own development, and as the basis for innovation, they can drive inclusive and sustainable growth.

28 https://unctad.org/system/files/official-document/ditc20082cer_en.pdf
29 https://media.nesta.org.uk/documents/a-manifesto-for-the-creative-economy-april13.pdf
30 https://www.csis.org/analysis/creative-economy-latin-america

While traditional philanthropy has played a key role in continuing to encourage the growth of the creative economy, innovative artists and cultural entrepreneurs have started to connect with impact investors to support a more just and sustainable global creative economy. Impact investing is a significant pool of capital to tap into. Driving aligned valued capital, pioneering programs, and identifying opportunities to invest in Latin America's creative economy will make a positive real impact in decreasing inequality.

Case Study 1: Creativity, Culture, and Capital: Impact investing in the global creative economy.

"Articulating the future" is the motto that describes Fundación Compromiso since its creation in 1994; and the future to come finds the organization actively walking its transition into the social impact investing environment. Creativity, Culture, and Capital: Impact investing in the global creative economy (CCC) is a joint initiative between Fundación Compromiso, Upstart Co-Lab (US), and Nesta Arts & Culture Finance (UK) that aims to connect impact capital to the creative economy.

Creativity, Culture, and Capital (CCC) began with the objective of bringing together the most representative voices on how impact investment and other innovative forms of capital are working to drive equity, opportunity, and sustainability through the creative economy, and it is actually shaping the basics of a Global Creative Fund. Furthermore, the initiative means to influence an investment strategy by using a wider range of investment tools to back the arts and culture. The CCC creative system is developing the platform and conditions to connect purpose aligned capital with cultural entrepreneurs and innovative artists. Investment and markets can do better and can definitely grow and professionalize in certain regions. The expectation is to assist and support this expansion by improving creative agendas, inspiring creative portfolios, and boosting cultural markets.

It seems like an ambitious goal but it is not; the first step involved a simple research study to highlight the best investment and sustainable practices in the creative economy sector. In January 2021, a first edition of the Cambiar por Creativity, Culture and Capital Global Report was launched to celebrate the United Nations' "International Year of Creative Economy for Sustainable Development". The report pulled together a collection of essays from around the globe illustrating the need and opportunity for impact investment to maintain and sustain the creative economy. Today, the program continues to grow in a second and third volume aiming to publish 100 essays by January 2022, a year after its birth.

Creativity, Culture and Capital is creating a rich resource of geographies, sectors, and experiences, and showcases a variety of initiatives delivering positive impact through creativity and culture and the innovative ways in which value-aligned capital is employed. One of the major challenges is to bring life to the CCC system and create an active and robust community that can collaborate and manifest where the field needs to go next. Currently, experts from Brazil, Chile, Egypt, Ghana, Kenya, and Mexico, and leaders from more than 26 different countries have come together to bring a global perspective to impact investing in the global creative economy. Next steps include the development of a platform that promotes quality exchange and creates traceability and data for the sector; and the development of a feasibility analysis to launch a first pilot to model a global venture. Creativity, Culture and Capital is a program that trusts in the power of art, design, culture, heritage, and creativity to benefit people, communities, and the planet – and that impact capital is a vital tool to support its positive growth and development. The collection highlights the need and opportunity for impact investment to support renewed substantial sector growth to 'build back better' following COVID-19.

Case Study 2: Cromática
Cromática is a training program that ensures a positive impact within cultural entrepreneurs and small creative businesses in the Latin America region. Created by Alterna, it identifies entrepreneurs and small growing enterprises (EPECs) belonging to the creative economy, with the potential to impact and, consequently, attack inequality in a systemic way. The program aims to close structural gaps by guiding EPECs in building more robust business models and encouraging them to integrate social impact into their products, services, and/or processes.

Alterna measures the social impact on people, communities, and the environment, evaluating the analysis and cross-checking of indicators collected through surveys and baselines with other variables. This process provides an understanding of the degree of sales and employment growth for companies, as well as the social and environmental impact generated after being part of a program or project.

In 2018, thanks to the collaborative work between mentors, curators, and allied specialists from the creative industries, Cromática strengthened the first cohort of 20 companies—the group was diverse: sustainable fashion, food festivals, publishing houses, digital applications for education, and film production. Cromática soon experienced success. Three years after the end of the program, the nomination of La Casa de la Producción for the Golden Globe® Awards filled Alterna with pride. A Guatemalan film production company that, driven by determination and courage, consolidated its business model with the film, La Llorona. Indeed, production sets, filming, and financing seem like fairly standard business models for most developed countries; however, it becomes a story of impact for countries with a virtually non-existent film sector.

The second edition of Cromática will be launched in September 2021 and is divided into four stages:

1. Identify 100 creative economy companies with the potential to grow and generate impact in Latin America through a call for proposals;
2. Accompany the identified companies through digital workshops and select the top 20 for a six-week, high-level coaching program focused on marketing and finance to design strategies for commercial growth and impact;
3. Nurture the ecosystem and increase the social capital of the cultivated companies, connecting them to high-level mentoring impact investors and their markets;
4. Finally, design and implement PR and communication strategies that give the sector and companies a unique positioning.

Alterna is also committed to providing financing in line with the needs of the EPECs. Therefore, with the support of B-Lab and Argidius foundation, it has launched the Catalyzer Fund as an innovative solution with flexible repayment conditions and credit tickets between US$10,000 and US$50,000, having placed more than US$600,000 in 22 companies. A new regional approach is possible thanks to additional funding from ADA funding from the Luxembourg-based NGO, ADA (Appui au Développement Autonome). Companies cultivated by Cromática will be able to apply to this fund, therefore closing the circle of promoting, enhancing, and investing in the arts.

Creativity and the arts are critical elements to finding the solutions to the systemic challenges that the world faces today. According to UNESCO "the creative economy has grown to become one of the great powerhouses of our times"[31]. It is among the most rapidly growing sectors of the world economy, generating nearly 30 million jobs worldwide and employing more people aged 15-29 than any other sector[32]. For those ready to participate in creating a better world through impact investing, the inclusion of arts and creativity are essential to the investment process and understanding that impact investing is an important new tool in building the more sustainable world many are eager to contribute to. Initiatives such as Cromatica and Creativity, Culture and Capital expect to continue to promote a global traction to boost growth and jobs in the cultural and creative sector and to contribute to its further growth.

31 https://en.unesco.org/news/cutting-edge-creative-economy-moving-sidelines
32 Creativity, Culture and Capital: Why Impact Investors Should Recognize the Untapped Potential of the Global Creative Economy: https://nextbillion.net/impact-investors-global-creative-economy/

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Expert voices

Social impact of culture: measuring for improving

New strategies for a more sustainable future

Now, maybe more than never in contemporary human history, **arts and culture need innovative strategies and models to continue generating value for society and people, enhancing their impact and moving towards sustainable development**. In particular, reporting frameworks, coherent with ESG topics – aimed at measuring and disclosing the impacts of cultural and creative organizations – may strengthen the relations with relevant public, private and investor stakeholders and contribute to improve transparency. Measuring impacts can also support in reflecting on "where we are" and thus "where we want to go". This brief paper aims at synthetically exploring the most common guidelines and standards that cultural institutions may use in these fundamental activities.

Many studies have recently focused on deepening **the impact of culture**[33], due to the recognition of the benefits arising from cultural participation, including **well-being, social inclusion** and **engagement**. Culture has the power to create decent jobs and economic growth, reduce inequalities, and build more peaceful and inclusive societies, by promoting the value of **diversity**.

The international community has also recognized the role of culture as a driver of sustainable development: the **Agenda for Sustainable Development** unanimously adopted by UN Member States in September 2015, comprising 17 Sustainable Development Goals (SDGs) and 169 specific targets, includes several explicit references to **cultural topics**[34]. Cultural organizations represent a key **driver for social change** oriented towards sustainable development, providing a platform for public debate and education.

The spread of the COVID-19 pandemic that has affected millions of people and generated a sudden and substantial impact on global economy and community, changing – probably forever – some of our common habits, has also **profoundly hit the arts and cultural sector**. The global health crisis, the uncertainty resulting from it, and the safety measures implemented all over the world have generated many difficulties to cultural and creative organizations. **The art system that we used to know**, made up by continuous events, fairs, auctions and exhibitions that made art professionals and enthusiasts travelling from a country to another to join unmissable networking-moments, **was forced to stop**. In this respect, the Next Generation EU Program, reconfirm the central role of culture in the recovery of the EU States.

33 Among others: Throsby, D. 2003. "Determining the Value of Cultural Goods: How Much (or How Little) Does Contingent Valuation Tell Us?", Journal of Cultural Economics 27 (3/4):275–85; Belfiore, E. 2015. "'Impact', 'Value' and 'Bad Economics': Making Sense of the Problem of Value in the Arts and Humanities.", Arts and Humanities in Higher Education 14 (1):95–110; Azmat, F., A. Ferdous, R. Rentschler, and E. Winston. 2018. "Arts-Based Initiatives in Museums: Creating Value for Sustainable Development.", Journal of Business Research 85:386–95

34 In particular, SDG 11 aims to ensure that the cities of tomorrow are "inclusive, safe, resilient and sustainable" and target 11.4 focuses on protecting and safeguarding "the world's cultural and natural heritage". Moreover, the Agenda aims to ensure "inclusive and equitable quality education and promote lifelong learning opportunities for all", highlighting the importance of culture for sustainable development.

Nevertheless, these organizations have shown great **timeliness and innovation** in the reaction against this unprecedented social and economic crisis, by fostering digitalization to continue to grant access to cultural goods, and trying to re-think their – sometimes-obsolete – business models and strategies. Efforts have been rewarded by the great participation and interest of the public, and the shared recognition of the **power of arts in *"bringing people together, inspiring, soothing and sharing"***[35]. Culture has provided moments of comfort during self-isolation periods, hope for a better future, and something in which everyone could recognize himself, rejoining society from the loneliness of their homes.

In this context, the cultural and creative sectors have the opportunity (and maybe the duty) to **re-think their strategies, looking for more suitable – *and more sustainable* – approaches to events and other activities.** The aim should be creating **instruments to prove accountability to relevant stakeholders,** but also to self-analyze the current and generated impacts, in order to improve performances for the sake of society.

There is still a lack of knowledge of impact measurements and guidelines on how to measure and assess impact[36], which could help in **increasing the social value generated by arts and culture**. Yet cultural and creative organizations could take inspiration from the profit and industrial sector and start with the **implementation of reporting activities,** aimed at analyzing their sustainability performances both from an economic point of view, and from an environmental and social point of view (ESG topics). Reporting activities represent the basis for measuring the impact, and constitute a **precious source of consciousness and awareness of the "status quo"** of the organization itself, for understanding the efforts needed to improve.

Cultural and creative organizations can refer to broadly known specific standards and guidelines aimed at monitoring, reporting and evaluating their impacts on society, such as the GRI Standards, the internationally recognized sustainability reporting standards[37] published by the GRI (Global Reporting Initiative)[38]. These Standards are aimed at creating *"a common language for organizations – large or small, private or public – to report on their sustainability impacts in a consistent and credible way"*, thus enabling organizations to be transparent and accountable with their stakeholders. Reports drafted in accordance to GRI Standards, or by reporting a selection of the Standards, must focus on what is relevant for the organizations and its stakeholders, providing *"an inclusive picture of material topics, their related impacts, and how they are managed"*[39]. Other sustainability reporting standards and guidelines, such as the Integrated Reporting Framework published by the International Integrated Reporting Council[40], or the *Sustainable Accounting Standards Board (SASB) Standards*[41] published by the SASB Standards Board, may also be considered.

These common guidelines and standards may be enriched by more specific KPIs[42], developed according to the organization's characteristics. These KPIs can be defined also by **taking inspiration to other internationally recognized frameworks,** such as the *UNESCO Thematic Indicators for Culture in the 2030 Agenda **(Culture|2030 Indicators)**.* This framework of thematic indicators aims at measuring and monitoring the *"progress of culture's enabling contribution to the national and local implementation of the Goals and Targets of the 2030 Agenda for Sustainable Development"*[43]. **Reporting activities may also be improved by analysis conducted with impact measurement methodologies,** such as the Social Return on Investment[44], which Guide was originally written in 2009 by the UK Cabinet Office to provide a clear framework for anyone interested in measuring, managing and accounting for social value or social impact. The Guide, updated in 2012, offers an overview of a complex methodology that is still being developed. This methodology may be used for measuring the **impact of an entire organization, but also of specific projects and initiatives,** providing a way for stimulating supporters and donors to sustain the organization's activities.

35 Ganz, E., "Even during COVID-19, art 'brings us closer together than ever' – UN cultural agency" in UNESCO News, 15 April 2020, https://news.un.org/en/story/2020/04/1061802
36 Marjelle Vermeulen & Karen Maas (2021) Building Legitimacy and Learning Lessons: A Framework for Cultural Organizations to Manage and Measure the Social Impact of Their Activities, The Journal of Arts Management, Law, and Society, 51:2, 97-112, DOI: 10.1080/10632921.2020.1851839
37 "GRI (Global Reporting Initiative) is the independent, international organization that helps businesses and other organizations take responsibility for their impacts, by providing them with the global common language to communicate those impacts. We provide the world's most widely used standards for sustainability reporting – the GRI Standards." Source: GRI website: https://www.globalreporting.org/about-gri/
38 GRI website: https://www.globalreporting.org/standards/
39 For further information, please refer to the website: https://integratedreporting.org/resource/international-ir-framework/
40 For further information, please refer to the website: https://www.sasb.org/
41 Key Performance Indicators
42 Source: https://whc.unesco.org/en/culture2030indicators/
43 Source: Social Value UK website, https://socialvalueuk.org/resources/sroi-guide/
44 Source: European Commission website, https://ec.europa.eu/info/business-economy-euro/company-reporting-and-auditing/company-reporting/corporate-sustainability-reporting_en

European Commission (EC) is also committed in developing rules aimed at increasing the transparency of organizations. Currently in force European law, under Directive 2014/95/EU – also called the Non-Financial Reporting Directive (NFRD), requires *"certain large companies to disclose information on the way they operate and manage social and environmental challenges. This helps investors, civil society organizations, consumers, policy makers and other stakeholders to evaluate the non-financial performance of large companies and encourages these companies to develop a responsible approach to business"*[45]. Yet, EC recently adopted a proposal for a **Corporate Sustainability Reporting Directive (CSRD),** which would amend the existing reporting requirements of the NFRD. The proposal extends the scope to all large companies and all companies listed on regulated markets (except listed micro-enterprises), requiring the assurance of reported information, and also introducing more detailed reporting requirements, including a requirement to report according to mandatory EU sustainability reporting standards. The new reporting framework will focus on the concept of double materiality, encouraging organizations to consider both the impact of ESG topics on the organization's value, and the organizations' impact on the environmental, social and economic context in which they operate.

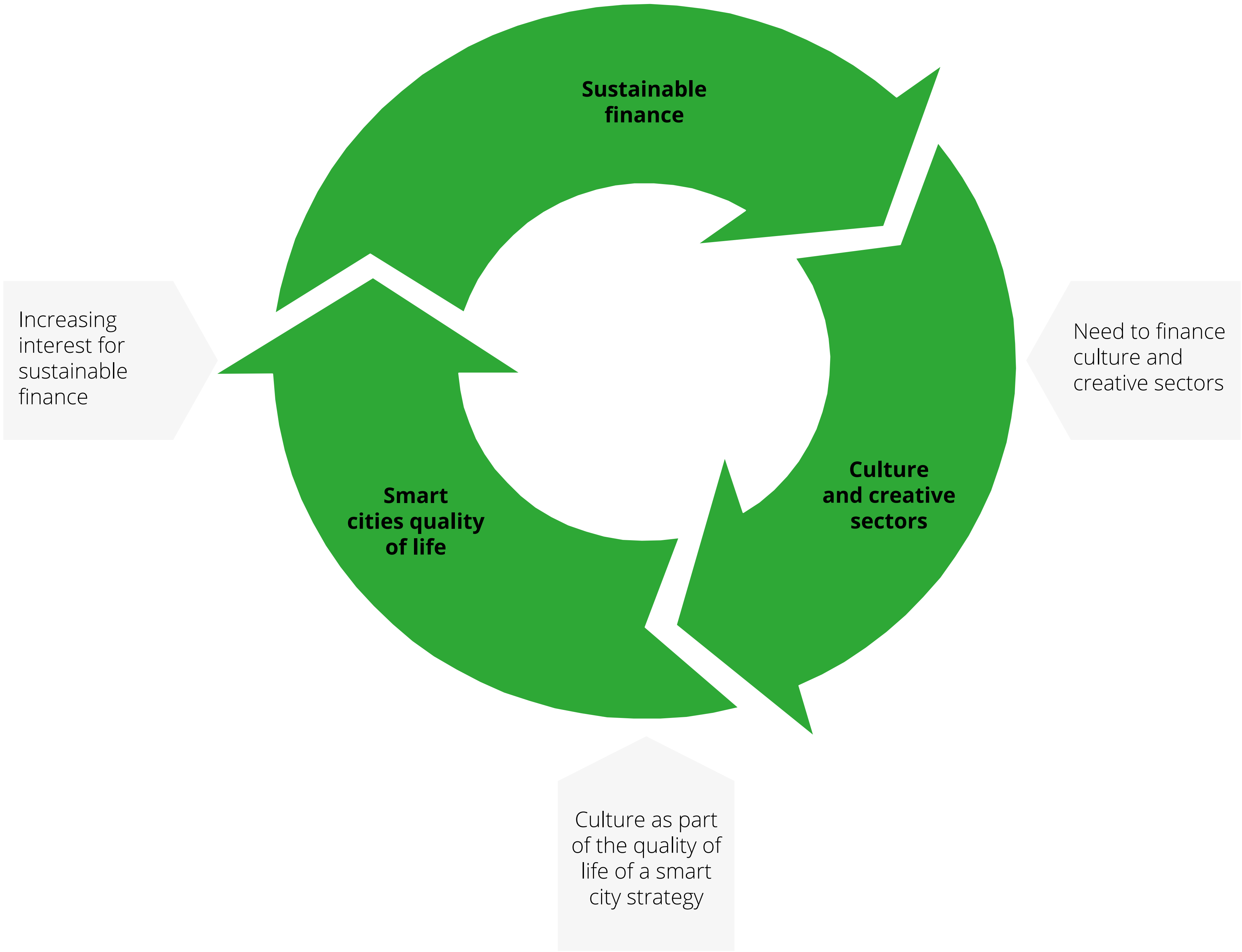
The above-presented context is strictly related to the increasing interest in **Environmental, Social, and Governance (ESG) investing, socially responsible investing (SRI), and impact investing:** a growing number of investors want to make a positive impact on society and the world at large, by investing their money. Without deepening the differences between these terms, it is clear that methodologies for measuring impacts are needed for investing strategies which include ESG factors, or which are aimed at helping an organization to complete a project or develop a program that benefit society.

In conclusion, since **culture plays a great role for society and sustainable development,** creative and cultural organizations need to **improve the methodologies through which they analyze and disclose their performances and impact.** This is particularly important in this post-pandemic period, since many of those organizations are struggling for remaining "alive" and relevant attention by the EU government has been dedicated to culture in the NGEU Program. **Reporting and measuring can enhance transparency towards stakeholders and strengthen relationships with society,** potentially favoring the engagement of new supporters and donors. These activities may also represent a **starting point for a self-analysis of the "as-is" situation**, in order to understand **how to improve, to define goals and target**, and to understand the actions needed for the benefit of society and of the world as a whole.

"since culture plays a great role for society and sustainable development, creative and cultural organizations need to improve the methodologies through which they analyze and disclose their performances and impacts"

45 The EC mandated the European Financial Reporting Advisory Group (EFRAG) to develop draft EU reporting standards in close collaboration with international initiatives such as GRI, TCFD, SASB, IIRC, CDSB and CDP. Source: Deloitte Luxembourg, CSRD: cornerstone of EU's sustainable finance strategy for quality investor ESG data, 24th June 2021, https://www2.deloitte.com/lu/en/pages/investment-management/articles/csrd-cornerstone-eu-sustainable-finance-quality-investor-esg-data.html?id=lu:2sm:3li:4Performance%2036::6fsi:20210624120000::5040404021:5&utm_source=li&utm_campaign=Performance%2036&utm_content=fsi&utm_medium=social&linkId=122227285

Part 3. Reinventing smart cities through culture



Another recent key development is the concept of smart cities. Culture and impact investment could be influenced by the role culture could play in a smart city strategy.

In this century, we can expect to see cities around the world that are enabled, powered and integrated by digital technologies. However, these smart cities will need to include more than just infrastructure and city services. An over-reliance on technology to drive urbanization could fail to attract citizens because the importance of culture was overlooked. The inadequate vision of urban sustainability, which often emphasizes economic and environmental indicators, can fail to grasp culture's vital role as a social glue and in creating thriving urban centers.

There is an increasing realization that urban smart cities must combine both technology and culture, because improving quality of life does not only require technology; it is also a question of connecting and inspiring people.

Pierluigi Sacco, Professor of Cultural Economics, Rector Delegate for European Projects and International Networks, IULM University, Senior Researcher, OECD - CFE/LEED and Valentina Montalto, Policy Analyst, European Commission discuss the role of culture and smart cities in their article on p.183.

As an example of the important role that the CCS play, Abu Dhabi government recently announced[46] it plans to invest US$6 billion in culture and creative industries for economic diversification.

As another example Victor Lo, chair of the M+ Board in Hong Kong, said:

"A truly great city needs to be more than a business powerhouse or a major tourist hub. The world's greatest cities inspire and enrich their residents and visitors, provide new ideas and the environment for creativity and innovation to thrive. M+ was our vision for what a 21st-century cultural institution in Asia could be, offering a Hong Kong perspective on global visual culture. That also meant creating a unique, world-class platform in Asia to foster exchange between Hong Kong and the world. Our mission for M+ was that it would also be a place to show our neighbors from the Greater Bay Area, South East Asia and all international visitors that Hong Kong has a vibrant cultural life on top of it being a business metropolis."[47]

46 The National News (www.thenationalnews.com), 'Abu Dhabi to invest $6bn in culture and creative industries amid economic diversification push', 8. June 2021
47 Victor Lo, Charman of the M+ Board, 'Why culture is key to Hong Kong's future as a world city', The Art Newspaper, 22.April 2021

With the growing recognition that CCS can support cities to become "smarter", more sustainable investment products may develop such as for example, the issuance of European Culture Creatives Cities impact bonds.

The advent of associations like the Global Cultural Districts Network (GCDN), which brings together diverse leaders in culture and urban development around the world, is also a testimony to the increasing importance of culture in urban planning.

With the growing recognition that CCS can support cities to become "smarter", more sustainable investment products may develop. For example, the issuance of European Culture Creatives Cities impact bonds, as mentioned in the Pier Luigi Sacco and Valentina Montalto article p.183, could soon become a reality. These cultural impact bonds could help develop a new generation of smart cities that can successfully integrate culture and creativity within an inclusive and sustainable urban growth strategy, whereby repayment of investments in culture and creativity would be subject to social and not simply financial impact. As an example, in 2018, Colombia issued its Naranja bond with the support of the Inter-American Development Bank[48] to finance its creative sectors.

Research into smart cities tends to focus on technology, architecture and infrastructure. However, an academic research paper called Art in Smart Cities[49], co-written by Marine Tanguy – CEO MTArt Agency[50] and Vishal Kumar – Centre for Advanced Spatial Analysis, The Bartlett, UCL, United Kingdom, highlights the importance of public art projects for our future cities and demonstrates that transforming cities through art is economically sustainable.

Although little empirical evidence and academic studies exist that measure public art's impact and role regarding its citizens, the aforementioned academic research collected data from two public art initiatives organized by MTArt Agency. Of the audience surveyed, 60% were willing to pay at least GBP 5 to have more public art in their local area; 84% were willing to pay at least GBP 2; and 84% said regular public art initiatives would increase their wellbeing. The findings suggested that Londoners were willing to pay for more public art in their local area.

It is essential that we better understand the economic and social value of public art initiatives in smart cities, because it will allow policymakers, planners and developers to better implement these initiatives in the future. With the increasing recognition that culture contributes to smart cities' quality of life and economic prosperity, it is also important to reinforce the need for innovation and the creation of financial products and services to support the CCS going forward.

Rosalina
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48 Banco Interamericano de Desarollo (BID), 'Colombia emite el primer bono naranja, con apoyo del BID', 29. November 2018
49 Tanguy, Marine & Kumar, Vishal, 2019. "Measuring the extent to which Londoners are willing to pay for public art in their city," Technological Forecasting and Social Change, Elsevier, vol. 142(C), pages 301-311
50 Founded in 2015, MTArt Agency is a certified B Corp® award-winning talent agency for the most exciting up and coming visual artists worldwide, and a creative agency that delivers exciting art-driven projects for public, private and cultural organizations around the world. Certified B Corp. B Corporations are a new kind of business that balances purpose and profi

Pierluigi Sacco
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Expert voices

The creative city dilemma

Why creativity can kill cultural vitality and how to raise sustainable creative cities

Are cultural cities also creative ones? Evidence—which we will discuss here—from the European Commission's Cultural and Creative Cities Monitor (CCCM) shows that this is still little more than 'wishful thinking'.

There is a kind of turning point, beyond which creative cities are at risk to become simply inaccessible to young and promising, but often low-income, cultural and creative professionals. To prevent this unintended consequence, cities need to carefully consider the potential fallacies of the creative city paradigm, integrating cultural diversity and social cohesion issues in their smart urban strategies.

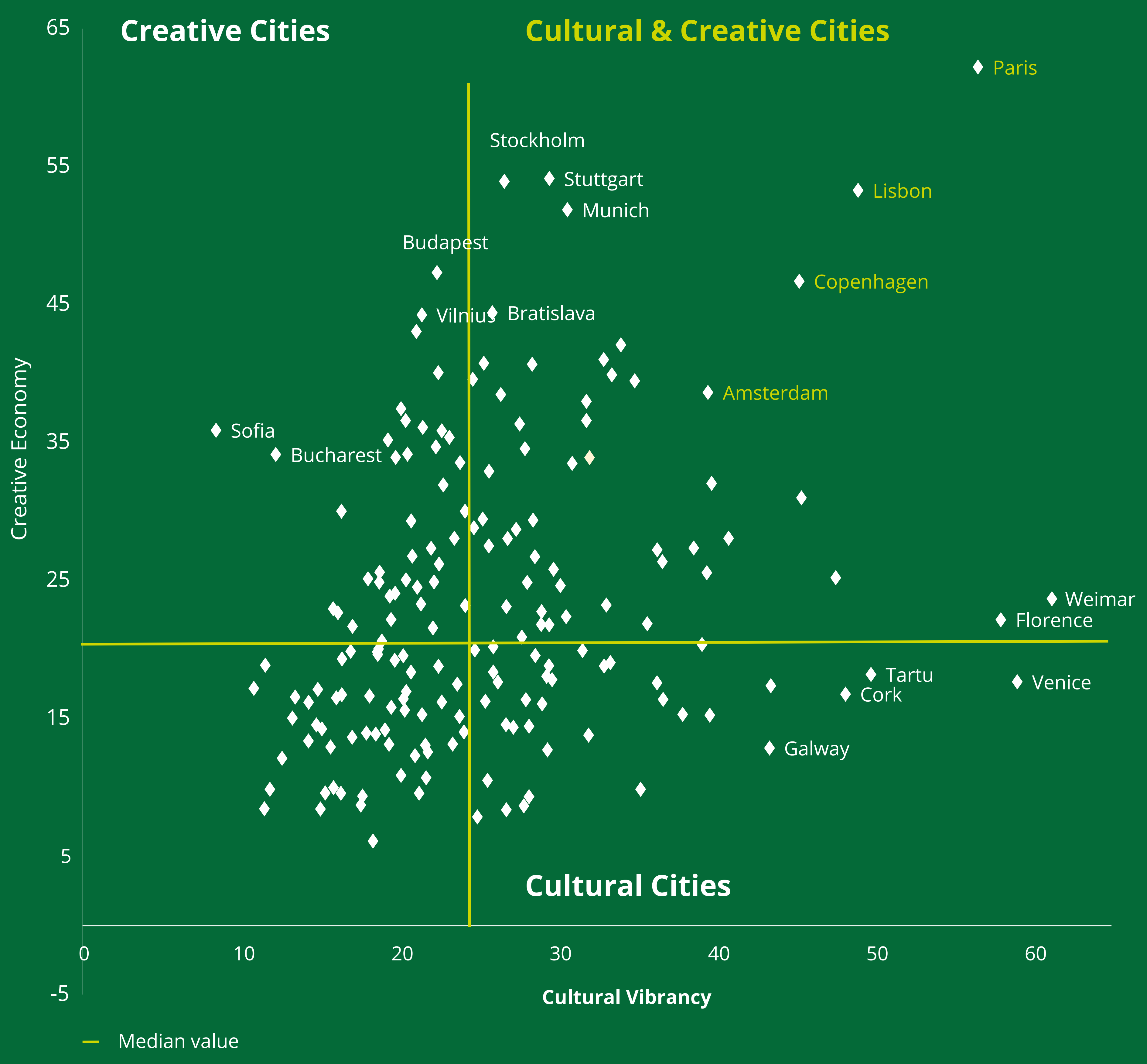
It is generally thought that culture and creativity are a powerful engine of economic and social growth, and this is all the truer for smart cities, which have the ambition to become global magnets of top talent and skills. The well-known creative class paradigm proposed by Richard Florida identifies the attraction of cultural and creative talent as one of the key drivers (if not the major one) in the long-term competitive success of cities, although there is now a growing awareness, as Florida himself recognizes, that social cohesion and inclusion are an equally important, critical condition for sustainable development. Failing to acknowledge this may easily backfire, turning promising, thriving cultural cities into exclusive 'golden preserves' that are basically inaccessible to young, low-income, but promising creative professionals.

These remarks suggest, contrary to what is commonly held, that there is no mechanical identification between a thriving urban creative economy, as measured in terms of GDP size, and a vibrant cultural scene, as measured in terms of the social, ethnic, and cultural diversity of the local cultural players. It may well be the case that a city manages to become a powerhouse in terms of its productive potential and competitive performance, but that, as a consequence of this success, it also becomes an increasingly inaccessible venue in terms of cost of living and availability of opportunities for younger and would-be creative professionals, slowly undermining its long-term positioning.

The most practical tool to test these intuitions on the basis of real data, at least for European cities, is the Cultural and Creative Cities Monitor (CCCM). The CCCM has been developed by the European Commission's Joint Research Centre (JRC). It features 29 culture-specific indicators for 190 cities in 30 European countries (EU-27 plus Norway, Switzerland, and UK) which have been selected using three internationally comparable criteria:

- Cities that have won or have been shortlisted for the title of European Capital of Culture;
- UNESCO Creative Cities; or
- Cities that host at least two major permanent cultural festivals.

Figure 74. Creative vs. cultural cities in Europe
Note: Scores are given on a 0-100 scale, where higher scores signal better performance. For methodological details see: https://composite-indicators.jrc.ec.europa.eu/cultural-creative-cities-monitor/docs-and-data



These indicators help us to measure the various aspects of cities' cultural and creative milieu, spanning the full size range from global metropolises to small, dynamic towns. Its objective is to support the development of evidence-based policies by providing policy makers and researchers with a solid and comparable evidence base, while keeping into account the specific socio-economic characteristics of each single city. In particular, the CCCM is able to identify actual strengths and areas of possible further development across peer groups of cities with comparable populations, income levels, and employment rates.

In addition to the 29 culture-specific indicators, the CCCM analyzes higher aggregate levels, as obtained by means of weighted averages: nine dimensions, three sub-indices, and a global index. And it is at the sub-indices level that our question may receive a meaningful answer by means of the CCCM database. The three sub-indices are:

- Cultural vibrancy, which measures a city's endowment of cultural infrastructure and its capacity to attract audiences;
- Creative economy, which assesses urban creative economies in terms of key indicators such as cultural and creative jobs, patents and new designs; and
- Enabling environment, which gauges the incidence of a number of tangible and intangible assets whose nature is not strictly cultural, but that strongly facilitate a city's dynamic positioning as a cultural and creative hub, such as human capital, openness, tolerance and trust, local and international connections, and quality of governance.

Not all successful cultural cities leverage upon the same competitive factors. Actually, the mix can be very different. Certain cities mainly leverage upon their cultural vibrancy (such as Paris or Lisbon). Others build on the size of their creative economy (such as London or Milan). Other cities have their main asset in the quality of their enabling environment, and in this regard UK cities, including medium-sized and smaller ones, are the uncontested leaders at the European level.

Designing policies that reflect the peculiarities of the specific urban environments is crucial. For instance, the limitations to the UK-directed inflow of international talents that have ensued from Brexit seriously threaten UK cities' future leadership and competitiveness by undermining their main asset—an issue that cannot be solved by selective immigration rules, in that young, would-be creative professionals often lack strong educational titles and generally start their careers supporting themselves through humble day jobs. Ergo, these would-be professionals have profiles that are easily skimmed away by the new UK selective immigration rules.

It is therefore important not to think of culture and creativity just as a one-dimensional driver, but to develop a more nuanced picture. The issue of the potential trade-off between creative economy and cultural vibrancy may be explicitly analyzed through the direct comparison of the two sub-indices at the European scale. The result is shown in Figure 1 for all the cities in the CCCM.

As it is easily seen from Figure 1, and contrary to what may be expected, there is no simple, positive correlation between the size of the creative economy and the cultural vibrancy of a city. There are of course many cities that excel on both indicators, but there are also many others that perform above the sample average on one scale, but under average on the other. And even within the cities that do well on both dimensions, there is not a clear hierarchy, as also in this case we find cities that do relatively better on one side than on the other, confirming the principle that each city has its own specific mix. For instance, Stuttgart, Stockholm, and Munich, while excelling on both dimensions, are much more creative than cultural, whereas in the same category Florence and Weimar are way more cultural than creative. Sofia and Bucharest are excellent on the creative side, but below average on the cultural. Vice versa, Bruges and Venice are excellent on the cultural side, but below average on the creative.

What this data tells us is that there is no simple recipe to help a city thrive by means of culture. Strategic goals may differ: one may be more interested in direct economic impact (so that the size of the creative economy is the primary concern), or in making culture a cradle of future creative talent (so that we should instead look at cultural vibrancy), or else we could decide that what we really need from culture is to strengthen our city's social cohesion and openness (in which case our main reference is the enabling environment).

So far, this conditional logic has been largely missing from most recent urban strategic visioning that has chosen culture as a main driver of change and prosperity. This may lead to disappointing outcomes, as the main strategic tradeoffs are ignored and unintended consequences materialize, with the undesirable result of blaming culture for what has in fact been poor strategic understanding of its potential and workings. If, on the contrary, we think of culture not as a 'magic wand', but as a complex, multi-dimensional playground which requires clear understanding and clear-cut strategic choices, there is the possibility of making of it a game changer at the urban scale, as the most successful examples of culture-driven urban development show us. Because at the top of the CCCM rankings in the various dimensions we find not only the usual suspects such as London, Paris, Milan, or Amsterdam, but also cities like Karlsruhe, Lund, Tartu, or Galway—which are not the first that come to mind when we think of the typical European cultural city—as well as well-known heritage cities such as Florence, Weimar, or Avignon. As we see, there are many different successful models, and this, essentially, means one thing: that every city can reasonably aspire to become a thriving cultural city, if only it is able to fully express its own potential and to build its own, highly specific mix.

The season of 'cultural magical thinking' of urban planners is over. Now is the time to venture into a new, more promising season of evidence-based, transformational cultural thinking that helps raise a new generation of smart cities, which successfully integrate culture and creativity in inclusive and sustainable urban growth strategies. European CCC impact bonds could widely serve this purpose, whereby repayment of investments in culture and creativity would be subject to social and not simply financial impact—from raising and retaining creative talent to addressing educational poverty to improving mental health through art and culture. A tool that would put creative cities at the forefront of social policy goals.

Expert voices

Author: Wondeur.ai Team

The cultural power of cities in a global cultural market

The creative economy is a growing contributor to national GDP; it empowers cities to attract talents, to spur innovation and to foster inclusive development and well-being. Musical creativity and cinematographic and literary inventiveness are, alongside contemporary visual arts, the beating hearts of this creative economy.

Recent technological advancements in AI and network theory are now making it possible to analyze how cities and their networks of tens of thousands of museums, non-profit organizations, and commercial galleries help spur and nurture creativity in the field of contemporary visual art.

The following analysis is an extract from an investigation of the cultural power of 3,000+ cities by Wondeur AI. It summarizes the findings for 15 cities across the following key dimensions:

- **Impact** represents the contribution of a city and its network of art institutions (commercial and non-commercial galleries, artist run centers, private and public museums, etc.) to both the artist's cultural recognition and the intrinsic value of their work;
- **Performance** is a measure of the curatorial quality of a city and its network of art institutions;
- **Risk appetite** is a measure of a city's tendency, with its network of art institutions, to showcase artists earlier than other cities; and
- **'Nesting hub'** is a measure of the contribution of each city to the creation of new star artists in the last 20 years.

This is the first step in measuring the cultural power and influence of cities on a global scale. We are looking forward to deepening this analysis in collaboration with cultural players in the years to come.

Results

Table 21. Global rank impact
'Global ranking of city impact' represents the impact of a city and its network of art institutions (incl. commercial and non-commercial galleries, artist-run centers, private and public museums, etc.) on both the artist's cultural recognition and the intrinsic value of their work.

Impact calculation is based on a measure (from 2010 to 2021) of each institution's contribution to the growth of the artist's cultural recognition and to the changes in the artist's intrinsic value.

For the signals considered, please refer to the methodology section.

Cities	Impact on all artists	Impact on female artists
New York	1	1
London	2	2
Paris	3	3
Los Angeles	4	4
Berlin	6	6
Madrid	12	15
Sydney	14	11
Amsterdam	15	26
Moscow	28	29
Mexico City	44	63
Tokyo	46	83
Milan	51	36
Beijing	86	125
Shanghai	101	84
Rio de Janeiro	125	61
Cape Town	269	201

Source: 2021 Wondeur.ai

Table 22. Global rank performance (over the last five years)
'Global ranking of a city's performance' measures the curatorial quality—calculated by measuring the growth of artists within three years of being shown or collected—of its network of art institutions.

This analysis is based on the measure of each institution's performance in a city per artist category from 2015 to 2021.

For the signals considered, please refer to the methodology summary

Cities	Performance for emerging artists	Performance for established artists	Performance for celebrated artists	Performance for star artists
New York	1	1	1	1
London	2	2	2	2
Los Angeles	4	5	5	5
Beijing	5	8	31	41
Berlin	6	3	3	4
Paris	7	4	4	3
Tokyo	8	20	24	18
Shanghai	9	6	30	31
Cape Town	23	23	35	79
Amsterdam	24	30	26	22
Milan	40	12	17	12
Madrid	43	18	13	14
Rio de Janeiro	53	52	59	40
Mexico City	56	19	14	20
Sydney	81	43	41	45
Moscow	87	73	34	86

Source: 2021 Wondeur.ai

Table 23. Global rank performance for female artists (over the last five years)
'Global ranking of the city's performance with female artists' is a measure of the curatorial quality— calculated by measuring the growth of women artists within three years of being shown or collected—of its network of art institutions.

This assessment is based on the measure of each institution's performance in a city per female artist category from 2015 to 2021.

For the signals considered, please refer to the methodology summary.

Cities	Performance for female emerging artists	Performance for female established artists	Performance for female celebrated artists	Performance for female star artists
New York	1	1	1	1
London	2	2	2	3
Los Angeles	3	5	5	5
Berlin	4	3	3	2
Beijing	7	29	31	13
Paris	8	4	4	4
Cape Town	9	47	16	155
Milan	17	15	23	18
Tokyo	21	43	11	61
Rio de Janeiro	32	96	161	31
Madrid	33	21	143	41
Mexico City	51	12	50	38
Amsterdam	54	35	19	37
Shanghai	55	11	28	29
Sydney	108	36	57	75
Moscow	119	114	103	224

Source: 2021 Wondeur.ai

Table 24. Global rank risk appetite
'Global rank risk appetite' measures the tendency of a city to show or collect artists earlier than other cities. This analysis is based on the measure of each institution's tendency to show or collect artists earlier than other institutions on a comparative global scale.

For the signals considered, please refer to the methodology summary.

Table 25. Global rank nesting hub
'Global ranking as a nesting hub' measures the contribution of each city to the creation of new star artists in the last 20 years.

This analysis is done first by considering all artists who started in 2000 and have gone on to reach the top 2% of artists worldwide in 2021, and second, by analyzing which cities were the most critical in their early development.

For the signals considered, please refer to the methodology summary.

Cities	Risk appetite rank	Risk appetite rank (female artists only)
London	7	1
Los Angeles	4	2
New York	8	3
Berlin	9	4
Sydney	6	5
Rio de Janeiro	3	6
Cape Town	2	7
Amsterdam	5	9
Paris	12	10
Milan	14	11
Mexico City	11	12
Madrid	15	13
Shanghai	13	14
Moscow	16	15
Beijing	10	16
Tokyo	17	17

Note: Ranking among 17 cities only

Source: 2021 Wondeur.ai

Cities	Rank nesting hub
New York	1
London	2
Berlin	3
Paris	4
Los Angeles	5
Amsterdam	8
Milan	11
Madrid	18
Mexico City	23
Tokyo	39
Beijing	63
Moscow	88
Sydney	94
Rio de Janeiro	119
Shanghai	121
Cape Town	148

Commentary

The cultural power of cities on supporting female artists; a few take-away points

by Veronique Chagnon-Burke, Independent Scholar, Co-Founder of WADDA the global research project on women art dealers and the former Academic Director at Christie's Education in New York.

The cultural power of cities depends partly on their capacity to sustain a healthy art ecosystem, where artists can not only benefit from a strong network of art galleries and art institutions, but more importantly, find affordable studios. If we consider affordable living condition as a necessity for artists—particularly for emerging artists—cities such as Paris and Berlin, which provide either subsidized studio spaces or affordable living spaces, should be better positioned than cities such as New York and London, to foster the development and success of new artists.

One could wonder then why New York achieves the top ranking across many categories. Possible explanations are that over the last few decades the financialization of art, the number of collectors who see art as an alternative type of investment, and the number of collectors who come from the financial world may account for the high ranking when it comes to the support of female artists. The last few years have seen a strong interest for the works of female artists, especially historical and established female artists, as the supply for similar works by male artists has been dwindling.

The risk-taking appetite of collectors for contemporary art is clearly seen in cities like New York and Los Angeles, in comparison, while Paris may be able to support female artists via institutions, there is less appetite for contemporary art and emerging artists among collectors.

The leading position of New York and London in support of female artists may also be a reflection of a stronger institutionalized gender parity in society at large, which could also account for the lower ranking of cities such as Mexico or Tokyo.

Female artists in the United States have also benefitted from the works that American feminist art historians have accomplished since the late 1970s, which then translated into important museum shows, and acquisition of works by established female artists. One can think about the recent acquisitions by the Museum of Modern Art of a piece by Carolee Schneemann; of the Whitney Museum of American Art of pieces by Ruth Asawa and Jay DeFoe; or by the Centre Georges Pompidou of a historical work by Regina Bogat. The increased visibility of these historical female artists is likely a comfort to the collectors who have invested in their works.

Methodology summary

This analysis (run in June 2021) spanned from 2000 to 2021 and examined 231,324 artists*, 29,534 public and private museums, commercial and non-profit galleries and artist-run centers in 3,664 cities across six continents. Key signals considered for the different AI engines included solo and group shows, museum acquisitions (donation and purchase), network dynamics and interdependencies (institutions to institutions, institutions to artists, artists to artists), impact on shows, network dynamics and institution bias on artists' careers and changes in value, dealers' selling prices and auction transaction prices (adjusted based on mispricing and speculative risks).

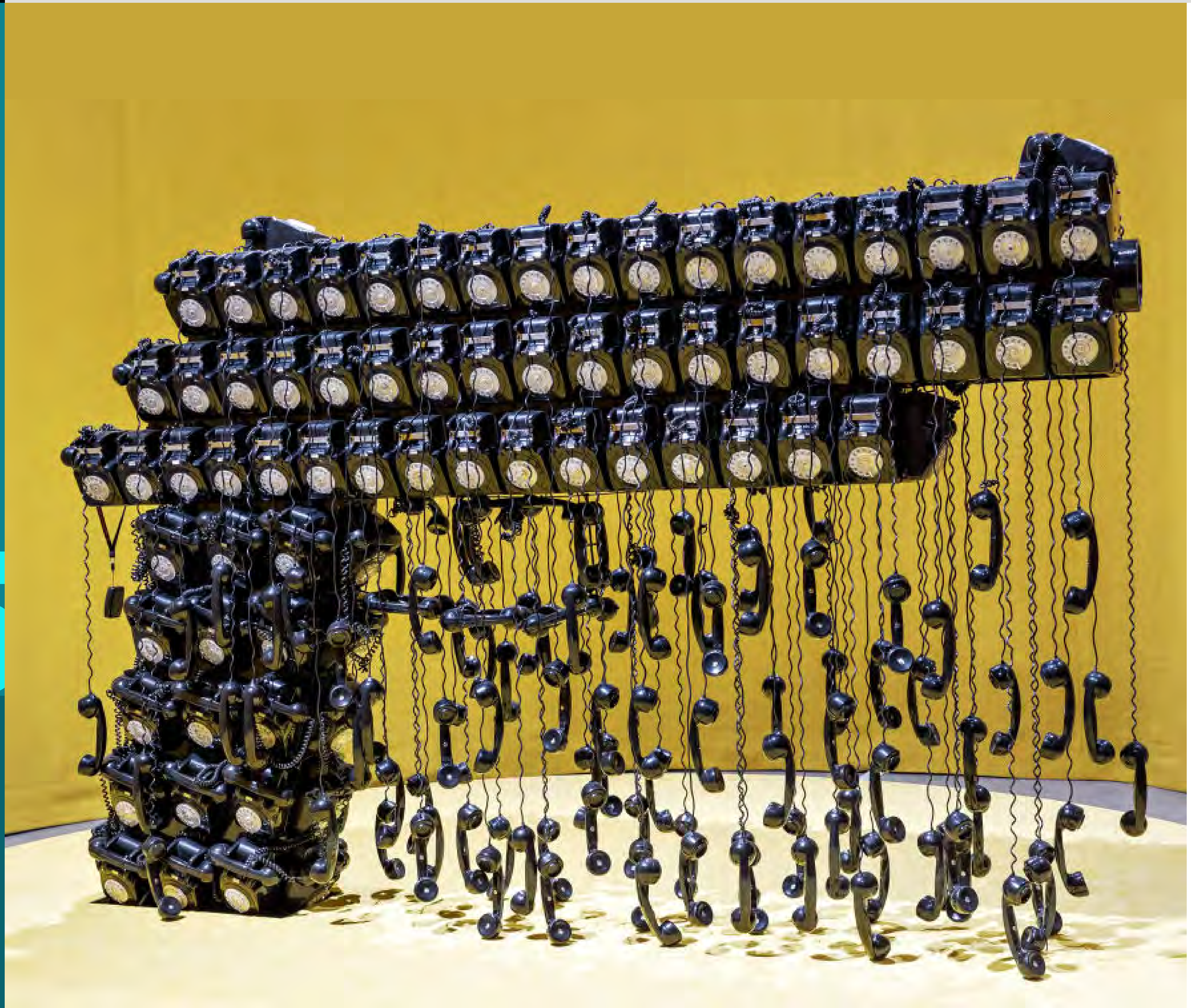
For the purposes of classifying artists by career stage, the following artist categories were used in this analysis:

1. Star artists (top 1% of artists)
2. Celebrated artists (the second 1%)
3. Established artists (the next 14%)
4. Emerging and underrepresented artists (the remaining 84%)

**Artist nationality was disregarded in this analysis. Cultural background, gender, age group, and primary medium were considered.*

Art-Secured Lending

05



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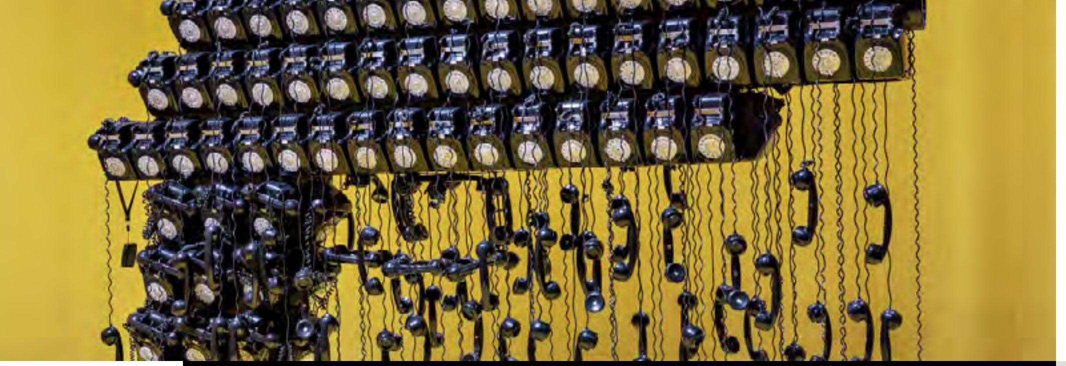

Highlights

Art-secured lending market

We conservatively estimate that the overall market size of outstanding loans against art could reach between US$24 billion and US$28.2 billion in 2021, a 10.7% average growth rate, and further grow to an estimated US$31.3 billion by 2022. We also estimate that art-secured loans to private collectors are in the region of US$21.6 to US$25.2 billion[1] in 2021, with the art trade (galleries and dealers) accounting for an estimated US$2.4 to US$2.8 billion.

The most significant change in the art wealth management space in the last 10 years

The way that collectors view their artwork has shifted in the last decade. Since 2009, we have seen the longest bull run in the history of the US stock market. The corresponding wealth effect, along with a prolonged period of low-interest rates, has fuelled the art market and benefitted collectors. In addition to collecting for aesthetic, intellectual and social reasons, collectors have increasingly been motivated by financial aspects, viewing their art as part of their overall balance sheet and a practical source of capital.

Asset-based lenders see strong growth during the pandemic

Our survey uncovers significant differences in growth rates between private banks and asset-based art lenders. Whilst private banks reported an average growth rate of 5% in 2020, asset-based lenders divulged an average growth of 21% on their art loan books last year. While this growth rate is expected to slow to an estimated 19% over the coming two years for asset-based lenders, it is projected to increase to over 9% for art-secured bank lending.

Transaction financing is a key driver in the art lending market

Using art-secured financing to buy art without having to sell other assets was a key driver for most (80%) of the art-secured lending providers surveyed this year. A further 67% of asset-based lenders said auction and private sale financing were the key reasons for demand in art-secured lending services, while half said bridge financing for a future sale was a key growth driver in the market. This finding was echoed by collectors, with 48% saying their main motivation for using their art collection to secure loans is to finance the acquisition of more art.

Hong Kong could become a strategic center for art-secured lending in the future

Both European and US-based lenders see the growth potential in the Asian market, with 30% saying Hong Kong will become a strategic center for art-secured lending services, followed by 20% who singled out wider Asia as a market with future growth potential.

Strong focus on private collectors

All the art-secured lenders surveyed rated private collectors as their most important client demographic, either by working with them directly or through their art advisors. Half the asset-based lenders rated galleries and dealers as their most important clients; however, only 25% of private banks said the same.

Most believe the art-secured lending market will remain niche: 80% of art-secured lenders said they do not believe art-secured financing will ever become a mainstream product and that it will remain a niche market.

Rosalina A Todo o Vapor
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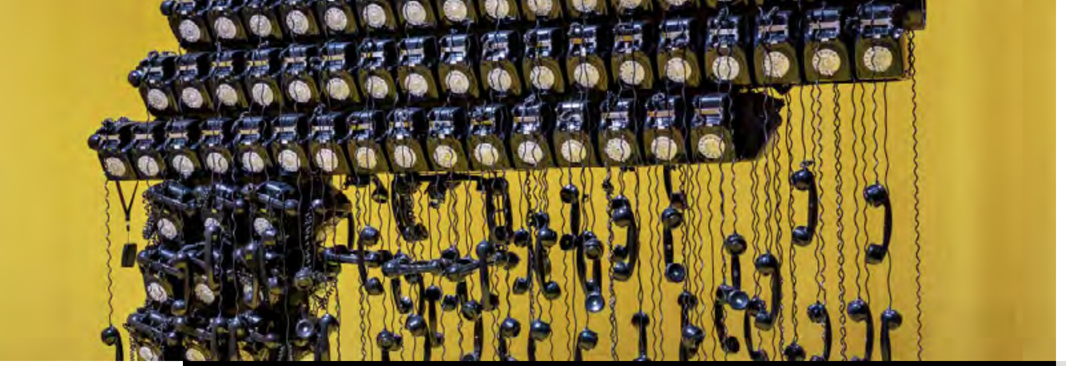
We conservatively estimate that the overall market size of outstanding loans against art could reach between US$24 billion and US$28.2 billion in 2021.

1 For the breakdown by borrower type, we used the findings from the TEFAF Art Dealer Finance Report 2018, and assumed that the ratio of private versus art-trade-related lending has remained constant since 2018, with 90% of art-secured loans going to individuals and 10% to galleries and dealers



The lack of a shared European legal framework for pledges requires a deep understanding of each European jurisdiction’s specifics and legal limitations.

Jurisdictional challenges impede growth
The lack of a uniform legal framework across different global art markets, such as the uniform commercial code (UCC) in the United States, is a major impediment to growth. For example, the lack of a shared European legal framework for pledges requires a deep understanding of each European jurisdiction’s specifics and legal limitations.

Technological development is taking place in the art-secured lending market
Improved technology and data insights will stimulate growth by supporting more nuanced decisions, including the type of collateral to accept and how much to lend.

Large share of wealth managers offer art-secured lending services
76% of wealth managers with an existing art-related service offering said they provided art-secured lending services, up from 50% in 2019. Half the wealth managers said this service was offered in-house and half through third parties.

Demand for art-secured loans set to increase
Almost half (49%) of collectors this year said art-secured lending services were some of the most relevant services that wealth managers could offer, with 52% of art professionals echoing this view. Of the wealth managers surveyed, 74% said they expected the demand for art-secured lending services to increase in the future, with 72% of collectors and 74% of art professionals saying the same.

Lack of knowledge
70% of private bankers said that a lack of knowledge about the art market was a key hurdle to providing art-secured lending services (compared with 61% in 2019). This signals that most private banks are still hesitant to fully embrace art-secured lending because their art market knowledge is insufficient to make informed decisions. The advent of increased data and research providers, better risk management tools and improved access to external knowledge and expertise could mitigate these concerns in the future.

J’Adore Miss Dior
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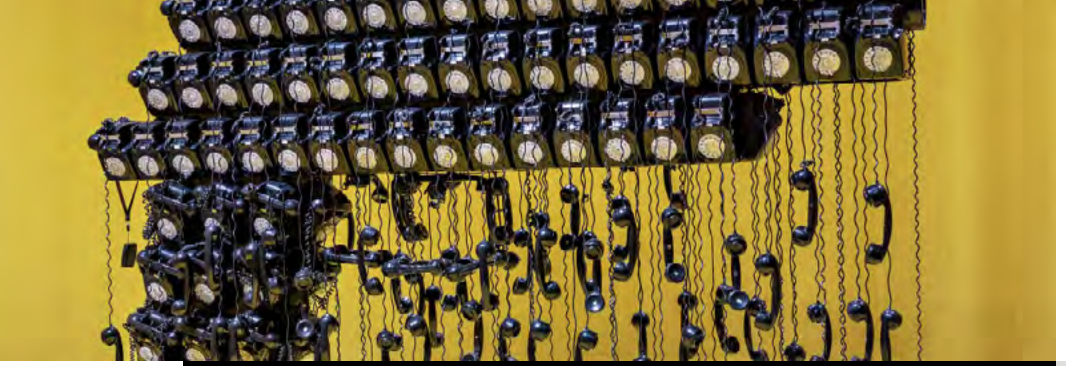

Introduction

This year's findings indicate that the COVID-19 pandemic and its impact on art market liquidity have triggered a renewed interest in art finance, particularly from asset-based art lenders. With the pandemic creating new liquidity needs, galleries and dealers are seeking new finance streams for their operations, while more collectors are looking for effective ways to manage art-related wealth. This trend catalyzed further growth in the art-secured lending market in 2020.

New in this year's report are the findings from our new dedicated Art Secured Lenders Survey 2021, which surveyed 11 art lenders consisting of four private banks and seven boutique asset-based lenders. As in previous years, we also present our survey results and feedback from collectors, art professionals and wealth managers, with added contributions from Bank of America, TPC Art Finance, Griffin Art Partners and Overstone Associates Limited.

With the pandemic creating new liquidity needs, galleries and dealers are seeking new finance streams for their operations, while more collectors are looking for effective ways to manage art-related wealth.

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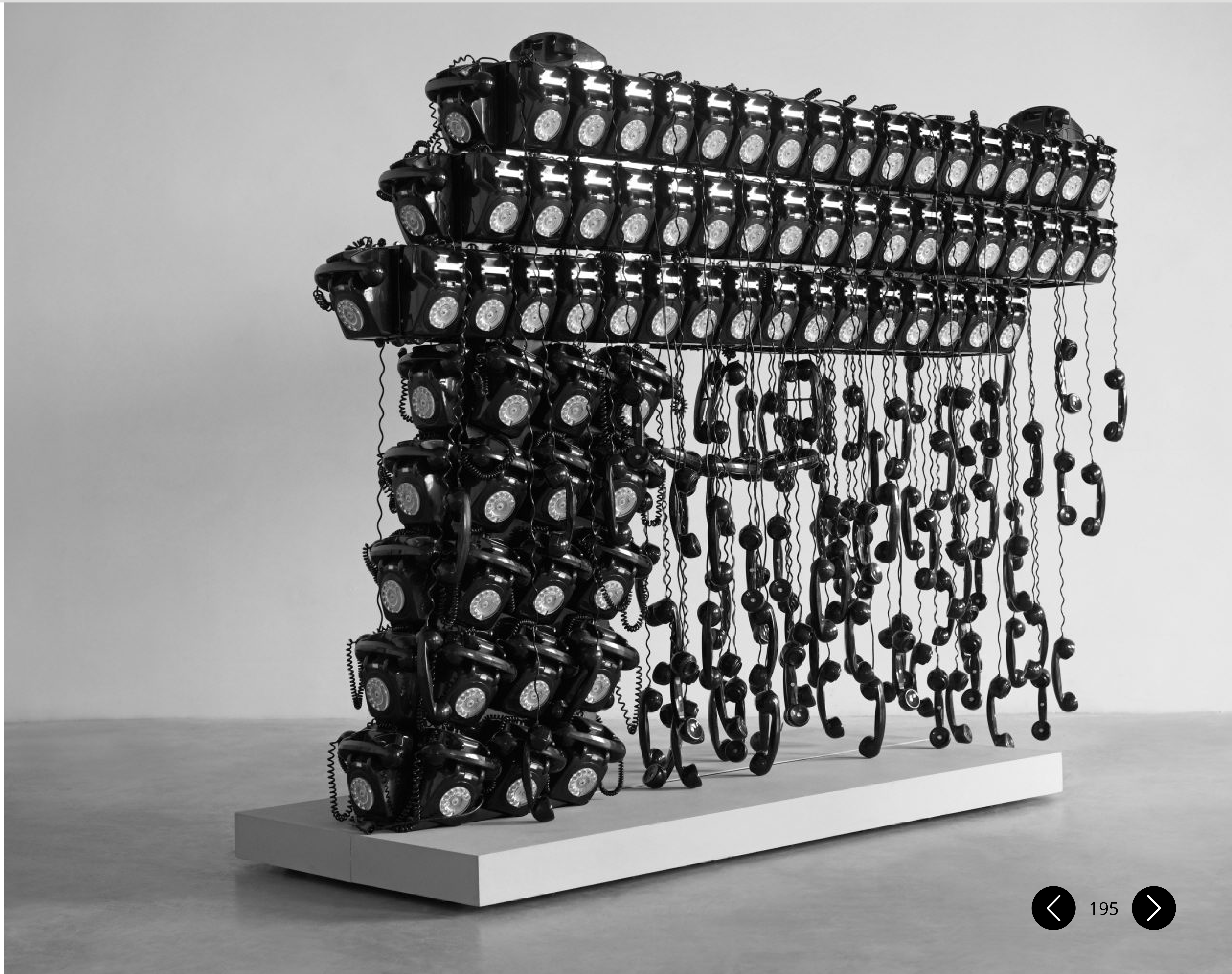
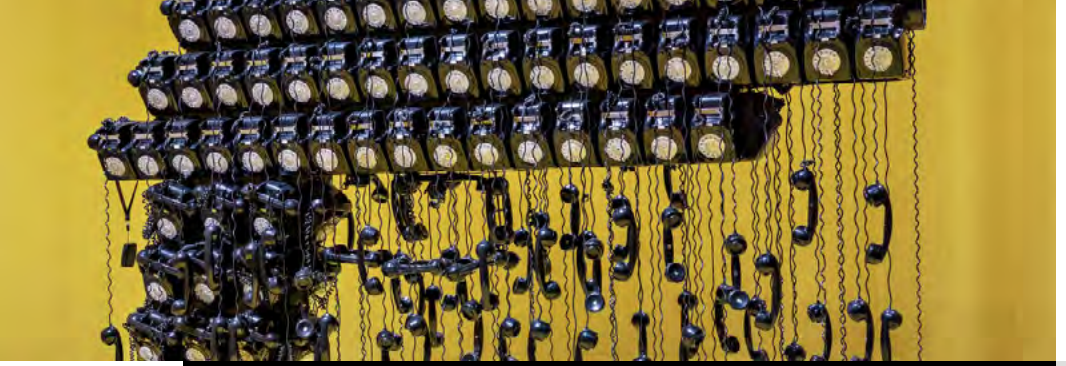




Size and structure of the art lending market

Based on past research from the previous edition of the Art & Finance report in 2019 and the findings from this year's new Art Secured Lenders Survey 2021, we conservatively estimate that the overall market size of outstanding loans against art could reach between US$24 billion and US$28.2 billion in 2021, up an estimated 10.7% from 2020.

Our survey findings among art lenders show significant differences in the growth rates of art-secured loans. Whilst private banks reported an average growth rate of 5% in 2020, asset-based lenders reported a double-digit average growth of 21% last year.

This suggests that, as private banks became more conservative and tightened their credit conditions during the pandemic, asset-based art lenders were able to fill the gap in the market for art-related finance needs.

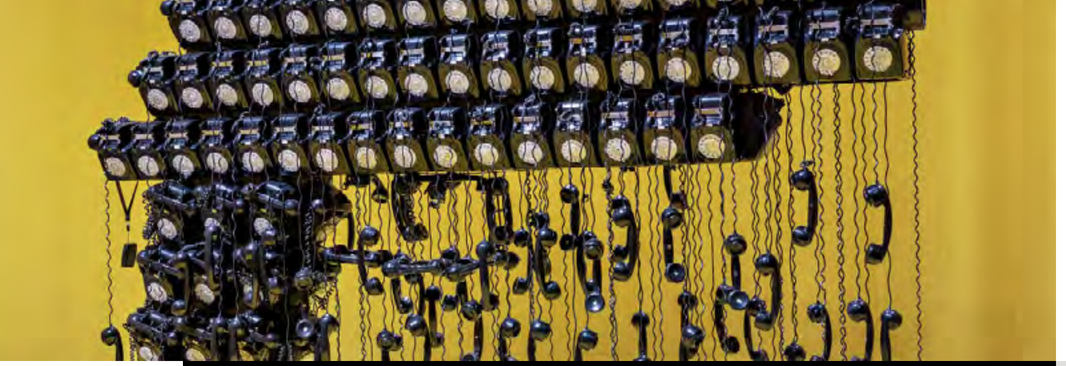
Art-secured loans in 2021 and 2022 are projected to grow by 9.4% per year for private banks and 19% per year for asset-based lenders, with the overall art-secured loan market reaching a projected US$26.6 billion to US$31.3 billion by 2022. We estimate that art-secured loans to private collectors are in the region of US$21.6 to US$25.2 billion[2] in 2021, with the art trade (galleries and dealers) accounting for an estimated US$2.4 to US$2.8 billion.

Table 25.

Funding sources	Non-exhaustive list of example providers		Estimated total art loan portfolio against art in 2019	Estimated total art loan portfolio against art in 2020	Estimated total art loan portfolio against art in 2021	Estimated total art loan portfolio against art in 2022
	• Citi Private Bank • Emigrant Bank Fine Art Finance • Deutsche Bank • Goldman Sachs • J.P. Morgan Private Bank	• Morgan Stanley • Bank of America • Westend Bank • Neuflize OBC • Northern Trust	US$18 to US$20 billion	US$18.9 to US$21 billion	US$20.7 to US$23 billion	US$22.6 to US$25.1 billion
Asset-based lenders	• Yieldstreet / Athena Art Finance • Artemis • AOI-Advisors • TPC Art Finance • Fine Art Group • Griffin Art Partners • Art Capital Group • Athena Art Finance	• Fine Art Partners • artLending.com • Borro by Luxury Asset Capital • Lombard Loan Real Assets GmbH • Art Finance Partners • Unbolted	US$1 to US$1.7 billion	US$1.2 to US$2.1 billion	US$1.4 to US$2.4 billion	US$1.7 to US$2.9 billion
Auction house finance	• Sotheby's • Heritage Auction	• Phillips • Artiana	US$1.3 to US$1.9 billion	US$1.6 to US$2.3 billion	US$1.9 to US$2.7 billion	US$2.3 to US$3.3 billion
Overall size			US$20.3 to US$23.6 billion	US$21.7 to US$25.4 billion	US$24 to US$28.2 billion	US$26.6 to US$31.3 billion
Estimated total loan size by borrower type						
Private collectors			US$18.3 to US$21.2 billion	US$19.5 to US$22.8 billion	US$21.6 to US$25.3 billion	US$23.9 to US$28.2 billion
Galleries/dealers			US$2 to US$2.4 billion	US$2.2 to US$2.5 billion	US$2.4 to US$2.8 billion	US$2.7 to US$3.1billion

Methodology: we have used the findings from the Art & Finance Report 2019 as a baseline to calculate the 2020 and 2021 figures. The average growth rates for 2020 and 2021 are based on the findings from the Art Secured Lending Survey 2021, and the average annual growth rates for private banks and asset-based lenders were applied to the 2019 figures. Private banks had a 5% average growth rate in 2020 and have an anticipated growth rate of 9.4% in 2021 and 2022, whilst asset-based lenders had an average growth rate of 21% in 2020 and have an anticipated growth rate of 19% in 2021 and 2022. For the calculations, we assumed that art-secured loans from auction houses saw the same average growth rates reported by the asset-based lenders surveyed.

2 For the breakdown by borrower type, we used the findings from the TEFAF Art Dealer Finance Report 2018, and assumed that the ratio of private versus art-trade-related lending has remained constant since 2018, with 90% of art-secured loans going to individuals and 10% to galleries and dealers

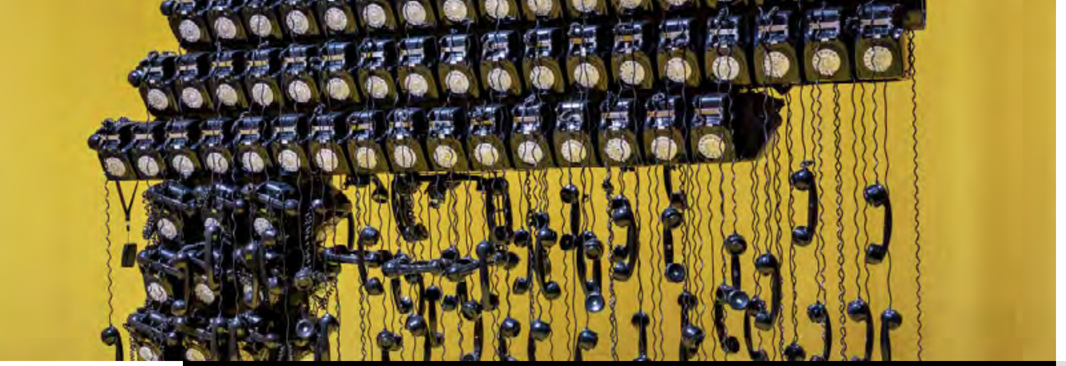


"The most significant change has been a philosophical shift in how collectors view their artwork. In 2009, we saw the beginning of the longest bull run in the history of the US stock market. The corresponding wealth effect, along with a prolonged period of low-interest rates, fueled the art market and has benefitted collectors. In addition to collecting for aesthetic, intellectual, and social reasons, collectors have an increasing focus on the financial component of collecting—they now view their art as part of their overall balance sheet and as a practical source of capital."

Bank of America Private Bank's Dana Prussian, Vice President and Art Services Specialist and Drew Watson, Senior Vice President and Art Services Specialist share their insights on how art lending has developed over the last 10 years.

"The most significant change has been a philosophical shift in how collectors view their artwork. In 2009, we saw the beginning of the longest bull run in the history of the US stock market. The corresponding wealth effect, along with a prolonged period of low-interest rates, fueled the art market and has benefitted collectors. In addition to collecting for aesthetic, intellectual, and social reasons, collectors have an increasing focus on the financial component of collecting—they now view their art as part of their overall balance sheet and as a practical source of capital." Bank of America Private Bank's Dana Prussian, Vice President and Art Services Specialist

I'll Be Your Mirror
©Luís Vasconcelos/Courtesy Unidade Infinita Projectos - 2018



Adriano Picinati di Torcello
Global Art & Finance Coordinator at Deloitte Luxembourg poses questions to Bank of America Private Bank's

Dana Prussian
Vice President and Art Services Specialist

Drew Watson
Senior Vice President and Art Services Specialist.

Expert voices

Art lending in 2021

The evolution of the art wealth management space

Adriano Picinati di Torcello (APT): What has been the most significant change in the art wealth management space in the last 10 years?

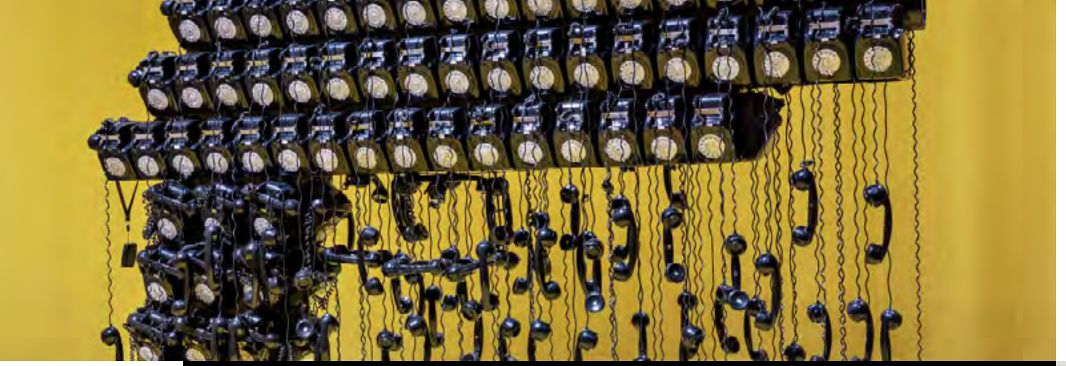
Dana Prussian (DP):
The most significant change has been a philosophical shift in how collectors view their artwork. In 2009, we saw the beginning of the longest bull-run in the history of the US stock market. The corresponding wealth effect, along with a prolonged period of low interest rates, fueled the art market and has benefitted collectors. In addition to collecting for aesthetic, intellectual, and social reasons, collectors have an increasing focus on the financial component of collecting—they now view their art as part of their overall balance sheet and as a practical source of capital.

APT: How has the industry adapted to this shift?

Drew Watson (DW):
With art taking an increasingly important stake in their balance sheets, collectors are turning to large institutions for expert advice on tax strategies, entity structuring, and fiduciary guidance. Art lending was once a one-off accommodative measure for the wealthiest, largest collectors at banks and large financial institutions. Now, coverage groups have taken shape, offering clients formalized art banking services and products, including art advisory, art lending, art planning, and consignment services. Art loans are regularly used not only to buy more art, but also, to unlock capital as part of a broader wealth building strategy.

APT: What are current growth obstacles in the art lending industry?

Dana Prussian (DP):
Growth is currently stymied by jurisdictional challenges in markets outside the United States. Today's art lending market is estimated to be worth from US$20billion to US$24billion—and nearly all of this is US-based as it depends on lenders' ability to perfect their security interest in art collateral under the Uniform Commercial Code (UCC). Europe, by contrast, does not offer an equivalent framework—many of its jurisdictions require the physical transfer of collateral, which does not allow for borrowers to live with their collections.



In practice, the recourse and non-recourse market segments face additional distinct sets of challenges. An obstacle in the recourse lending space is the limited number of UHNW individuals with balance sheets and collections that meet certain bank's selective lending criteria. In the non-recourse segment, predominantly driven by specialty lenders, art loans can be expensive and require warehousing the art (something that many collectors prefer not to do).

What was the impact of COVID-19 on your business?

Drew Watson (DW):
In the early days of the pandemic when there was increased volatility in financial markets, we saw collectors shift from marketable securities lines to art lines to reduce margin call risk (art collateral is valued once a year rather than marked to market daily). Once markets stabilized, the low interest rates and stable art valuations actually provided a favorable environment for continued growth in our art lending book. Markets-driven collectors that comprise the majority of our client base (such as hedge fund and private equity principals, real estate developers, and business owners) put art lines in place as part of a balance sheet arbitrage strategy, to have dry power as assets went on sale, or to buy more art in a socially-distanced art world.

What future challenges does the art lending industry face?

Dana Prussian (DP):
In terms of future challenges, an increase in interest rates may impact the demand for art loans, because the opportunity cost to borrow would become lower while the cost of borrowing would rise. It also remains to be seen how aggressively the new generation of wealth (in particular tech wealth) will collect art. A decrease in future demand for art in the next rising generation of wealth could also lower demand for complimentary goods and services, such as art lending.

A&F: Do you think technology plays a role in overcoming any of these obstacles?

Drew Watson (DW):
Better technology and data insights will lead to continued growth by supporting more nuanced decisions about what kind of collateral to accept, how much to lend, etc. In the future, lenders will become more data-driven in their underwriting processes, including how they assess risk, address concentrations, and manage overall loan collateral portfolios. We are already seeing better analytics and data management tools roll out. The next step in making financial institutions more comfortable with art as an asset class, is using more actionable data insights to drive formalized decision-making processes.

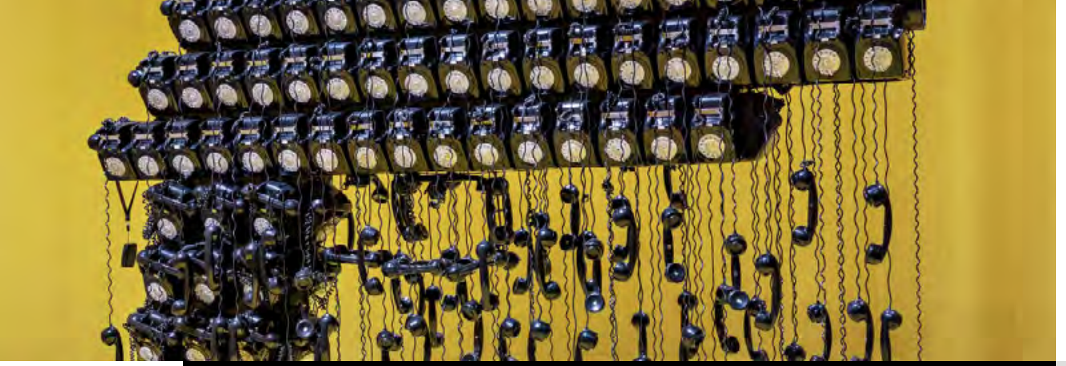
A&F: What other trends are you seeing in the art lending industry?

Dana Prussian (DP):
Increased competition is a major trend, especially as the art market and financial services sector continue to converge. More banks are developing a strategy on art beyond usual exhibition/event branding and client entertainment. Likewise, more traditional art world players like Sotheby's are ramping up their focus on financial segments. This competition is a signifier that the art lending, as well as the broader art banking space, is an attractive market, despite its inherent challenges.

Why collectors are choosing art lending in 2021

- Historically low interest rates;
- Art values have remained stable through the pandemic;
- As an alternative to selling art during the pandemic;
- To help reduce margin call risk compared to borrowing against stock during volatile times;
- To avoid potential capital gains tax given the elimination of like-kind exchanges for art;
- For dry powder to quickly re-deploy capital;
- To guarantee works at auction;
- Balance sheet arbitrage;
- To use as a working capital line for a private business; and
- To pay estate taxes or fund a trust without having to sell the art.

The next step in making financial institutions more comfortable with art as an asset class, is using more actionable data insights to drive formalized decision-making processes.



Survey findings 2021

Art secured lenders—survey findings 2021

Figure 74. What was the average growth rate for your art lending book in 2020?
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021

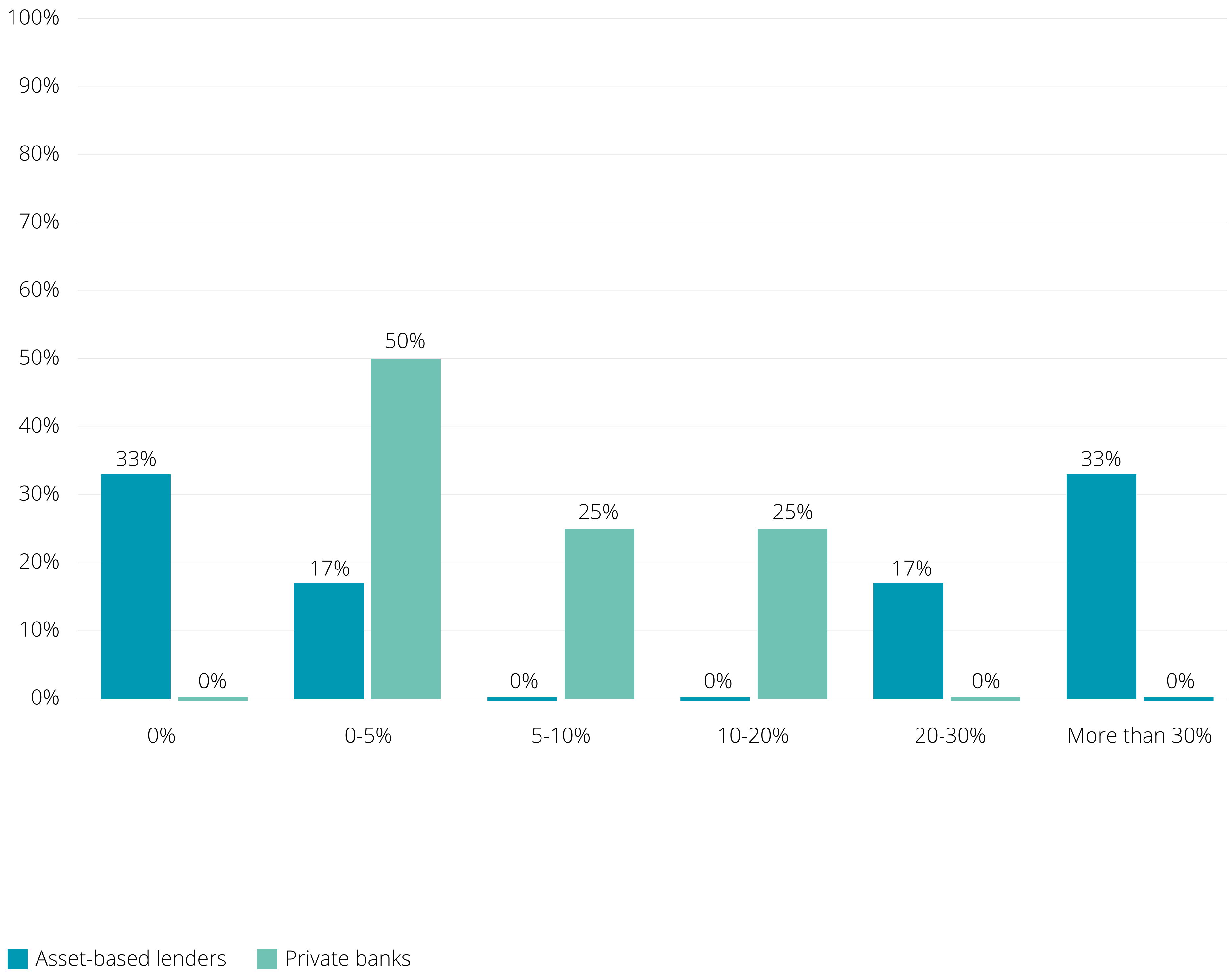
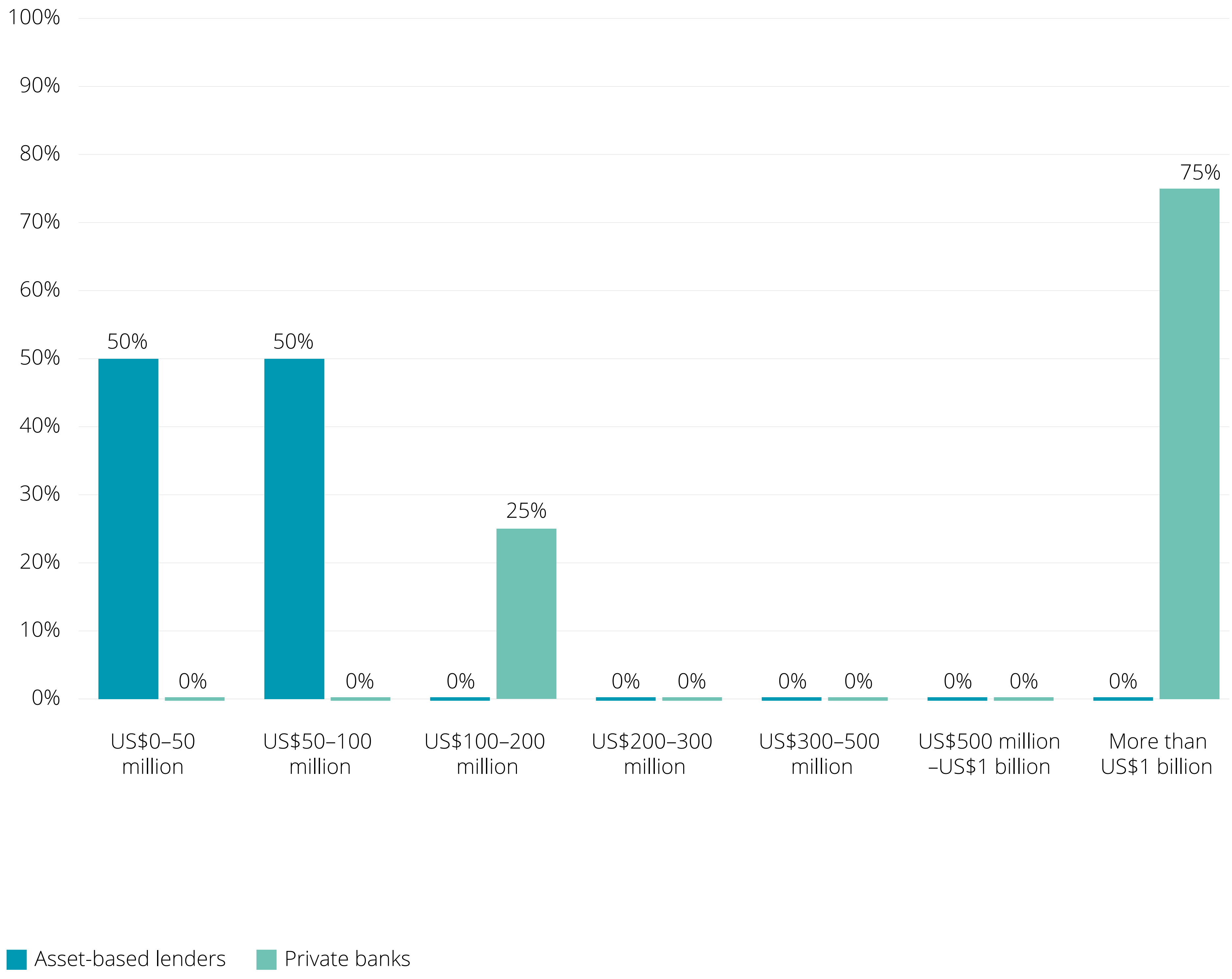


Figure 75. What is your estimated size of your current art secured lending book?
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021



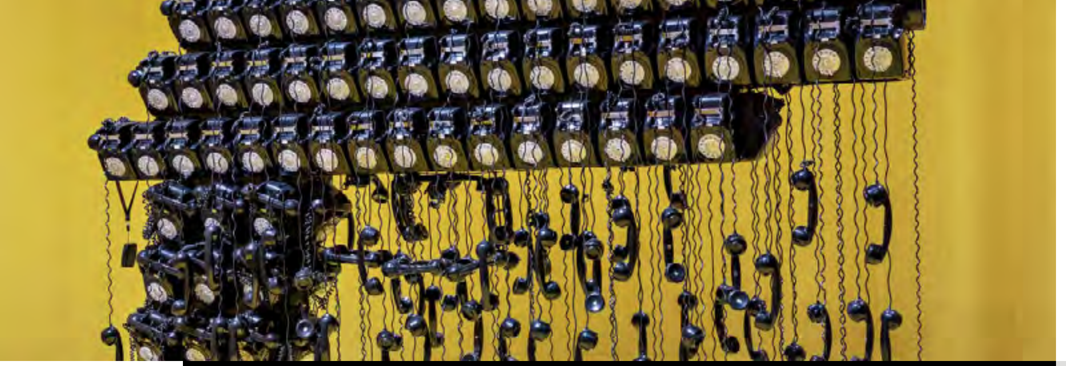


Figure 76. What is the level of interest you typically charge for an art secured loan?
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021

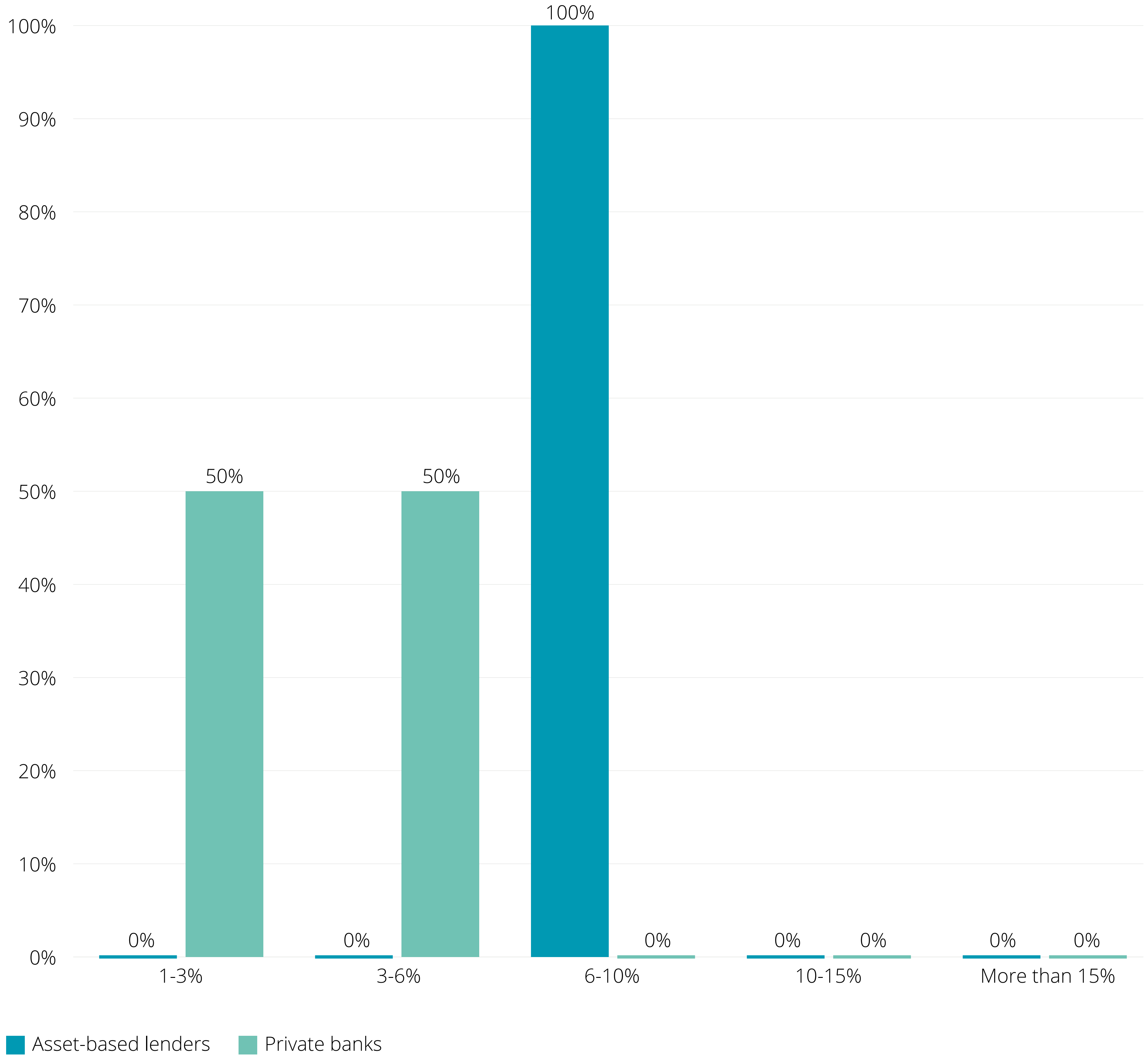
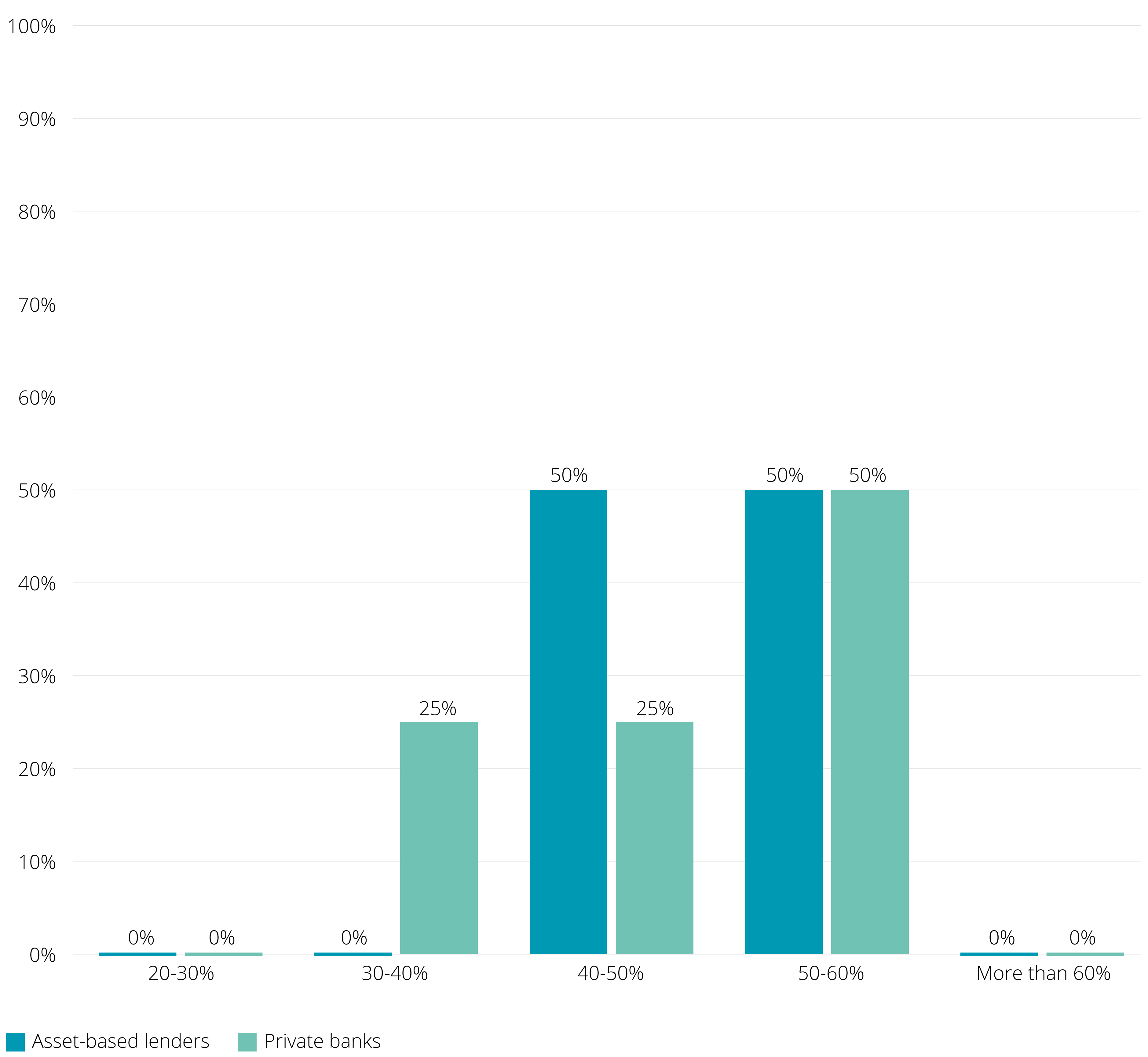
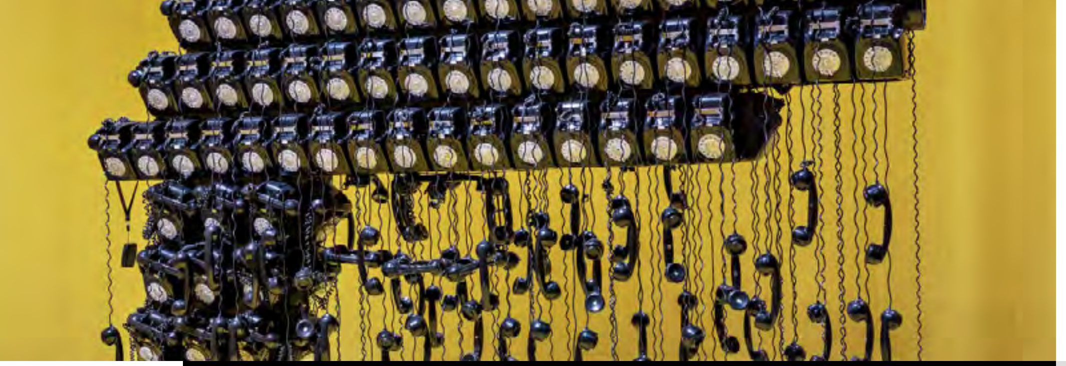


Figure 77. What is the average LTV you apply to an art-secured loan?
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021





The art lending market's average growth rate was 7% in 2020

The average growth rate of the art lending market slowed during the pandemic, mainly due to more restrictive lending among private banks during a period of heightened uncertainty. Whilst private banks reported an average growth rate of 5% in 2020, asset-based lenders reported a double-digit average growth of 21%, as collectors, dealers and galleries sought new sources of liquidity.

Average size of the art-secured loan book

Three of the four private banks surveyed had art-secured loan books of more than US$1 billion, with one private bank stating their loan book had between US$100 million and US$200 million secured against art. The average art loan book size for the seven asset-based lenders surveyed was an estimated US$50 million.

Cost of funding:

All the asset-based lenders surveyed reported they charged between 6% and 10% in interest on art-secured loans, suggesting the average funding costs for asset-based loans have dropped to single digits. Two of the private banks surveyed reported interest charges of between 1% and 3%, whilst the remaining two banks reported interest charges of 3% to 6% on art-secured loan transactions.

Loan-to-value

Two out of the four private banks surveyed typically apply a 50–60% loan-to-value (LTV) ratio on art-secured loans, with one private bank typically using a 40–50% LTV and another applying a lower 30–40% LTV. Asset-based lenders apply a similar LTV to private banks, with half of these asset lenders applying a 40–50% LTV and the remaining half typically using a 50–60% LTV ratio.

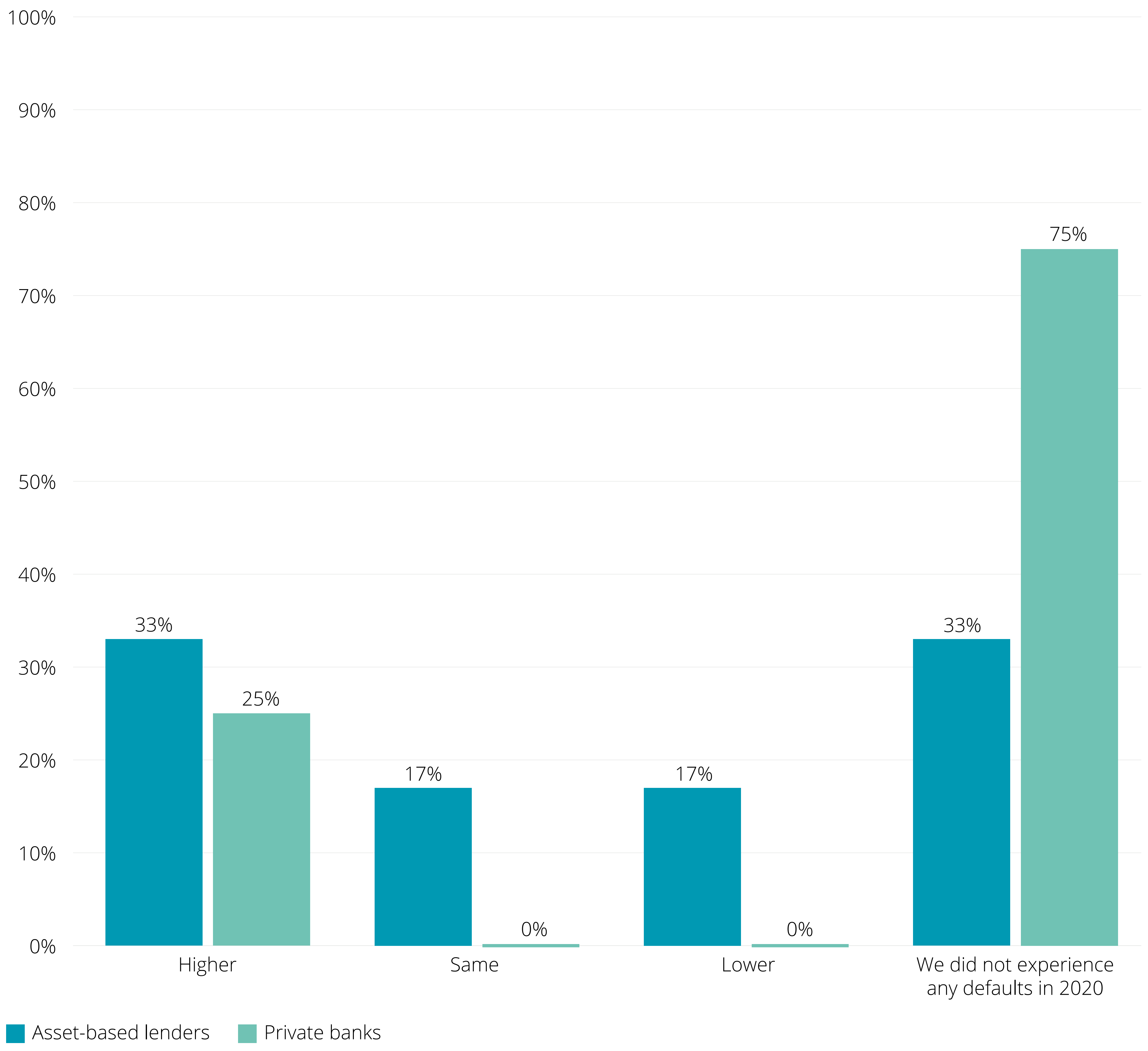
Most lenders did not experience higher default rates in 2020

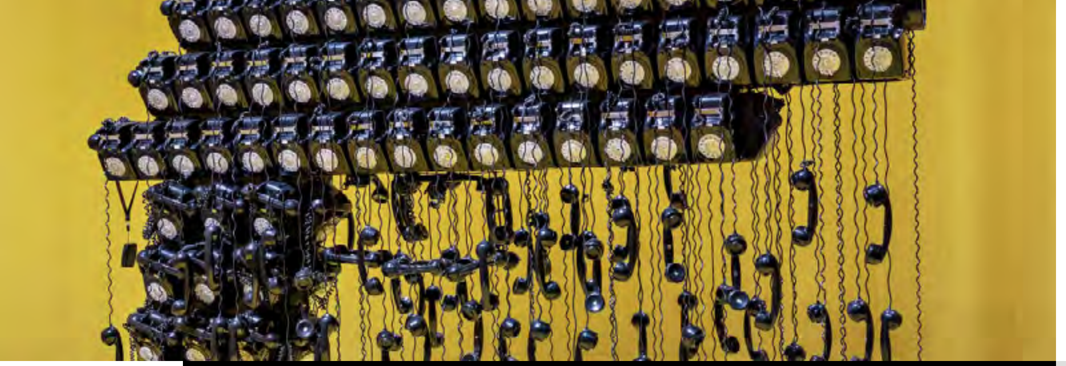
Half the art-secured lenders surveyed said they did not experience any art loan defaults during 2020. Nearly one-third (30%) of the asset-based lenders surveyed had experienced a higher default rate, but 34% said it had been lower or the same as in 2019. A third (33%) of asset-based lenders reported no defaults during 2020. Among the four private banks surveyed, three had not experienced any defaults last year and one reported higher default rates than in 2019

What was the level of defaults during the pandemic compared with 2019?

Figure 78. In your experience, what was the level of defaults during 2020 compared to 2019?

Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021





Joe Charalambous
President TPC Art Finance

Naomi Baigell
MD TPC Art Finance

Case Study

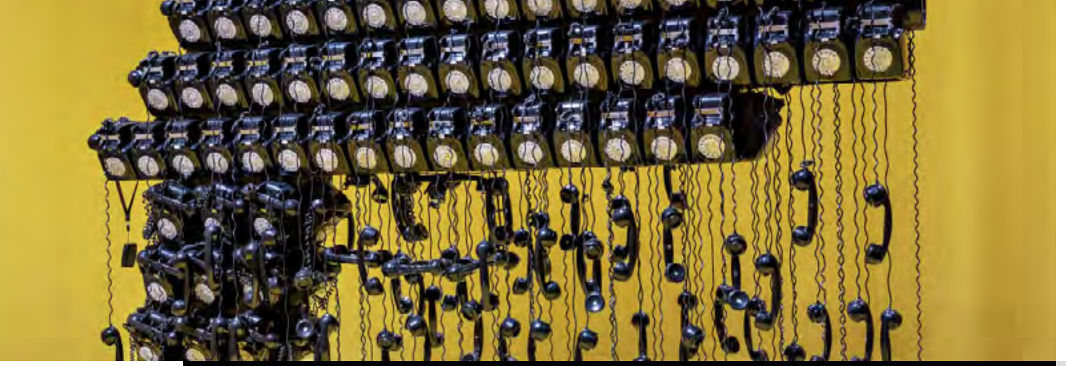
Post-pandemic art financing in the non-banking market

How responses to COVID-19 altered the art market, the impact on specialty lenders, and the ongoing effects on specialty lending practices going forward

While 2020 saw the largest global art market contraction since 2016, the decline did not lead to fewer art-backed loans. Instead, the COVID-19 pandemic led to increased interest in art-secured lending. Some specialty lenders saw more than a 75% increase in requests from 2019, as private collectors looked to unlock equity from assets that were not impacted by the initial shock of the pandemic. This was particularly true among collectors who operate in the middle of the market, where activity began to surge once galleries and auction houses pivoted due to the challenges posed by COVID-19 and expanded their virtual presence.

Interest rates and the middle market

Lower interest rates have helped to spread awareness of art-secured lending and have created more demand. Rate changes can affect the lending practices of bigger banks, but they tend to offer art financing as an accommodation to a subset of their client base who seek loans beginning at US$10 million and have significant assets under management (AuM). TPC Art Finance, which caters to the upper middle of the market, remains largely unaffected by changes in rates and offers loans solely against collections of artworks starting at $500,000 with an ability to offer financing equal to other institutions. Similarly, inflation or any other market inflection does not seem to immediately impact the art lending space. Overall, the art market tends to lag behind such macroeconomic shifts, if it is affected at all. Instead, education about the economic benefits of borrowing against a work of art, in lieu of selling, has a greater influence. Through borrowing, collectors can avoid capital gains and other tax implications, and redeploy funds as they see fit. As firms like TPC Art Finance continue to be accessible and further streamline the process, we hope to see an increase in activity. With this broader lending base, collections and collectors that may have been overlooked by banks can benefit from the same opportunities and leverage more recent entrants to the secondary marketplace.



The pandemic also leveled the playing field, breaking down barriers of communication.

This is where the market is at its most dynamic and where art-secured lending will likely see the most significant growth in coming years. The ultra-contemporary (artists born in the mid 1970s or later) segment of this market is particularly strong—the total generated by global sales increasing by 142% from March 2019 ($35.7 million) to March 2021 ($86.7 million) at auction alone, with the majority of sales in this category happening privately or through galleries[1]. Collectors in this sector are often newer to the market and more inclined to recognize that works of art can serve as a smart financial solution for their short-long term investment strategies. Regardless of differing rates, many collectors at this level, and even above, may not have ample capital, other AuM, or a large enough collection for their banking institutions to support a loan against said collection. Rather than wait to benefit from significant value appreciation, a collector can immediately seek liquidity through art-backed specialty lenders to continue to add to their art collection or diversify their portfolio with other investments.

There has been a heightened use of new technologies, including digital sales platforms, data aggregation tools, and advances that allow for higher quality and dimensionality of imaging and display, which has generated increased participation in online sales and brought in new collectors. This has fostered a greater amount of comfort in the idea of using art as leverage.

Breaking down barriers

The pandemic forced galleries and auctions to move to online platforms, which helped to further democratize the market, while the adoption of virtual platforms meant that more collectors could be exposed to new pieces and artists. The comprehensive set of digital tools are now actively being used to view art in the non-physical world allowing the average number of times a work is viewed to multiply exponentially.

The pandemic also leveled the playing field, breaking down barriers of communication. Anyone could plug into numerous panels through various online portals and listen, learn, and educate themselves about collecting. Dealers, gallerists, and even artists also became more accessible since everyone was suddenly a direct message or an email away.

Third, by moving online, auctions could take place with greater frequency. Surprisingly, participation did not ebb. Rather, there was increased activity in bidding globally, which ultimately led to higher hammer prices. Christie's reported in May 2021 that the auction house has seen online registrants surge 26% from May 2020, that a total of 5.5 million global viewers from around the world tuned into their livestream auctions, and that bidders across 15 sales hailed from 58 different countries.[2]

These factors converged to make the middle market more dynamic. Increased participation then led to an increase in the need for financial services—and industry leaders see no reason why these trends will not continue.

Art-lending and the auction market

The auction market is an important aspect of the loan underwriting process because it offers transparency into an artist's depth of market. Increased frequency of auctions and increased sales means more data, which allows lenders to better assess potential risks associated with lending against specific artists and works of art produced during specific time periods.

An examination of Shara Hughes' performance is illustrative of this point. Following her inclusion in the 2017 Whitney Biennial, her work has experienced a sharp and sustained increase in hammer prices that have far exceeded estimates. The hammer price of I don't Deserve These Flowers, for example, increased by more than 1600% between 2017 and 2021, and outperformed mean estimates in the two sales by a factor of 3.75 and 5.94, respectively. The performance of Water Tower, which saw sales in 2018 and 2020, reveals a similar trajectory, both in terms of the increase in hammer price (260%) and factors by which the two sales outperformed mean estimates (2.5 and 3.5, respectively).[3]

1 Julia Halperin, Which Segment of the Art Market Grew the Most in Last Month's Mega-Sales? We Crunched the Numbers, June 24, 2021, available at https://news.artnet.com/news-pro/may-2020-art-auction-1982975
2 Christie's, Hong Kong Auctions May 2021, available at https://www.christies.com/auctions/hong-kong#overview_Nav
3 TPC Art Finance (2021) sourced from Artnet

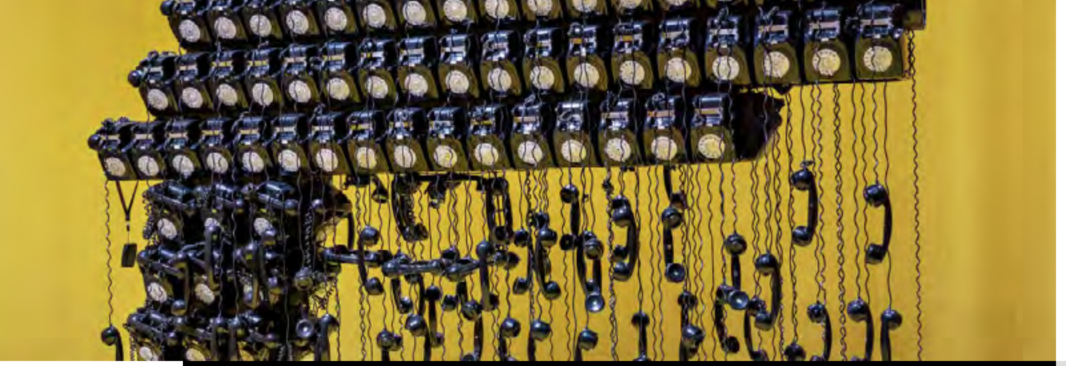
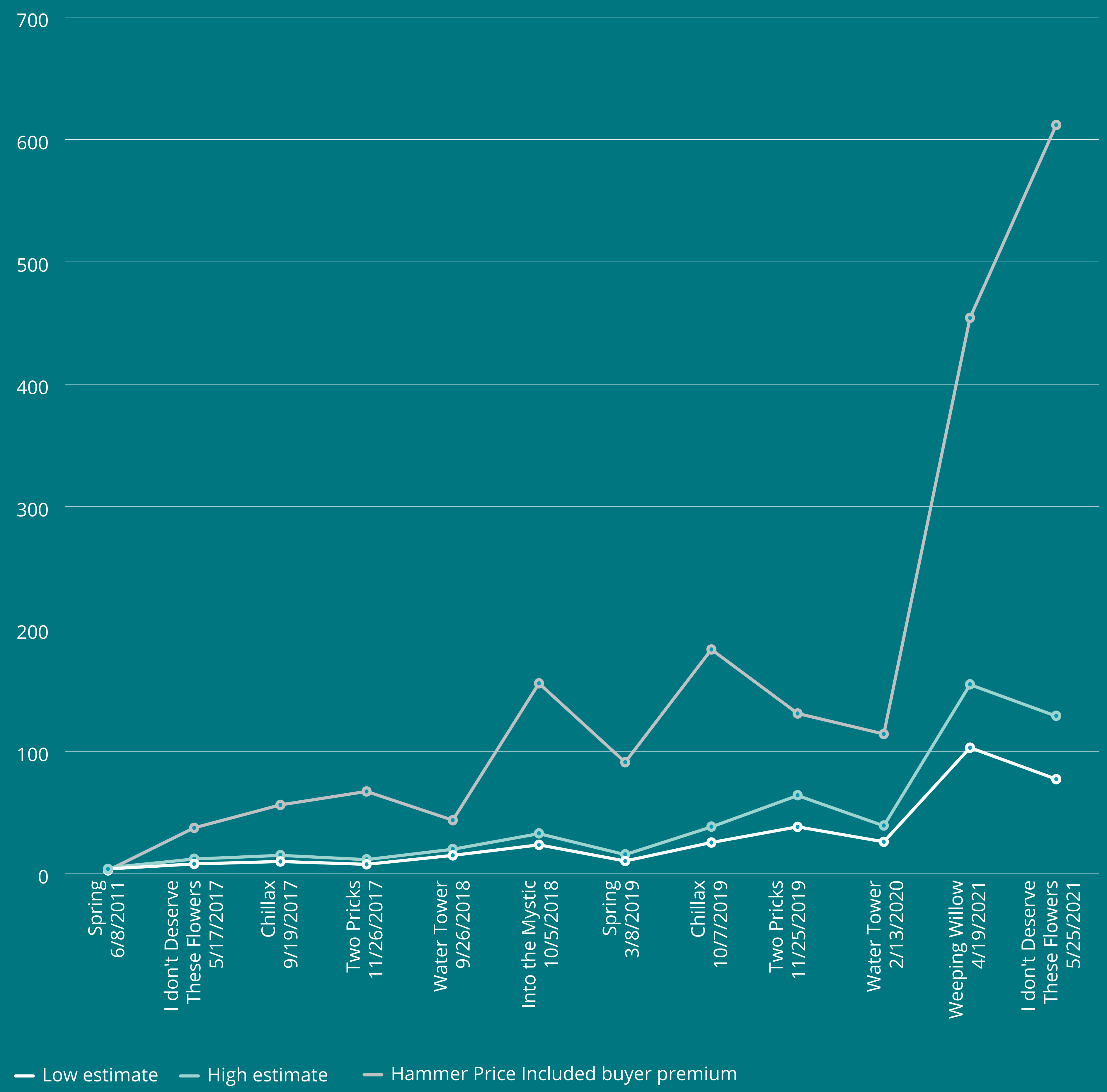


Figure 79. Shara Hughes estimates & sales ($1000s)



Given these trends, collectors who are seeking capital may prefer to retain works by artists like Hughes. Taking out a loan affords them the opportunity to not only borrow against these works now, but to upsize the value of their loan should the works continue to increase in value. Specialty lenders offer them the opportunity to do so, thereby catering to a part of the market's ecosystem that is younger and more active. Furthermore, as these individuals' collections grow and their interest in more valuable works of art increases, their reliance on art-secured lending will likely continue, both growing the industry and popularizing the practice.

Trends in Asia

In 2020, China maintained an 18% share of the market, placing the country behind only the US (44%) and the UK (20%), but maintained the largest market share for works below $50,000 and works between $50,000[4] and $1 million. The latter price segment includes works of art that could be used to secure a loan through a specialty lender, which presents a clear market opportunity for specialty lending in Asia. There is a growing belief that Asia will soon emerge as a major hub to source loan activity to be rivaled only by the US.

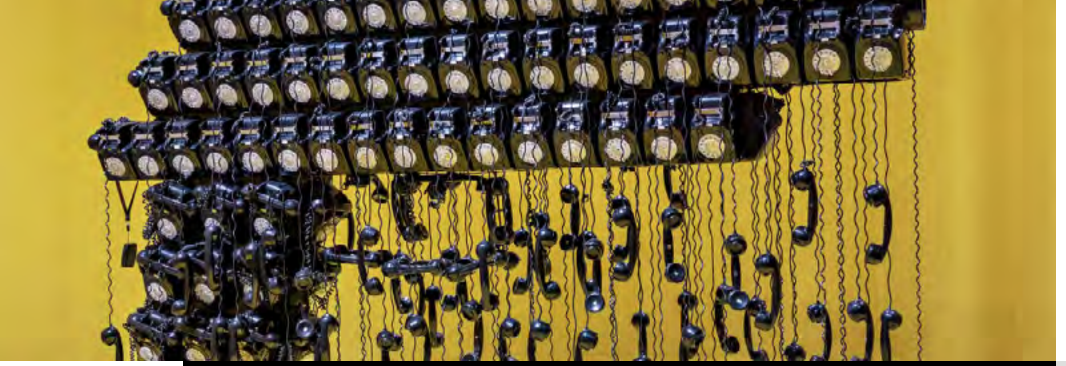
Asian collectors tend to be younger, more comfortable buying art for the first time, and more capable of adapting to market dynamics, which suggests that they may follow in the footsteps of American collectors. They will likely recognize the use of art financing tools in a manner akin to American collectors, even if homegrown infrastructure to facilitate these deals has not emerged at this time. Given that there are relatively few ways to obtain a loan within some parts of Asia, most notably China, specialty art lenders from the US could become a source of capital for these collectors. They may recognize that specialty art lenders offer them the opportunity to leverage their existing holdings, further fueling growth in the space.

Final thoughts

We are now in a new generation of the art market and one in which we hope transparency and technology will continue their presence and growth as it has proven to encourage new peer participation. It is anticipated that this will increase the utility of specialty art lending and help fuel growth and activity.

Bespoke art financing provides resources and opportunities designed to support individual liquidity needs. As the lending market evolves over the next five years, we expect to see a shift in how loans are structured in line with more traditional financing products, including insurance policies that remove the default and valuation risk, in turn enabling lenders to increase loan-to-values and offer borrowers more competitive rates. These new methods of reducing risk and larger loan pools will also mean that securitization becomes a bigger possibility. The industry has grown and will continue to do so as collectors get more savvy, educated, and truly look at borrowing against works of art as an opportunity, not a necessity.

4 Claire McAndrew, The Art Market 2020, available at https://d2u3kfwd92fzu7.cloudfront.net/The_Art_Market_2020-1.pdf

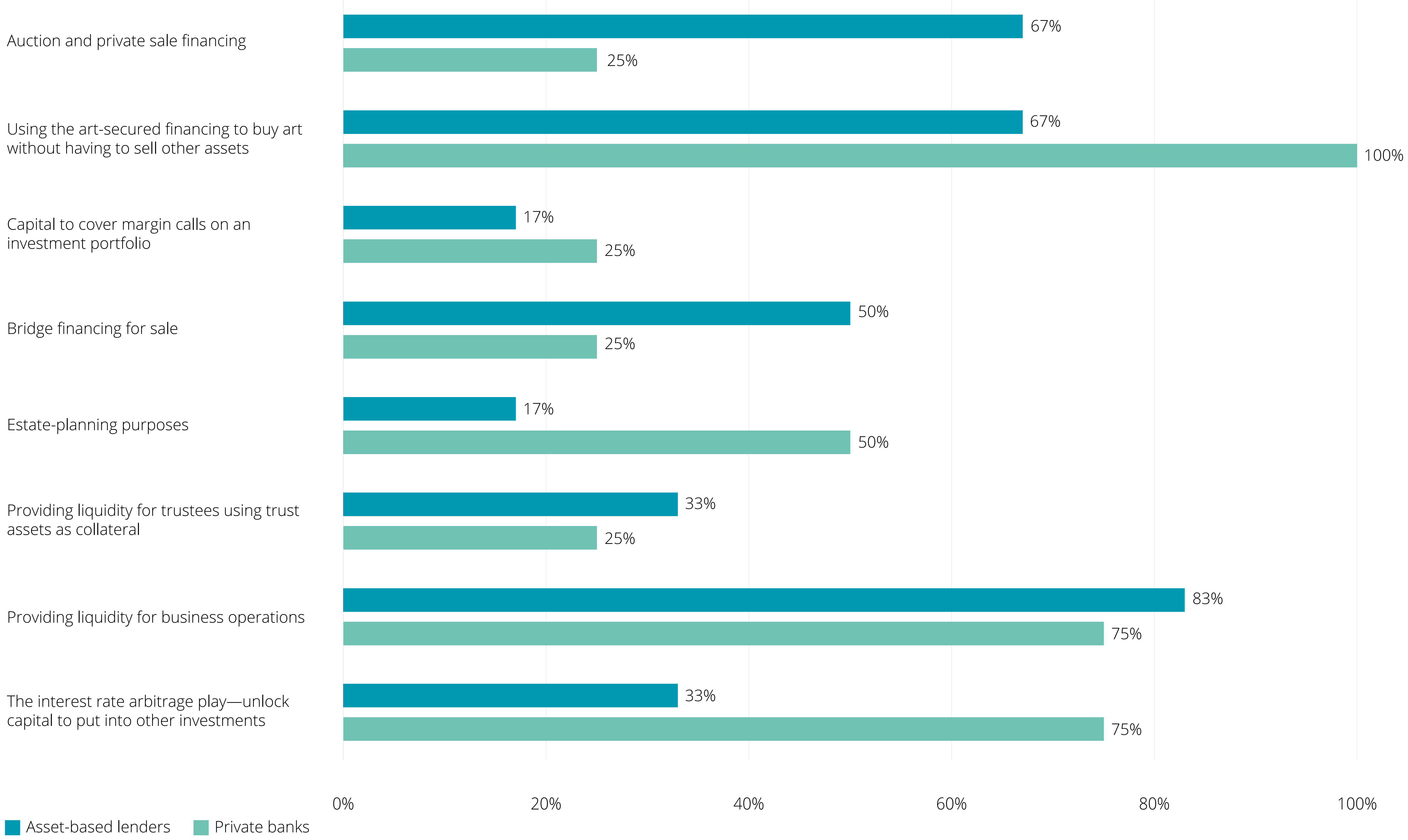


Art secured lenders—survey findings 2021

Demand drivers for art-secured lending

Figure 80. What are the most important "demand drivers" for art-secured lending services over the last 2 years?

Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021

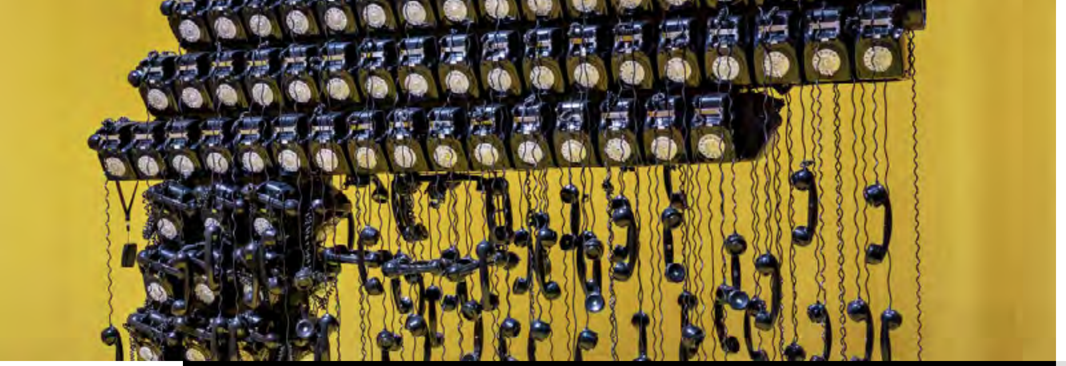


Transaction financing is a key demand driver

All the private banks surveyed said using art-secured financing to buy art without having to sell other assets was a key driver for their art-lending business, and 67% of asset-based lenders said the same. A further 67% of asset-based lenders said auction and private sale financing was a key driver for the demand in art-secured lending, compared with 25% of private banks. Half the asset-based lenders said bridge financing for a sale was a key growth driver in the market, compared with 25% of private banks.

Providing liquidity for business operations:

75% of private banks indicated that the need for liquidity for business operations was a key driver for art-secured loans, and 83% of asset-based lenders said the same.



Among private banks, 75% said that unlocking capital for other investments was a key reason why clients used their art-secured lending services.

Interest arbitrage
Among private banks, 75% said that unlocking capital for other investments was a key reason why clients used their art-secured lending services. However, as asset-based lenders charge higher interest on their loans, only 33% identified this as a key driver for demand.

Estate planning
Half the private banks surveyed said that estate-planning issues were key drivers for the demand for art lending services, with only 17% of the asset-based lenders saying the same. Nearly a third (30%) of private banks said providing liquidity for trustees using trust assets as collateral was also a key motivation, with 33% of asset-based lenders saying the same.

In the article on p.208, Griffin Art Partners explains the importance of considering the cyclical nature of art trends. Tracking market metrics and constantly gleaning first-rate information is necessary for art market players and collectors wishing to market-time their artwork acquisitions and sales.

Solitário
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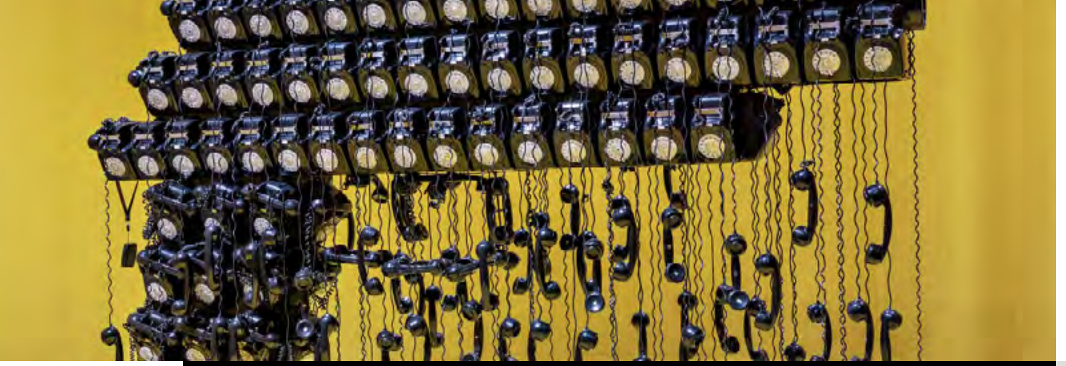


Aymeric Thuault
Director, LINK Management

Aude Lemogne
Director, LINK Management

Xavier Ledru
Managing Director, REYL Prime Solutions, REYL Wealth Management

Case study

Navigating a volatile market

Griffin Art Partners offer insight on the art-lending sector, evolving trends, and the implications for collectors

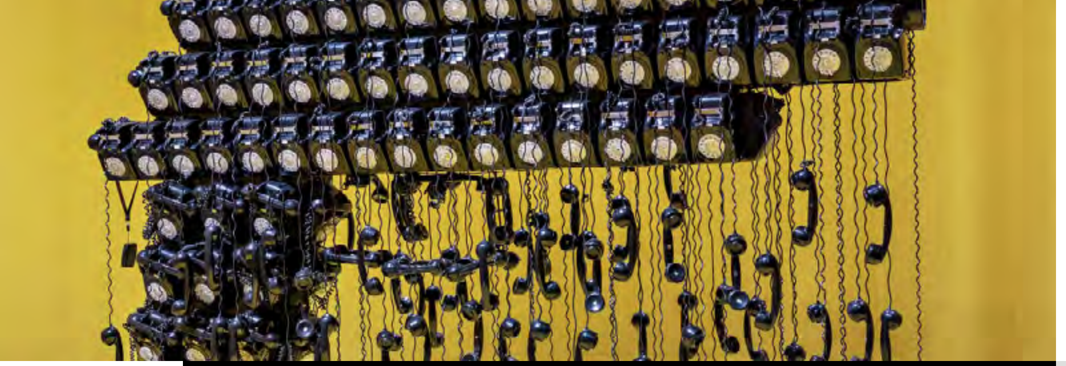
The art market has undergone several fundamental shifts in the past twelve months, adapting at a velocity rarely observed in recent years. One of the most notable changes to the art market as it rides the waves of the COVID-19 pandemic, has been the advent of a 'new normal' in terms of collecting trends, which impacts the whole landscape of the contemporary art market while also creating ripple effects on earlier art periods.

The significant movement in terms of taste (particularly strong in the United States) meant that some of the mature white male artists, who commanded intense competitive bidding a few years ago, have experienced a reversal of fortune in favor of a younger generation of artists dealing with the ideas of identity, race, and gender—or IRG themes as coined by Scott Reyburn[5]. Thus, the older generation of contemporary artists such as Richard Prince, Rudolf Stingel, or Jeff Koons find themselves stuck in a momentum reversal.

In 2020, Jeff Koons' yearly auction turnover decreased by a whopping 97%. Rudolf Stingel's turnover decreased by 84% while his bought-in rate almost doubled from 33.3% up to 60%—an all-time high.

At the same time, Christie's offered at their 20th Century evening sale in May, female artists like Alice Neel, Grace Hartigan, and Lee Krasner, along modern heavy-weights such as Picasso, Mark Rothko, and Giacometti. This is particularly striking when you consider the fact that Alice Neel's yearly turnover at auction was below EUR1 million in 2018. Just recently, in May 2021, a single work of Neel sold for over EUR2 million at Christie's.

5 Arttactic Podcast, 14 January 2021



This move for more inclusion and diversity is shaving off value for a number of 'blue-chips artists'. One of the most emblematic illustrations of this taste rotation was the Christopher Wool word painting 'OH-OH' that crashed at Christie's evening sale, not drawing a single bid despite a modest estimate (US$8-12 million). Even though this was not a very fresh work, as it had been shopped around on the private market quite a bit a few months before, this poor result for one of Wool's most coveted pieces of work epitomizes this current trend. This decline in prices translates into a thinner auction turnover and in an increased bought-in rate, two key metrics for an art lender in order to assess the implied liquidity on an artist market[6].

While some of these artists will most certainly tempt back collectors' favor, more speculative ones may find it harder to recoup their peak prices. Artists—who benefit from a stable collectors' base committed to the artist in the long-term and not just in for a quick profit—should recover over time. It may even make sense to be counter-cyclical and acquire quality works while everybody seems to be chasing the younger IRG artists.

Another meaningful evolution we have observed is a much stronger focus on the intrinsic quality of artworks, particularly in the Modern art segment, and to a lesser extend in the Post-War segment. For example, the bought-in rate of Klimt's works on paper sold at auction[7] has increased by 50% from 2019 to 2021.

On the other hand, the percentage of works selling above the high estimate has remained stable, increasing slightly from 26.5% in 2019 to 28.5% in 2021. As higher quality works tend to sell above the high estimate, it seems that collectors now refrain from bidding on lower quality works[8]. This trend can be observed in several Modern artists and thus these minor works on paper and inferior quality works have seen their valuation decrease. The natural selection process is unfolding more rapidly, induced by the shift in collecting focus.

These shifts necessarily impact art lenders' loan portfolios as they impact collectors' assets. Thus, it is critical to understand the underlying dynamics of these trends and most importantly, complement public auction data with insight on the specifics of each artist's market (quality and resilience of collector base, control of supply by an estate, and a disciplined gallery). One basic conclusion one can draw, is that—unsurprisingly—diversified art portfolios have demonstrated, once again, far more overall resilience.

Ultra-contemporary shooting stars and NFTs

Of the 2,500 high-net-worth-individuals surveyed by the UBS Art Market Report[9] in 2021, two-thirds indicated that their interest in art collecting has actually increased over the past year.

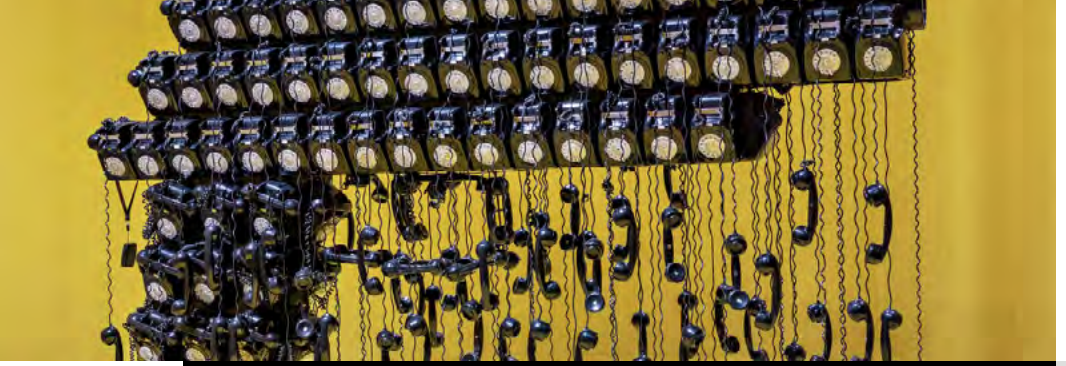
And among those high-net-worth-collectors, Asia-based[10] millennials were the biggest spenders, with 30% of them reporting they had spent more than US$1 million in art acquisitions in 2020.

Naturally this shift in collectors' demographic is not only exacerbating the focus on digital art and young and upcoming artists (who are usually hard-to-get in the primary market), but has also direct consequences on the traditional promotional structure of the art market. The inclusion of historic non-fungible tokens (NFTs) at cross-category auction sales—such as the Christie's evening sale—reflects the interests of this very active younger generation of collectors, particularly in Asia.

Can the ultra-contemporary shooting stars of the millennials be easily pledged as collateral? The 'comparative market data' approach for appraisals makes little sense in such a volatile segment of the market. A great illustration of the volatility of some of these young emerging stars is Kaws, whose works generated stratospheric performances at auction in 2019. However, last year Kaws' market had already shrunk by 77% versus 2019, and if the current trend persists until the year end, the total auction turnover could decrease again by another 44% in 2021.

It is very difficult to predict such a brutal reversal, but a key observation is that trends are getting shorter, as price explosions are followed by a substantial price correction within a couple of years. Many of the younger emerging artists will suffer from such volatility, which affects their long-term potential. Indeed many artists will never recover from such a drastic price correction in their early career, as collectors suddenly rush to sell their works altogether. The 'boom and bust' of Zombie formalism in 2014 and the fate of those artists remains a good cautionary tale. The Asian audience (a major acquisition force since the pandemic) can also quickly disappear, as we have seen post-2011, even though the current economic and political context remains very different.

6 Mark Grotjahn is another example of the 'male goes stale phenomenon'. In 2017, his auction volume reached a record EUR27.5 million, while total auction volume for 2020 tanked at EUR2.5 million (as of end of June 2021, auction volume still lingers at EUR2.8 million). Meanwhile his bought-in rate for 2020 shot up to 50% (compared to 14.7% in 2017)
7 Only works on paper with a low estimate of at least EUR10,000 have been taken into account. (LINK Management analytics)
8 Equally, looking at the number of works on paper that sold within the range of the low and high estimate at auction, that percentage decreased from 30% to 19% from 2019 to 2021
9 The Art Market 2021, Art Basel UBS report, prepared by Dr. Clare McAndrew, p266
10 The Art Market 2021, Art Basel UBS report, prepared by Dr. Clare McAndrewp266



Would you consider NFTs as collateral for art-lending purposes?
Definitely not at this stage. First of all, NFTs display exponential volatility. Not only are the prices of NFTs currently immensely volatile, but the underlying cryptos used for payment are themselves undergoing extreme price movements. Furthermore, it appears that the safety of the technological protocol has been over-estimated. One of the main advantages of an artwork issued as an NFT, lies in its absolute uniqueness. An NFT cannot be replicated, thus crypto investors consider that much of the implied value of a NFT derives from its scarcity and uniqueness. However, a hacker has recently managed to produce a copy of Beeple's NFT 'Everydays: The First 5000 Day', which was sold in March for US$ 69 million. He has even published a website, where the newly minted ('sleepminted') copy is currently for sale[11]. We may be in the early stages of a new art form, but it is far too early to make it eligible for an art lender.

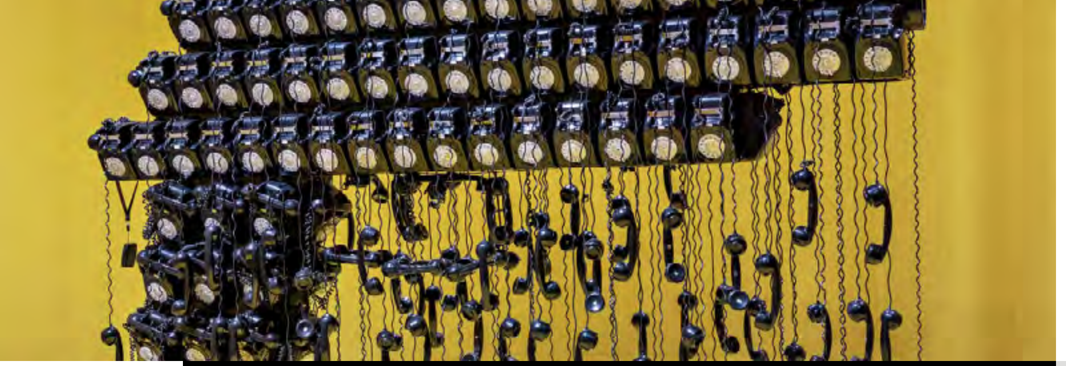
The art-lending industry
Before the pandemic, we had already observed a concentration of players not only in the US, but also in Europe, being taken over by direct competitors or financial institutions looking to diversify their product offering into art. This concentration is a sign that traditional business models derived from the financial industry may not always be suited to the scope of art-lending. There can be discrepancies between the size of the capital funding those ventures, and the actual size of the loan book after a few years of activity, putting pressure on those companies to generate new deals, which could lead to under-estimating risks. It is essential in this industry to be able to choose transactions with the most appropriate collateral, where the chain of ownership is clear and the quality of the underlying artworks undisputable. Banks remain quite reluctant to offer non-recourse art loans, and prefer to work with boutique lenders to satisfy a specific need. The typology of collectors has remained the same in terms of wealth, even though there is growing interest from a younger generation.

Before the pandemic, we had already observed a concentration of players not only in the US, but also in Europe, being taken over by direct competitors or financial institutions looking to diversify their product offering into art.

In Europe, the art-lending industry is still held in the hands of a few specialized players, and the lack of a European-wide legal framework for pledges demands a great understanding of the specifics and legal limitations of each European jurisdiction. There is no project in the near future to harmonize legislations and the fragmented legal landscape remains a brake to the streamlining of processes. For those with collections spread out across multiple jurisdictions, it can sometimes make the legal aspect a very important and time-consuming component of the structuring of each deal.

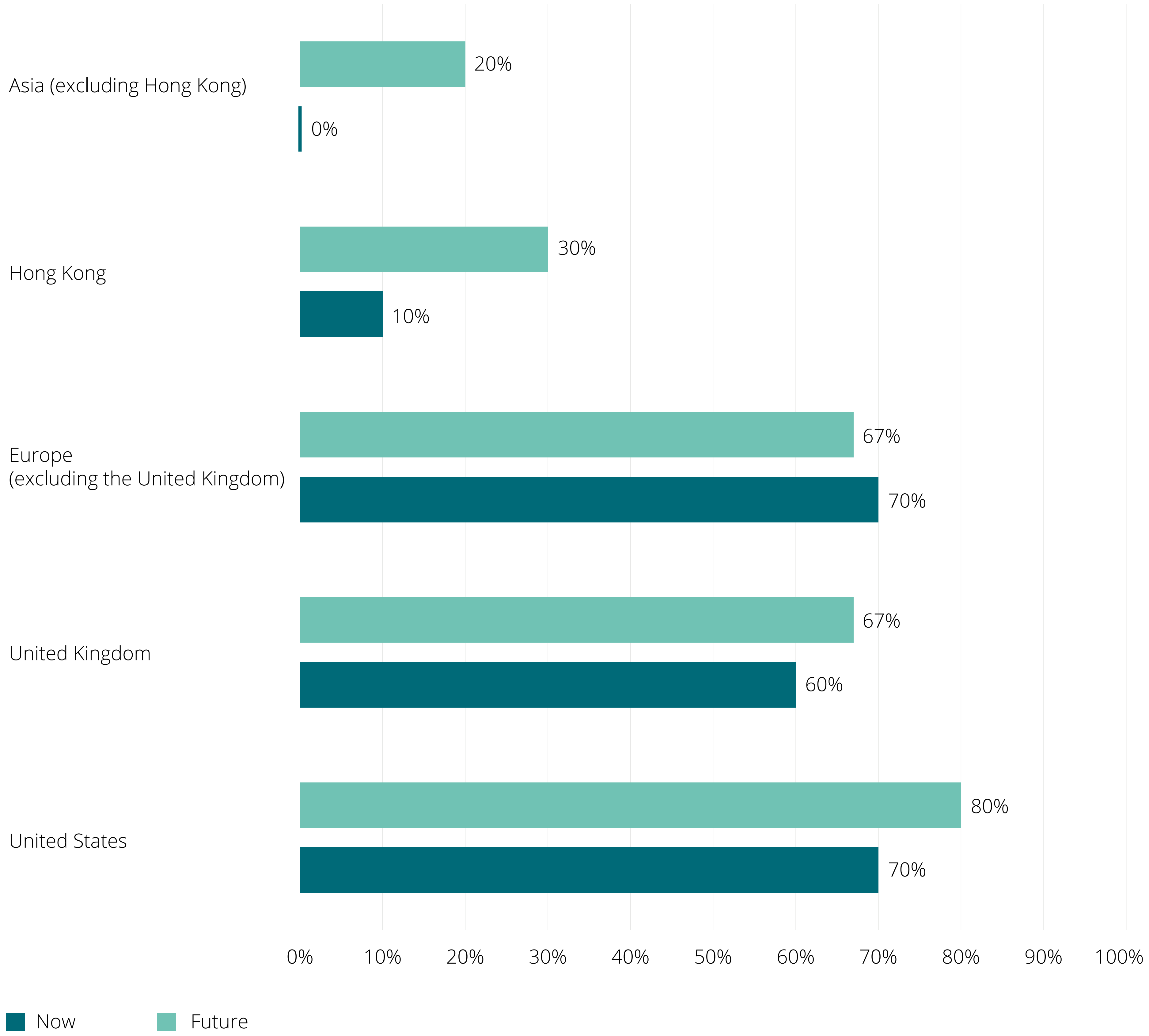
To conclude, beyond the legal diligence that is required when it comes to selecting artworks—whether as collateral for an asset-backed loan or for an acquisition—one needs to keep in mind the cyclical nature of art trends. Thus tracking market metrics and constantly gleaning first-rate information is a necessary exercise for art market players that are bound by narrow time horizons—a defining feature of the art-lending business. Equally, collectors that wish to market-time their acquisitions and sales of artworks, need to anticipate the cyclical phases that govern most artists' price evolutions.

11 Artnet, The Gray Market: How a Brazen Hack of That $69 Million Beeple Revealed the True Vulnerability of the NFT Market (and Other Insights), 21 April 2021



Key regions for art-secured lending business—now and in the future

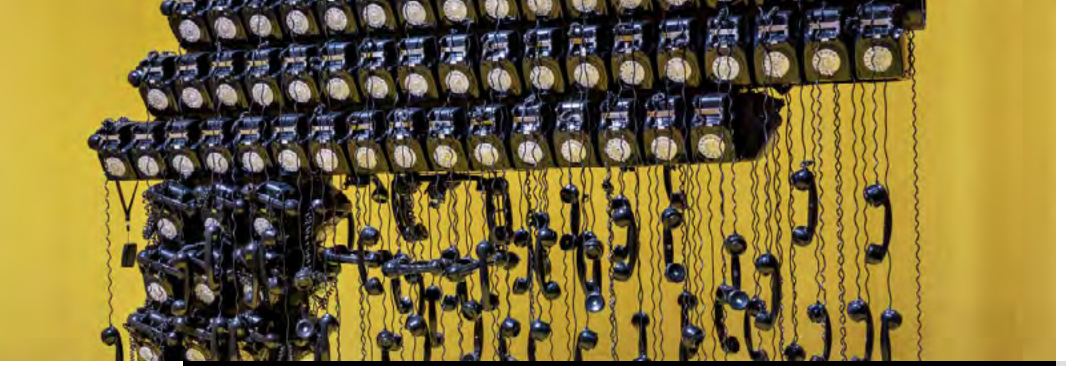
Figure 81. Which of the following regions are most important for your business at the moment?
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021



Hong Kong could become a strategic center for art-secured lending in the future
70% of art-secured lenders identified the United States and Europe as the most important regions for art-secured lending, with 60% singling out the United Kingdom as a key region. The parity between the United States and Europe is likely to be a sample size effect, as five of the art lenders surveyed are based in Europe and five in the United States. However, it is interesting to note that these lenders see the Asian market's potential for growth, with 30% saying Hong Kong will become a strategic center for art-secured lending services, followed by 20% who identified wider Asia as a market with future growth potential.

30% of art lenders say that Hong Kong will become a strategic center for art-secured lending services.

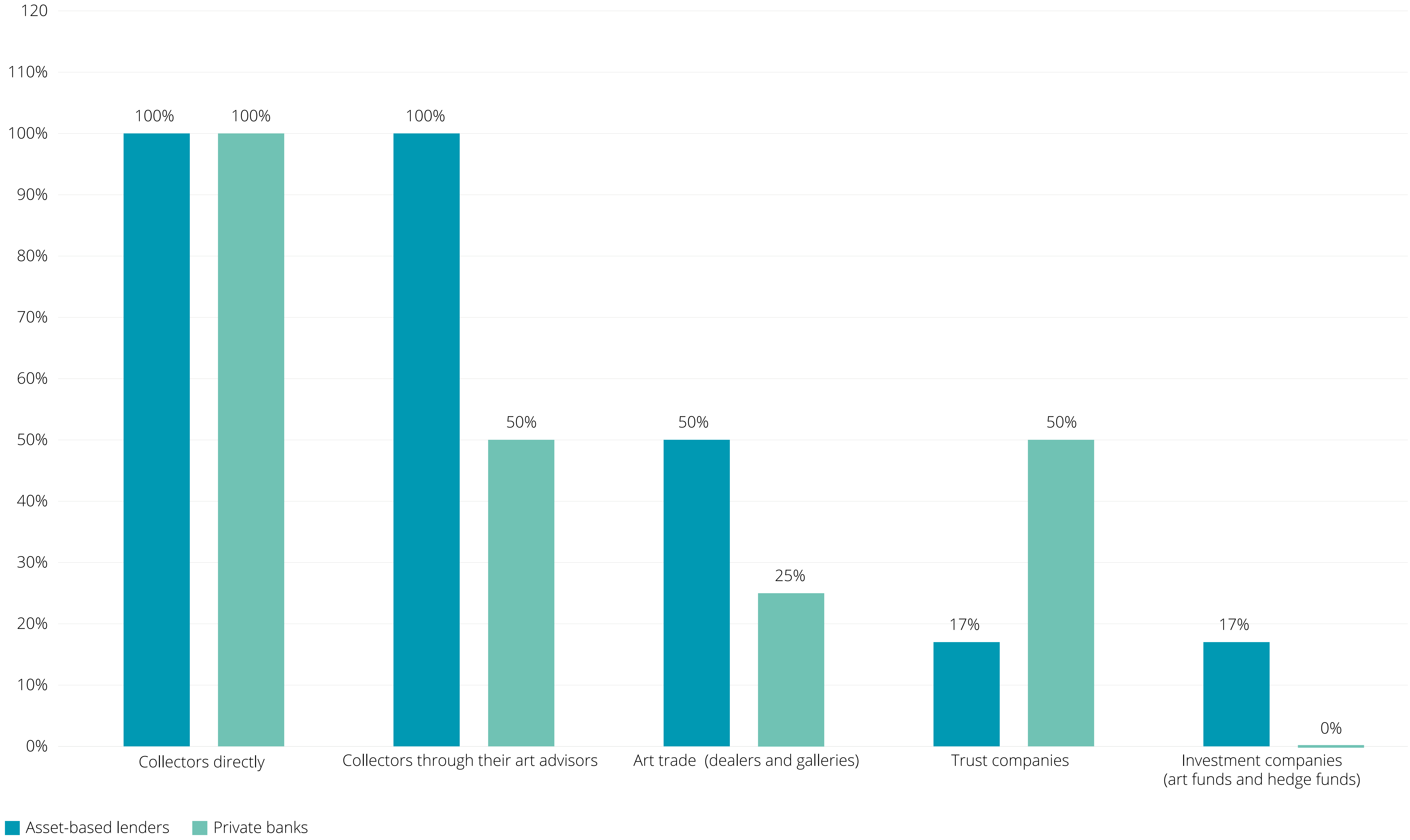
Dorothy
©Unidade Infinita Projectos - 2007-2010



Important client groups

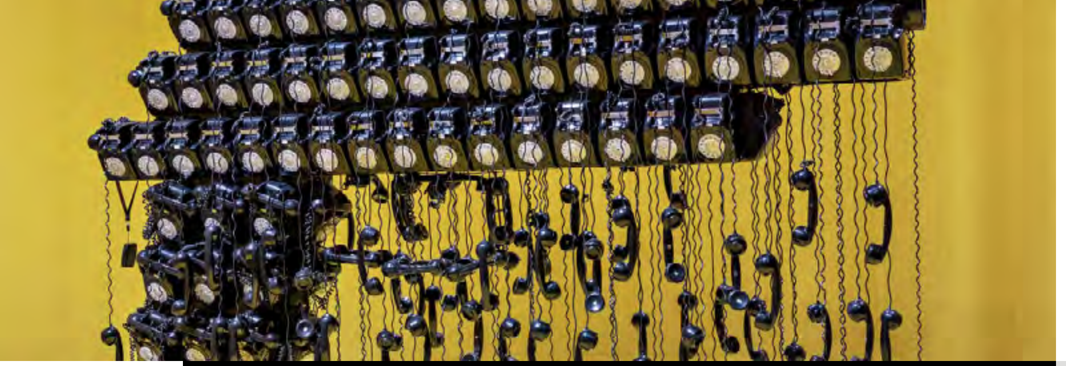
Figure 82. Over the last 12 months, who would you rank as your most important group of clients?

Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021



Strong focus on private collectors

All the art-secured lenders surveyed rated private collectors as their most important client demographic, either by working with them directly or through their art advisors. Half of the asset-based lenders rated galleries and dealers as their most important clients; however, only 25% of private banks said the same. Half the private banks identified trust companies as another important client group for their art-secured lending services, compared with 17% of asset-based lenders. Only 10% of art-secured lenders rated investment companies as an important client group at the moment.



Future

Figure 83. In the long-term, do you see art secured lending becoming a standard financing tool, the way we would look at mortgages for real-estate?
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021

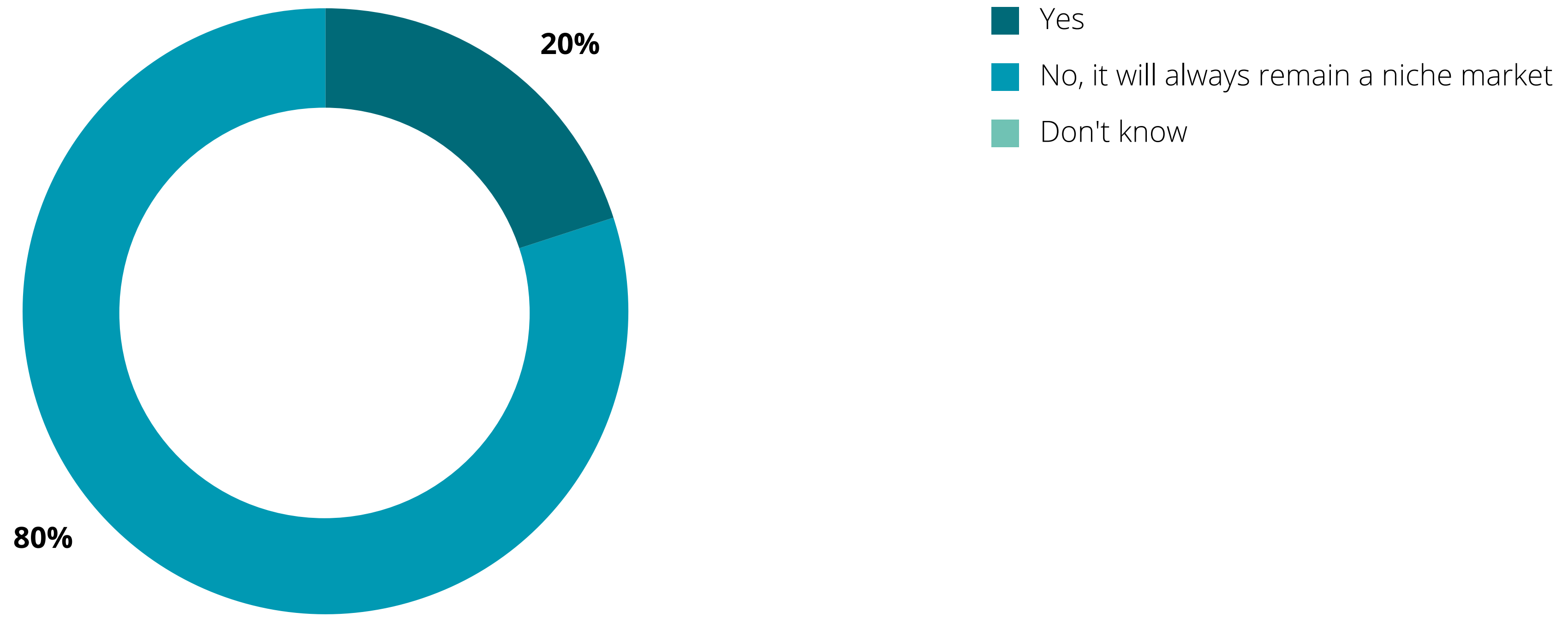
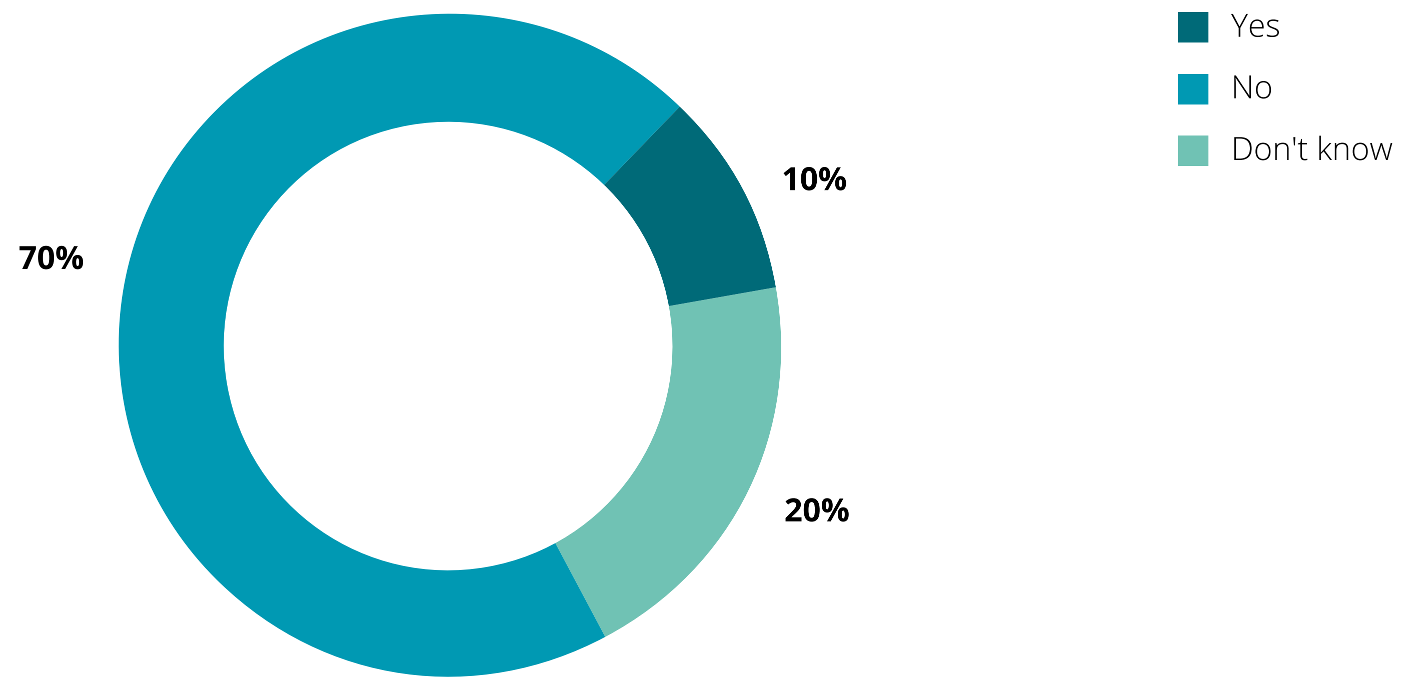
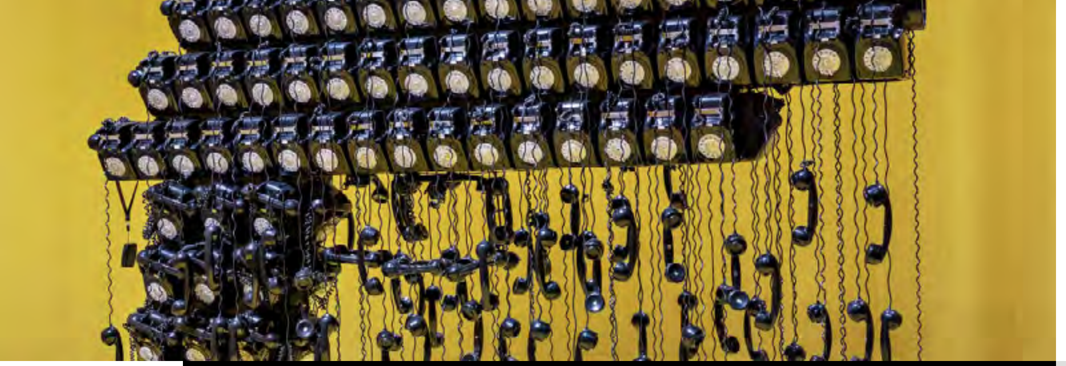


Figure 84. Do you consider it realistic that the art secured lending market has the potential to reach $500 billion in outstanding loan in the foreseeable future?
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021



Most believe the art-secured lending market will remain niche
80% of art-secured lenders do not believe that art-secured financing will become a mainstream product like mortgages in the real-estate market, believing it will remain a niche market. However, 20% believe there is significant potential for art-lending services going mainstream in the future, with 10% believing the art-secured lending market could reach US$500 billion. With the current market size less than 5% of this future potential, there is much room for growth; however, certain challenges must first be addressed as illustrated on figure 87 on p.215.

Can the tokenization of non-bankable assets like art support further growth in this sector? While only the future will tell, the technological developments around blockchain mean we should watch this space. In the article in Section 6 on p.249, Look Lateral explores how this approach could potentially work.



Wealth managers, collectors and art professionals—survey findings 2021

Figure 85. % of wealth managers offering art-secured lending services
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021

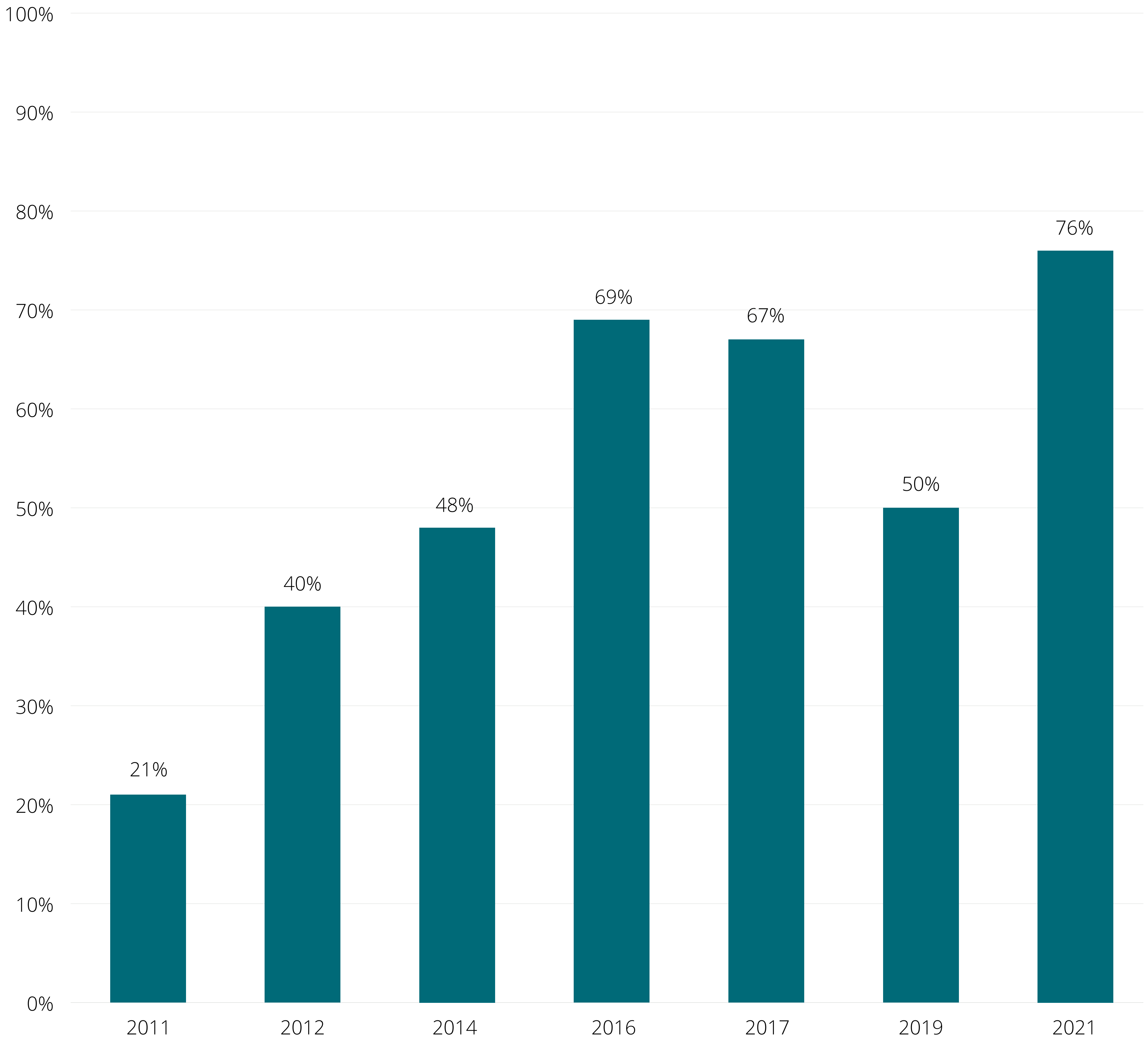
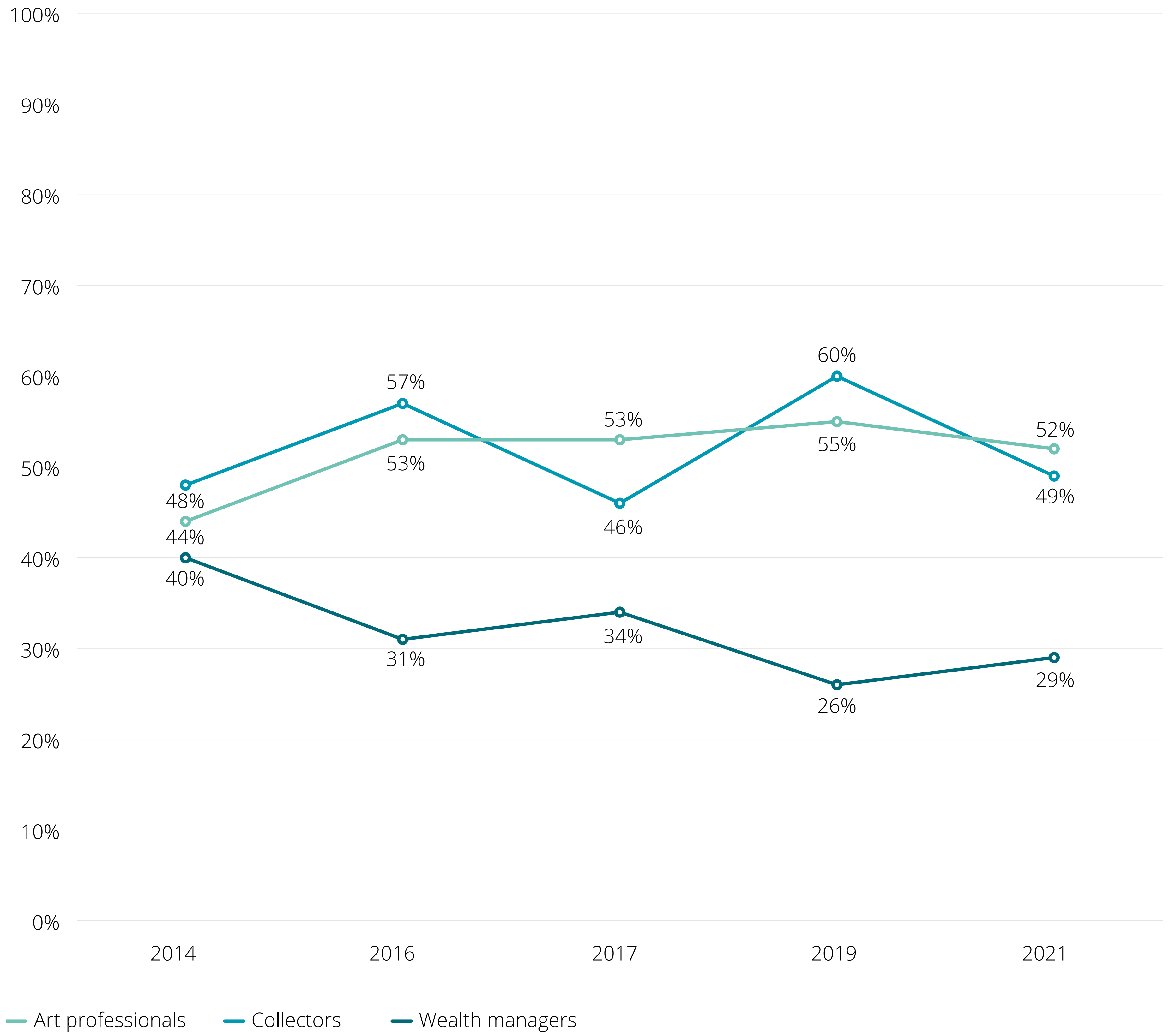
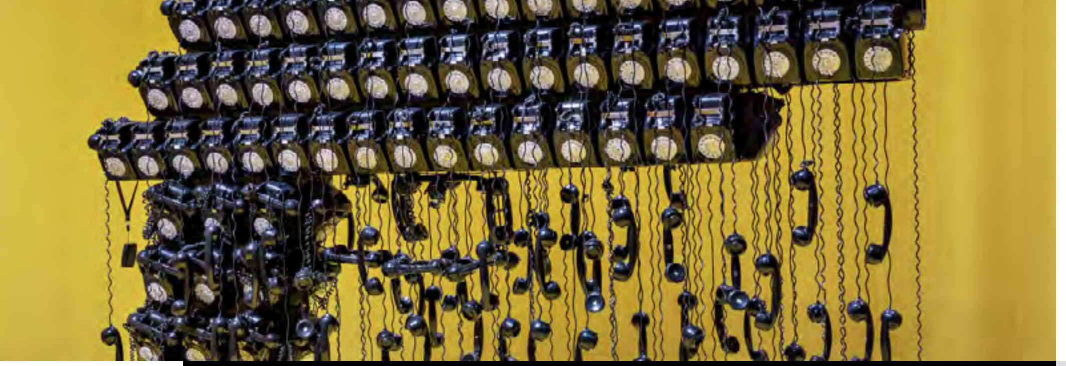


Figure 86. Gap Analysis: How relevant is art secured lending to you and your clients vs what wealth managers are focusing on in the coming 12 months
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021





More wealth managers are offering art-secured lending services

76% of wealth managers with existing art-related services said they offered art-secured lending services, up from 50% in 2019. It is the highest reading over the last 10 years. Half of these wealth managers offered this service in-house and half through third parties. This uptick in the number of wealth managers providing art-related financing corresponds with the art-secured lending market's growth over the last year [see p.xx]. Nearly one-third (28%) of wealth managers said the COVID-19 pandemic had triggered a growing interest in art-secured loans from their clients, with 33% of art professionals saying the same. Over the next 12 months, 29% of wealth managers said art-secured lending services would be a strategic area of focus, compared with 26% in 2019.

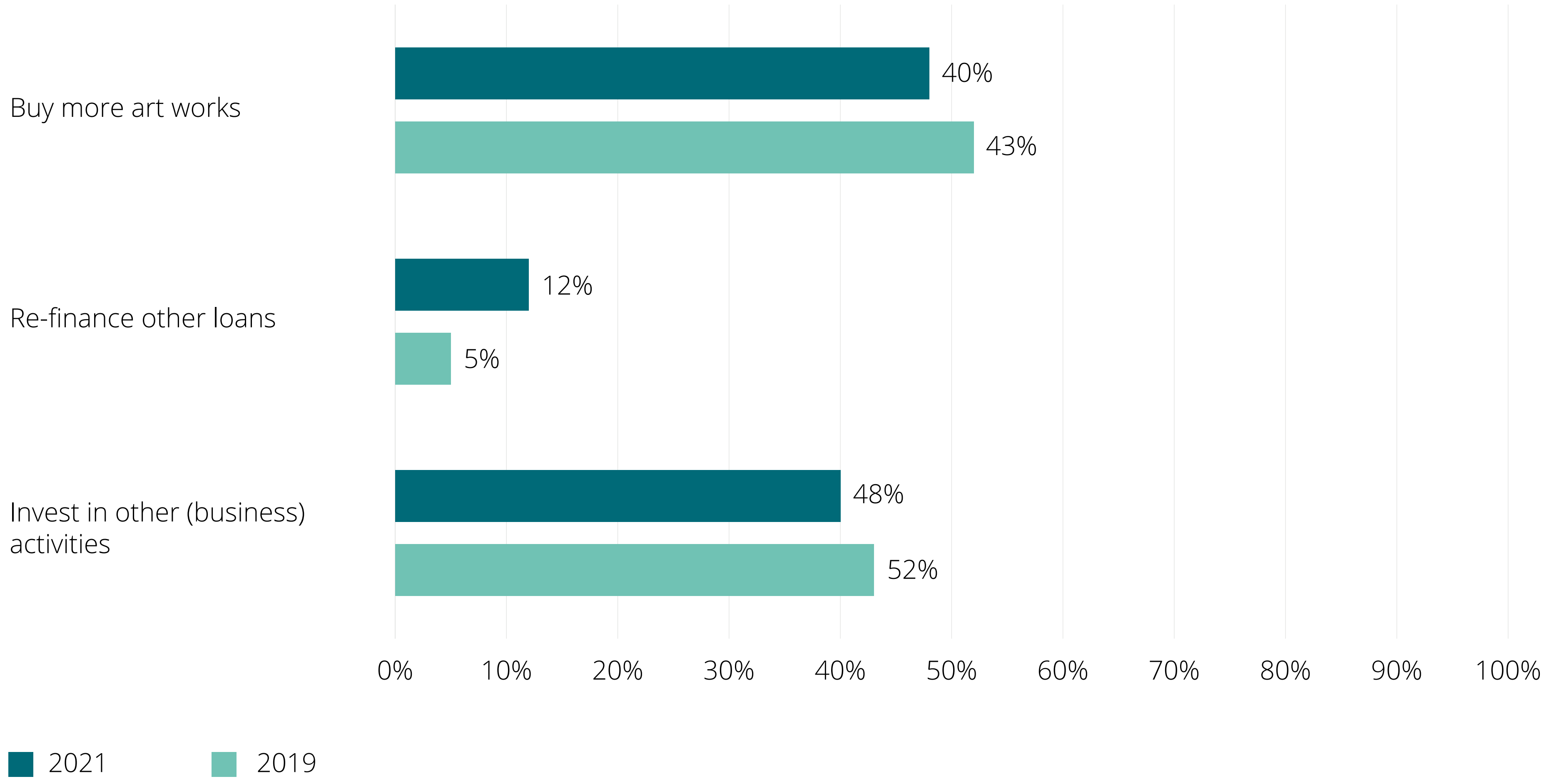
Collector demand for art-secured loans

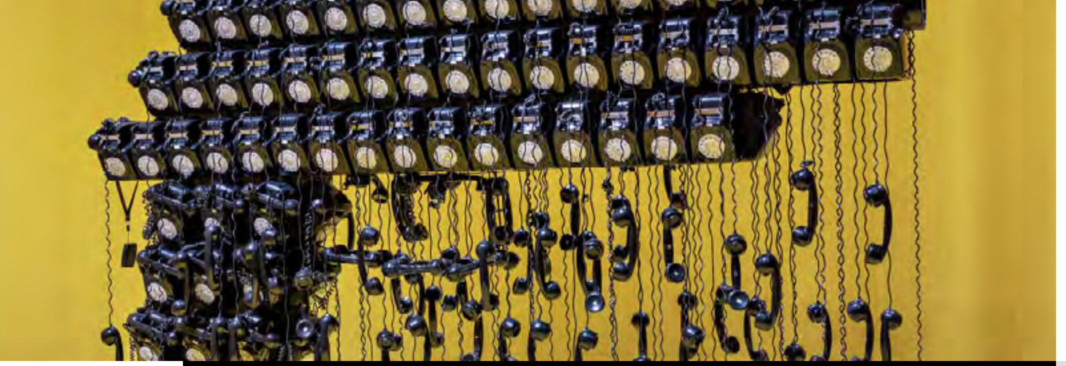
Almost half (49%) of collectors this year identified art-secured lending services as some of the most relevant services that wealth managers could offer, with 52% of art professionals echoing this view. Most (74%) wealth managers said they expected the demand for art-secured lending services to increase in the future, with 72% of collectors and 74% of art professionals saying the same. In this year's survey, 6% of collectors said they had used their art collection or an artwork as collateral for a loan, but 51% said they would consider it.

Key reasons for using art as collateral for loans

This year, 48% of collectors said their main motivations for using their art collection to secure a loan would be to finance the acquisition of more art, 40% said they would use it to invest in other business activities, and 12% said they would use it to refinance existing loans. Most (70%) wealth managers stated that, in their experience, collectors predominantly use the loan proceeds to invest in other business activities, 19% said they would use it to finance new art purchases, and only 11% would use their art collection as collateral to re-finance existing loans. This suggests that collectors are using non-traditional art lenders (asset-based lenders) for acquisition finance, rather than relying on their banking relationships.

Figure 87. Collectors: What are or could be the main reasons/motivations for using art as collateral for a loan?
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021





Lack of liquidity
Art market illiquidity remains private banks' biggest concern, with 73% saying this is a key hurdle in providing art-secured lending services, up from 66% in 2019.

Lack of knowledge
70% of private bankers said that a lack of knowledge about the art market was a key hurdle for providing art-secured lending services, compared with 61% in 2019. This signals that most private banks are still hesitant to fully embrace art-secured lending because their art market knowledge is insufficient to make informed decisions. However, with data, research and analytical tools increasingly available on the market, this concern is likely to be addressed soon. For example, we have seen new initiatives like Artmaven, a marketplace connecting verified experts from the global art market with employers, organizations and collectors. These initiatives could be a valuable resource for the wealth management industry to find the right expertise and knowledge.

Risk assessment: 65% of private bankers identified the difficulty in measuring and assessing risk as a key hurdle to incorporating art-secured lending in their art and wealth service offering, down from 71% in 2019. With improved data and new models and tools for art risk management entering the market (see p.218), we are likely to see more private banks entering the art-secured lending space.

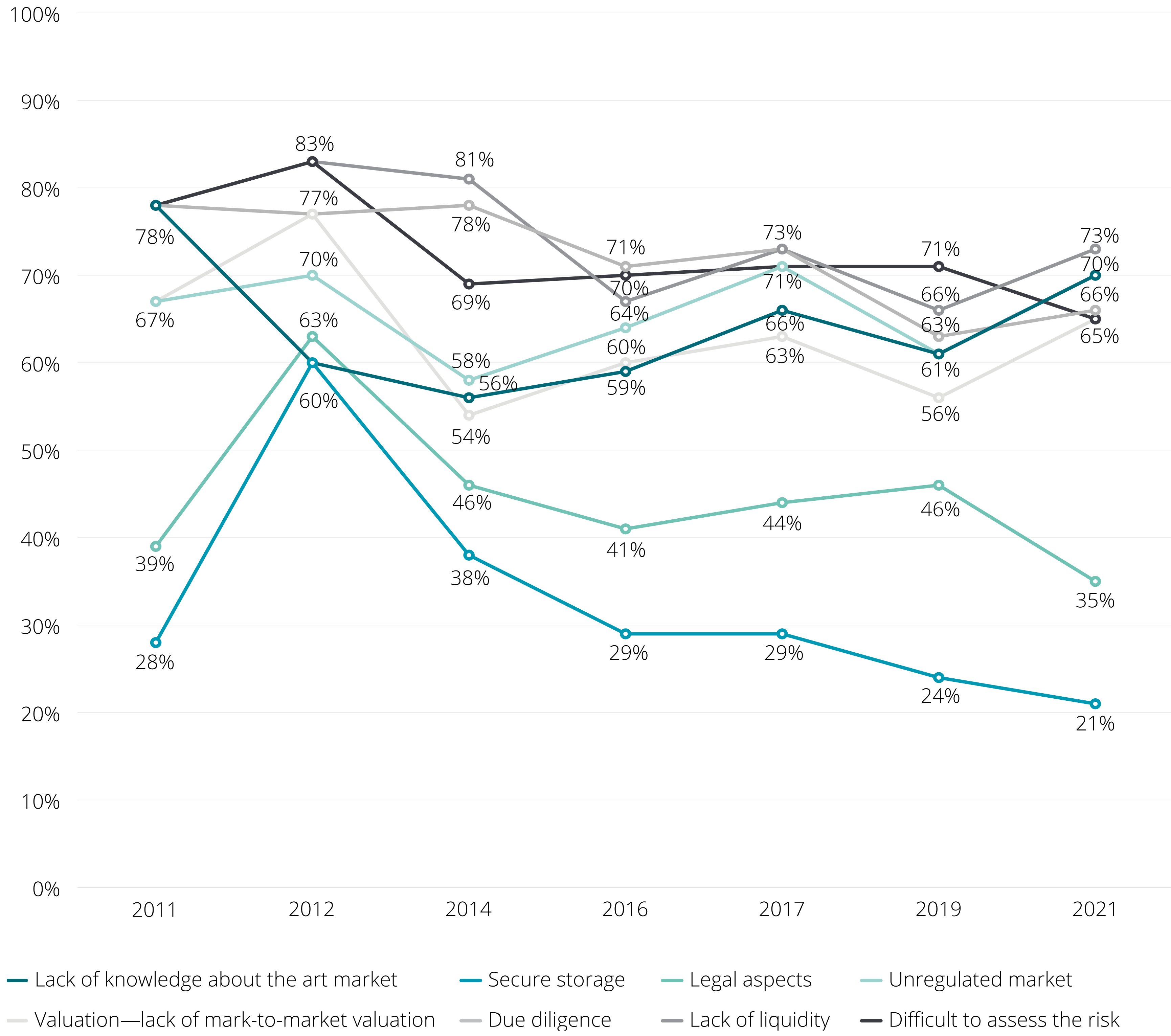
Due diligence
Private banks also identified performing due diligence on artworks used as loan collateral as a major issue, with 65% saying this was one of the key hurdles this year, up from 56% in 2019. Again, solutions could be on the horizon, with blockchain technologies gaining mainstream interest as a potential title register and provenance tracking tool. The new EU and US anti-money laundering (AML) regulations are also likely to boost the art market's transparency, potentially improving the due-diligence process.

Valuation risk
Valuation is another concern among private bankers when it comes to art-secured lending, with 66% identifying this as one of the main hurdles (up from 63% in 2019). The current market volatility has made valuation more challenging. With the advent of big data and artificial intelligence (AI), new companies are moving into the art valuation space alongside the traditional appraiser community, and we anticipate that the combination of better data, new technologies and human expertise will become the hybrid model of the future.

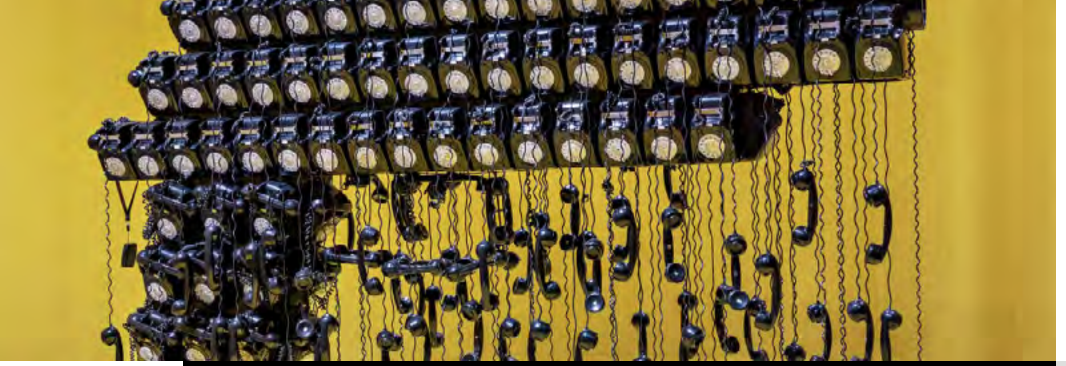
Unregulated market
70% of private banks felt that the unregulated nature of the art market was a key challenge when offering art-secured loans, compared with 61% in 2019.

Art-secured lending: what are the key challenges when using art as collateral for a loan?

Figure 88. What do you feel are the main hurdles for providing art lending/using art as collateral to the bank's current clients?
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021



Private banks are still hesitant to fully embrace art-secured lending because their art market knowledge is insufficient to make informed decisions.



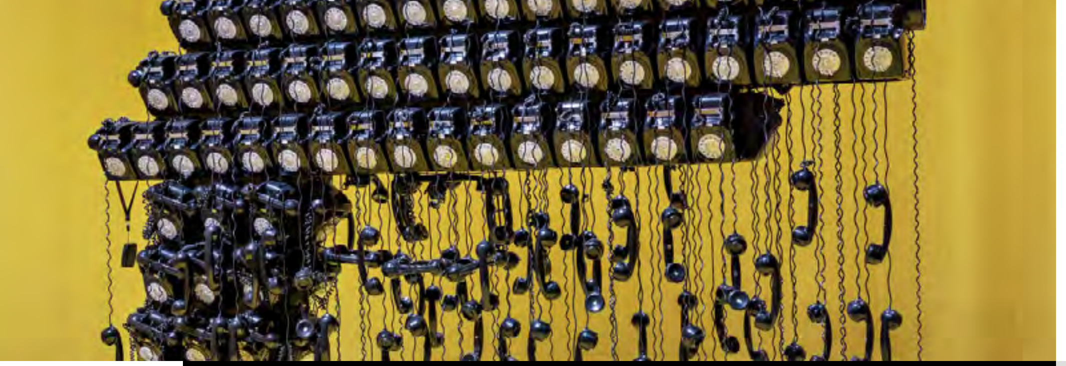
For example, Belgium is one of the rare European countries where its national pledge law favors the use of art as collateral.

Coração Independente Dourado
©DMF, Lisboa/© Unidade Infinita Projectos - 2004

Legal aspects
35% of private banks reported that legal aspects were a key challenge when offering art-secured loans, compared with 46% in 2019. This number is low considering the jurisdictional challenges in offering these services. The lack of a uniform legal framework across different global art markets (similar to the UCC in the United States) is an important factor. In its article on p.208, Griffin Art Partners highlights that the lack of a European-wide legal framework for pledges demands a deep understanding of each European jurisdiction's specifics and legal limitations.

For example, Belgium is one of the rare European countries where its national pledge law favors the use of art as collateral. Under Belgian law, a pledge is validly constituted by merely concluding a pledge agreement. There is no need for the dispossession of the pledged asset to render the pledge effective vis-à-vis third parties. This feature is critically important in the art sector, considering the cost of transport, insurance and maintenance of artworks. For non-possessory pledges, the pledge is perfected through its registration with the National Pledge Register, a virtual register where pledges are recorded for a maximum fee of EUR500. The register also offers the possibility to consult the situation of any Belgian legal or natural person regarding their assets that have been pledged.

Technological development is also taking place in the art-secured lending place
Better technology and data insights will lead to continued growth by supporting more nuanced decisions, including the type of collateral to accept and how much to lend, as reported by Dana Prussen from Bank of America. A UK FCA-regulated fintech, Overstone Art Services, has developed risk monitoring tools dedicated to art-secured lending. In its article on p.218, Overstone Art Services shares its views on the development of the art-secured lending market. And, new developments around the tokenization of non-bankable assets, such as security tokens (STOs), could catalyze future growth in the art-secured lending market by using art STOs as a pledge. In its article on p.249, Look Lateral explores how this could be applied.



Chen Chowers
Head of Operations,
Overstone

Case study

Managing liquidity risk in the art market

Risk monitoring tools and the development of the art-secured lending market

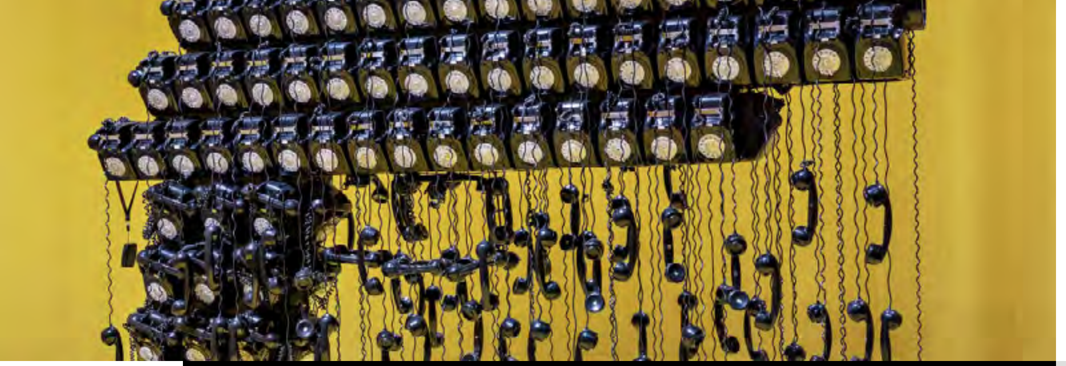
Through years of experience in the market, FCA-regulated fintech, Overstone has come to see that the main barrier to unlocking art as an asset, is the lack of a systematic, repeatable, and transparent process of assessment, on par with other asset classes. While art valuation has been performed for centuries, the missing link to the financial industry is understanding liquidity.

If art is to be treated as a financial asset, we must be in a position to measure and communicate risks with appropriate financial metrics. This could allow the unlocking of a vast opportunity, moving beyond what is today a highly manual, subjective, opaque, and unregulated activity. The combination of liquidity and risk tools along with the current changes in regulatory environment, including the recent introduction of the fifth anti-money laundering directive (AMLD5), are steps towards creating the necessary infrastructure for this new asset class.

Recent developments in the art-secured lending space

In late March of 2020 when the European markets were realizing the rapid advance of COVID-19, uncertainty and ensuing volatility were the general response. The following months were characterized by a continued search for liquidity, whether to answer margin calls, or take advantage of unexpected investment opportunities. In that first week of volatility alone, Overstone saw inquiries from collectors for loans against art collections surge by over 400%. Art, 'the last unleveraged asset', was suddenly reconsidered by even the most traditional institutions and collectors as a (much needed) source of liquidity. A traditional Swiss-based private bank had been tentatively examining the art secured lending proposition for a year prior, however not taking proactive steps. Following a surge of requests from their clients, our art backed lending platform was onboarded within a week.

Demand for art-secured lending has been growing steadily over the last few years, with 2020 seeing an exponential rise, in what we believe is an inflection point for the art-secured lending industry. The behavior of the markets has underlined the importance of liquidity versus static value. When the financial markets experienced volatility and liquidity was required, it was art, the most underleveraged asset that could most easily release it. Collectors realizing a new source of liquidity, and institutions who have now begun to lend against art, will not backtrack. From our standpoint across the market, and based on work with both borrowers and lenders, we conclude that the industry is heading on a route of rapid growth, as 2020 has been instrumental in bringing art-secured lending to the mainstream of private banking and wealth management.



Demand shift for art-secured lending services

Overstone has been engaging with major global private banks for years, enabling them to begin offering art-secured lending in Europe and the US, and currently expanding to Asia, allowing the risk departments to understand downside risks, and providing a powerful relationship tool for private bankers. This position has enabled Overstone to observe the profound shift the industry has undergone. While the bigger banks tend to take long periods of time to discuss and onboard a new service as unique as art-secured lending, the process has accelerated significantly in the last year. This was unequivocally due to a rise in client demand which prompted the banks to seek ways to incorporate the service. The pattern was clear. In the early days of COVID-19, Overstone was approached by collectors and family offices searching for lenders, and a month following Overstone was approached by the banks. The onboarding of at least half a dozen new private banks in Europe and the US to our platform can be attributed to the events of 2020. At least double that number are in advanced stages of examination. The growth of players active in the sector is contributing to more awareness among others, and Overstone has recently started working with Avaloq to ease future integrations and offerings for new banks.

This accelerated pace of the big institutions however, pales to other industry players: the smaller European and American local banks. These operate as a hybrid of a financial institution and a startup. With close relationships to their local clientele, significantly less internal process, and a more outsourced approach to services, their pace of incorporation of art-secured lending is swift and completed within a couple of months.

Challenges facing financial institutions that want to offer art related services

Art-secured lending has been steadily growing in recent years, however the size of the industry compared to the opportunity is negligible. The value of art used as leverage compared to its potential is so modest, art can still be classified as an unleveraged asset. A large-scale development and adoption of art-secured lending was hindered in the past by the age-old challenge of 'lack of communication'. Art has historically been valued for its aesthetic qualities, a concept foreign to the financial and tech industries, whilst the art market relies on its own internal codes and standards. Concepts of systematic, objective valuation, downside measurable risk, and transparency, all required by financial services and technology companies, are similarly challenging for the art industry.

Overstone's risk monitoring tools

Overstone has worked closely with select risk departments in major financial institutions over the last 5 years to develop the Art Risk Monitor™ score (ARM™), a measure of the liquidity and volatility risk of individual art works. Often overlooked, and in essence the flip side of value, liquidity measures whether an artwork can be sold at an expected price in current market conditions, at a specific point in time. The ARM™ score is a tool to measure the downside risk. The algorithms feed off a triangulation of publicly available and proprietary data, including over 10,000 artists and 2.5 million sale results, covering any artist with presence in the secondary auction market, from the Renaissance and up to the hyper-contemporary auction stars. Scores are irrespective of medium but require existence of significant data.

The ARM™ is scored on a scale of 1-100, with 100 being the most liquid. A low liquidity score indicates a lack in depth of market and demand, affecting the sale performance of a work, impacting if the work sells or not, and how high will the price achieved be. The ARM™ score is a percentile, and force ranks all objects in the market. Thus, a work with a score of 75, will be more liquid than 75% of the works that have appeared in the overall art market in the last 5 years. The distribution of the scores is in a bell curve, and many more art works will have a score around 50, which will be the average, than works which score in the extreme high or low percentiles.

The liquidity score changes dynamically as auctions occur in the market. We have found that a trend in liquidity is typically a leading indicator to future price changes, as it hints at a drop or rise in demand levels.

Price volatility and elasticity for art are statistically lower than most assets, the critical factor of market risk, is liquidity, the ability to sell at a given point in time. This is measured per object, and two objects by the same artist could have a very different liquidity and market depth. Two works by Fernand Léger can be used as an example, *Le Campeur, 1er état*[12], sold by Sotheby's in May 2019, received an ARM™ score of 67, and sold above the high estimate. Composition *(Éléments mécaniques)*[13] by the same artist, was offered by Christie's in October 2020, received an ARM™ score of 31, and was not sold. Each object is scored based on over a dozen parameters. The market of the artist is not the sole defining factor, but a context for the different interactions between these parameters. This contributes to different scores and performances as seen above for the two works by Leger.

What does this mean for lenders and borrowers?

Understanding the specific risks associated with each work, rather than being blinded by a famous artist, enables banks and collectors to create better, less risky collaterals. This contributes to an optimized risk/reward portfolio and more accurate, potentially higher, LTV's. The understanding of risk is an important step in treating art works as an asset.

When examining the robustness of the ARM™ score performance, as in the scatter chart below, we measure the ratio of the price achieved versus the estimate of the work. Any work sold at 85% of the low estimate or below, is considered a disappointing performance. Overstone back-tests its algorithm, by comparing auction results to scores given to the works. The graph below showing results from the Christie's ONE sale in July 2020, the X axis with ARM™ scores, the y axis with performance as ratio of the low estimate. There is a clear trend of increasing performance the higher the ARM™ score.

12 https://www.mutualart.com/Artwork/LE-CAMPEUR--1ER-ETAT/CC6E15A6D78682F4
13 https://www.mutualart.com/Artwork/Composition--Elements-mecaniques-/FA45CE366B417858

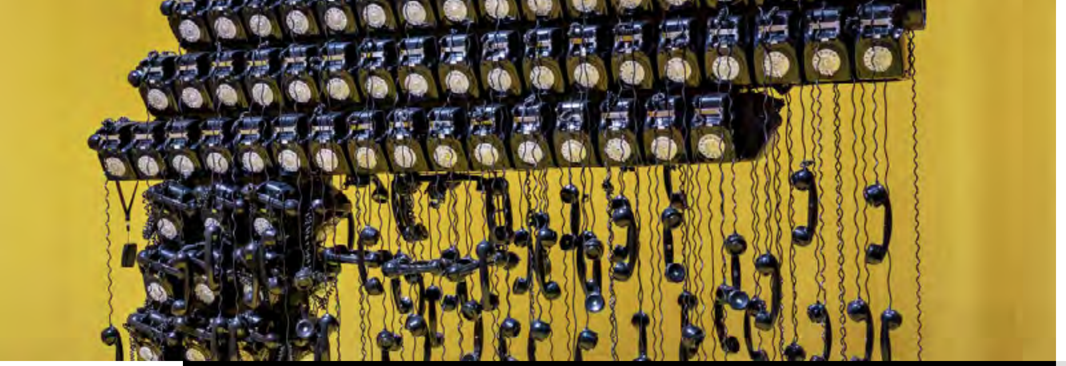
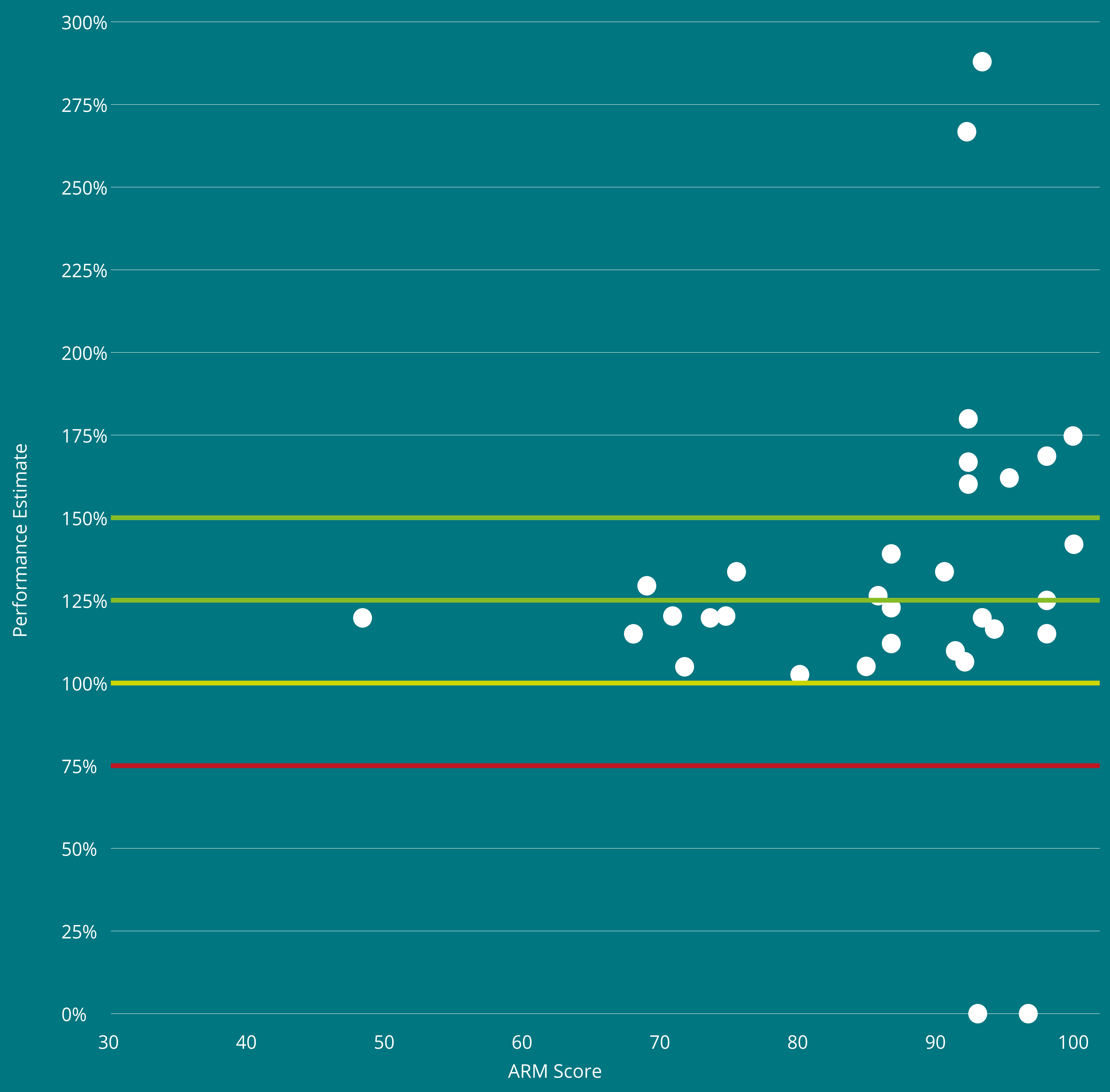


Figure 89. One Auction
Scatter chart of Christie's ONE auction sale results in July 2021: Performance vs. ARM™ scores



Key challenges for the future and how best to address them

As the field accelerates growth and new players arrive eager to claim territory, caution is called for. The more art is used as collateral, the higher the potential risk of market flooding should another global event generate a financial crisis. Data and research shows an interesting development in 2020, underscoring the importance of understanding a work's liquidity profile: while the art market had a significantly lower volume of sales during 2020, the value did not drop at the same rate. The items that are most liquid had higher realized prices versus their estimates compared to previous years, suggesting that even in a market downturn, highly liquid art assets will still sell well.

From Overstone's cross-industry work, we have noted that the liquidity metric is the missing link between the traditional valuation, which while suitable for the art world is not understood by external industries, and potential cross-industry partners. This link is what will allow growth at scale for art-secured lending. So far, most art finance products have been ad-hoc with a subjective or internal valuation process and risk making decisions. The key to growth-at-scale for art-secured lending and additional art finance products is a standardized, replicable process which considers the criteria of different industries.

Art & Investment

06

Altas Frequências
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Highlights

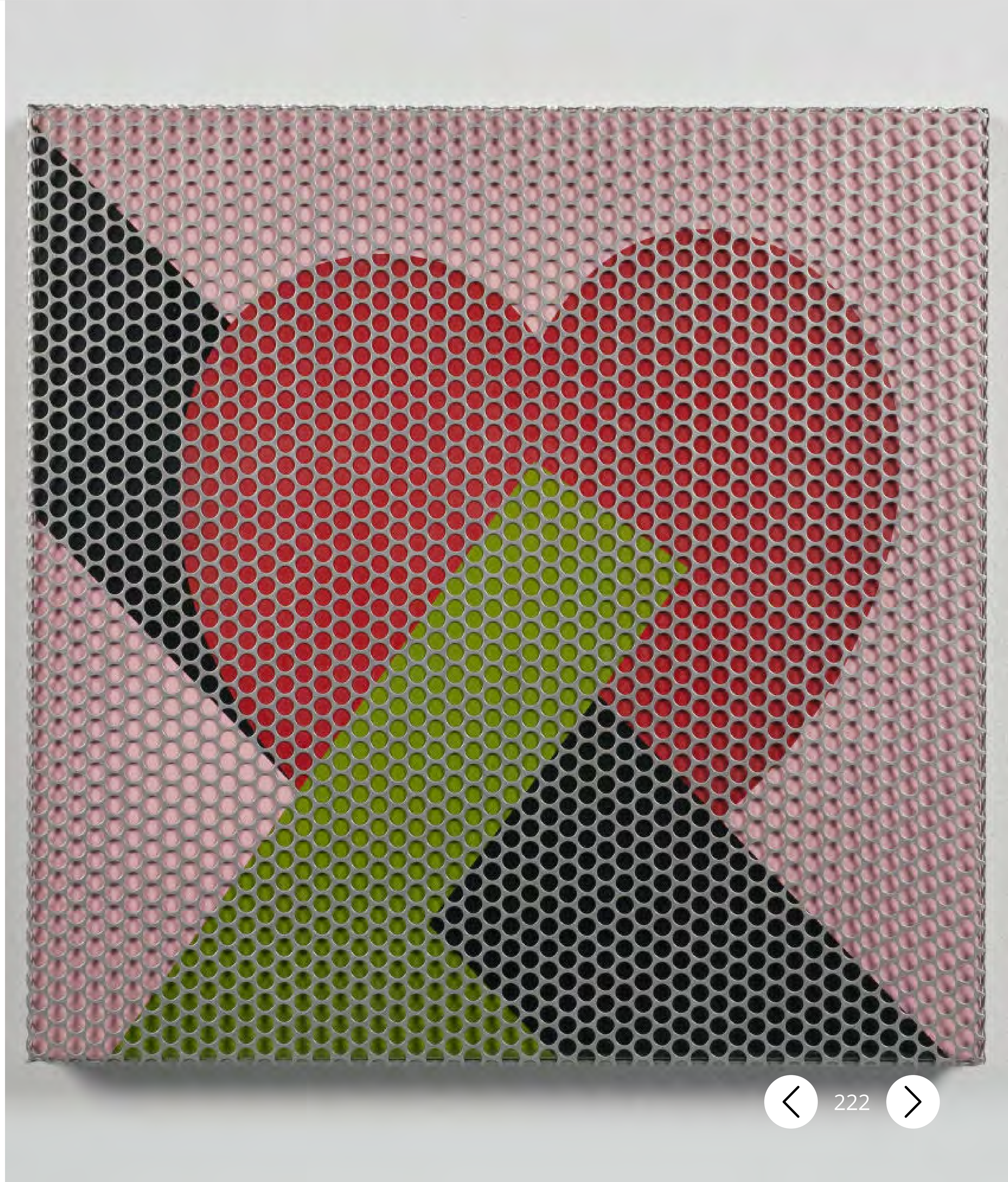
Artnet's indices display strong short-term returns for art and more moderate returns in the long run.
Despite an unprecedented and economically tumultuous 2020, the Artnet Index for Fine Art bullishly recovered from the second half of 2020 into the first half of 2021. The index produced a 4.9% compound annual growth rate (CAGR) between 2005 and 2020, and even a mildly positive return of 0.8% from 2019 to 2020. Looking at the Fine Art market's returns trajectory, investment cycles both in the short-run and long-run depict the reliability of art as an asset class during economic turndowns.

Strong performance across most art collecting segments in the first half of 2021
All but two of the art movements monitored by Artnet have gained momentum in the first half of 2021, with indices increasing between 3% and 38% year-over-year. Two of the strongest categories were Post-War and Contemporary Art. Following significant growth in returns after 2009, the two art movements have consistently and aggressively outperformed the S&P 500, continuing to surpass the financial indicator throughout 2020 and the first half of 2021. The Index for Global Post-War Art expanded by 38% in the first half of 2021, compared with the same period in 2020.

Art as a store of value
Art is regarded as a value-preserving asset class. The strong positive correlation between art and gold can indicate investors' perception towards art more as a value-preserving asset class than as an investment vehicle. Similar to gold, artworks are less susceptible to risks associated with financial market crashes than stocks and bonds. Because of art's intrinsic value as an object of wealth, art has historically been able to rebound and even grow faster than traditional asset classes during financial turmoil. This pattern was evident following the 2008 financial crisis. While the Artnet Index for Fine Art was able to recoup its peak value by 2011, the S&P 500 took five years to regain its standing. This pattern seems to hold true in the data Artnet continues to collect as global economies re-adjust following the latest health crisis.

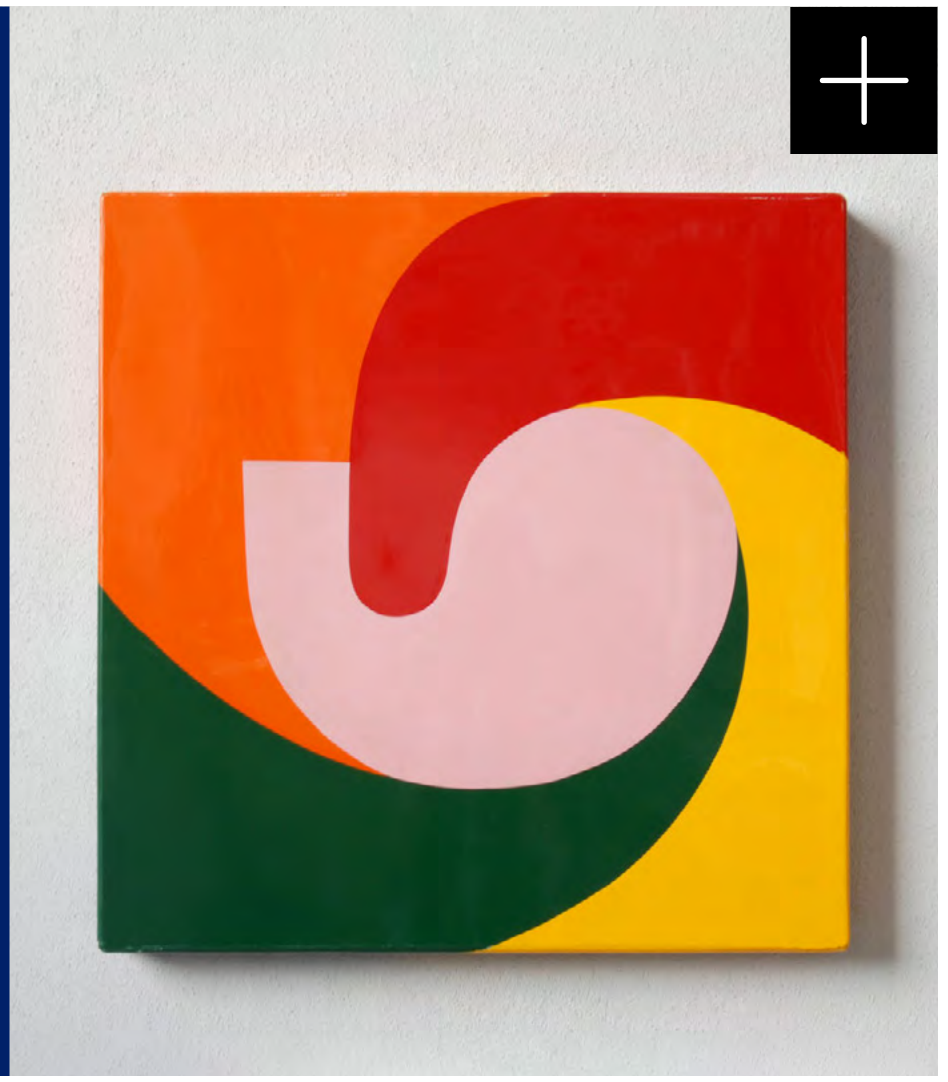
Direct investment and physical ownership of art remain core ownership models
Despite the increasing interest in new ownership and investment models for art and collectibles, 88% of collectors and 84% of art professionals believe that direct investment in art (i.e., the outright ownership of artwork) will be the most common form of art investment going forward, and 58% of wealth managers said the same.

Artnet's indices display strong short-term returns for art and more moderate returns in the long run.



Wild at Heart

21% of wealth managers said social impact investment products in culture would be of interest to their clients.



Fibra
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New interest in alternative forms of art ownership
In this year's survey, 33% of wealth managers said their clients had expressed an increased interest in non-fungible tokens (NFTs), fractional ownership (29%), art investment funds (25%) and social impact investment in culture (21%). Interestingly, 64% of collectors said the COVID-19 pandemic had triggered a new interest in alternative art investment products, with 65% saying that NFTs had generated the most attention. However, as the NFT market is currently unregulated, it is unlikely that wealth managers will embrace this in the short term. But as the market for asset-backed tokens (or security tokens) continues to develop, we will likely see increased interest among wealth managers in this area.

Younger collectors more tuned into recent developments in art investment products and services
64% of younger collectors[1] expressed a strong interest in NFTs (compared with 18% of older collectors) while 43% said fractional investment linked to artworks interested them, which is significantly higher than 17% of older collectors. During COVID-19, 86% of younger collectors had seen an increased interest in art investment products and services, compared with 61% of older collectors.

Social impact investment products
21% of wealth managers said social impact investment products in culture would be of interest to their clients (compared with 28% in 2019), with 28% of collectors and 31% of art professionals also identifying this as an area of strong interest. In line with global trends around social impact and an increasing focus on environmental, social and governance (ESG) investing, we are likely to see this interest grow in the future—71% of younger collectors surveyed said they were drawn to social investment products in art and culture, compared with 15% of older collectors.

Fractional ownership and tokenization
29% of wealth managers said they believed fractional ownership and tokenization of art and collectibles could become investment products of interest to their clients (up from 10% in 2019), with 26% of art professionals saying the same (up from 19% in 2019). Collectors remain slightly more cautious, with 21% saying this would be an investment product of interest (compared with 19% in 2019). This trend could attract a new investor base to the art market and support new philanthropic and social impact investment strategies like crowdfunding and co-ownership.

Traditional art investment funds see a revival among wealth managers
25% of wealth managers said art investment funds would be the most compelling type of investment for their clients (up from 17% in 2019), with 30% of art professionals saying the same (down from 38% in 2019) and 28% of collectors (down from 33% in 2019).

Security tokens and non-bankable art assets (nBAs)
A new financial infrastructure is developing around nBAs, which also includes art and collectibles. This could open up new opportunities for the wealth management sector to generate additional fee revenue, based on the estimated US$1,481 billion of art and collectible wealth held by ultra-high net worth individuals (UHNWIs) in 2020.

Security tokens enters the museum world
A recent initiative in Belgium, called Rubey, is offering a new alternative model of museum funding and collection financing. The Rubey Security Token Offering (STO) provides a new way of artwork funding for museums, in combination with long term artwork custodianship. This STO seeks to deliver both social value and revolutionize how we think about art investment.

1 The sample is based on 16 individuals out of 114 collectors surveyed in total. Although the sample size is small, these findings still highlight significant differences between the younger generation of collectors (under 35 years old) and the older generation of collectors (over 35 years old)

Introduction

The financial aspect associated with art and collectibles ownership has grown in importance since our last survey in 2019. More of today's collectors, particularly of the younger generation, are motivated to use art and collectibles as a portfolio diversification tool, a hedge against higher inflation, and a way to seek higher investment returns.

This section is divided into the following parts:

1. **Artnet: Past performance of art as an asset class**
   This part includes an art market performance analysis by Artnet that examines the performance of different art categories and art market segments between 2000 and the first half of 2021, including a comparative analysis of other asset classes.
2. **Sygnum Bank: Survey findings around art investment products and stakeholder preferences**
   In addition to art investment funds and direct investment in art, we have expanded this year's survey to include a more in-depth look at blockchain-based art investment products like asset tokenization, including the recent NFT phenomenon. We have studied the motivation and demand of both younger and older collectors regarding these new investment products, and how they could affect the art investment market in the future.
3. **Look Lateral Group: Digital assets, tokenization and fractional ownership**
   Building on our survey findings, we have invited several contributors to discuss the potential of this new technology, with articles from Sygnum Bank and Look Lateral.

Part 1. A post-pandemic look at the performance of art as an asset class

Cápsula
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Michaela Ben Yehuda
Senior Analyst, Business Intelligence, Artnet

Robert Cacharani
Manager, Business Intelligence, Artnet

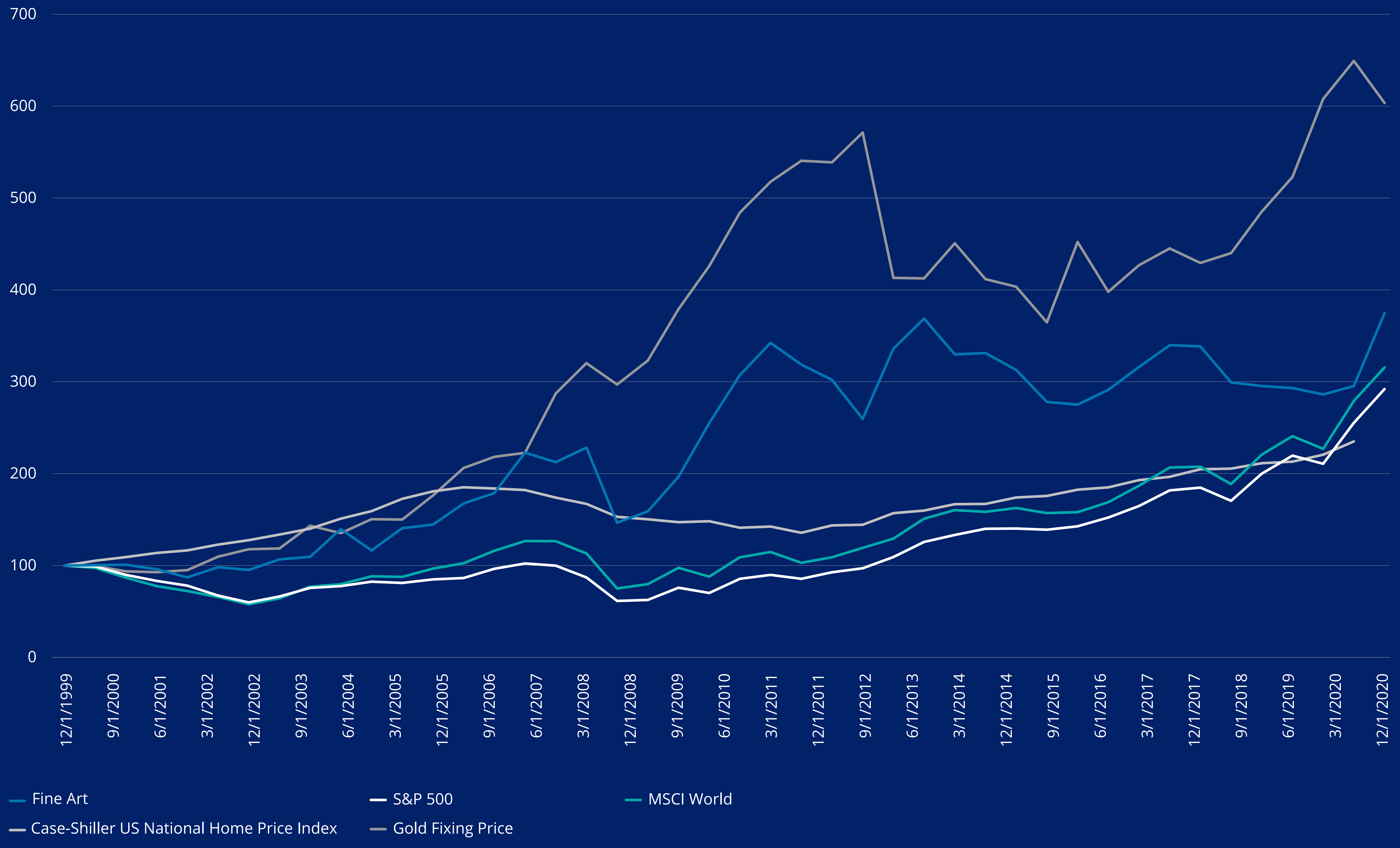
Expert voices

A post-pandemic look at the performance of art as an asset class

Evaluating the performance of art as an asset class through an early post-pandemic lens, the Artnet indices display strong short-term returns for art and more moderate returns in the long run. Despite an unprecedented and economically tumultuous 2020, the Artnet Index for Fine Art bullishly recovered from the second half of 2020 into the first half of 2021. The index produced a 4.9% compound annual growth rate (CAGR) between 2005 and 2020, and even a mildly positive return of 0.8% from 2019 to 2020.

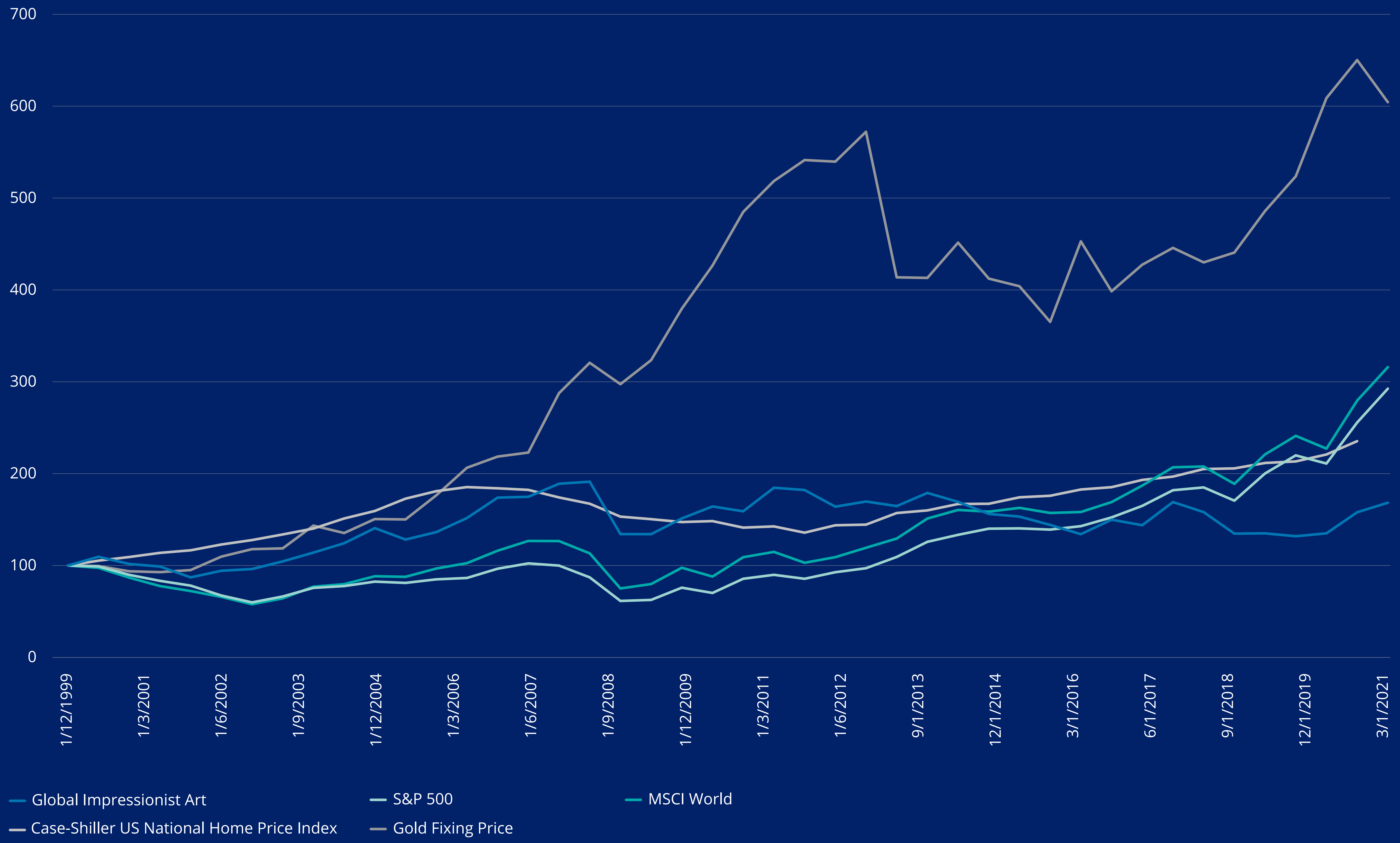
Looking at the Fine Art market's returns trajectory, both the short- and long-run investment cycles show art's reliability as an asset class during economic turndowns. Like the S&P 500, the Artnet Index for Fine Art has outpaced its pre-COVID-19 values, with both indices bouncing back stronger than before despite the continuing uncertain times. The former index rose from 286.6 in mid-2020 to 375.2 in mid-2021, while the latter increased from 211 to 292.5 in the same time frame.

Figure 90. Artnet Index for Fine Art
2021© Artnet Worldwide Corporation



While the Artnet Index for Fine Art is telling of the market's robustness at a given time, the art market's varying and shifting segments often perform independently of each other. A closer look at certain market sectors provides investors with additional insight into the strengths and weaknesses of specific collecting categories. Overall, all but two of the art movements we monitor have gained momentum in the first half of 2021, with respective indices increasing between 3% (European Old Masters) and 38% (Global Post-War Art) year-over-year.

Figure 91. Artnet Index for Global Impressionist Art
2021© Artnet Worldwide Corporation

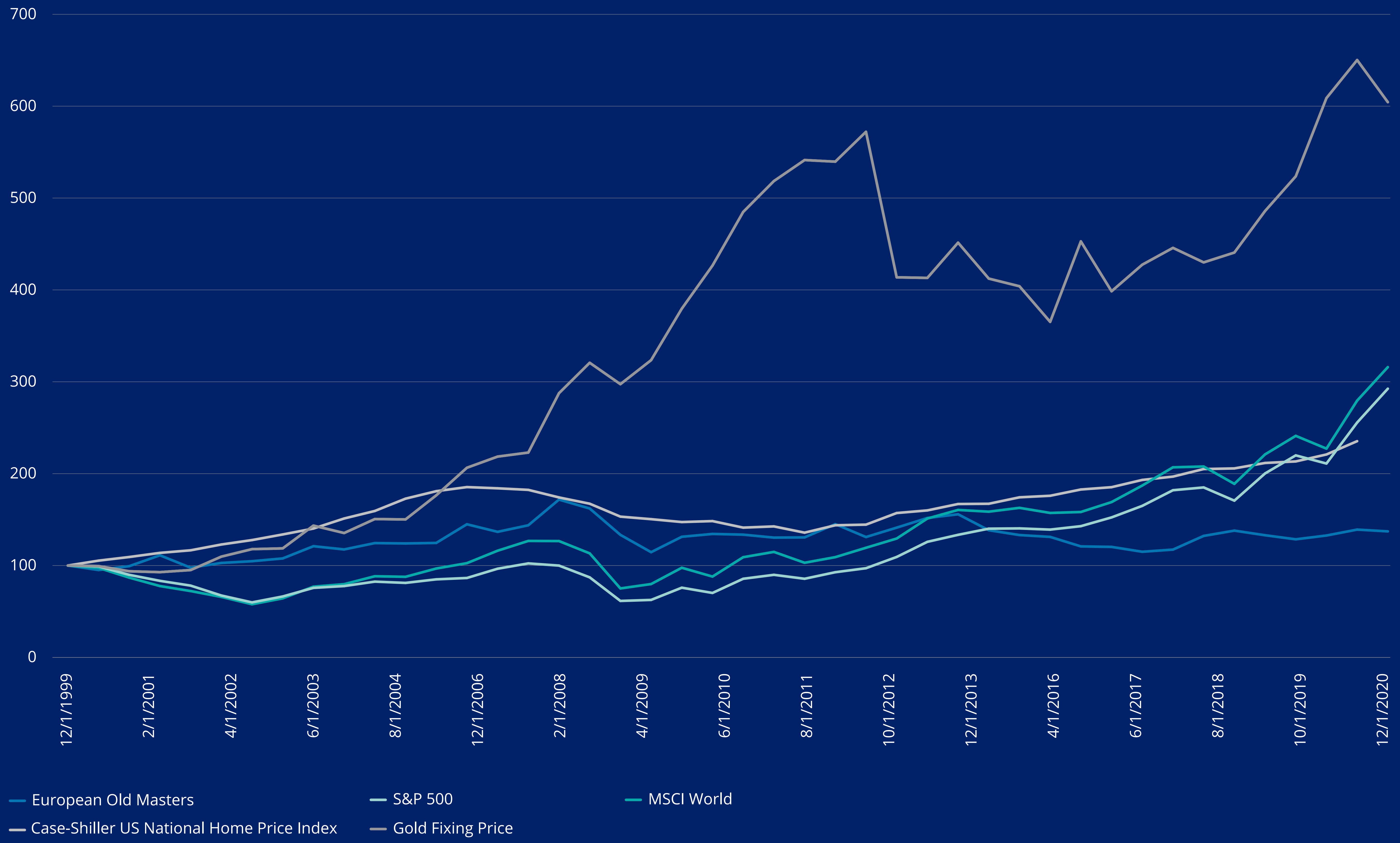


Notably, the Global Impressionist Art sector was only briefly affected by the pandemic's various lockdowns and sale postponements. Although the Artnet Index for Impressionist Art dropped to one of its lowest points between the second half of 2018 and the first half of 2020, the returns rose relatively steeply to gain back momentum most recently, suggesting that artworks by blue-chip artists retain value during economic crises.

After two years of the Global Impressionist Art index barely reaching a value of 135, the first half of 2021 saw a rise to 168.4 for the art movement. The collecting category has struggled to remain at pace with the S&P 500 since 2016. However, the two indices have reacted similarly to global events, both surpassing pre-pandemic values by the end of the year[2]. Looking at different investment cycles, Impressionist Art is especially promising in the short run, producing an almost 20% CAGR between 2019 and 2020.

2 mid-2018 to mid-2020

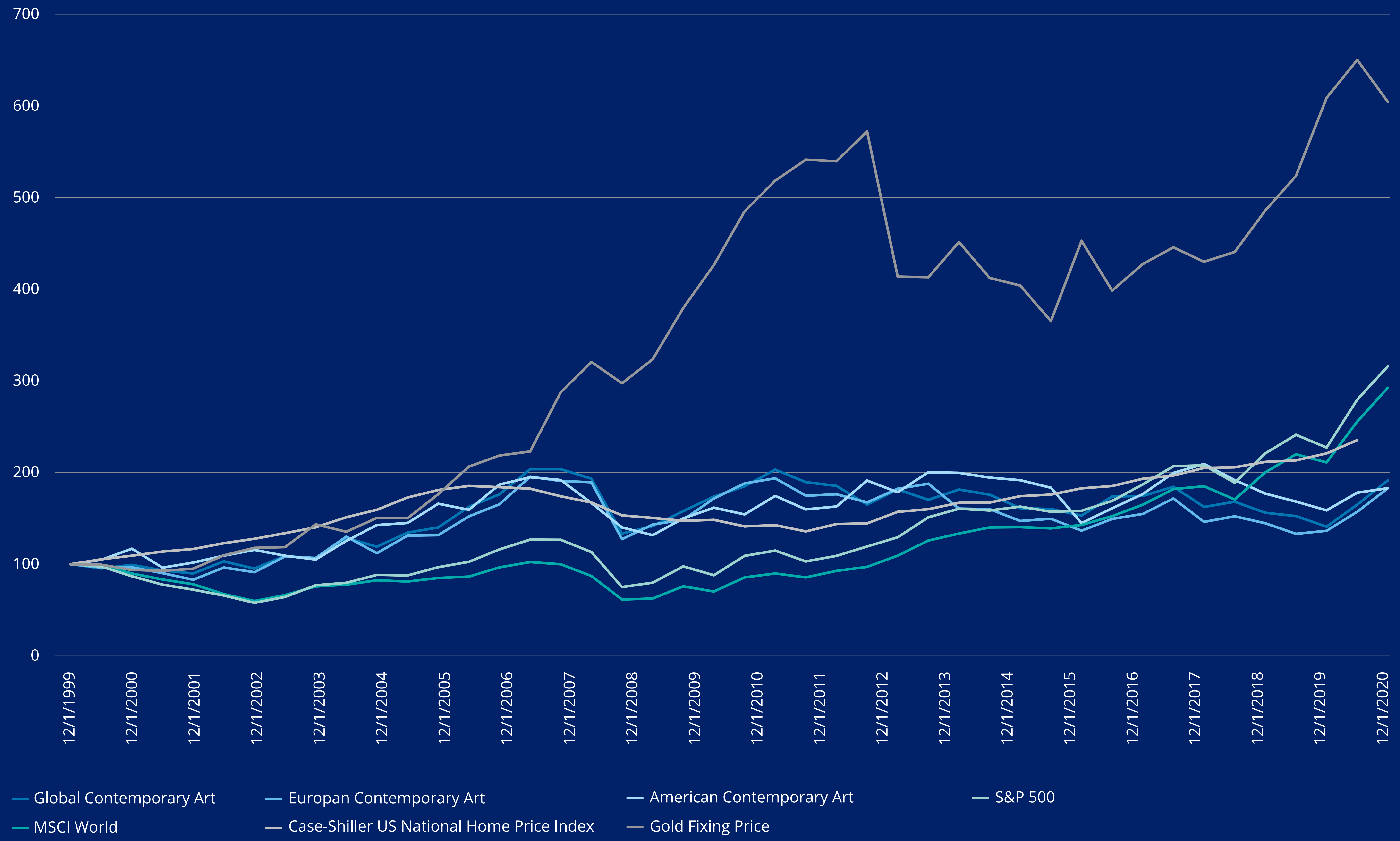
Figure 92. Artnet Index for European Old Masters Art
2021© Artnet Worldwide Corporation



The market for Old Masters tells a similar story. The genre's index has stabilized at a level below the financial indices we use as comparatives, as collectors' appetite has weakened over the last decade. The category's total sales value historically reached more than US$750 million a year globally, while in recent auction cycles sales have accumulated closer to US$600 million. However, the Index for European Old Masters suggests a potential comeback for the genre, reaching a six-year peak of 139.1 in the first half of 2020 and trending upwards overall since 2017. Like the Impressionist Art sector, the positive trend is reflected in the category's short-term growth rate as well.

The European Old Masters sector produced an 8.1% CAGR over the last year, keeping pace with the Index for Modern Art, one of the stronger movements in the field. Unable to reach the values preceding the 2008 financial crisis, the market for European Old Masters stagnated throughout the 2010s. However, unlike previous iterations, long-term investment cycles have suggested positive, albeit modest, returns.

Figure 93. Artnet Index for Modern Art
2021© Artnet Worldwide Corporation



Two of the strongest categories for collectors are the Post-War and Contemporary Art sub-markets, which typically complete between US$4 to 5 billion in transactions at auction per year. In 2020, Post-War and Contemporary works accumulated US$3.9 billion in sales. The Artnet indices for both categories only reflect the global pandemic's effects in the short term. Following a significant growth in returns after 2009, the two art movements have consistently and aggressively outperformed the S&P 500.

Both art indices continue to surpass the financial indicator throughout 2020 and the first half of 2021, restabilizing to quickly surpass pre-pandemic values after a strong recovery in the auction market. The S&P 500 and the Index for Global Post-War Art expanded by 39% and 38% respectively in the first half of 2021, compared with the same period in 2020. The latter index reached a 20-year peak of 400.8 for its latest value.

Figure 94. Artnet Index for Post-War Art

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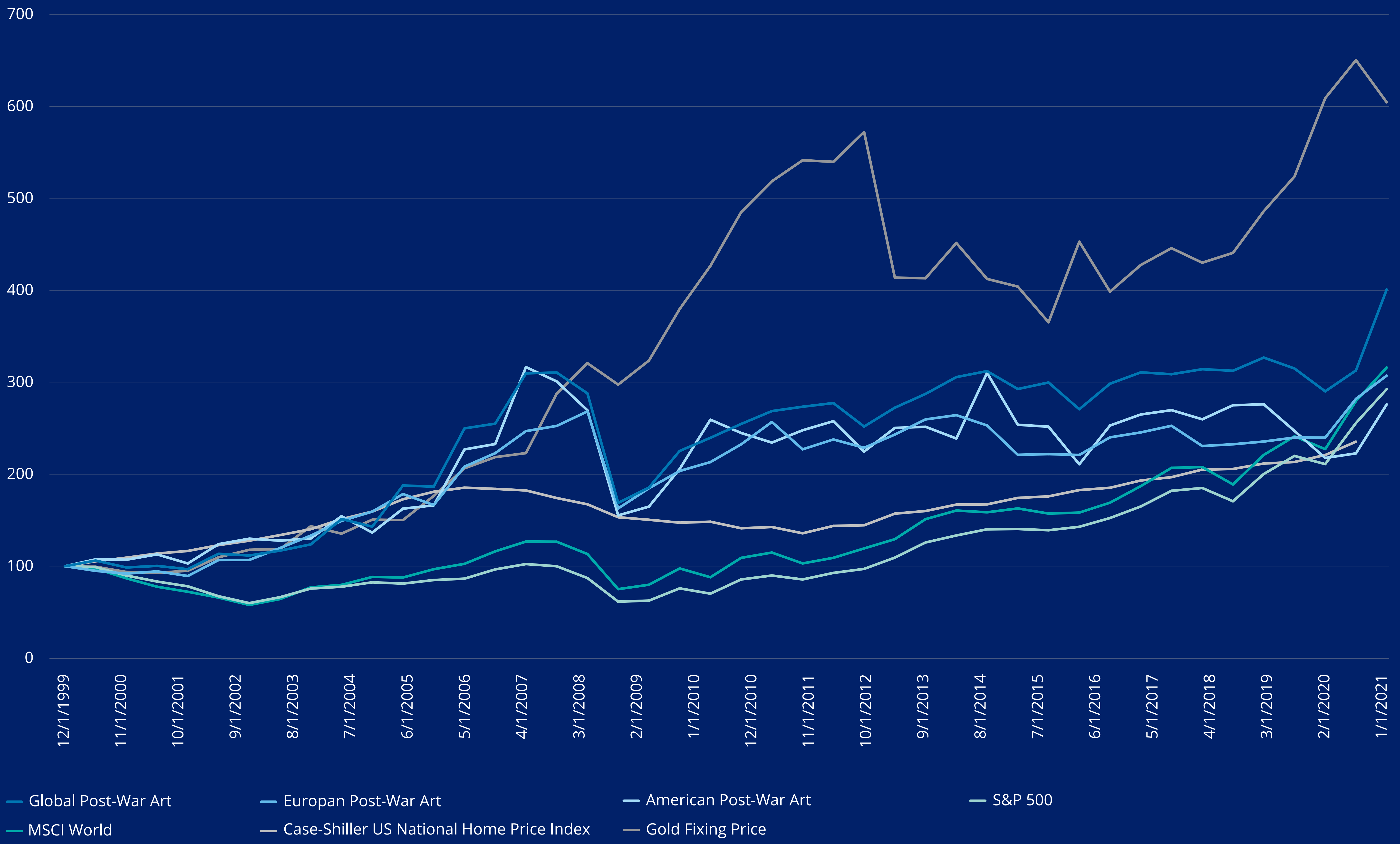

Figure 95. Artnet Index for Contemporary Art
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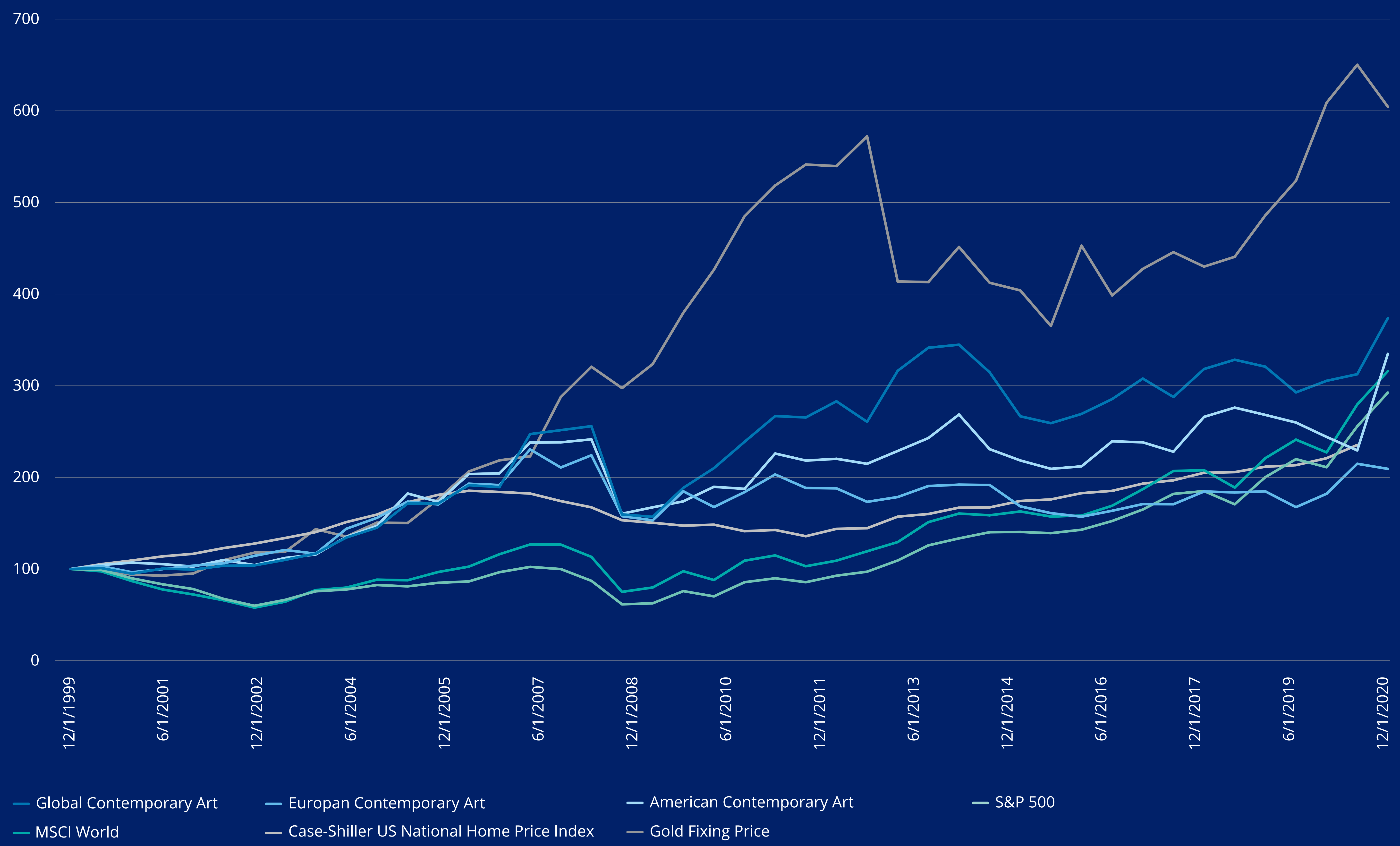

Interestingly, and unlike previous periods, European artists in both categories buoyed their respective markets in 2020, while the market for American artists suffered as the number of big-ticket lots made by American Contemporary artists at auction was significantly lower during the pandemic. The Index for American Contemporary Art was the sole category to decline in the second half of 2020, even temporarily dipping below the S&P 500 for the first time in two decades in 2020. However, Global and American Contemporary Art have certainly regained momentum in the first half of 2021, expanding by 22% and 37% year-over-year respectively.

Looking at the movements' respective CAGRs, the 12-month return for Global Post-War and Contemporary Art tell different stories in the short run. Global Contemporary Art reached 6.8%, one of the highest values from the categories we monitor. Contrastingly, Global Post-War Art produced the only negative, albeit modest, return of -0.5%. The short-term shifts could suggest the growing presence of a middle market for the art category, which has been supported by the recent availability of technological platforms. While the high-end market, which is more heavily dependent on in-person viewings, cooled down temporarily, online viewing rooms and live streams worked effectively for artworks of lower price ranges.

Figure 96. Artnet Index for Fine Chinese Paintings & Calligraphy
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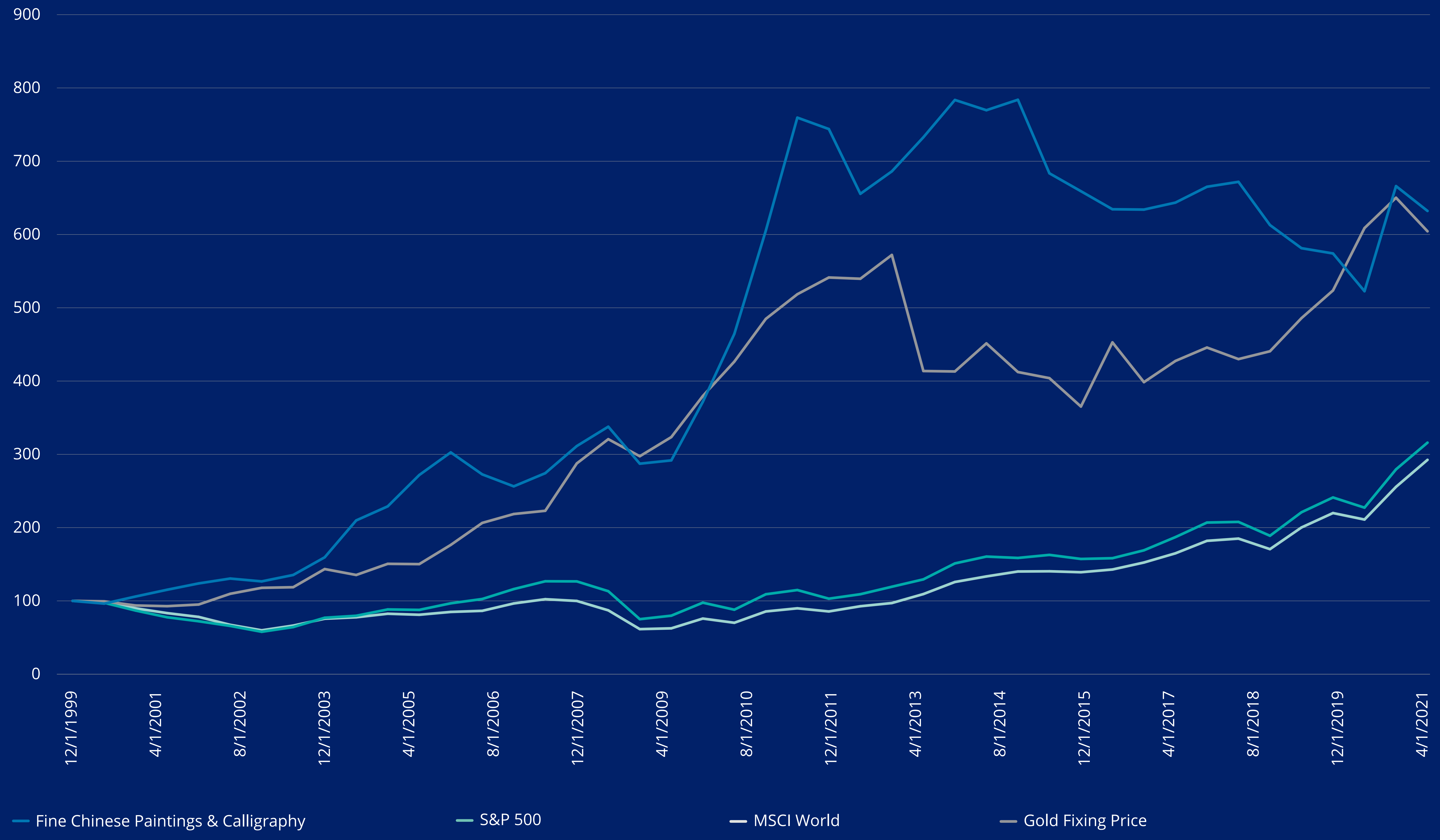


Looking at the Chinese art market, the Artnet indices for 20th Century & Contemporary Art and Fine Chinese Paintings & Calligraphy trended differently than in previous years. Typically a much more volatile but stronger collecting category, the Index for Fine Chinese Paintings & Calligraphy reached a 10-year low of 522.6 in the first half of 2020, continuing a downward spiral started in 2015 and likely exacerbated by China being the first country to lockdown in response to COVID-19.

However, the category staged the strongest comeback in the second half of 2020. Speedily regaining its momentum within six months of the drop, the category for Fine Chinese Paintings & Calligraphy recovered lost ground and even outpaced its pre-pandemic values by the end of the year. Most recently, the index saw a modest correction in the first half of 2021, settling at a value of 632.1.

The success of Fine Chinese Paintings & Calligraphy works can be attributed to the large Chinese collector base they attract, as well as China's unparalleled comeback in sales in the second half of 2020. While the country experienced an incredible 84.9% drop in total sales value year-over-year in the first half of 2020, it closed off the year practically on par to 2019, according to Artnet's Intelligence Report[3]. Vastly supported by the growth in the buying power of Chinese collectors, the category is typically one of the strongest we monitor, and reflective of the Chinese economy's overall state.

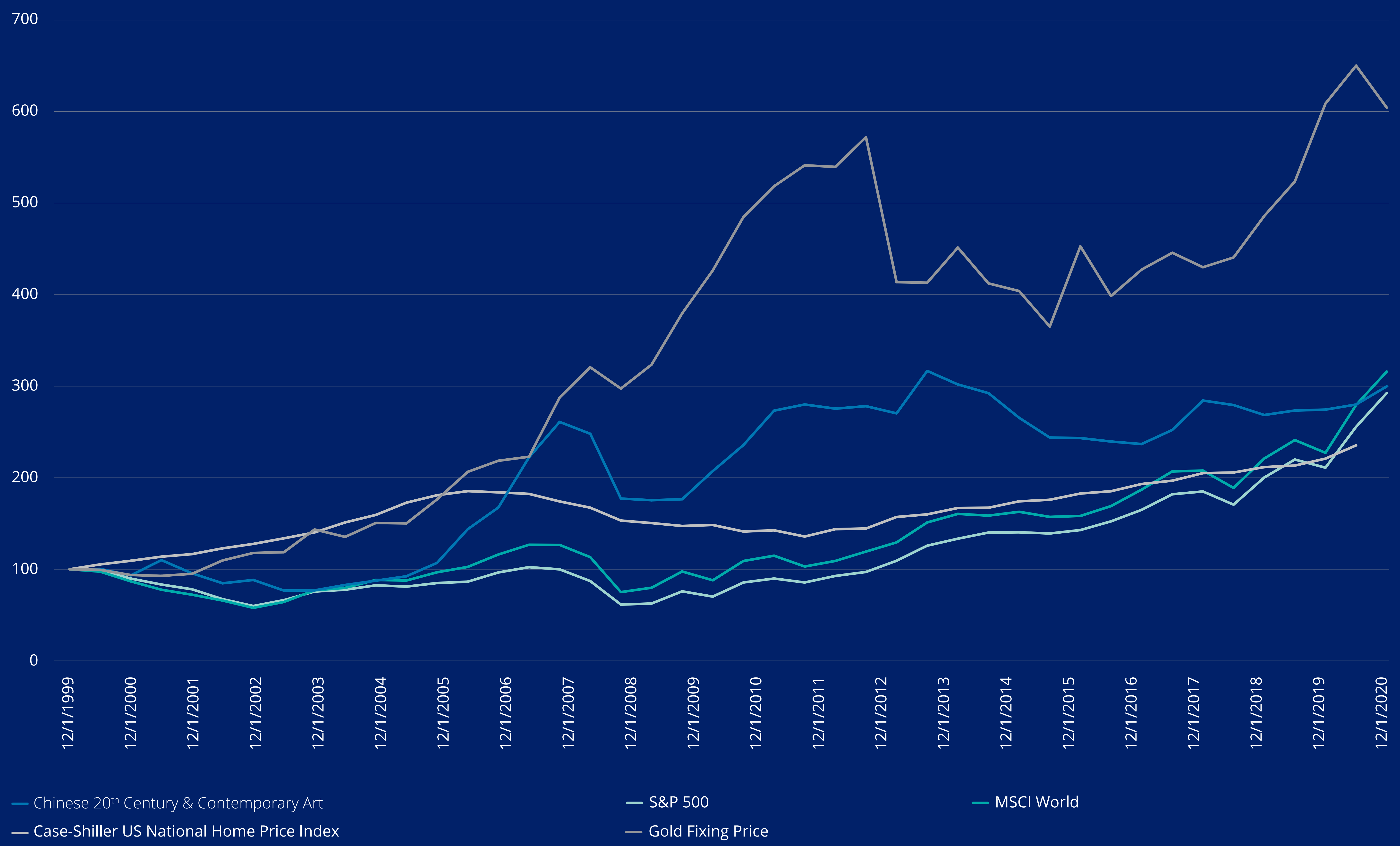
3 Artnet, 'Artnet Intelligence Report', artnet.com, Artnet News, 2021, https://www.artnet.com/artnet-intelligence-report/, (accessed 19 July, 2021).

In contrast, returns for the less volatile Chinese 20th Century & Contemporary Art market have stabilized, increasing at a healthy and consistent rate. The index for the genre initially grew bullish in 2005 through 2011, significantly outpacing the S&P 500 and other collecting categories. However, the pace has settled at a healthy level since 2018, seemingly unaffected by the shifting global economies of the last few years.

Returns for Chinese 20th Century & Contemporary Art continue to outpace the S&P 500 through the first half of 2021. This consistency can be rationalized by the genre's ability to attract a diverse pool of buyers. Initially supported by interest from an international collector base, Chinese 20th Century & Contemporary Art has garnered increasing local interest and continued support by a new class of Chinese buyers in more recent years.

According to data from the *Global Chinese Art Auction Market Report*[4], total sales value for Chinese art has dropped significantly in recent years. However, both Artnet indices for Chinese artworks suggest a much milder decline in value for blue-chip artists, indicating a shift from quantity to quality in this market.

Figure 97. Chinese 20th Century & Contemporary Art
2021© Artnet Worldwide Corporation



4 'Global Chinese Art Auction Market Report 2019', artnet.com, Artnet News, Artnet and the China Association of Auctioneers, 2020, https://cn.artnet.com/en/chinese-art-auction-market-report/, (accessed 19 July 2021)

Taking a closer look at the return on investment over different time periods, we observe positive CAGR in the long run across all art price indices in this report. Between 2019 and 2020, Artnet indices showed particularly strong positive CAGR for various collecting categories. The best performing art categories for the period were Global Impressionist Art (19.7%), Fine Chinese Paintings & Calligraphy (16.9%), Global Modern Art (8.4%) and European Old Masters (8.1%).

Among the various fine art collecting segments, the Index for Global Contemporary Art, along with both indices for Chinese art, generated the most consistent returns over the past 15 years, with positive CAGR across all investment cycles. Chinese 20th Century & Contemporary Art, followed by Fine Chinese Paintings & Calligraphy led the sectors with the strongest 15-year CAGR percentages. Global Post-War Art return rates increased in value on par with the length of the investment cycle.

Table 26.

Artnet indices and financial indices	12-month return	5-year CAGR	10-year CAGR	15-year CAGR
Fine Art	0.8%	1.2%	-0.4%	4.9%
European Old Masters	8.1%	1.2%	0.4%	0.8%
Global Impressionist Art	19.7%	1.8%	-0.1%	1.0%
Global Modern Art	8.4%	0.6%	-1.1%	1.1%
Global Post-War Art	-0.5%	0.9%	2.1%	3.5%
Global Contemporary Art	6.8%	3.8%	2.7%	4.1%
Fine Chinese Paintings & Calligraphy	16.9%	0.2%	1.0%	5.4%
Chinese 20th Century & Contemporary Art	2.5%	2.8%	1.7%	6.7%
S&P 500	16.3%	12.9%	11.6%	7.6%
MSCI World	15.9%	12.2%	9.9%	7.3%
Case-Shiller	10.4%	6.0%	5.2%	1.8%
Gold Fixing Price	24.2%	12.2%	3.0%	9.1%

*Returns are calculated up to the end of 2020.

Art particularly attracts investors because it is regarded as a value-preserving asset class. Similar to gold, artworks are less susceptible to risks associated with financial market crashes than stocks and bonds. Because of art's intrinsic value as an object of wealth, art has historically been able to rebound and even grow faster than traditional asset classes during financial turmoil. This pattern was evident following the 2008 financial crisis. While the Artnet Index for Fine Art was able to recoup its peak value by 2011, the S&P 500 took five years to regain its standing. This pattern seems to hold true in the data we are continuing to collect as global economies re-adjust following the latest health crisis.

Art is also particularly attractive to investors due to astounding resale success stories such as Edvard Munch's 1904 painting, *Summer Day*, which was first purchased at auction for US$10.8 million. When the work resurfaced 15 years later at Sotheby's Modern Renaissance Cross-Category Sale in March 2021, the work earned a 107% increase in value, selling for more than US$22.3 million with premium, according to the Artnet Price Database. Munch's profitable painting is one of many artworks to soar in value upon returning to auction.

When dealing with indices, it is important to note that, while indices are helpful reference points for the performance of top-selling artists over time, investors should consider their limitations and restrictions. As lack of transparency and illiquidity have always been unfavorable characteristics associated with investing in art, we recommend that investors recognize the methodology behind the indices to leverage the data in the most advantageous way.

Evaluating the various risks specific to artworks is crucial for investors interested in allocating capital in the sector, as they differ from the risks associated with traditional assets. Unlike bonds and the stock market, for example, the art industry lacks market transparency. Stock performance and bond prices are monitored consistently and adjusted constantly to reflect shifts in the industry. Additionally, prices are public and transactions are regulated.

In contrast, the art market is more uncertain and obscure. Market transparency is an obstacle in the field: dealers keep details of sales private, galleries do not publicize artwork pricing, and buyer information is often undisclosed. Although efforts to shed light on the art market's obscurities are ever-growing, and pioneered by products such as Artnet's Price Database, buyers are still reliant on appraisers' knowledge and analysis. Auction houses also cater to clients who prefer to sell their works through private transactions rather than public biddings, meaning the entire market is never fully accessible.

Government regulations or the lack thereof also create risks for investors. Although art markets do not typically place strong restrictions on pricing and commission rates compared with financial markets, trading policies are ever-changing region to region, which is a factor of concern for investors making international deals.

This issue recently materialized during the US-China tariff wars in 2018 and 2019. Although an additional tariff on Chinese art and antiques exported to the United States only kicked in late in 2019, back and forth negotiations and rising trade tensions between the countries resulted in a weakening of collectors' confidence and a more cautious attitude among buyers and art investors. Auction house activity in mainland China experienced modest yet significant contractions, with total sales for Chinese art and antiques reaching a decade low of US$3.7 billion in 2019, according to Artnet's latest *Global Chinese Art Auction Market Report*[5].

Similar trends have developed in Europe, with countries like Germany and Italy ratifying laws to regulate these countries' art markets. By placing unprecedented requirements on art exports, art owners were required to have licenses to legally trade art assets. As a result, both the Italian and German art industries saw a decline in total sales value in the years preceding the respective ratifications. At the same time, neighboring European countries such as France saw art sales spike, likely absorbing works sold by German and Italian collections attempting to liquidate their assets before the regulatory changes.

Along with lack of market transparency and unpredictable regional market regulations, the low liquidity and heterogeneity of art pieces are additional risks associated with art as an asset class. Works of art are illiquid, as they are hard to exchange for cash compared to bonds and stocks. Additionally, artworks' authenticity, provenance, attributions and potential for forgery are risks that investors are aware of when investing in art. The quality of a work, such as its craftsmanship, technical skill and physical durability, can also be a concern, as the price of a work is largely affected by these factors. Due to the nature of the asset class, works of art are heterogeneous and one of a kind rather than exchangeable. Ultimately, the financial rate of return is difficult to calculate due to the uniqueness of each object of exchange.

5 See note 2 above.

Along with the risks and limitations associated with investments in the art market, it is worth noting how various art categories correlate with other asset classes for investors looking to diversify their asset allocations. Consistent with the results of our previous reports, all but one of the art categories we track have the strongest positive correlation with the price of gold, compared with other asset classes reviewed in the study. The strong positive correlation between art and gold could indicate investors' perception that art is a value-preserving asset class rather than an investment vehicle.

In contrast, Artnet indices for European Old Masters and Global Impressionist Art display the lowest correlation with the S&P 500 and MSCI World, compared with other collecting categories. Artnet's indices for Global Post-War and Contemporary Art show the highest correlation with the S&P 500, while the Chinese indices showed average correlations across all the financial indices.

Table 27.

Artnet Indices	Volatility	Correlation with S&P 500	Correlation with MSCI World	Correlation with Case-Shiller	Correlation with Gold Fixing Price
Fine Art	20%	0.64	0.73	0.58	0.89
European Old Masters	12%	0.23	0.34	0.51	0.54
Global Impressionist Art	14%	0.23	0.36	0.43	0.65
Global Modern Art	15%	0.34	0.47	0.53	0.72
Global Post - War Art	18%	0.70	0.79	0.78	0.83
Global Contemporary Art	16%	0.72	0.80	0.72	0.87
Fine Chinese Paintings & Calligraphy	17%	0.56	0.64	0.52	0.89
Chinese 20th Century & Contemporary Art	0.17	0.62	0.71	0.57	0.91

*Correlations are calculated from 2000 to H1 2021.

Despite the various risks associated with the art market, there is an added benefit unique to art as an asset class unlike any other object of wealth. Although capitalizing on the art market always involves a word of caution from investors, artwork owners are typically passionate and fond of the object of interest, regardless of its monetary value. Whether a painting hangs in a living room, or a sculpture greets visitors in a public space, the non-financial worth of a piece of art is unparalleled to any other asset class.

Notes

I. Data sources for Artnet and financial indices

1. All data for the Artnet indices is based on information reported to the Artnet Price Database Fine Art and Design as of:

Year(s)	Data pulled as of
2000–2021	19 July 2021

2. All prices are converted from their original currency to USD, based on the exchange rate on the day of the sale. All prices are adjusted to include the buyer's premium.
3. The Artnet price index employs a hedonic regression framework that explicitly defines an underlying stochastic process, allowing to treat the volatility parameter of fine art as the object of interest. The model can be estimated using maximum likelihood in combination with the Kalman filter. More about the Artnet indices methodology can be found in this paper.
4. Data for **S&P 500** is sourced from Yahoo Finance (link).
5. Data for **MSCI World Index** is sourced directly from MSCI (link).
6. Data for **S&P/Case-Shiller US National Home Price Index** is sourced from the Federal Reserve Bank of St. Louis (link), which originally sources the data from S&P Dow Jones Indices LLC.
7. Data for **Gold Fixing Price** is sourced from the Federal Reserve Bank of St. Louis (link), which originally sources the data from ICE Benchmark Administration Limited (IBA).

Table 28.

Art category	Index description
Fine Art	All artists were considered for this category.
European Old Masters	Works created by European artists born between 1250 and 1820.
Global Impressionist Art	Works created by artists born between 1821 and 1874, excluding single-nationality Chinese artists.
Modern Art	Works created by artists born between 1875 and 1910, excluding single-nationality Chinese artists.
Post-War Art	Works created by artists born between 1911 and 1944, excluding single-nationality Chinese artists.
Contemporary Art	Works created by artists born after 1944, excluding Chinese artists.
Fine Chinese Paintings & Calligraphy	Works created by Chinese artists in traditional brush and ink manner.
Chinese 20^{th} Century & Contemporary Art	Works created by Chinese artists adapted in Western Art manners.

II. Data scope for Artnet indices

1. Artnet indices are rebalanced annually, according to the top 100 performing artists, as defined by total sales over the previous 3 years, with the exception of **Fine Chinese Paintings & Calligraphy** and **Chinese 20^{th} Century & Contemporary Art**, which are limited to the top 50 artists.
2. Indices are composed of auction sales of paintings and works on paper produced by the top 100 performing artists in the category.
3. The art categories are defined as follows:

III. Disclaimer

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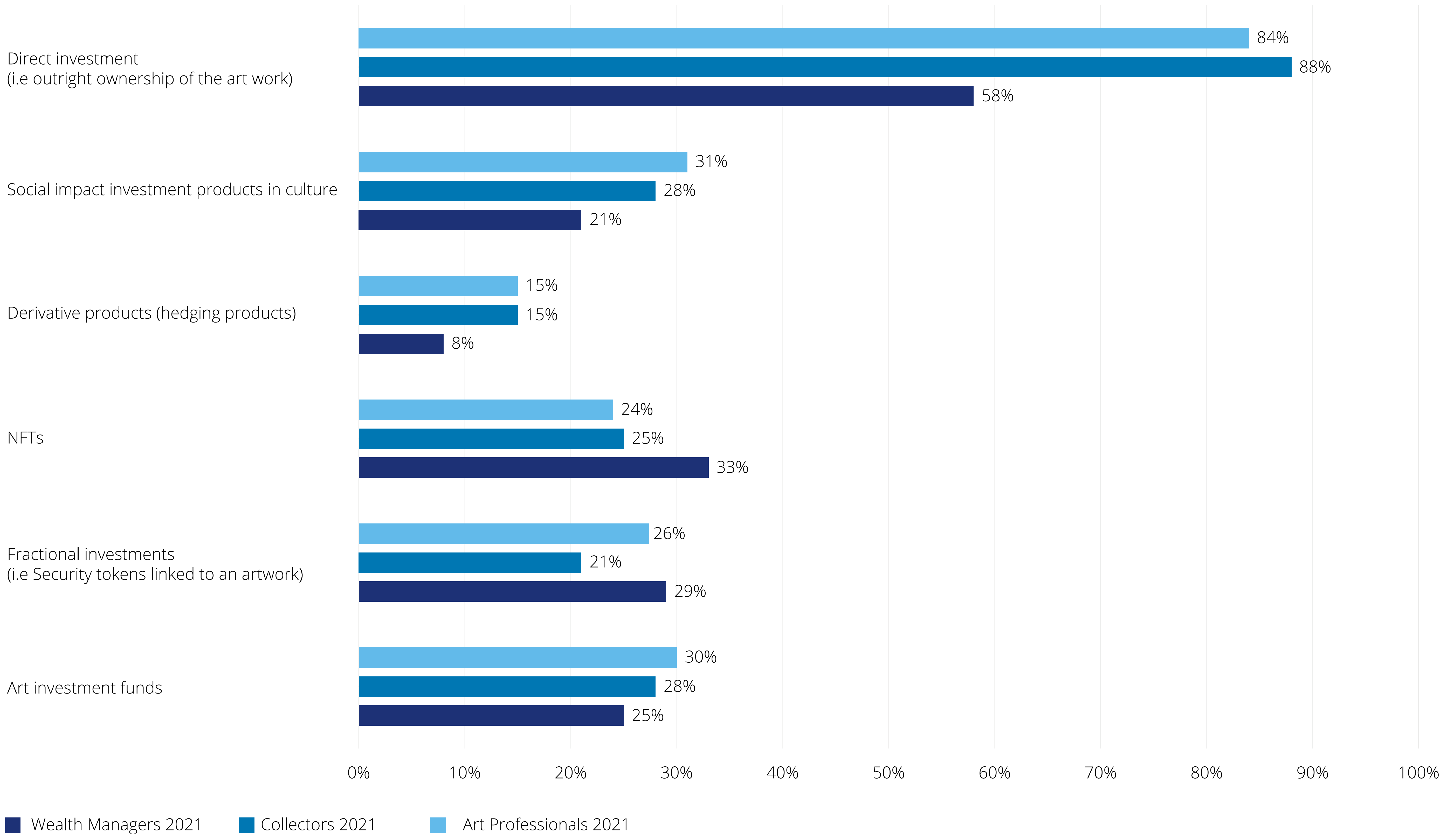
Part 2. Survey findings 2021

Figure 98. In terms of investing in art, which of the following art investment products would be of most interest to you?
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021



COVID-19 triggers new interest in alternative forms of art ownership
During the COVID-19 pandemic, 33% of wealth managers said their clients had expressed an increased interest in NFTs, fractional ownership (29%), art investment funds (25%) and social impact investment in culture (21%). Interestingly, 64% of collectors said the COVID-19 pandemic had triggered a new interest in alternative art investment products, with 65% saying that NFTs had generated the most attention.

Direct investment and physical ownership
58% of wealth managers believe that direct investment in art (i.e., the outright ownership of the artwork) will be the most common form of art investment among their clients, with 88% of collectors and 84% of art professionals stating the same. This suggests that traditional ownership and investment in art are likely to stay, corresponding with the strong emotional value that collectors associate with art ownership and collecting.

Alternative markets for art investment emerging
However, there is no doubt the market for new and alternative art investment products is expanding, especially outside the traditional art market. The NFT market's growth has generated a renewed focus around investment and ownership of digital art and collectibles—33% of wealth managers said they believed NFTs would become an art investment product of interest to their clients, with 24% of art professionals and 25% of traditional art collectors saying the same. However, as the NFT market is currently unregulated, it is unlikely wealth managers will embrace this in the short term. But as the market for asset-backed tokens (or security tokens) continues to develop (see articles from Look Lateral on p.249 and Sygnum Bank on p.247), we are likely to see increased interest among wealth managers in this area. To learn more about the difference between NFTs and security tokens, see Section 7, p.252.

Fractional ownership and tokenization
29% of wealth managers said they believed fractional ownership and tokenization of art and collectibles could become investment products of interest to their clients (up from 10% in 2019), with 26% of art professionals saying the same (up from 19% in 2019). Collectors remain slightly more cautious, with 21% saying this would be an investment product of interest (compared with 19% in 2019) while 88% prefer to own the artwork outright. However, it is very likely that fractional ownership and the increasing growth around tokenization of assets could attract a new investor base to the art market and support new philanthropic and social impact investment strategies like crowdfunding and co-ownership.

Traditional art investment funds see a revival among wealth managers
25% of wealth managers said art investment funds would be the most compelling type of investment to their clients (up from 17% in 2019), with 30% of art professionals saying the same (down from 38% in 2019). Although the art investment fund market has failed to gain mainstream traction, there are hints of a renewal of interest, with several new funds being launched in 2020 and 2021 [see p.xx]. Of the collectors surveyed, 28% said art investment funds would be of interest to them (down from 33% in 2019). With the emergence of fractional ownership and tokenization platforms, some art funds could be tempted to invest in security tokens further down the line.

Social impact investment products
21% of wealth managers said social impact investment products in culture would be of interest to their clients (compared with 28% in 2019), with 28% of collectors and 31% of art professionals also identifying this as an area of strong interest. In line with global trends around social impact and an increasing focus on ESG investing, we are likely to see this interest grow and new models and vehicles to emerge in the coming years. More details on this in Section 4.

Figure 99. Wealth managers: In terms of investing in art, which of the following art investment products would be of most interest to you?
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021

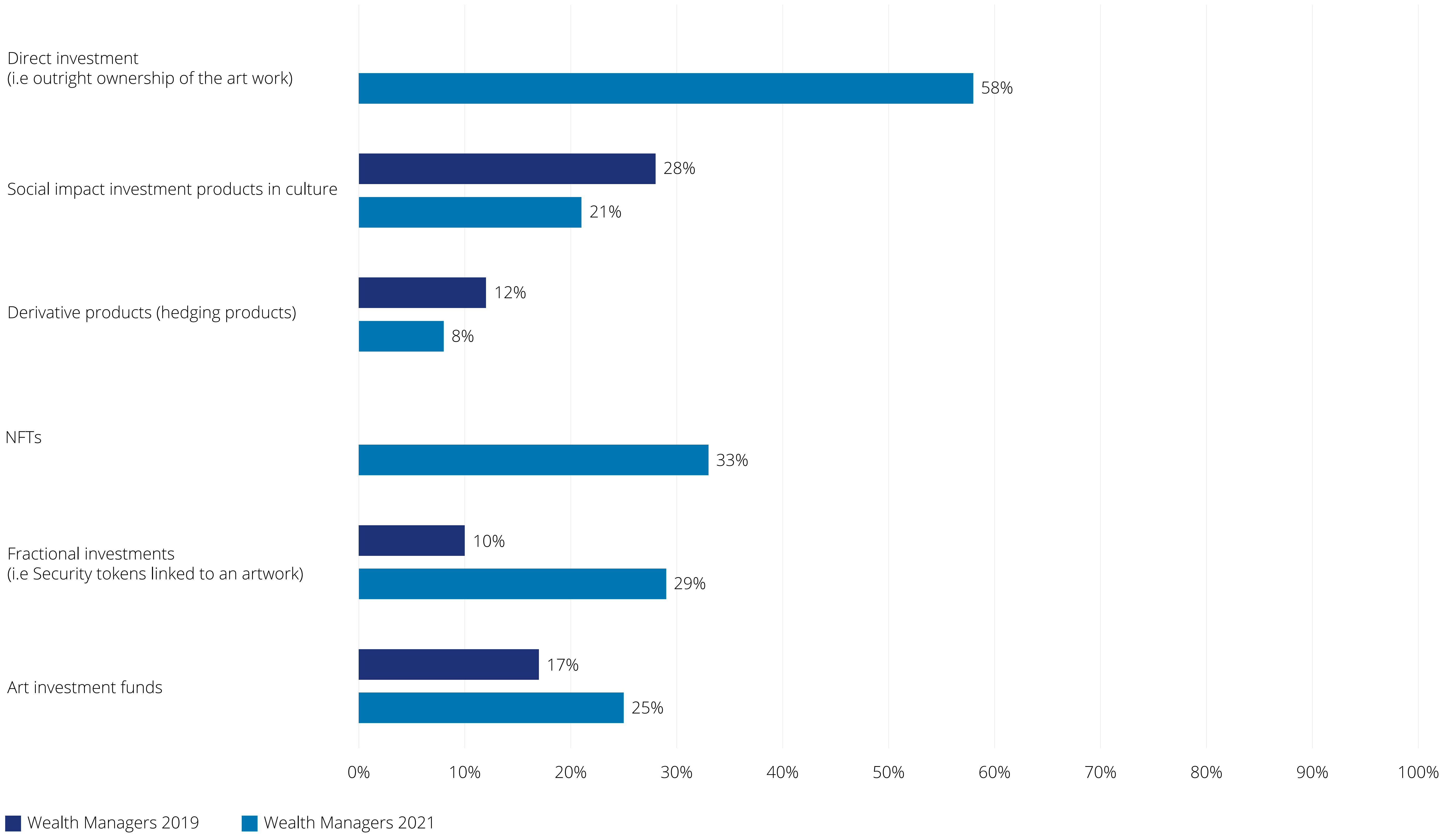
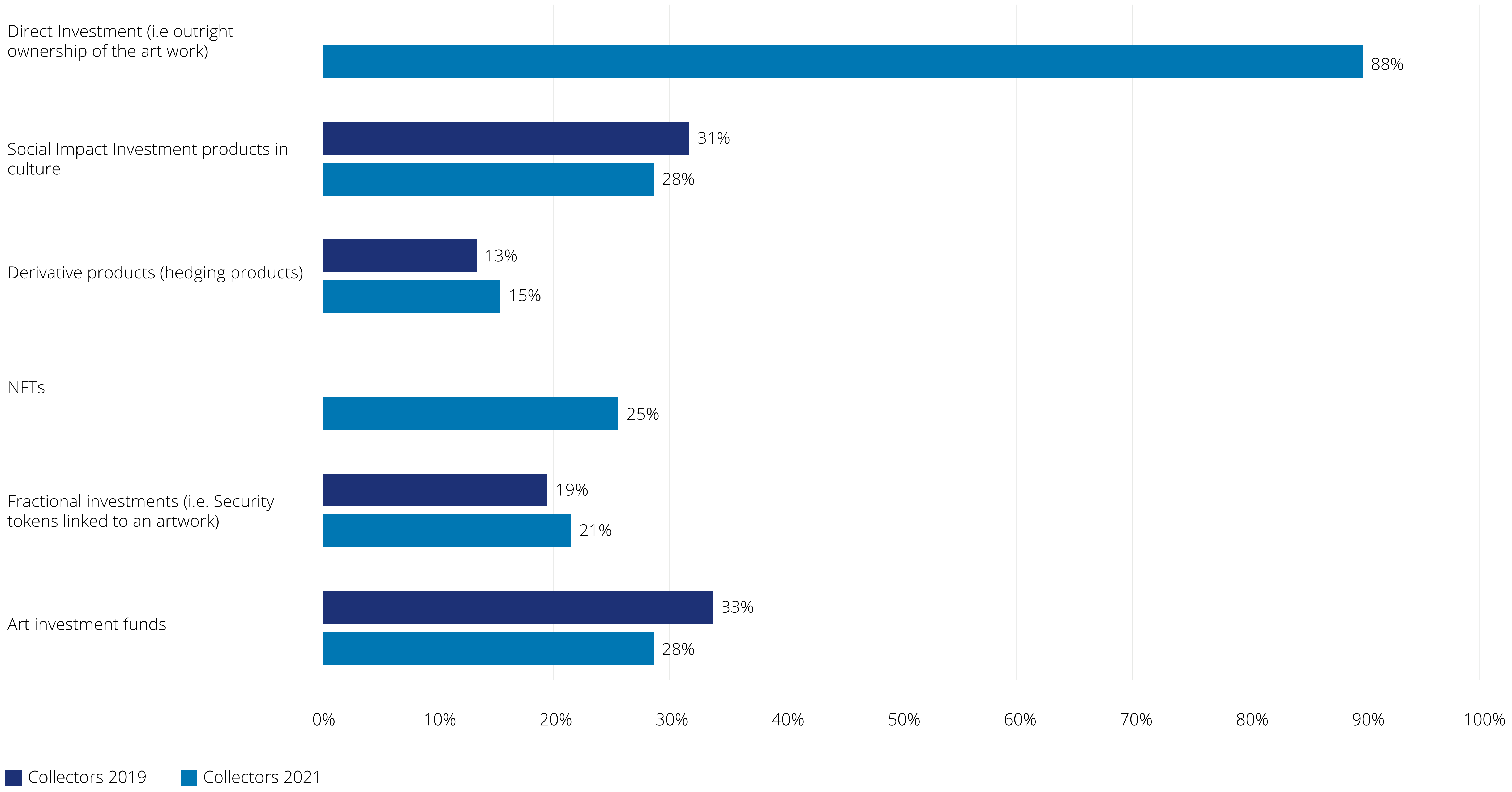


Figure 100. Collectors:In terms of investing in art, which of the following art investment products would be of most interest to you?

Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021



Supermercado
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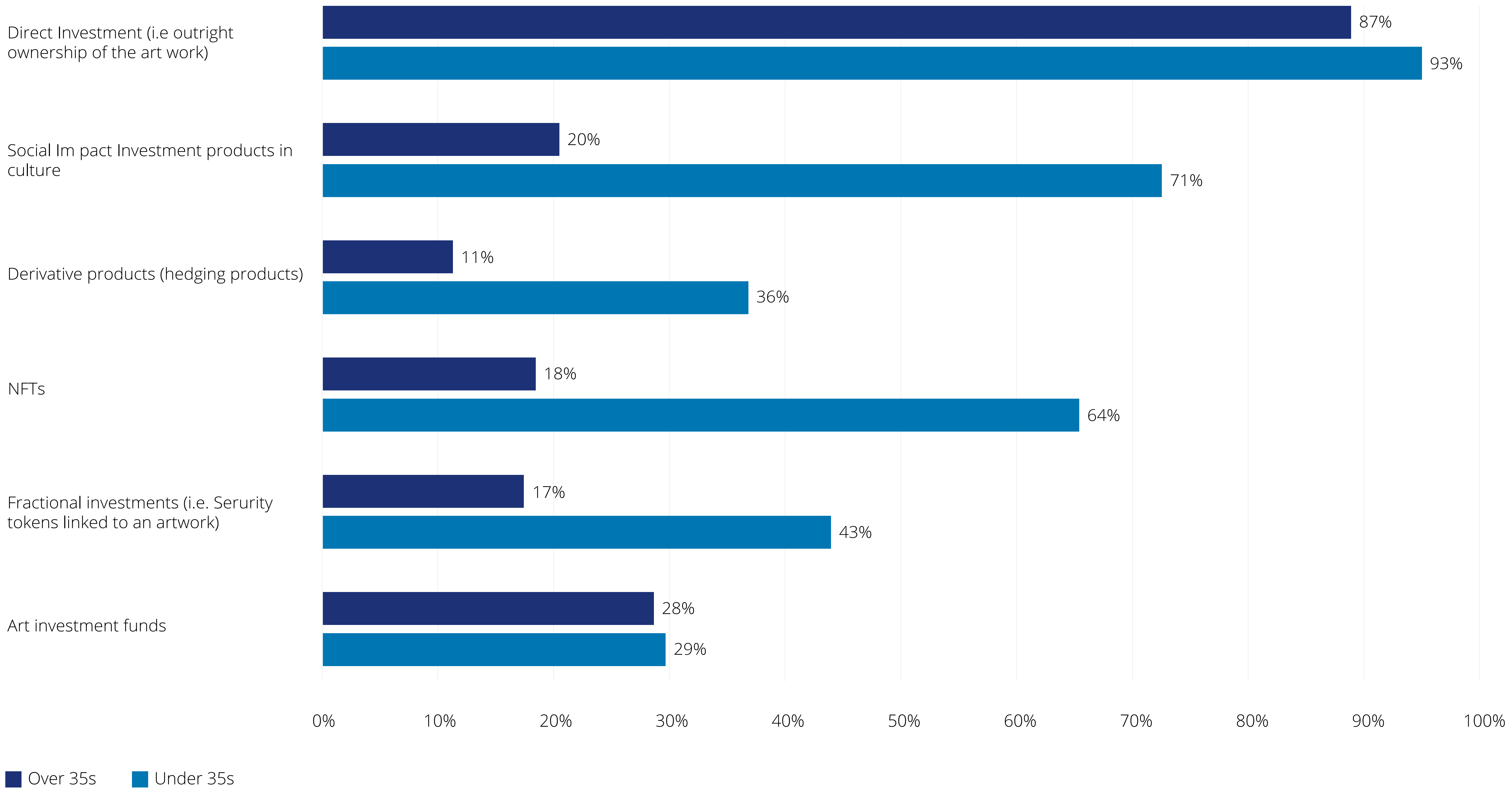
NextGen Collectors—a different perspective[6]

Figure 101. In terms of investing in art, which of the following art investment products would be of most interest to you?
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021



Most younger collectors strongly interested in social impact investments
71% of younger collectors surveyed said they were interested in social investment products in art and culture, compared with 15% of older collectors. This again demonstrates the younger demographic's stronger interest and awareness around purpose-led investment in art, which is reflected in their motivations for buying art in the first place. The wealth management industry must recognize the significance of social impact investment to engage the next generation of clients about issues of importance to them.

Younger collectors more tuned in to recent developments in art investment products and services
64% of younger collectors[7] expressed a strong interest in NFTs (compared with 18% of older collectors) and 43% said fractional investment linked to artworks would be of interest, significantly higher than 17% of older collectors. During COVID-19, 86% of younger collectors had seen an increased interest in art investment products and services, compared with 61% of older collectors.

During COVID-19, 86% of younger collectors had seen an increased interest in art investment products and services.

6 See also NextGen collectors—a different perspective in Sections 2 and 7, p.122 and p.264
7 The sample is based on 16 individuals out of 114 collectors surveyed in total. Although the sample size is small, these findings still highlight significant differences between the younger generation of collectors (under 35 years old) and the older generation of collectors (over 35 years old)

Part 3. New developments: art investment products and services

In our previous Art & Finance reports in 2017 and 2019, we introduced the development of a new generation of art investment products, such as fractional ownership models. The market for these products has evolved further in the past two years, with the launch of NFTs and new asset tokenization products (such as security tokens) for art and collectibles.

This section takes a closer look at some of the emerging trends in the traditional art investment fund market, as well as new developments around the tokenization of non-bankable assets. We explore how these new models could affect the development of a regulated market emerging around art and collectible assets, as well as the growth and future development of the art and finance industry and the art market as a whole.

Art investment funds update: will the art investment fund industry re-emerge?

After years of stagnation in the art investment fund market, there are signs that a new generation of art funds is emerging. The art market's continuing strength, coupled with the increasing fear of higher inflation, could provide a fertile ground for more traditional forms of art investment. While it is challenging to put a specific number on the market's size, as most art investment funds operate under the public radar, we have witnessed some new initiatives in the making in the last two years. Future will tell us if they have been successful.

On the back of a booming market for African art, KIISA ART and The Art 4 Africa Fund has announced an anticipated launch date for January 2022. The fund will focus on the established and blue-chip modern and contemporary African and diaspora art market, with the aim of investing 50% in art works by female artists. KIISA ART also aims to make a social impact on the contemporary African art market by directly supporting initiatives that provide patronage to arts and educational institutions across Africa and the diaspora.

In April 2021, Artemundi announced[8] the launch of the Guernica V. Fund with the aim of raising US$200 million. The fund is focused on high-end museum-quality art spanning the impressionist, modern, and post-war periods. It has a duration of three years, of which two are dedicated to investment strategies, and has a minimum internal rate of return (IRR) target of 17% net of fees and expenses.

Another art fund, ArtsGain, authorized in October 2020 by the Spanish National Securities Market Commission (CNMV), is open to qualified investors to jointly invest in art, including artworks, antiques and collectibles.

The Pop Art Value Collection Fund, registered by the Liechtenstein Financial Market Authority, is in the process of being launched by MERIT Alternative Investments GmbH. It aims to become an important and high-quality collection of pop art icons, including artists like Andy Warhol, Roy Lichtenstein and Keith Haring. The fund will only buy artworks that are at least 30% below their actual market value through special situations (such as estates, distress sales and auctions) and through the network of the fund's experts. The fund plans to exhibit the collection at various places, including museums and institutional spaces. The minimum investment in the fund is set at EUR100,000.

Petricca & Co Capital Ltd, an independent global asset management company, is in the process of initiating the set-up and management of ART ISLAND Fund, based in London, with over USD 500 million of assets. The ART ISLAND Fund will initially focus on Modern and Contemporary Art, and the first collection consists of 1500 works of art spanning both the early twentieth century to the present times. ART ISLAND Fund also plan to apply the most recent possibilities related to the tokenization of assets, where modern and contemporary art, classic cars, diamonds and other rare collectibles will be tokenized by PhygitalArt.

Vitrail_2
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8 Source: Il Sole 24 Ore: 'Artemundi lancia Guernica V. Fund', 11 April 2021 - link https://www.ilsole24ore.com/art/artemundi-lancia-guernica-v-fund-AECvrE

Fractional ownership—the new age of art investment?

As demand grows for art investment services—with 53% of collectors surveyed this year professing an interest, compared with 51% in 2019 and 37% in 2017—new art investment models are emerging. The last few years have seen the launch of new types of fractional art ownership models aimed at democratizing the multi-billion art investment market.

Currently the market for fractional ownership is split into different strands, both in terms of regulation and the underlying technology used. We have non-blockchain fractional ownership models, such as Masterworks (fine art), Otis (collectibles) and Rally (collectible cars), which are all regulated by the US Securities and Exchange Commission (SEC). And, we have also started to see blockchain-based fractional art ownership models (tokenization) evolve from the 2017–2018 unregulated initial coin offering (ICO) boom to a regulated format of security token offerings (STOs). The first art STO was launched in July 2021 through a partnership between Artemundi and Sygnum Bank, see article on p.247. Curio AG is another example of this trends by offering the possibility to invest in tokenized cars.

There are also new developments around fractional ownership of digital art, and the Art Exchange[9] recently launched a pilot project that uses two types of art tokenization: unique (NFT) and interchangeable. While interchangeable tokens allow an artwork to be collectively owned (allocating shares via blockchain and selling to multiple buyers), non-interchangeable NFTs are not limited to digital sales; they can also be used to confirm the provenance, authenticity and uniqueness of a work.

In August, the security token market capitalization broke the US$ 1 billion based on a Security Token Market publication[9]. According to a report by area2invest[10], a security token marketplace, the market could reach a CAGR of 56.9% and is poised for exponential growth to reach a market size of US$3 trillion by 2025.

The tokenization of art and collectible assets, empowered by blockchain and smart contracts, could truly innovate the art industry. Converting physical assets into digital tokens opens up a range of possibilities, from broadening the investor base to boosting liquidity. Niccolò Filippo Veneri Savoia from Look Lateral discusses in detail the possible applications of STOs in the art market in his article on p.49.

One of the main obstacles to the growth of the security token offering (STO) market is the highly regulated financial world in which it must operate, with many moving parts like legacy systems, intermediaries, and powerful incumbents with vested interests. Therefore, regulatory uncertainty continues to pose the most significant impediment to asset tokenization. Security regulations currently vary significantly from jurisdiction to jurisdiction and no international regulatory framework currently exists for STOs. In its article on p.269, Section 7, Deloitte Luxembourg examines some of the regulatory developments in the STO market. While only a few countries have currently implemented a legal definition for digital securities and security tokens, this space is developing fast and is one to watch.

Despite this market's recent traction, fractional investment models are still to convince the art market. However, this year's Art & Finance survey shows a small increase in interest, with 21% of collectors (up from 19% in 2019) and 26% of art professionals (up from 19% in 2019) stating they were interested or very interested in fractional investment products for art and collectibles. And 29% of wealth managers (up from 10% in 2019) have also professed their interest, likely driven by a wider debate and awareness among wealth managers about asset tokenization, such as debt, equity and asset-backed tokens.

Fractional ownership and tokenization: 29% of wealth managers said they believed fractional ownership and tokenization of art and collectibles could become investment products of interest to their clients (up from 10% in 2019).

9 https://blog.stomarket.com/security-token-market-cap-breaks-1-billion-shows-signs-of-exponential-growth-eb4dd472c54b
10 Area2invest,'STO 101: Security Token Offerings: Anatomy & Context, June 2021, Whitepaper'

Security tokens and non-bankable art assets—new opportunities?

Non-bankable assets
Distributed ledger technology (DLT) and tokenization could provide investors with direct access to non-bankable assets and niche sectors, such as art, classic cars, luxury watches and jewelry as well as wine and wineries, to name just a few.

With global personal wealth (financial and non-financial) estimated at US$260 trillion, it is estimated that nBAs, such as real estate, own businesses, art, and passion assets, account for around 30% or US$78 trillion[11]. With a new financial infrastructure developing around nBAs, this could open up new opportunities for the wealth management sector to generate additional revenue streams and fees from the estimated US$1,481 trillion of art and collectible wealth by UHNWIs in 2020.

By advocating the value of nBA investing, wealth advisors can push the boundaries of their advisory services. However, there are some challenges to overcome, including valuation, risk monitoring, accessibility and liquidity, as well as developing platforms to operate these business services efficiently.

Art as a non-bankable asset
The tokenization of art is already in motion. In July 2021, Artemundi and Sygnum, a digital asset bank, partnered to tokenize Picasso's *Fillette au béret* painting[12] see article on p.247.

The art market serves as an ideal example for the issuance, purchase and exchange of tokens that represent a physical asset. A recent report[13] by Avaloq, titled "Non-bankable assets – investing in a new era", discusses the potential benefits and use cases for creating security tokens from art and collectible assets. For example, a closed-end fund model could be adopted to invest in fine art, where the artwork is sold at some point in the future and token owners would be compensated for their participation. Alternatively, the tokens could be traded freely in a market where anyone holding more than 50% of the tokens could call the rest at an agreed premium over the market value.

The report also outlines other potential revenue sources, such as the asset's usage, exploitation rights and obligations that could be represented and negotiated separately from its ownership, specified by a smart contract or "experience token". For example, proceeds from exhibition ticket sales could be combined with ownership tokens to generate cash flow.

Kerry Ryan, Director, Industry Solution Go to Market, Salesforce US, states that wealth managers need to expand their perspective on non-bankable assets (i.e., passion investments, real estate and business ownership) to bolster their revenues.[14]

However, security tokens are not only relevant to investors. The public sector could also use them as a potential future fundraising tool, such as museums, and open up new types of creative and mutually beneficial collaborations between the private and public sector (see article by Bernadine Bröcker on p.150, Section 3).

Janela
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11 Source Accenture – Orbium Wealth Management C-Level Survey 2020 : The Industry Playbook (netdna-ssl.com) p.6
12 Source: Sygnum, Sygnum Bank and Artemundi tokenize a Picasso on the blockchain, 15. July 2021. Link https://www.insights.sygnum.com/post/sygnum-bank-and-artemundi-tokenize-a-picasso-on-the-blockchain
13 Avalog Non-bankable assets – investing in a new era March 2021 report p11
14 CapGemini World Wealth Report 2021 p.34

Security tokens can be used to finance the creation of a future work art too.

Altas Frequências
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Financing the creation of a future work of art—artist case study: Jens W. Beyrich
Jens W. Beyrich, a Luxembourg artist renowned for his innovative exhibition at the Luxembourg International Airport (2018-2020), and commissioned by the Post Philately of Luxembourg to design its 2021 Christmas stamps, harnesses new ways to present his artwork to investors and pre-finance his cultural projects.

An STO is intended for interested parties to co-own the *Icosahedron*, world's first sculpture, created by Jens W. Beyrich, with a marquetry of lozenges presenting interwoven 2D- and 3D-symmetries. Four tokens at a nominal value of €125,000 each will be issued on a regulated Luxembourg fintech platform alongside the 2021 Christmas stamps by November 2021, to share and hold the sculpture as an underlying asset. The tokens are limited to professional investors only. The polyhedron was part of the Luxembourg International Airport exhibition (2018-2020) and later shown at Nosbaum Reding Gallery.

Jens W. Beyrich's concept of intertwining symmetrical structures cannot be observed in nature. A further development of the *Icosahedron* are the *Star Spheres*, shown at the 58th Biennale of Venice (2019).

The artist received recently permission to show a scaled-up *Star Sphere* in the Pantheon in Rome. The sculpture's contemporary symbolism and historic ambiance will complement the jubilee of the Pantheon—celebrating in binary code its 100-000-000-000 year since its foundation in 27 BC.

To pre-finance the construction of the Star Sphere for the Pantheon exhibition, AACI Art, Antiques and Collectibles Investment S.A. based in Luxembourg, now proposes interested parties to invest in contemporary art by issuing Tracking Stock* with an attributed ISIN[15]. The nominal issue is €2.5 million, divided into 20 shares of EUR125,000 each.

*Tracking Stock is a new investment tool launched by the Luxembourg government in July 2016 (article 1853 of the Luxembourg Civil Code). These shares serve to obtain liquidity for specific ventures or projects managed by the issuing company, without requiring investors to participate in its general business.

15 International Securities Identification Numbers (ISIN)

Andreas Gerber
Head of New Business
Sygmun Bank

Real-life application

The art market of the future

Digital ownership of art on the blockchain

Tokenization opens up the traditional art market to investors...
The traditional art market is one that is based on physical ownership, with face-to-face interactions required to evaluate an artwork and facilitate transactions. It is also a market that is complex with many participants, challenging to navigate without deep knowledge of art and personal connections. Add to this the fact that prices of bluechip art present further financial barriers to entry and it is clear why art is viewed as an asset class accessible only to an elite segment.

These pain points are the reason why the concept of digital ownership on the blockchain, or tokenization, has gained increasing traction in the market. Tokenization can lower entry barriers and 'democratize' access to art. By creating digital ownership tokens that can be issued and traded, buyers and sellers are able to connect directly through digital platforms. Owners or creators of art can make their work available to investors globally, and a secondary market for liquidity can be created. In addition, fractionalization of ownership is possible, meaning investors can purchase a share of an artwork, instead of the (sometimes very costly) whole.

If the full potential of tokenization is realized, investment in all kinds of art, including historical masterpieces, can be made accessible to a broad range of investors, with a more liquid market that provides price transparency—transforming the art industry from what it is today.

...but legal uncertainties around ownership can arise
The excitement around art tokenization is accompanied by a healthy skepticism—a natural response to a nascent technology, also fueled by a Non-Fungible Token (NFT) hype that saw digital artist Michael Winkelmann, aka Beeple, sell an NFT of his work, '*Everydays – The First 5000 Days*', for US$69 million. However, this issuance raised many legal questions around ownership and intellectual property rights when it comes to tokenizing art.

Most importantly, tokens can be fungible or non-fungible—fungible tokens are identical and can be exchanged for one another, whereas NFT are unique and therefore not interchangeable. NFTs do not involve fractionalization of an asset and result in a different use case compared to fungible tokens, where each token represents an equal share of an asset. These two use cases - fungible and non-fungible tokens - have different legal requirements, but only fungible tokens support the concept of asset fractionalization and co-ownership.

Then there are general legal issues. Firstly, there is the risk of fraud—the possibility that the work on sale is not authentic, or that the issuer does not own the work and therefore does not have the right to sell it. Secondly, the terms of ownership, or the rights related to holding a token of the artwork, need to be clarified. And thirdly, the legal basis on which the ownership rights are defined must also be ascertained.

While tokenization can make art investment more accessible, investors need to be aware of the various legal issues that may arise.

New Swiss law provides a strong base to develop a legal framework for tokenization

Putting tokens on the blockchain is therefore just the tip of the iceberg, and a relatively straight-forward technical challenge that was solved some time ago. It is the embedding of tokenization into legal frameworks and operational banking processes and systems that will make it a viable solution and unleash the potential of tokenized assets for both issuers and investors.

The Swiss parliament has adopted the Federal Act on the Adaptation of Federal Law to Developments in Distributed Ledger Technology (DLT). This Act adapts existing regulations to account for DLT developments and comes into force in two parts. The first part introduces a new category of "ledger-based" securities which are represented on the blockchain (i.e., tokenized assets) and has been live since 1 February 2021.

The token issuance was priced at CHF4 million, with 4,000 tokens issued (CHF1,000 per token) and a minimum subscription amount of five tokens or CHF5,000.

This means that for asset tokens, transfer and ownership records on the blockchain are now considered legally binding. While this does not necessarily solve the legal issues of ownership on its own, it provides a clear and solid base on which a legal framework for tokenization can be built and ensures the efficient transfer of tokens between buyer and seller. These legal considerations and framework constitute key elements of Sygnum Bank's ethos. In a lighthouse project with Artemundi, Sygnum has tokenized the *Fillette au béret*—an oil on canvas painting by Picasso - setting-up a robust legal structure for art co-ownership.

Case Study

Sygnum Bank and Artemundi tokenize a Picasso on the blockchain

Sygnum is a regulated Swiss bank, which specializes in digital assets. Its fully integrated, institutional-grade tokenization solution covers the end-to-end life-cycle of a security—from primary issuance, settlement, and custody, to secondary trading.

Artemundi is a leading art investment company that manages more than US$1 billion in art, with long standing experience in international art markets. The company helps clients to manage their art portfolio and has always advocated for more transparent practices within the art industry.

Sygnum and Artemundi collaborated to tokenize Picasso's *Fillette au béret*, providing an example of how tokenization can transform art into a tradeable, bank-grade security on the blockchain.

The artwork

The *Fillette au béret*, painted by world-famous artist Picasso in 1964, is an oil on canvas artwork which has been exhibited in various museums worldwide. The painting has been subject to Artemundi's proprietary examination protocols and an independent third-party valuation.

The issuance

The token issuance was priced at CHF4 million, with 4,000 tokens issued (CHF1,000 per token) and a minimum subscription amount of five tokens or CHF5,000.

Tokenization structure

In art tokenization, it is common to use a special purpose vehicle (SPV), which owns the artwork. The investor owns tokens in the SPV, with only indirect ownership in the artwork. In this issuance, Sygnum developed a model to tokenize ownership directly, introducing new roles to support this—namely, an administrator, manager (of the asset), and custodian, along with other participants such as an appraiser and insurer. Based on existing legal frameworks combined with the recent Swiss DLT amendments, an investor's ownership is legally recognized and can be transferred with a token under Swiss civil law.

Fractional ownership

The structuring of terms was also done to support co-ownership, with an administrator and manager taking care of issues related to the artwork (such as insurance, custody, loan of painting to museums, etc.) and voting rights for token holders on matters such as an early exit. This is different from tokenization through NFTs, a process which is not set up for fractionalization of ownership.

Exit

An investment horizon of five to eight years was defined for the issuance, and the administrator commits to initiate an auction process after a period of five years, with a time horizon of three years to complete the sale. However, an early exit can be triggered one year after the issuance, and token holders can vote to decide this. Tokens are also tradeable on SygnEx, Sygnum's digital asset trading platform, providing a secondary market for an earlier exit.

Trust paves the way forward for tokenization

The certainty of ownership and clarity of terms are critical in paving the way forward for tokenization. Without this secure base, investors will not have full confidence to invest in asset tokens, whether in art or other verticals, and this will limit the adoption and scalability of this new technology. In this case study, Sygnum has provided a legal model for art tokenization which empowers investors to invest with complete trust. As a regulated bank, all assets and issuers on its platform have been vetted, and onboarding and transaction monitoring tools designed for the digital asset economy ensure compliance with anti-money laundering and counter terrorist financing standards of the Swiss banking industry.

Fully integrated and institutional grade, Sygnum's tokenization solution enables issuers to create unique investment opportunities by connecting participants seamlessly on one platform, resulting in the convergence of global public and private markets. Investors can invest in a direct and fractional manner in asset classes previously seen as hard to access such as venture capital, mid cap, real estate, art and collectibles in general.

About Sygnum

Sygnum is the world's first digital asset bank. With a banking licence in Switzerland and a securities dealer and capital markets services licence in Singapore, Sygnum empowers institutional and private qualified investors, corporates, banks and other financial institutions to invest in the digital asset economy with complete trust.

The structuring of terms was also done to support co-ownership, with an administrator and manager taking care of issues relating to the artwork (such as insurance, custody, loan of painting to museums, etc.) and voting rights for token holders on matters such as an early exit. This is different from tokenization through NFTs, a process which is not set up for fractionalization of ownership.

Niccolò Filippo Veneri Savoia
CEO, Look Lateral Group

Case study

Security tokens + art

The FIMART value proposition

In 2020, the global stock of artworks and collectibles was estimated at US$1.7 trillion. However, the main constraints of this stock are its extreme illiquidity and opaque profiles, which makes it difficult to fully take advantage of the asset class' specificities. The trading of artworks and extending loans guaranteed by artworks, represent the two main ways of creating liquidity in this market, but they often both require in-depth knowledge and complex procedures to be practiced by non-professionals.

The Financial Market of Art—or FIMART—is a regulated Italian subsidiary of the Look Lateral Group, which aims to build a FinTech ecosystem that allows every actor in the art world to monetize their assets. It is based on a vision in which traditional financial instruments will be progressively upgraded and/or replaced by digital securities or security tokens.

The company has developed a tokenization protocol that defines how tokenized assets are generated, issued, sent, and received while complying with all necessary regulations in different jurisdictions in order to create a safe and transparent financial exchange of digital securities for art-related assets.

This protocol allows the creation of alternative digital securities, financial instruments that provide liquidity, and diversification advantages to issuers and to investors through the use of smart contracts based on the ERC1410[16] security token. Each type of art security is a clear case study, carefully designed for a specific need or player.

Aiming to launch in Q1 of 2022, this transformation will expand investment opportunities and increase security, automation, and efficiency across the entire financial sector.

Basic token protocol
The basic art-backed token represents common fractional ownership in a specific artwork, where a pre-specified portion (up to 49% because currently, no less than 51% of the artwork must still be owned by one individual or organization which has its physical possession) of an artwork is tokenized, and fungible tokens (fractional ownership shares/ units) are sold to interested parties during the Art Public Offering (APO). The majority owner maintains possession[17] and is responsible for keeping the collateral safe, secure, and free from damage beyond normal wear and tear. The transaction is automatically recorded onto an Ethereum blockchain accessible to all token holders. The ownership conferred via the token purchase is guaranteed by a contractual agreement that can be terminated through voluntary sale transaction by the token investor or other terminal events.

16 "ERC1400" is the standard for the newly proposed securities-based token. The new standard is mainly to design a set of common interfaces by combining the fungible of the token with the securities-related business scenarios
17 Owner, most likely galleries, museums, foundations, companies, etc. could maintain the work in their premises provided a few requirements are met

Finally, a well-functioning and regulated secondary market for the art-backed tokens opens up the art market to new capital and facilitates FIMART's mission of "unlocking the value in art" to become a reality.

Enhancements to the basic token
The enhanced features of the basic art-backed token are:

1. Periodic profit share payments;
2. Buyback option;
3. Interest-bearing debt tokens; and
4. Buyback obligation.

Each provides a series of specific advantages for galleries, museums, foundations, collectors, and corporate collectors, according to the characteristics of the different security tokens.

Periodic profit share payments
This is a security token that provides periodic profit share payments to the investors. The cash flow sources that will fund the profit shares are merchandising and museum entry revenues, promised interest payments, and other revenues that will come through the interactions within the FIMART platform. Dividend payments occur through the automatic execution of smart contracts that include a specific percentage of financial rights. This type of tokenization was created with institutions and galleries in mind to monetize their assets while maintaining artworks' ownership. Meanwhile, investors can buy shares of the artwork and diversify their portfolios and earn a periodic dividend as if it was a passive income. For example, a museum can assign a % of ticket revenues and/or % of merchandising revenues related to an artwork. In addition, the tokens holders will receive a % of any other transaction on FIMART, such as a user who pays one dollar to read a document about that artwork.

Buyback option
The buyback option allows or provides the repurchase of tokens based on the terms and information set out in the smart contract. This is designed for galleries to repurchase artworks' tokens at a predetermined price allowing the future sale of the physical artworks on the traditional market.

Tokens with the buyback option feature allow the owner (issuer of the tokens) to buy back some or all outstanding tokens at a predetermined price per token. If the owner exercises this option, the token holders must surrender theirs in exchange for the predetermined price that is either the higher of the current market price, or the issue price plus a percentage premium at any given time. If the market price has gone up, token holders will benefit—and even if the market price has declined, they are still protected. This option allows the owner to take back full ownership of the artwork while token holders are guaranteed an exit at a price above the issue price.

The buyback option's advantage is to obtain liquidity without selling the physical artwork or waiting for a collector/buyer. For example, if a gallery needs immediate liquidity and, upon not finding a collector interested in buying the artwork, it can instead list the work on FIMART with the buyback option. The gallery obtains immediate liquidity from the tokens' sold, but has the guarantee of possibly repurchasing the tokens if it finds a buyer for the entire physical artwork.

Interest-bearing debt tokens
With this interest-bearing—or art-lending—token option, FIMART will enable art owners to obtain liquidity quickly, developing a particular type of interest-bearing, finite maturity debt token secured by a portion (less than 50%) of an appraised, insured, signature-tagged art asset.

Art-lending tokens are issued to facilitate borrowing by an owner against a portion of their art asset. In this case, the owner (borrower) maintains 100% ownership, but can monetize the art asset for a certain time period (maturity). Smart contracts allow this type of security token to provide loans using artworks as collateral, where the underlying tokenized asset is a fixed maturity and interest rate loan that pays interest to token holders twice a year. When the fixed maturity period ends and all promised interest payments are made, the borrower repays the principal. In the event of nonpayment of interest or principal to the token holders, the loan is in default, and if not rectified, debt tokens may turn into equity tokens (as coded in the smart contract), deferring ownership of the underlying artwork. In other words, when the borrower defaults, lenders take the artwork.

For example, a collector can receive immediate liquidity through a loan, using artworks as collateral. The loan has a maximum duration of five years, during which the collector fulfills the repayment of the loan on a monthly basis with a fixed interest rate. The tokens' holders will receive the partial repayment every month.

Buyback obligation
FIMART, through art-lending tokens, developed the buyback obligation that requires the repurchase of shares sold in a predefined time frame. An example could be a museum that decides to temporarily monetize part of the collection to have immediate liquidity, expecting to buy back the tokens after a set time.

Tokens that have the buyback obligation feature require the owner (issuer of the tokens) to buy back some or all of the outstanding tokens at a predetermined price per token. When the issuer of the tokens initiates the repurchase, the token holders will surrender their token(s) in exchange for the repurchase price. The repurchase price is the lesser of the current market price or the issue price plus a X% premium at any time determined by the issuer. This feature obligates the issuer of the tokens to take back full ownership of the artwork in a specific amount of time, while the token holders are guaranteed an exit, and the issuer's annual financing cost is capped at X% per year. If the market price has increased, the issuer will reestablish full ownership at a lower and predictable cost.

The buyback obligation's advantage is to obtain immediate liquidity by a loan, without selling the physical artwork and the possibility of repaying the loan in a single solution but at an increasing interest rate over the years. For example, if a gallery needs immediate liquidity and, upon not finding a collector interested in buying the artwork, it can instead list it on FIMART with the buyback obligation. Essentially, it's a collateral loan, but the gallery has the advantage of waiting until the ideal moment to repurchase the tokens within the fixed period of time, without a monthly repayment.

FIMART and its use of fungible and non-fungible tokens
FIMART combines fungible tokens (FTs) to represent the artworks' shares or common art securities that are traded on FIMART, and non-fungible tokens (NFTs) to define and create a particular right. The platform uses the latter for specific reasons only. For example, the NFT could represent the possession's right, or in case of buyback option or obligation, the NFT represents the right to reconsolidate the artwork buying back the other fungible tokens.

Security tokens + art = new sources of capital
FIMART believes that these unique security token protocols create opportunities for all players in the market to generate new sources of capital.

For cultural institutions and museums, the platform provides them with alternative ways of increasing their funds without relying on donations, government grants, or having to deaccession artworks in times of need.

For galleries, tokenizing their works allows them to receive immediate liquidity from artworks that can be sold later on the conventional art market. For investors (institutional, professionals, and privates) and collectors, art security tokens present the possibility of diversifying assets by investing in artworks they may not previously have had access to. Collectors can obtain the necessary liquidity so as to expand their collection or for other needs without having to sell the physical artworks.

In addition, it is hoped that this format will contribute to the increased accessibility of art, particularly among new collectors such as millennials. Those looking to invest in collecting for the first time, will find opportunities presented by the well tracked information shared by the curators, critics, and technicians who contribute to the FIMART ecosystem.

An innovative mindset and new technologies will provide the opportunity to develop fractional ownership investment mechanisms in a regulated, stable, and efficient environment.

For cultural institutions and museums, the platform provides them with alternative ways of increasing their funds without relying on donations, government grants, or having to deaccession artworks in times of need.

Art & Technology

07

Neoblanc
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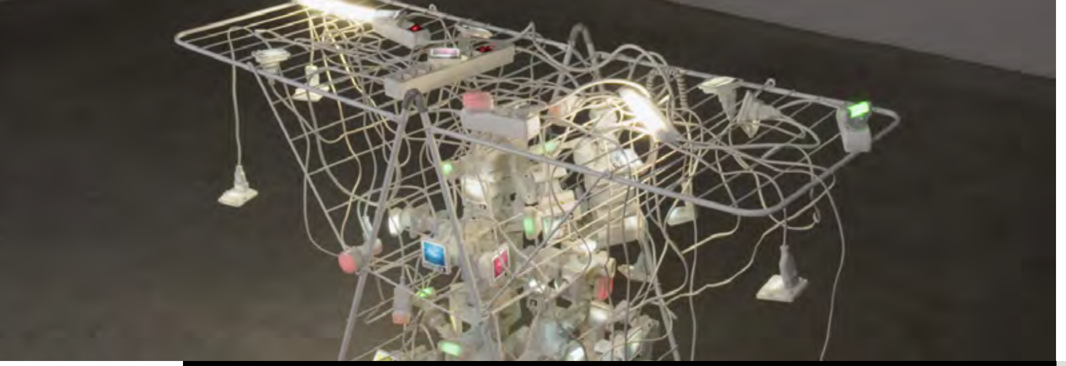

Highlights

The digitalization of the art market has entered a new era
Over the last 18 months, the COVID-19 pandemic has sparked more digital innovation, experimentation and risk-taking than in the past decade alone, and the traditional art market is on the cusp of a new era, potentially redefining what it means to be a 21st-century art business.

The maturing art technology industry is a key enabler for the art and finance industry
In the art and tech ecosystem over the last 10 years, the number of specialized players addressing the various friction points faced by the art and finance industry continues to grow and gain maturity. The digital transformation sweeping the art market is likely to drive more efficiency and growth.

Technology could bring art and finance closer together
Art technology companies could help bridge the gap and address many of the current frictions between the art market and the wealth management industry. Better integration of art market analytics and collection management systems, technology facilitating cost-effective due diligence, and new technology-driven investment products could open the art market up to the wealth management industry.

Blockchain technology is going mainstream
Recent developments in and adoption of blockchain technology could solve many of the concerns raised by wealth managers and art market stakeholders—52% of wealth managers (up from 18% in 2019) believe blockchain technology could have an important impact on their ability to further develop art-related services as part of their wealth management offering.

The growing market for decentralized finance (DeFi) could catalyze further integration between the art market and the wealth management industry
New developments in DeFi, such as security tokens, could accelerate wealth managers' interest in non-bankable assets like art and collectibles. This could boost the development of various art wealth management services, such as art-secured lending services, art investment, fundraising and new philanthropy models.

Airflow
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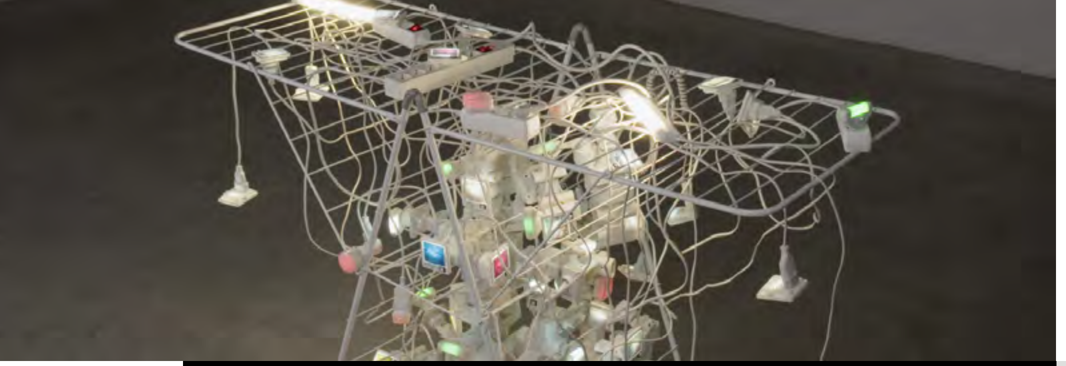


85% of younger collectors said blockchain technology could transform the way business is currently being conducted.

Esposas
©Peter Mallet/Courtesy Haunch of Venison, London - 2005

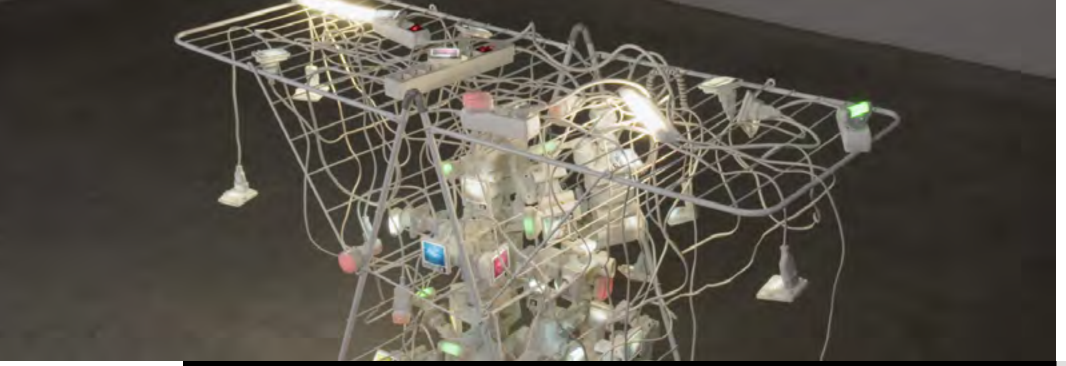
Collection management tools could help better integrate art in wealth reporting
53% of wealth managers said new and improved art collection management tools will help them develop an art-related wealth management service offering, and are closely associated with wealth managers' increasing focus on embedding art-related wealth in their client reporting.

Improved art due diligence tools and services: wealth managers strongly believe that technology will improve the provenance tracking and traceability of art (80%), mitigate authenticity risks (67%), enhance valuation processes (61%) and boost the overall transparency of the art market (79%). This will facilitate a cost- and time-effective due-diligence process and could open up the market to more participants.

Information and education
75% of wealth managers said new technology and online platforms are very important in improving access to art market information and education (compared with 68% in 2019). Both art collectors (81%) and art professionals (78%) felt the same way.

Broadening the collector base
56% of wealth managers said new technology and online platforms are likely catalysts for bringing new audiences to the art market (compared with 49% in 2019). Both art collectors (67%) and art professionals (71%) also said this would expand the collector base.

Most younger collectors believe technology will be a major game-changer in the art and wealth management industry
Overall, younger collectors think technological development will have a large impact on the art wealth management industry over the next two to three years. The vast majority (92%) of younger collectors said augmented reality (AR) and virtual reality (VR) will have a significant impact, compared with 38% of older collectors. While 85% of younger collectors said blockchain technology could transform the way business is currently being conducted (compared with 52% of older collectors) and another 85% of younger collectors believe that big data, analytics and artificial intelligence (AI) will have an impact on the art and wealth management industry going forward, significantly higher than 57% of older collectors.



Introduction

For this year's report, we have divided the art and technology section into three parts:

Part 1: survey findings 2021
This section examines how art and finance stakeholders (wealth managers, art professionals and collectors) view technology's impact on the art market and whether it can catalyze further adoption and growth in art and wealth management services.

Part 2: blockchain and tokenization
Here, we take a closer look at some of the new developments around blockchain and tokenization. Contributions from Deloitte Luxembourg's Technology team, Deloitte Japan and Startbahn explore the wider impact of these new developments on the art market's future, from regulatory issues to blockchain as social infrastructure.

Part 3: data and technology ecosystem
A new ecosystem of art technology services has emerged in recent years. This section provides an overview of some of these services and the companies behind them. A contribution by Arte Generali examines how new technologies can impact the art ecosystem, specifically regarding collection management, certification, authentication, provenance, and predictive systems.

Digital transformation in the art market

The digitalization of the art market has entered a new era. Over the last 18 months, the COVID-19 pandemic has sparked more digital innovation, experimentation and risk-taking than in the past decade alone, and the traditional art market is on the cusp of a new era, potentially redefining what it means to be a 21st-century art business.

The COVID-19 pandemic severely impacted the global art market during the first half of 2020, as art fairs, galleries, auctions, and museums struggled to adapt to the new restrictive world of lockdowns and social distancing. However, the pandemic also accelerated the transformation and adoption of new digital strategies across the art industry, from new online art gallery models, art fairs and viewing rooms, such as Art Basel's Online Viewing Rooms (OVR).

We have also seen the emergence of new hybrid auction formats, introduced by Sotheby's in June 2020, which combine new digital livestream formats with traditional in-person auctions. With evening auctions now being streamed on YouTube and Facebook, the traditionally insular auction world is finally opening up to new audiences and spectators.

A new ecosystem of art technology services has emerged in recent years. This section provides an overview of some of these services and the companies behind them.

Netless'07
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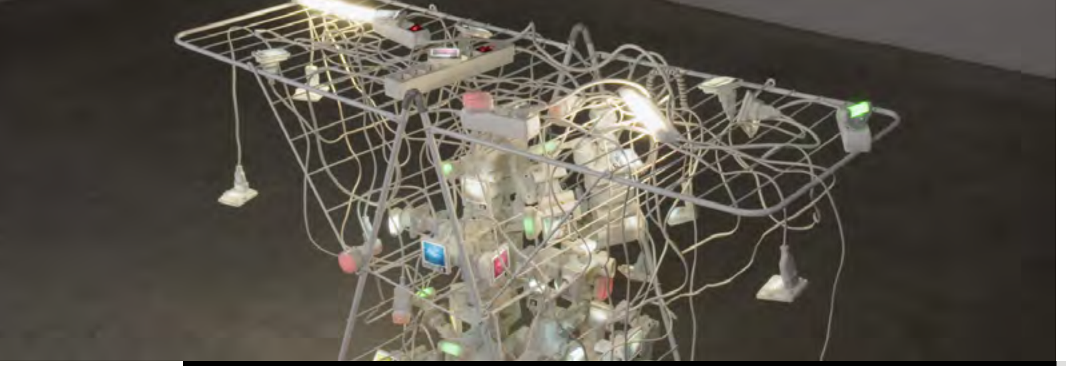


For wealth managers, the pandemic has intensified existing pressures in the industry, such as changing customer expectations driven by younger tech-savvy demographics, increasing competition, and declining margins.

There is a renewed focus on blockchain and its specific use case for the art market, such as a tool for provenance tracking, ownership registration and more recently non-fungible tokens (NFTs) and digital collectibles. This digital transformation is democratizing the art trade by providing easier and broader access to the art market and helping develop new ownership models. The increasing adoption of digital tools and online channels also boosts transaction transparency and market liquidity.

For wealth managers, the pandemic has intensified existing pressures in the industry, such as changing customer expectations driven by younger tech-savvy demographics, increasing competition, and declining margins. But like the art industry, these changing market dynamics also present an opportunity for wealth managers that are willing and prepared to adapt. By building on their existing relationships, wealth managers are well-positioned to create operating models that place users at the center of decision-making to meet the evolving demands of the market, clients and regulators.

This transformation can be aided by investing in new technology infrastructure. A recent report by Deloitte Canada[1] highlighted a few key aspects of this digital transformation:

- Building an end-to-end digital client onboarding solution that goes beyond traditional risk/return profiling, while harnessing gamification to boost customer experience;
- Providing digital access to customized research and targeted content;
- Enabling hybrid advisory solutions for needs-based investing around life goals and personal values (e.g., sustainability, impact investing and private equity); and
- Enabling "mass customization" of client reporting along pre-defined parameters.

Another aspect of increasing importance is integration with third-party service providers. If wealth management firms improve this integration process, art collection management systems and art market data could be fed seamlessly into wealth management platforms and client reporting.

Art technology companies could help bridge the gap and address many of the current friction points between the art market and the wealth management industry. Better access to big data and art market analytics, integration of art collection management systems, technology facilitating cost-effective due diligence, and new technology-driven investment products could drive future growth in art and wealth management-related services.

We are delighted to feature a series of global expert contributions providing insights into new developments and trends on art & Technology, such as

Tipping point—the continuation of a beautiful relationship between technology and art, Paul Lee, Partner & Global Head of Research for the technology, media, and telecommunications (TMT), Deloitte UK

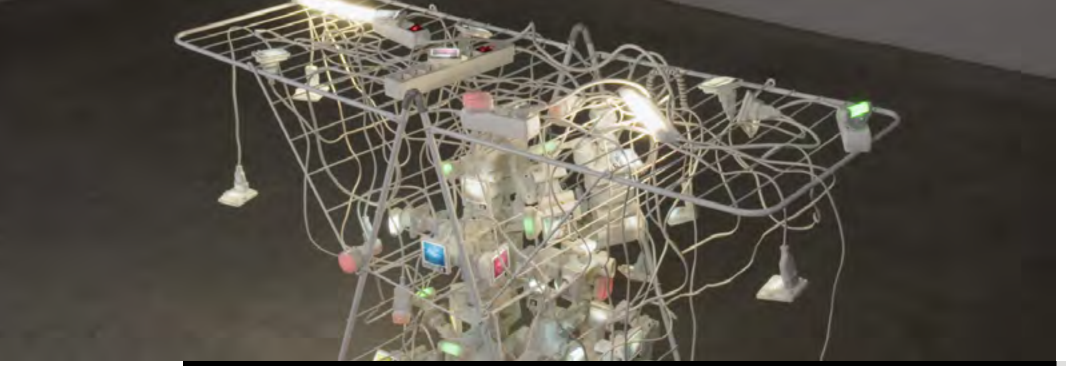
The ArtTech phenomenon—technology's impact on art insurance, Jean Gazançon, CEO, Arte Generali

Art & Blockchain: unlocking new opportunities thanks to decentralized models, Jesus Pena Garcia, Senior Manager; Giulia Pescatore, Manager, Antonio Victoria, Analyst; Kristijan Sacer, Analyst, Deloitte Luxembourg

From monetization to sector resilience—blockchain as social infrastructure? Josephine Ayako Yamada, Manager, Deloitte Japan; Taihei Shii, CEO, Startbahn Inc; Kensuke Ito, Senior Researcher, Startbahn Inc

Cultural revolution: art's emerging digital ecosystem, Chris Bentley, Head of Fine Art & Specie, UK & Lloyd's, AXA XL

1 Deloitte Canada: ca-en-finance-wealth-tech-infographic-aoda.pdf



Paul Lee
Partner, Deloitte UK and the Global Head of Research for the technology, media, and telecommunications (TMT) industry at **Deloitte**.

In his global role, Paul has authored over 80 TMT reports, including **Deloitte's** 15th annual Predictions for the Technology, Media and Telecommunications series.

Expert voices

Tipping point

The continuation of a beautiful relationship between technology and art

Technology is fertilizer for the art world. It enables more people to express their creativity via new digital tools. It makes art more inclusive and thus valuable to society because works can be delivered to and enjoyed by audiences wherever they are. It gives rise to more forms of art, such as digital filters, which may one day become as important as the images they are applied to.

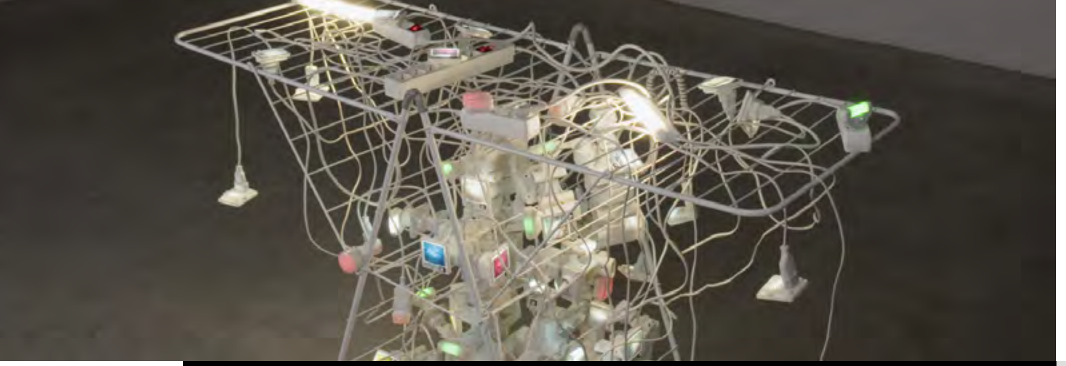
Technology will continue to shape and reshape the art world, and its fullest impacts have yet to be felt. This much is highly probable; what is far harder to discern and what this article will endeavour to identify, is some of the imminent tech-enabled tipping points for the art world. Tech will empower the art world, even if not everyone wins.

One of the boldest questions to ask is whether technology removes the need for art to be physical to be valuable to collectors and museums, as well as wider society.

The current state: art is physical, unique, and fragile
Art today is predominantly physical: tangible constructions of oil paints on canvas, or sculptures of various materials, housed in physical locations, with occasional tours for the most famous of pieces. A current example of this is the collection of Van Gogh self-portraits that will be exhibited at London's Courtauld Gallery in 2022. Valuable art also exists in the darkened archives of collections which lack the wall space to show everything.

Physical art is majestic, but is also fragile and vulnerable. It can decay and crumble. It can be stolen or vandalized. It is also static: once finished, it does not iterate. The physicality of art determines how it is enjoyed, and monetized. The digitization of art, either in creating digital facsimiles, or digital-first art, changes that.

Digital content is intangible, imperfect, but can always be iterated
The idea that art needs to be physical will likely increasingly jar with the ever more accepted assumptions around digital content, whose value is a function of its intangibility, and its ease of replication, distribution, and storage. Digital content is not unique; perfect facsimiles can be created effortlessly. Iterations are always possible, and readily applicable, via software updates. Indeed, digital content is innately time limited—it is released and consumed in the knowledge that is ephemeral and will be displaced by a superior version. Code can be corrupted, but does not decay, and it can always be reinstalled.



When one thinks of art, one tends not to think of operating systems, but this is as much an aesthetic endeavor, as it is a technical one. The annual refresh of an operating system tends to bring a new design identity, as well as new functionality. It can make a phone—which at one level is a compact picture frame, hewn out of glass and metal, and powered by a supercomputer—feel like a brand-new device. New operating systems always include some new functionality, but the majority of new code exists to make existing processes work better.

The video game has showcased the demand for digital-only creations

When thinking of art, video games tend not to be top of the list, but over time, video games will become increasingly valued for their artistry, as the underlying technology permits. The first video games were pixelated and clunky because that was what was possible then, but we are now on the cusp of very high-resolution games, with 8K video standards permitting 33 million pixels per frame. Over the lifetime of the games console, which is fifty years young in 2022, multiple game brands have persisted over that time, with each new console generation largely telling the same story, but via an ever-richer, more challenging digital canvas. There is a parallel between the upgrade to a video game, and that of an operating system.

The video game ecosystem, across all devices (PC, console, and smartphone) has arguably become one of the foundations of the digital-first art market. A mere decade ago, the idea of paying for digital artefacts within a video game was novel, and often sneered at. Today, the idea of buying digital skins to dress an avatar, has become commonplace.

Over the coming years, the artistry applied to creating such a skin, or any other form of digital art, is likely to become ever more complex and enduring, because technology enables and promotes this. Beeple, whose EVERYDAYS: THE FIRST 5000 DAYS sold as a non-fungible token (NFT) for US$69 million in March 2021, is one of many artists who work solely or predominantly with digital creations. Beeple's success will no doubt attract other creators, as well as other collectors in the long term.

The non-fungible token (NFT) makes digital unique

Throughout history—from the printing press to the camera, and from the photocopier to the screenshot—technology has tended to enable the replication of media, with ever greater fidelity. And that is likely to continue. However, one of the main roles of the NFT is to apply uniqueness, or at least a limit on the number of copies, of a piece of digital artwork.

NFTs generated lots of eye-popping headlines in 2021 because of their novelty: whilst people may be more accustomed to the idea of digital-first art or other memorabilia, the sums paid are unfamiliar, and hence shock.

NFTs are a nascent, emerging technology, but mesh the rising interest in digital art, the maturing of blockchain technology as well as improvements in digital creative tools and displays. NFTs still need to address issues around security and sustainability, but as these are resolved, adoption should ramp up.

The advance of the digital display will accelerate the digitization of museums and galleries and the way they engage with society

When people discuss technological advance, they often think of raw processing power. For the art world, a critical enabler is the screen. Screens have been on a slow, steady, and relentless trajectory towards perfection over the last seven decades.

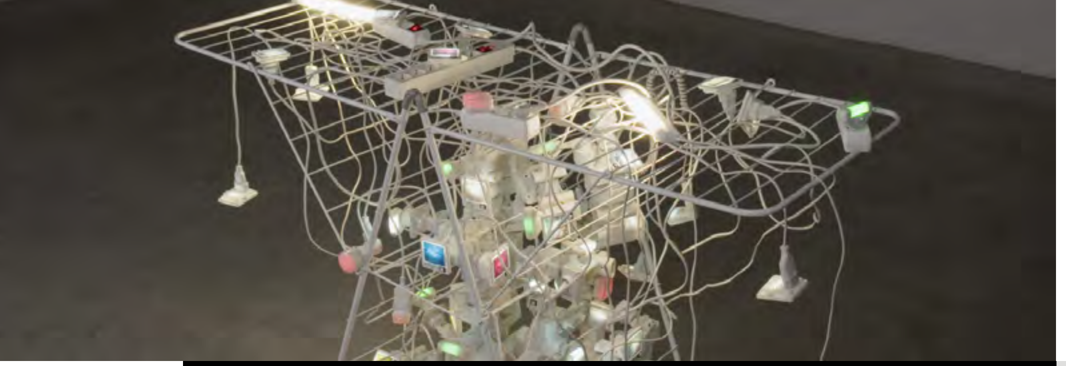
In the last ten years, the caliber of all screens within smartphones, computers, television, cinema screens, and outdoor displays have all improved across the axes of pixel count, color range, and brightness. Consumers are being guided to expect the perfect screen, which should arrive by the end of this decade. This perfect screen should make it almost impossible to tell, at first glance, whether one is looking through a window or gazing at a monitor.

The arrival of the (near) perfect screen enables museums, galleries, and homes to consider migrating to digital displays to showcase art. Museums and galleries could deploy screens as a complement to physical artworks, or use screens as a way to display content from the archives which otherwise would not be readily accessible to the public. Homes could display museum artworks on 100-inch screens in static form, or as vast screensavers. Or they could have arrays of screens which show an owner's collection.

The digitization of the cinema may foretell the future of the art exhibition

Technology enables the most valued art works to be duplicated. Exhibitions, whether permanent or travelling, are valued because they are originals. However, consumers also value, and indeed have always valued replicas, be they limited edition lithographs or mass-produced posters, or indeed projected 4K movies in a cinema, paired with spatial audio.

Considering the latter example, is it equally (or more) valuable to project over-sized, high-fidelity, large scale digital copies of iconic art onto a specially treated white surface as it is to show the original, possibly encased in glass so as to prevent damage from the elements, or, lamentably, from saboteurs? Would the former be better for the owners of the original art works, for the public, for the democratization of art?



A multiplex cinema consists of multiple rooms projecting 4K images onto a specialist screen, complemented by an array of speakers. Analog reels of film have been substituted by digital copies which do not suffer from repeat usage, and do not get lost or damaged whilst being transported. Consumers enjoy cinemas as they offer large, immersive screens. Can art museums or galleries bring the best art to more people through the digitization of content and better displays or projectors?

Not all art can be faithfully digitized; the three-dimensional nature of sculpture cannot be replicated on a 2D screen of any caliber. This is where emerging technologies such as virtual reality (VR) may come in, with their ability to show images captured with 360-degree cameras. Every technology has trade-offs, and with VR a major constraint is the cost of capture, and also the cost of quality VR devices, with requisite resolution.

Over the coming years, immersive art experiences are likely to become increasingly popular at museums and galleries, bathing their visitors in color, often complemented by bespoke soundtracks.

The digitization of content changes the nature of ownership

For decades, mainstream consumer ownership of content was based on ownership of physical content. Shelves were dedicated to housing and displaying books, LPs, and DVDs. But, with every year, this form of ownership has moved to subscriptions, offering the right to consume. There are now hundreds of millions of subscribers to TV programs, movies, music, books, and video games. The same piece of content can be owned—subject to a fee—by everyone.

A variation on this model is fractional ownership of a digital or physical artwork. A piece of art could be owned by a finite number of people, each of whom could have the right to display the artwork. Ownership can be within an NFT or fungible asset-backed tokens offered during a security token offering (STO), which can include a contract stipulating the number of co-owners and commissions flowing back to the artist applicable on resale.

NFTs and other types of blockchain application could be applied to existing artworks, assisting in the authentication process and making the art market more efficient.

The algorithm as an artwork

As well as digitized artworks and digital-only art, there is likely to be a growing volume of digital artworks that were created by algorithms. At the simplest levels, these include art modified by filters, which are an application of artificial intelligence. Most smartphones purchased in the last year are likely to apply filters by default, accentuating elements, such as the blueness of the sky, or the whiteness of clouds, as per general consumer preferences. Some smartphones also now have sufficient power to create artistic affects, such as converting a photo or video into a pencil-like sketch.

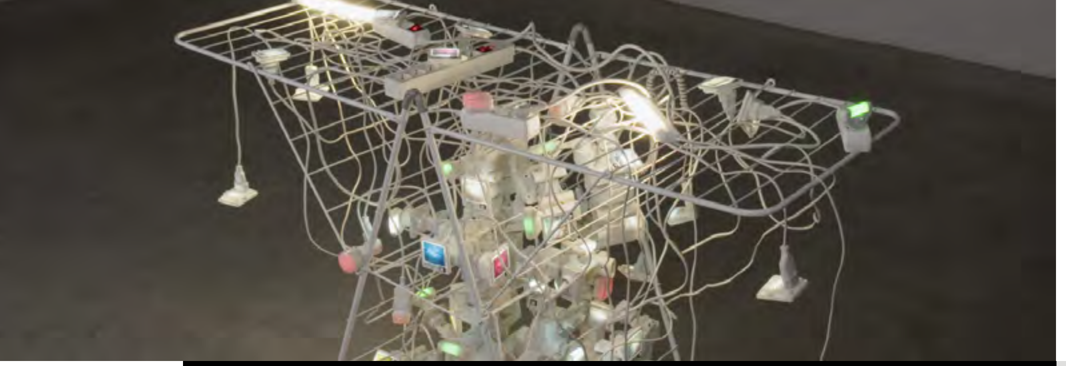
This machine learning approach to tweaking existing images can also be applied to creating brand new images that never existed before. These could include 'a brown horse standing on a grassy field' or 'a happy young child opens a present on her birthday' with the image created based on key words inputted by a user and derived from the billions of real images ingested by a supercomputer. An extrapolation of this approach could be the request to create 'a portrait of a seated woman, gazing at the viewer, smiling softly, set against an imaginary landscape'.

The idea of an omniscient supercomputer being able to craft a Mona Lisa on-demand may feel questionable, but is this tipping point really that distant? Artificial intelligence is the aggregation and application of historical human intelligence: is algorithmic art really that abstracted from conventional creative processes?

Technology's impact is gentle, relentless, and inexorable

The impact of technology on a daily basis is imperceptible: it is moisture in the air, whose droplets accumulate over time. In the long-run, technology is a wave, with ever-growing strength. Per the assertion in the introduction, tech will empower the art world, even if not everyone wins. Art institutions should ensure their digital strategies are ready to ride the technologically-enabled changes that are imminent and inexorable.

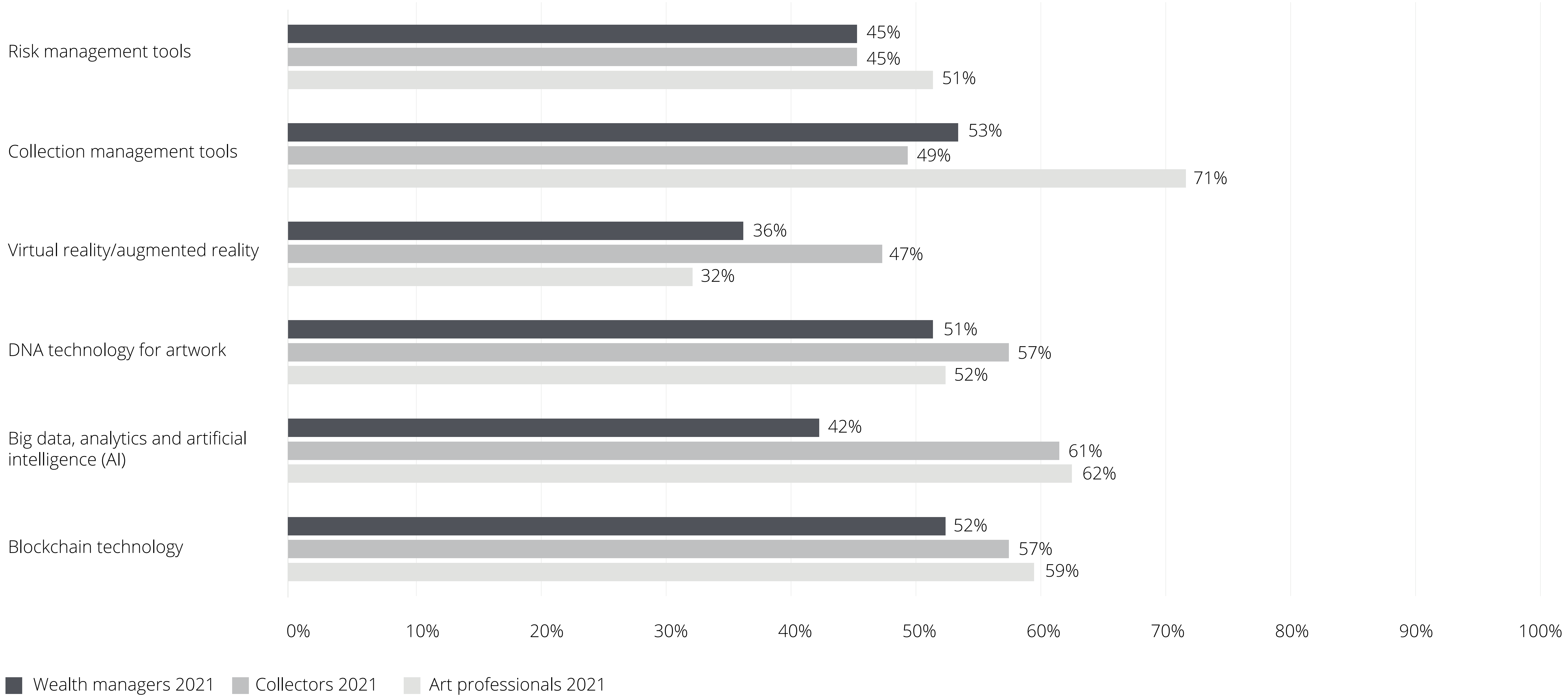
NFTs and other types of blockchain application could be applied to existing artworks, assisting in the authentication process and making the art market more efficient.

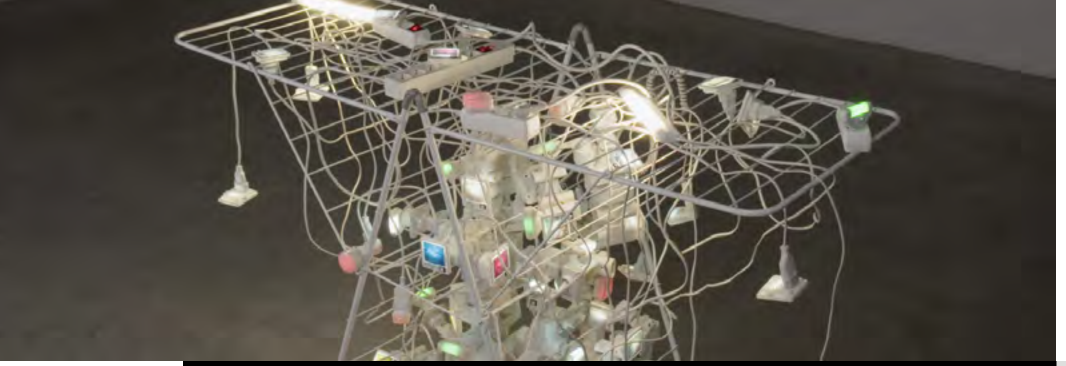


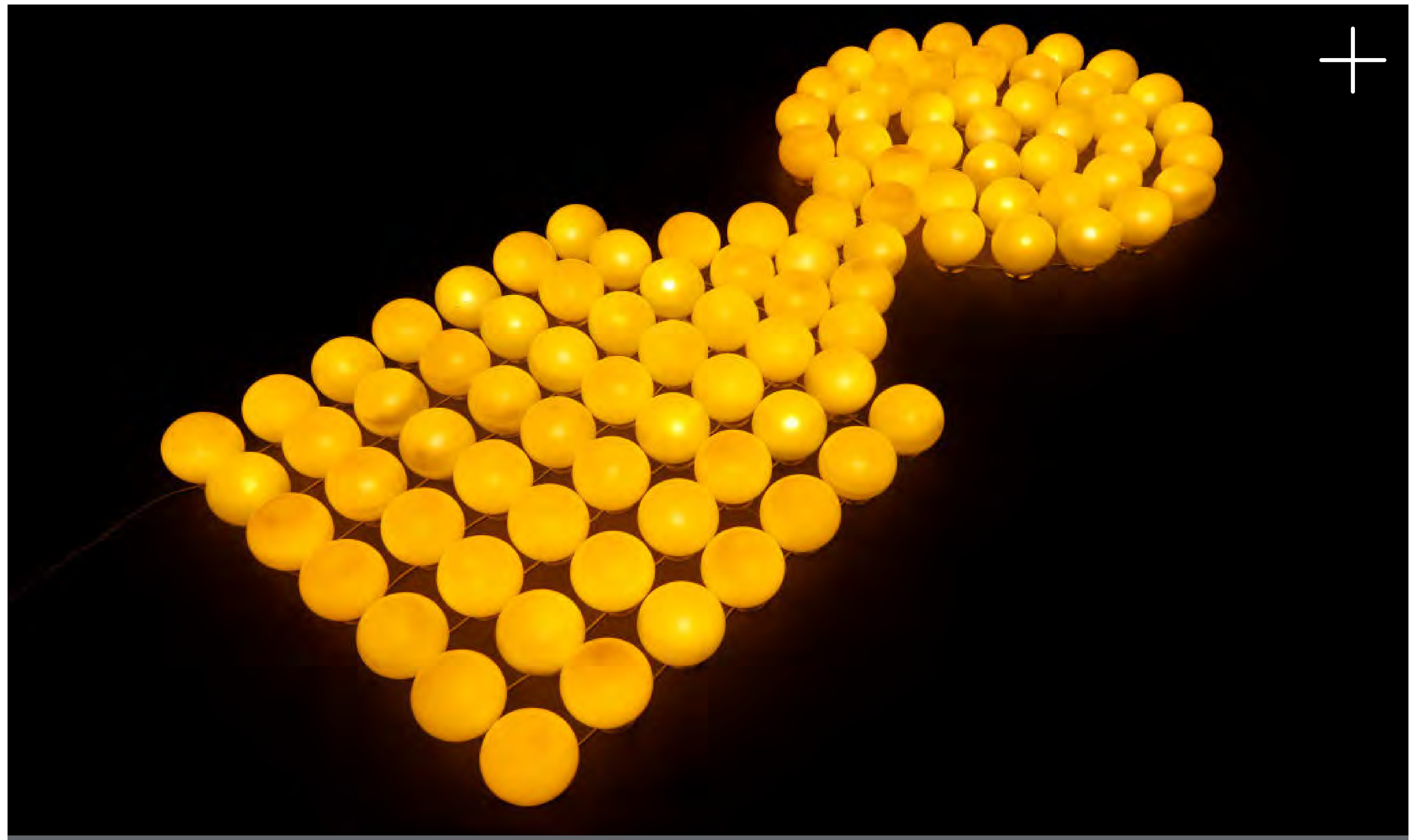
Part 1. Survey findings 2021—technology

This year's findings show growing confidence across all stakeholders about technology's role in improving and further developing art and wealth management services to reduce risks, increase engagement and broaden the collector base.

Figure 102. Which of the following technologies do you think could have the most impact on the development of art and wealth management services in the next two to three years?







52% of wealth managers (up from 18% in 2019) believe blockchain technology could have an important impact on their ability to develop art-related services as part of their wealth management offering.

Pop Luz
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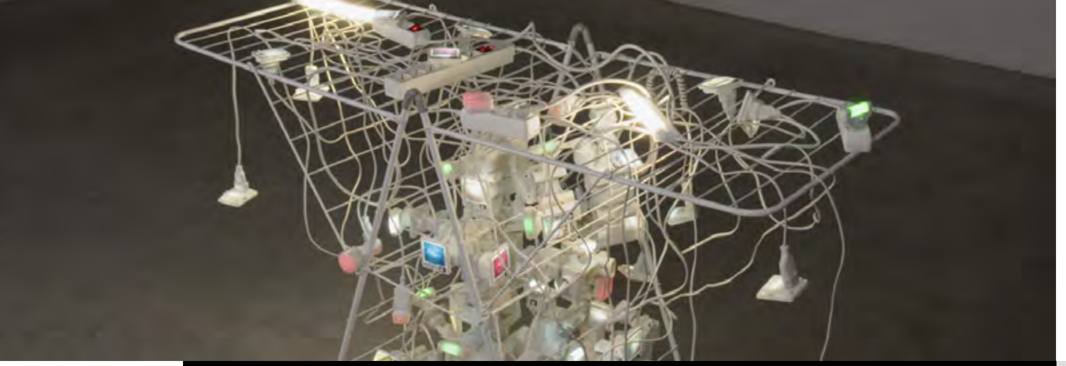
- **Risk management tools**
  45% of wealth managers said technologies aimed at better understanding and managing art-related risk will have the biggest impact on the development of their service offering around art investment services and art-secured lending. Nearly half (45%) of art collectors and 51% of art professionals also thought risk management technologies would be important to further develop and expand the practice of art wealth management.

- **Blockchain technology goes mainstream and could solve many wealth managers' and art market stakeholders' concerns**
  52% of wealth managers (up from 18% in 2019) believe blockchain technology could have an important impact on their ability to develop art-related services as part of their wealth management offering. As private banks are increasingly embracing blockchain technology in their core business, we will likely see a growing focus on this area going forward. Of the art collectors surveyed, 57% also believe blockchain technology will have a major impact (compared with 23% in 2019), while 59% of art professionals said the same, compared with 36% in 2019.

- **Collection management tools**
  53% of wealth managers said that new and improved technology around art collection management tools will have the biggest influence on the development of art-related wealth management services. This is closely associated with wealth managers' increasing focus on embedding art-related wealth into their client reporting. Of the art professionals surveyed, 71% believed collection management systems will have the most important impact, compared with 49% of collectors who said the same. In the article on p.311 in Section 8, Deloitte Legal Italy examines collection management platforms and the legal aspects of the digitalization of art collections.

- **DNA technology for artworks can help provenance tracking and prevent forgeries**
  51% of wealth managers believe recent developments around DNA and fingerprinting technologies for art will have a significant impact on the development of art and wealth management services (compared with 45% in 2019). With 77% of wealth managers surveyed saying authenticity, provenance and the risk of forgeries and misattribution were the greatest threat to the art market's reputation this year, new technologies that address these concerns could significantly boost wealth managers' trust when incorporating art in their service offering. Also, 57% of collectors and 52% of art professionals believe technologies aimed at addressing concerns around authenticity and provenance would be impactful.

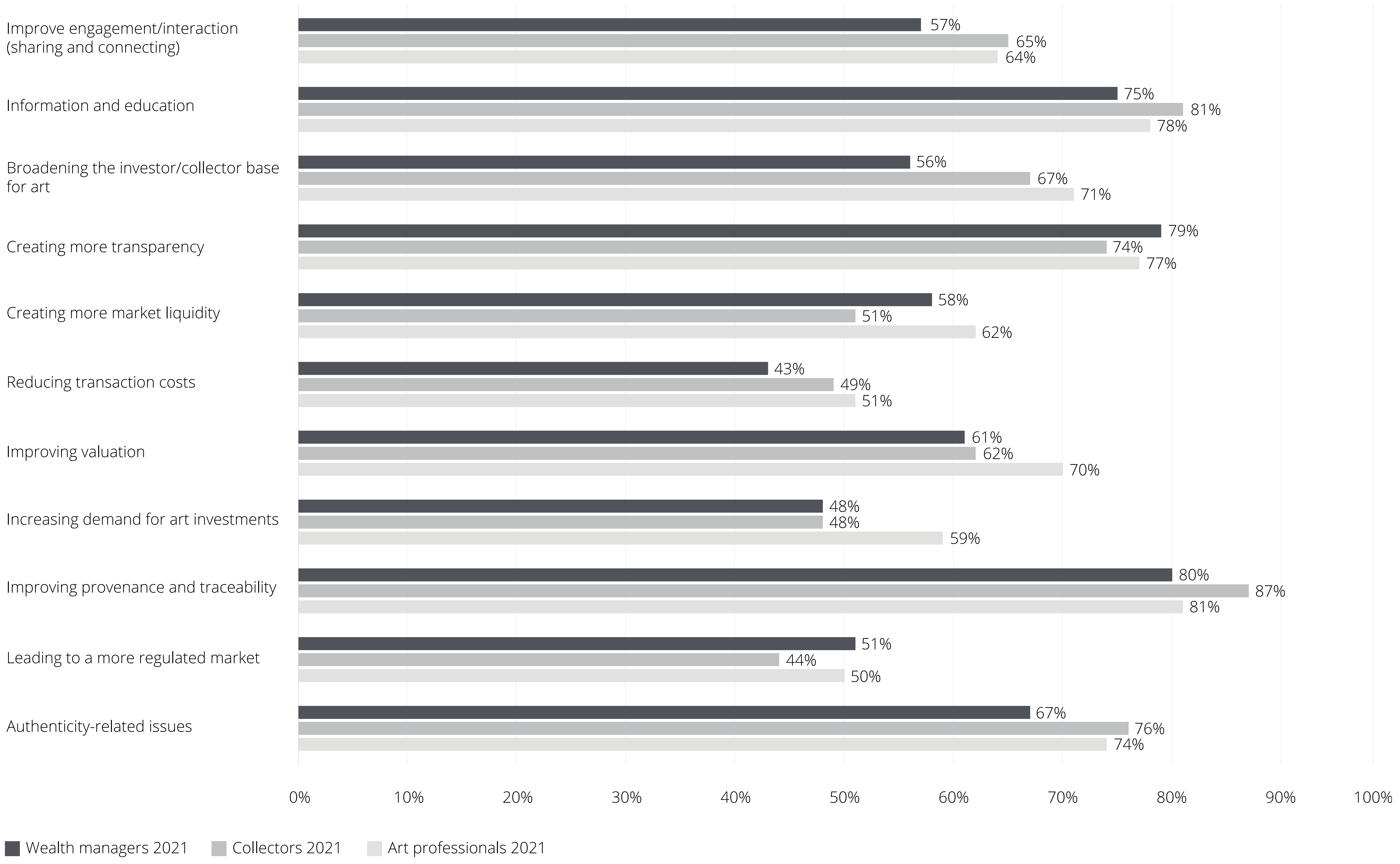
- **Big data and AI**
  With these technologies being increasingly embraced by many industries and revolutionizing existing practices, the art market is no different, adopting big data and AI to improve its valuation, pricing and authenticity processes and boost customer experiences in the art market. Of the wealth managers surveyed, 42% believe big data and AI will have a positive impact on their ability to offer art-related services; however, they are less convinced than collectors and art professionals about their applicability and impact. Both art professionals (62%) and collectors (61%) believe big data and AI will have a positive impact, viewing these new technologies as a way to standardize, scale and professionalize existing art-related services. Wealth managers' skepticism in this area could be due to a lack of trust in art market data, as big data and AI will do little to address these problems, besides potentially amplifying existing mistrust.

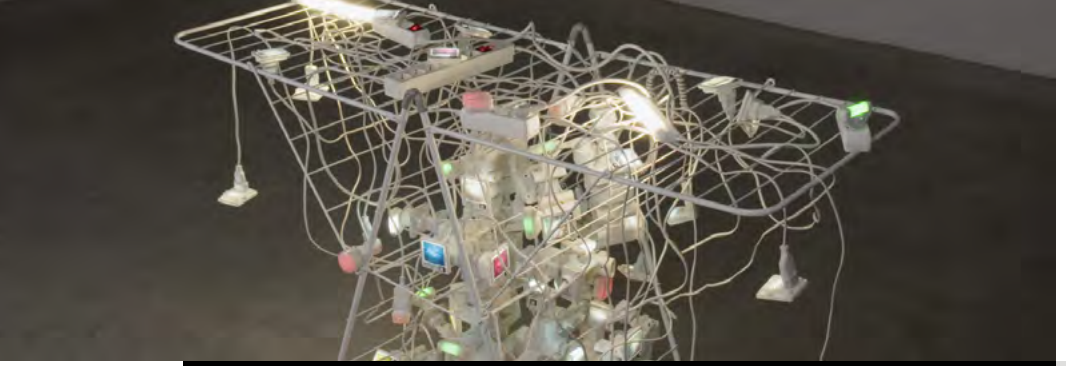


VR and AR

36% of wealth managers believe VR, AR and mixed reality could be important tools for their business in the future (compared with 18% in 2019). The COVID-19 pandemic and its related social restrictions forced the art market to embrace new and innovative ways to create client experiences and engage with corporate collections and philanthropic projects. While a return to the physical world is hopefully on the horizon, these technologies are here to stay, and could be effective client engagement tools when combined with more traditional, offline art entertainment. Nearly half (47%) of collectors and 32% of art professionals also believe AR and VR could become effective tools for wealth managers for both client engagement and their art advisory service, research, due diligence and collection management. These tools will also likely help art market stakeholders engage with younger audiences.

Figure 103. Key areas where online art businesses and new technology can make an impact





Key areas where online art businesses and new technology can make an impact

Improving provenance and traceability
80% of wealth managers believe new technologies like blockchain will improve provenance tracking and traceability (compared with 79% in 2019), with 87% of collectors and 81% of art professionals saying the same.

Authenticity
67% of wealth managers believe technology can help address issues and risks regarding authenticity (compared with 69% in 2019). DNA technology, blockchain registers and AI are some of the new technologies applied to this area of risk. Both collectors (76%) and art professionals (74%) also believe these technologies could help mitigate authenticity risks.

Information and education
75% of wealth managers said new technology and online platforms are very important in improving access to information and education about the art market (compared with 68% in 2019), with collectors (81%) and art professionals (78%) saying the same.

Creating more transparency
79% of wealth managers said the art market's move to digital has increased its transparency (compared with 76% in 2019), while 74% of collectors and 77% of art professionals also said that online businesses and technology were important in increasing transparency in the art market going forward.

Improving valuation
as the art market starts to apply big data, machine learning and AI to various aspects of art-related services, 61% of wealth managers believe these technologies would improve valuation services (compared with 58% in 2019). Both collectors (62%) and art professionals (70%) also believe that the advent of big data and AI could significantly impact how valuations are carried out today. Although some valuations at the higher end of the art market will still likely be performed by human experts, or a combination of human experts and machine learning, there is huge scope for technology in valuations at the lower end of the market, which accounts for most objects in the art market.

These services could considerably reduce the cost of insurance and valuation, while also acting as pricing and valuation tools for art buyers. They would also help wealth managers offer passive portfolio management services around art and collectibles based on their clients' risk profiles. This will likely lead to greater price transparency and, ultimately, higher confidence and trust in the art market.

In addition to valuation, new data and analytical tools can also substantially improve the way wealth managers monitor and manage risk.

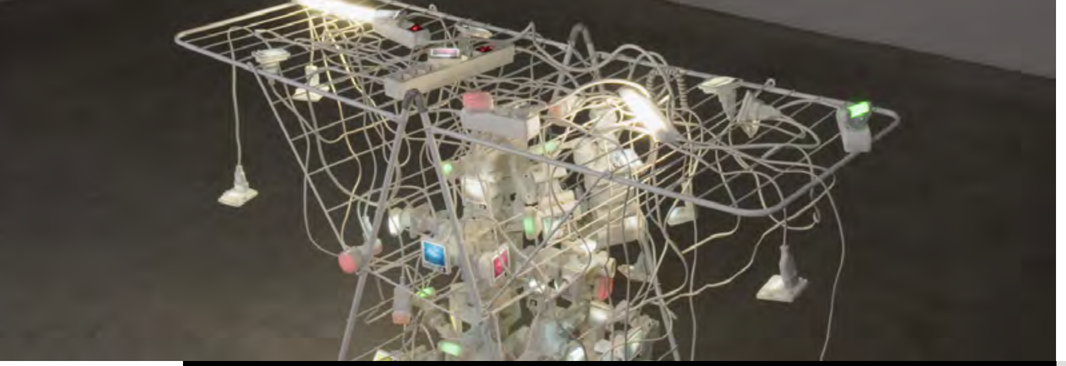
Broadening the collector base
56% of wealth managers said new technology and online platforms will likely help bring new audiences to the art market (compared with 49% in 2019). Both art collectors (67%) and art professionals (71%) also said this would expand the collector base.

Improve engagement and interest
57% of wealth managers believe online art businesses and new technologies will boost engagement and interest in art and the art market, with 64% of collectors and 67% of art professionals saying the same. As technologies like VR and AR continue to improve the online user experience, and with the wide adoption of social media to reach new audiences, the art market has opened up and created new engagement gateways for new and existing audiences.

Creating more market liquidity
58% of wealth managers said the growth of the online art market and increasing adoption of new technologies will have a positive impact on market liquidity going forward (compared with 51% in 2019), while 51% of collectors and 62% of art professionals said the same. With online sales surging during the COVID-19 pandemic, there are already strong signs that liquidity at the lower-to-medium end of the art market is increasing, allowing a broader range of buyers and investors to access the art market.

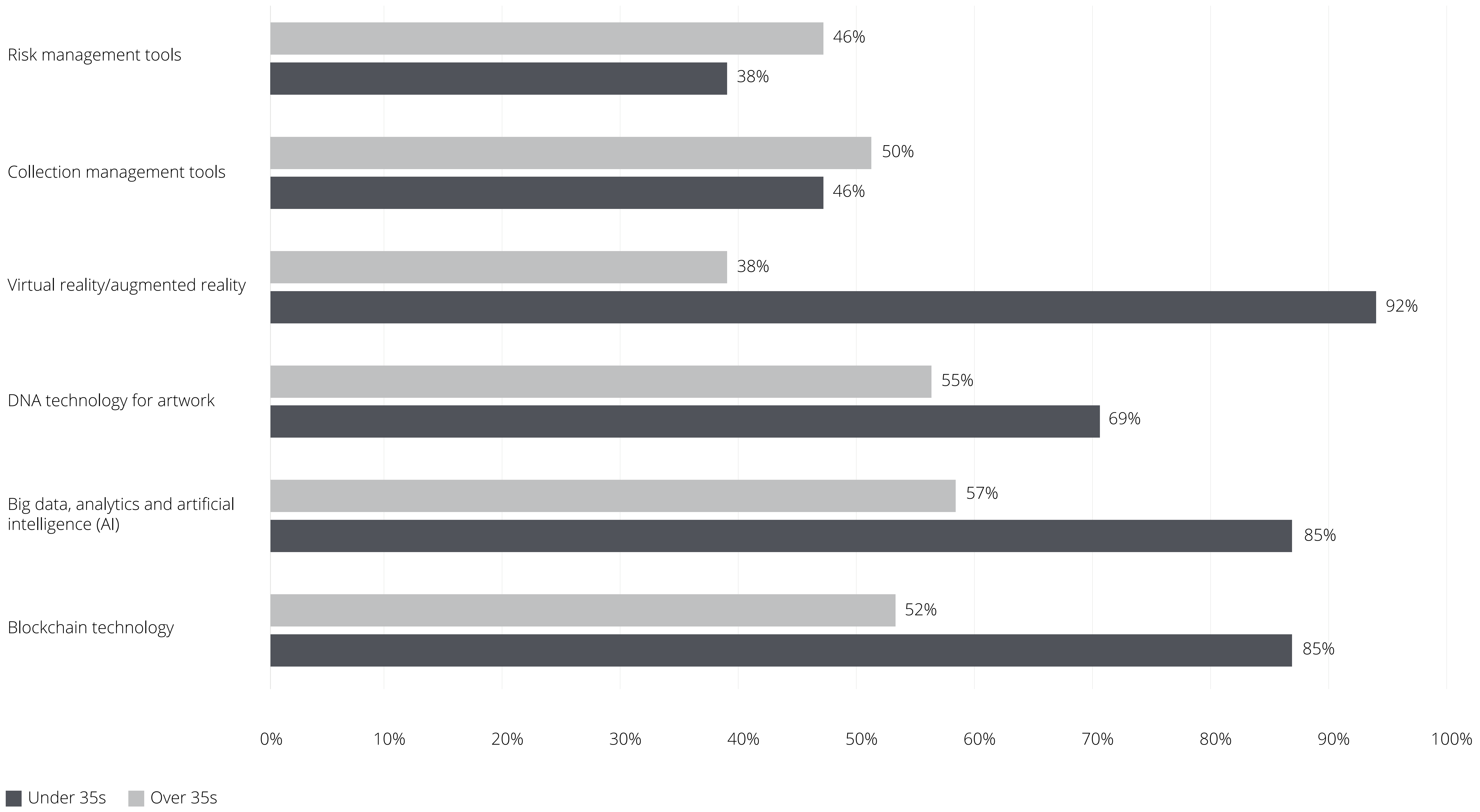
Increasing demand for art investment: almost half (48%) of wealth managers believe online art businesses and technology will increase the demand for art investment (up from 35% in 2019), with 48% of collectors and 59% of art professionals agreeing. The combination of increased data, better pricing tools, more liquidity and fewer concerns about issues such as authenticity could lead to higher demand for art investment services. Also, technology has allowed for new types of art investment products, such as fractional ownership, tokenization and NFTs, which has greatly stimulated the appetite for art investment in the last year. See Section 6 for more information on art investment.

Jean Gazançon, Arte Generali CEO, explains in his article on p.266 how new technologies can impact the art ecosystem, particularly regarding collection management, certification, authentication, provenance, and predictive systems.



NextGen Collectors—a different perspective[2]

Figure 104. NextGen collectors: which of the following technologies do you think could have the most impact on the development of art and wealth management services in the next two to three years?



2 See also NextGen collectors—a different perspective in Section 2 p.122 and Section 6 p.241.

Most younger collectors believe technology will be a major game-changer in the art and wealth management industry

Overall, younger collectors think technological development will have a large impact on the art wealth management industry over the next two to three years. The vast majority (92%) of younger collectors believe AR and VR will have a significant impact (compared with 38% of older collectors). While 85% of young collectors said blockchain technology could transform the way business is currently being conducted (compared with 52% of older collectors) and another 85% believe that big data, analytics and AI will have an impact on the art and wealth management industry going forward, significantly higher than 57% of older collectors. New advances in technology around DNA and creating unique artwork identifiers were also considered important, with 69% of younger collectors saying this would have an impact over the next two to three years (compared with 55% of older collectors).

Technology will drive more transparency and new engagement

The vast majority (92%) of younger collectors believe technology will help the art market become more transparent, compared with 70% of older collectors. Of the younger collectors surveyed this year, 85% believed increased transparency will ultimately lead to more engagement, and 92% felt it would broaden the collector base further. This indicates technology's importance as an enabler for the younger generation, and will likely become a key competitive factor for the wealth management industry in attracting a new generation of clients.

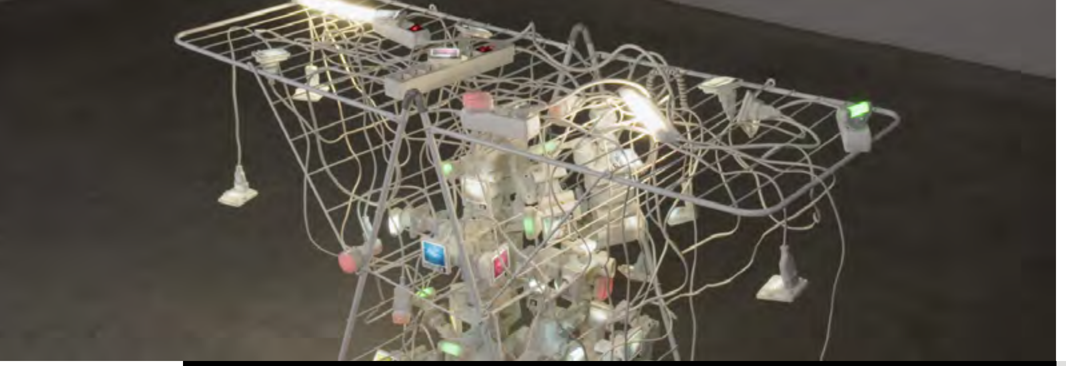
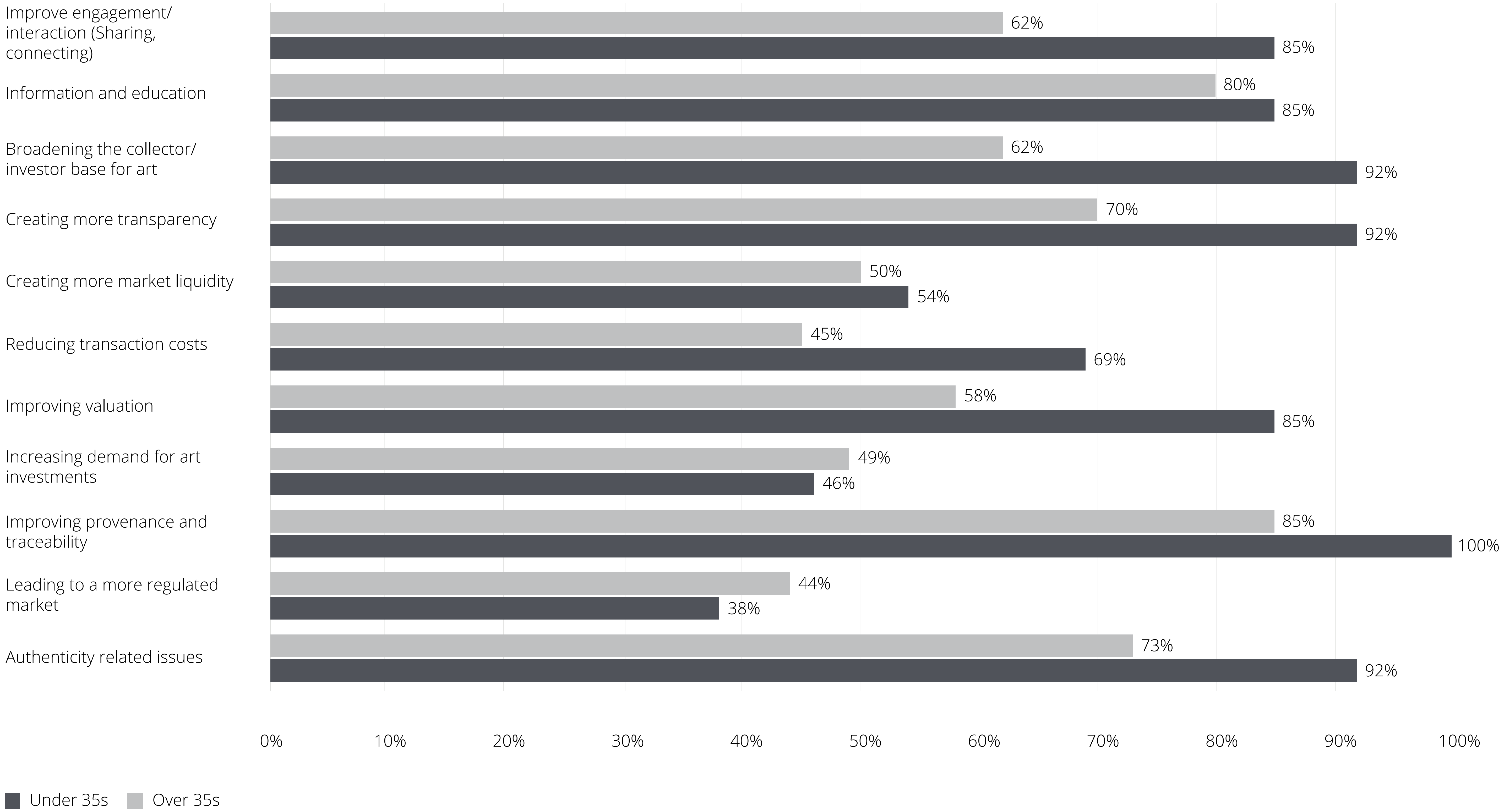
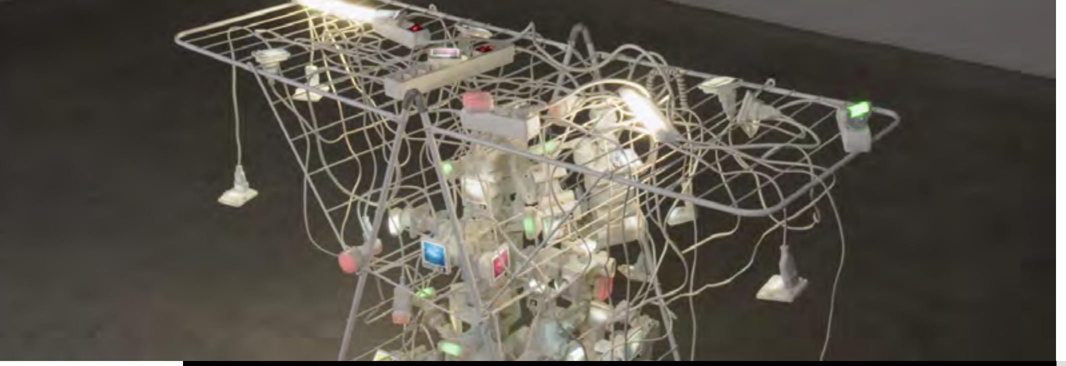


Figure 105. Key areas where online art businesses and new technology can make an impact





Jean Gazançon
CEO, ARTE Generali

Expert voices

The ArtTech phenomenon

Technology's impact on art insurance

The implementation of technological advancements in the world of art is met with hope, but also concern. Both feelings are understandable. Many players along the value chain struggle to navigate through the innovations inundating the market and fear their job will be replaced by artificial intelligence. This is why, I believe, it is key to understand technology and use it with a purpose in mind, which should be that of providing operators with tools that support, but not replace human expertise, and, ultimately, improving quality of life. Building on my experience leading an art insurer that is also a pioneer in ArtTech, I will try and dispel some of the concerns around technology applied to art.

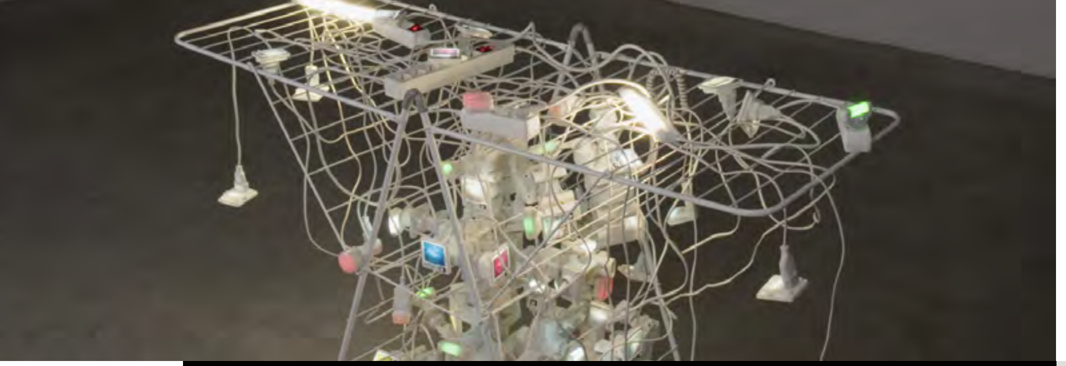
Since the introduction of connectivity, digitization, robotics, and other technologies in the industry and in our everyday life, expectations that this would result in an astonishing impact on productivity and growth have mounted—after all, this phenomenon was renamed "The fourth industrial revolution"[3]. To everyone's dismay, however, productivity and growth remained stagnant throughout the 2010s[4].

This is the paradox of technology: using it is not enough, you also need to know how to use it and why. This paradox also applies to the art ecosystem and the art insurance niche, my field of work. As innovations multiply, art market players and collectors may find themselves confused.

A quick summary of some key technologies impacting the world of art and art insurance could be helpful:

1. Collection management solutions allow collectors to digitally archive artworks with their supporting documentations, such as proof of provenance or the latest condition report;
2. Certification, authentication, and provenance tools, based on Blockchain, record, certify, and secure transactions so that they cannot be altered over time. Such tools are particularly effective when the first certifier is the artist him or herself, so that the artwork's history can be traced back to its actual origin. Non-Fungible Tokens (NFTs) can be included in this category.
3. Predictive systems, powered by AI and neural networks, assist collectors in their investment and divestment decisions based on the analysis of a vast amount of market data and—in the most sophisticated cases—of emotional and attitudinal factors.

3 Klaus Schwab, The Fourth Industrial Revolution (World Economic Forum, 2016).
4 Reuters, "Productivity stagnant despite global stimulus: WEF," October 9, 2019.



The app also offers MarketTrends, a plug-in powered by AI that compares the user's collection with millions of art market signals to provide an analysis of the value performance of an artist.

Despite the potential of these technologies, they may lead to frustrations—partly because of their complexity and the resulting information asymmetry, and partly because they are yet to bring tangible simplifications in terms of bureaucracy.

ARTE Generali has launched an app that uses these technologies to transform the frustration into happiness and peace of mind. The app gives collectors the opportunity to virtually store images and documents of their artworks as well as to receive, within a few clicks, a remote evaluation from a certified expert. After the evaluation, the art collector obtains a digital, unalterable certificate.

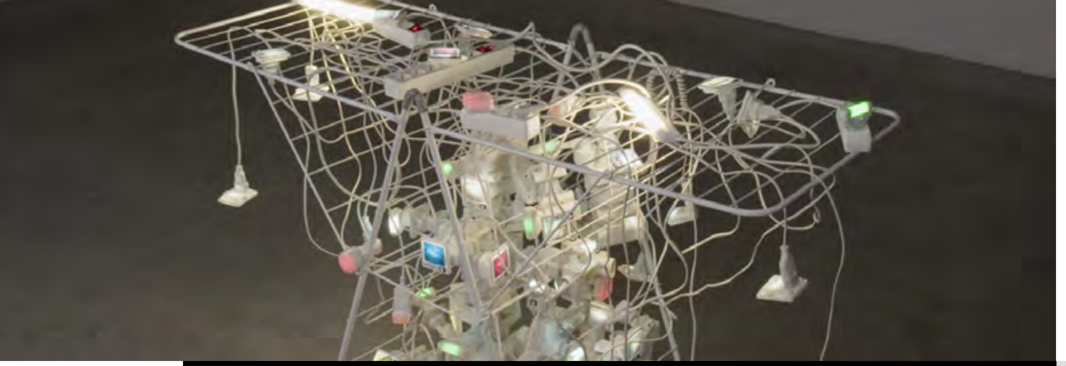
The app also offers MarketTrends, a plug-in powered by AI that compares the user's collection with millions of art market signals to provide an analysis of the value performance of an artist. MarketTrends is an example of a type of innovation that supports, but not replaces humans. This tool, developed by the Toronto-based start-up Wondeur.AI, aims to deliver quantitative data (of which the art market has been historically poor), to aid art collectors, advisers, and appraisers, whose emotions and competence remain undisputed. Such a tool is key in enhancing the management of a collection.

As art insurers, we can do our part to dissipate concerns and raise hope around technological progress—of course, always fulfilling our traditional duties of protecting and indemnifying, which remain essential. We can assist the stakeholders along the art value chain by offering better and more personalized services, and helping art lovers to enjoy the experience of collecting to the fullest.

As someone extremely passionate about art, I know how important this is. This is technology with a purpose. This is technology that improves the quality of life. This is the new humanism mentioned by Giovanni[5], whereby the technological advancement proceeds mano a mano with creativity, in all its new shapes.

- New technologies impact the art ecosystem in several ways, particularly when it comes to collection management, certification, authentication, provenance, and predictive systems;
- The ARTE Generali app exemplifies the response of art insurance to the ArtTech phenomenon; and
- Art insurance supports art market players and seeks to improve collectors' life quality (of which art is an important component), leading to a new humanism.

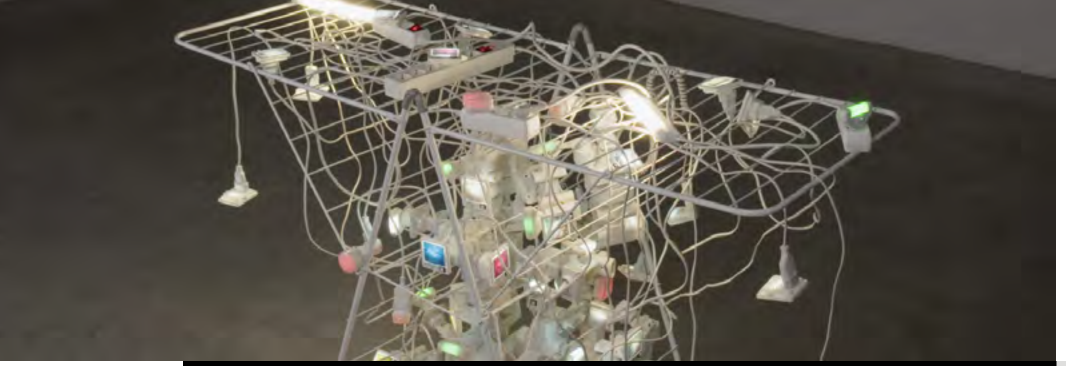
5 Article : New Humanism and Art Insurance By Giovanni Liverani



Part 2. Blockchain and tokenization

Deloitte Luxembourg explains in the article on p.269 how blockchain and tokenization can improve the way art is traded and enable new forms of ownership. Deloitte Japan in its discussion with Startbahn Inc in the article on p.273 introduces the possibility for blockchain technology to potentially serve as social infrastructure to improve the Japanese art market.

Jardim do Éden
©Jonathan Shaw/Cortesia The New Art Gallery, Walsall - 2007



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Expert voices

Art and blockchain

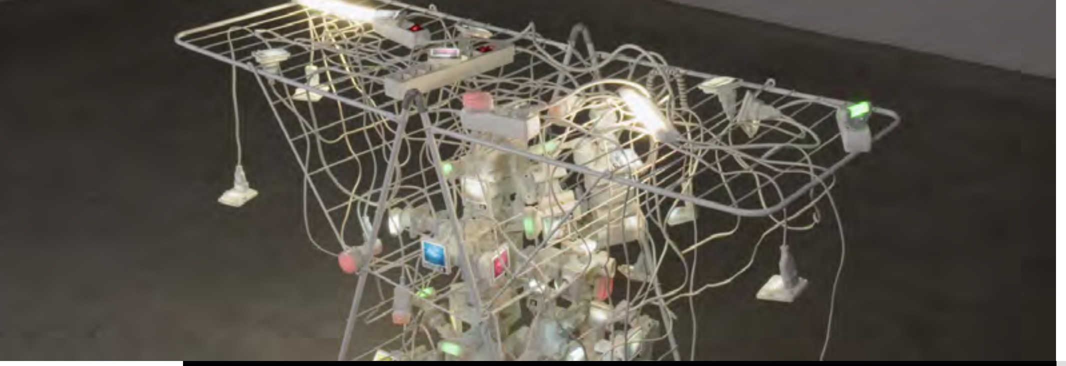
Unlocking new opportunities thanks to decentralized models

Blockchain and Distributed Ledger Technologies

In order to explain the effect of blockchain on the art world, we would have to first explain what blockchain is. In simple terms, blockchain can be explained as a database that is shared across a network of computers; it is decentralized, which means that every computer (also called "node") has an exact copy. The network does not have a central point, which means if a computer tries to corrupt the network, the other "valid" computers will prevail and the fraud will not succeed.

Similarly to blockchain, Distributed Ledger Technologies (DLTs) keep a digital record (or ledger) of an event distributed across a network of computers. Trust is enabled by cryptographic algorithms and a consensus mechanism, ensuring that the ledger can only be updated when a majority of the participants agree on the change. This makes the digital record extremely secure and transparent, as every single transaction on the network is visible in the ledger. Thus, DLTs do not require central authorities or intermediaries such as banks and notaries to authenticate and verify transaction validity. This simplifies the execution of transactions between parties, allowing them to interact directly with each other (peer-to-peer).

DLTs can be broken down into three types: public, private, and permissioned. In public networks (e.g. Bitcoin blockchain), anyone may join and create, buy or sell the currency native to the network (e.g. Bitcoin cryptocurrency). Private networks are those that can only be accessed by specific people whose identities need to be verified beforehand, and permissioned networks are a mix between the private and public networks, where governance and rules define the user roles and how they operate within the network.



Impact of blockchain on the world
With blockchain-as-a-service growing at a rate of double-digit annual percentage, we believe the future will bring a more complex, but flourishing ecosystem between blockchain and art. Deloitte appears to share this idea and realizes the potential of manifesting art through blockchain and digitalization. One the most recent projects that came from Deloitte Luxembourg's Innovation Lab is ArtTracktive, a platform that aims to solve traceability issues in art by recording interactions between all parties involved on a blockchain in processes such as lending and selling. Parties interact with the blockchain through a web application in order to record their actions from the introduction of the piece, to its certification and the notification of sell/lend, all the way to the shipping and customs clearing.

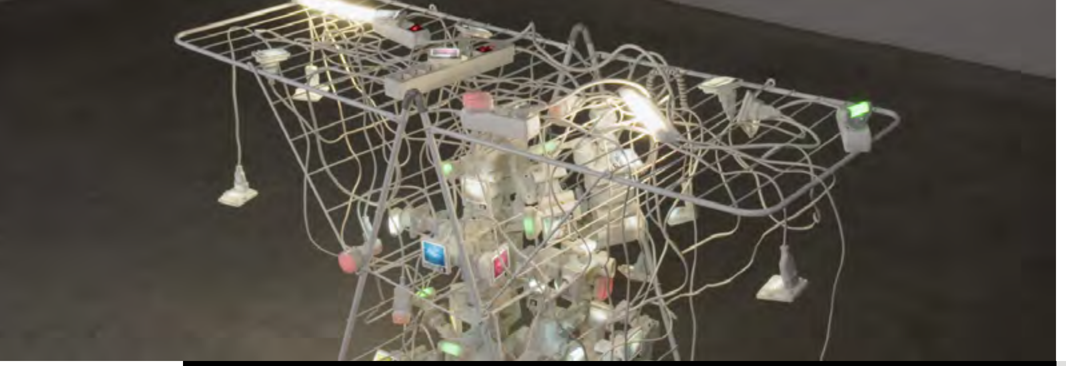
In addition to this proof-of-concept, and because the demand in the market regarding non-fungible tokens (NFTs) and trading with digital art is so high, the Innovation Lab has developed a new prototype combining existing platforms to provide a new user-centric approach. This new prototype highlights the feasibility of connecting all the members of the art ecosystem in order to create a transparent marketplace and a reliable investment platform at the same time.

One thing the future will certainly bring is an increasing number of digital art and digital artists. With more artists going digital, we will most likely see big auction houses following the example of Christie's. We expect this blockchain-art ecosystem to expand in the near future and onboard different parties as well as institutions. Due to an increasing number of cryptocurrency payments, we would not be surprised to see not only FinTech companies but also large financial institutions offering crypto wallet services as well custody services for digital assets and art.

Tokenization
DLTs outline the rules for different types of tokens . One of them is Bitcoin, which is a payment/exchange token. Others can either be utility tokens or security/equity tokens. Utility tokens are similar to vouchers in the sense that they can be redeemed to access and use a product or service provided by the token issuer. Security/equity tokens entitle the holder to equity-like benefits, such as the ownership of assets and entitlement to use them, dividend distribution (profit sharing), and voting rights. Finally, payment/exchange tokens are a means of payment for a good or service.

Table 29. Digital asset (token) categories

Security tokens	These are tokens with special characteristics which are similar to traditional instruments such as shares, debentures, or units in a collective investment scheme. *Example: Science Blockchain Token*
Utility tokens	Utility tokens seek to provide value to investors by giving them access to a future product or service. *Example: Filecoin*
Cryptocurrencies	Cryptocurrencies are the most common type of digital assets and they use cryptography for security, designed to work as a medium of exchange. *Example: Bitcoin*
Non-fungible tokens (NFTs)	An NFT certifies a digital asset as unique and can be used to represent various digital and phygital types of files.



Tokenization opportunities in the artworld

Security tokens
According to Raiffeisen Bank International1, in 10 years' time the way we currently trade securities will be gone. By 2030, most securities will be tokenized and even though Raiffeisen reports that the majority of investors are not currently asking for exposure to security tokens, they are beginning to demand a trading experience for stocks that is similar to cryptocurrencies. They want transparency, liquidity, and instant settlement. As we have seen, distributed ledger technology can solve these problems, which is why trading assets on DLTs is inevitable.

Today we can see that trading tokenized traditional stocks is becoming increasingly popular. For example, the daily trading volume on Binance and FTX of tokenized traditional stocks such as Tesla (TSLA) and Apple (AAPL) is exceeding the monthly trading volume for all security tokens on popular security token exchanges such as tZERO, MERJ, Open Finance Network, and TokenSoft. The daily trading volume for tokenized traditional stocks surpassed US$4 million in one day in early May on Binance and FTX, versus US$3.9 million for the whole month of April on tZERO, MERJ, Open Finance Network, and TokenSoft. Currently, the total security token market's capitalization is hovering around US$700 million and is expected to reach US$1 billion by 1 August 2021.

One of the main concerns with securities is the ratings attributed them. Security tokens can be rated by rating agencies in the same way that traditional securities can. Among the first security token offerings (STOs) to be granted a credit rating, was the one of Société Générale, which secured the best possible rating of Aaa/AAA from both Moody's and Fitch respectively[6].

Another opportunity that arises with tokenization comes with non-bankable assets (nBAs). These are considered to be all types of illiquid assets, often focused on the more exclusive ones. This is the case, for example, with rare pieces of art and collectibles, real estate, intellectual property, or private equity. They are significantly harder to deal with than liquid assets, such as cash or stocks, and are often not accepted by financial institutions as collateral. Tokenization, however, has the potential of transforming nBAs into liquid assets, making them accessible to a much wider audience[7].

Custody of these elements
To define custodianship, it is worth looking at it within the context of traditional capital markets. Generally speaking, custodians are institutions that provide customers with an array of financial services including the likes of trade settlement, exchange, clearing, and corporate action execution. However, one of their most notable roles is in the safekeeping of investors' assets. Custodians are like vaults, holding investors' assets in both electronic and physical form, charging investors a fee in exchange for maintaining them securely[8].

They enter into agreements with investors, whereby the asset remains temporarily in the custodian's safekeeping, subsequently being returned to the investor upon request. Custodians harness their market expertise to minimize the risk of fraud, theft, or loss to those assets. Within this framework, custodians play a vital role in facilitating the safekeeping of investor's assets and ensuring market efficiency.

Non-fungible tokens
With blockchain challenging the *status quo*, even auction houses have recognized the value of introducing blockchain and tokenization into the world of art. Auction houses offer the sale of art work in NFTs , use crypto currencies as a method of payment, and use blockchain to guarantee the proof of authenticity with artwork.

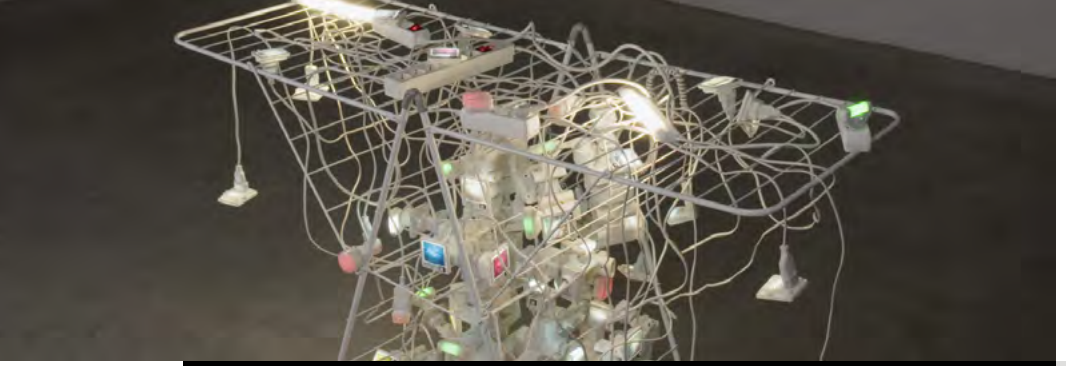
In order to better understand what a non-fungible token is, we would first need to define what is "fungibility". Fungibility is the ability of an asset to be exchanged or substituted with similar assets of the same value. Non-fungible tokens can be described as cryptocurrencies, but unlike Bitcoin, every one of them is unique and thus has a unique value. They are stored on a blockchain ledger, which contains encrypted information regarding the ownership of the asset.

Non-fungible tokens can be used, for example, to digitally represent works of art, which can then be traded easily on the DLT while keeping a digital record every time the piece changes ownership.

NFT use cases include
Digital art: Tokenizes real world artworks to promote authenticity and offer ownership to the artist;

- Fashion: Helps to digitally verify the ownership information of luxury items and accessories to reduce the risk of counterfeits;
- Sports: Offers tokenized sports game tickets issued on blockchain as well as preventing counterfeit merchandise; and
- Gaming: Allows in-game elements to be tokenized and exchanged with other peers.

6 Hays, Demelza, Gehra, Katharina, Thoma, Silvan, Liebi, Martin, McCormack, Urszula, Khurdayan, Rika, Schneider, Lee, Boehnke, Lewin, Spicher, Dominik, Smith, Marius, Völkel, Oliver, Hollmann, Bryan ,and Flury, Andy. The Security Token Report. Crypto Research Report and Cointelegraph Research. 2021
7 Bulling, Nils, Meyer, Philippe, Palm, Sebastian, Morton de Lachapelle, David,and Studer, Daniel. Non-bankable assets – investing in a new era. Avaloq, an NEC Company. 2021
8 Deloitte. A Market Overview of Custody for Digital Assets: Digital Custodian Whitepaper. 2020



The players
There is a number of involved parties in the art-blockchain ecosystem. While in the future the ecosystem will most certainly grow, we can distinguish a few key players already established:

The artist
By using different software tools, the artist creates his own digital artwork. The artist can even make a video-clip, tweet, or an audio file and convert it into an NFT. Given the fact that everyone in theory can simply download a digital artwork and own it, the artist can create an NFT from his art work, meaning that even though there can be many copies of the piece, there is only one legitimate owner (or more, depending how the NFT is structured). Therefore, the artist can sell 10 "limited print" artworks by selling 10 NFTs. The artist can also incorporate royalty fees, which would mean that with every resale of his artwork, the artist can get paid a certain amount of cryptocurrency.

The buyer:
When buying a digital art piece, the buyer purchases the work with cryptocurrencies and receives the image (or download) plus a unique proof of purchase that cannot be duplicated and proves that this person is the owner. Additionally, the buyer can also incur "gas prices", which simply translates as transaction fees—some of which can be very high.

The art auction house: Whether physical or online, art galleries usually take care of the listing of the artwork and hosts the NFT, hence charging a fee to the buyer. The most prolific example of an art auction house's presence in this arena is Christie's sale of Beeple's work—which sold for, in excess of US$69 million (the artwork is linked to the price of cryptocurrency, Ethereum and since the price of the Ethereum changes constantly, so does the price of the art work).

Museums:
See article A Token Gesture: Can Philanthropy Benefit from the Growth of Blockchain Technology? from Bernadine Brocker – Weider Section 3 on p.149.

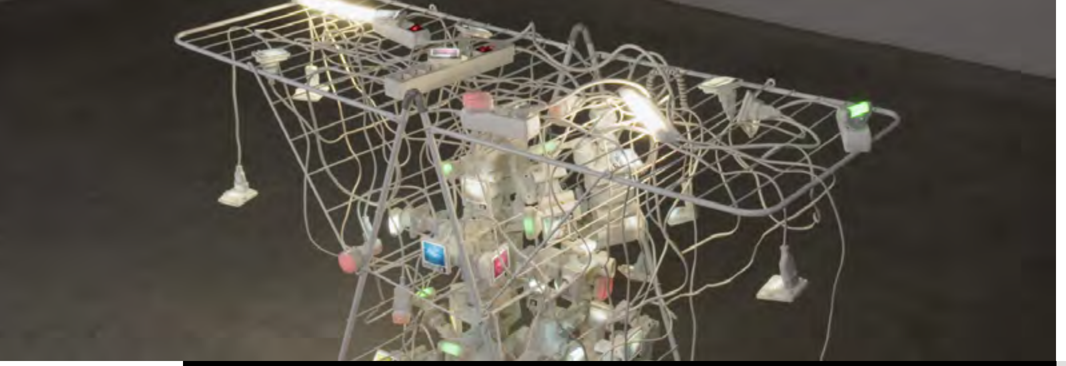
Regulatory framework and possible challenges
While the regulatory framework for digital assets is steadily developing, the regulators still have a long way to go to be able to cope with the accelerating number of FinTech companies offering innovative products and services. During the last few year there has been a number of new blockchain-related initiatives that were founded and backed by the European Commission such as Blockchain for Climate Action or European Blockchain Services Infrastructure, amongst others. The European Commission clearly states that it supports a pan-European framework and hopes to avoid legal and regulatory fragmentation. Likewise, US regulators are currently working on a cryptocurrency legislation based on a federal level to combat increasing criminal activity in terms of digital assets. In China the situation is significantly different. Activities relating to cryptoassets and cryptocurrencies are strictly regulated, many of which are forbidden. However, the country is focusing on developing the first Central Bank digital currency in the world with trial periods already ongoing in several Chinese cities[9].

Security token regulations:
- **US:** Reg. A+ is a securities law exemption that allows issuers to raise money from a crowd of retailers up to US$75 million. This allows many security tokens to be offered to professional investors, although issuers need to get their offering approved by the SEC.
- **European Union:** The European Commission adopted several legislative proposals as part of its Digital Finance Strategy. Importantly, security tokens fall under the Markets in Financial Instruments Directive II (MiFID II), and not under the Markets in Crypto Assets Regulation (MiCAR).
- **Switzerland:** The Swiss Parliament adopted the Federal Act on the Adaptation of Federal Law to Developments in Distributed Ledger Technology (the DLT bill) in September 2020, which enables security tokens to be issued on blockchains without traditional intermediaries. The bill also allows security token issuers to create secondary trading venues for their investors.
- **China:** Security tokens are currently prohibited.

Conclusion
As mentioned, DLTs can not only improve the way art is traded by keeping a secure digital record of every owner, but it can also enable new forms of ownership and introduce smaller players into the market. The co-ownership of tokenized art will establish the new standard for collectors, investors, and art galleries to increase their portfolio and investment. This will shift the paradigm of art investment and the regulations tied to them, creating a more accessible, fair, and democratized art ecosystem.

Furthermore, it can complement the rise of digital art, which faces many challenges when it comes to establishing the authorship and authenticity of a piece. Regulators around the world show a keen interest in DLTs, with the EU and US in particular seeking to avoid legal fragmentation in their own territories, thus implicitly making the adoption of DLTs much simpler than the alternative approach.

9 Clifford Chance. Non-Fungible Tokens: The Global Legal Impact. 2020.



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Kensuke Ito
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Expert voices

From monetization to sector resilience

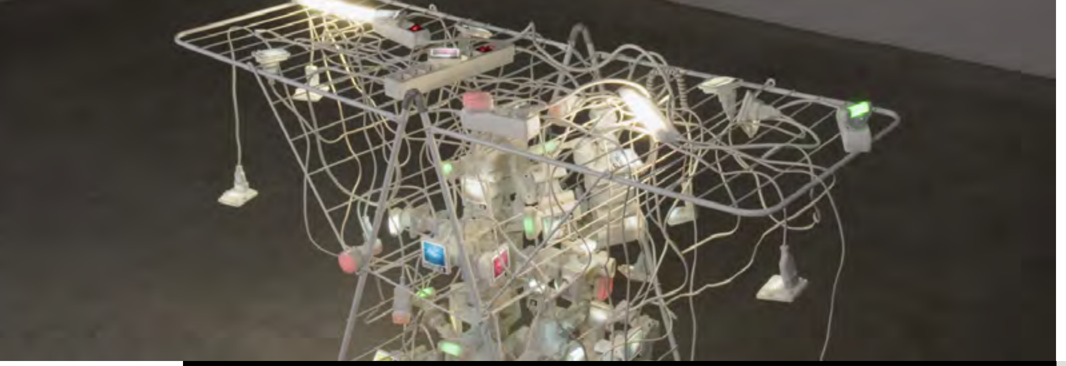
Blockchain as social infrastructure?

There is a growing recognition in Japan as to art as an asset class in response to the global uncertainties resulting from the pandemic. At the same time, impact investing and social responsibility are slowing attracting younger generations of wealthy collectors. While pre-pandemic discussions focused on monetization through art, the period of pause has led many to consider the needs of artists and sustainable growth of the market. Policymakers and creative entrepreneurs are turning their eyes to the industrial foundation for the arts and cultural sector.

However, due to the experience of loss in the late 90's, the strong perception of art as an unsafe market remains in Japan, causing decline in the number of art professionals and art-centric businesses. The lack of regulatory guidelines for money laundering through art in Japan and valuation standards cause many to hesitate embarking on the collecting journey. The market size has remained around USD $60 billion over the past 10 years[10]. Similarly, financial institutions continue to take cautionary approach to art-related services despite growing interests from wealth management clients.

The foundation of the Japanese art market has not shared the same evolutionary path as other growing Asian art hubs. In response, recent discussions have focused on enhancing cross-departmental coordination to support growth of the arts and creative industry. Current discussion spans from the introduction of resale royalty to offering support to creative enterprises with a strong focus on STEAM[11] skillset. Through such efforts, blockchain is receiving renewed focus in Japan for its potential to serve as social infrastructure for the Japanese art industry. Deloitte interviewed blockchain-based ArtTech Startbahn on leading the discussions with key stakeholders.

10 Agency of Cultural Affairs Government of Japan, Japan Art Industry Market Research Report 2020, 2020
11 An approach to learning that uses Science, Technology, Engineering, the Arts and Mathematics as access points for guiding student inquiry, dialogue and critical thinking



Josephine Yamada: A change is taking place in Japan where policymakers and art professionals are increasingly coming together to discuss how to build a sound foundation for the art market. Could you share your experience in partaking in the debate?

Taihei Shii
There is a growing interest from policymakers in positioning art at the core of growth strategy. The Cabinet Office, Ministry for Economy, Trade and Industry, Agency for Cultural Affairs, and the Municipal Government of Tokyo seem united in their desire to build resilience through the power of creativity. Though their overarching vision and focus areas have commonalities, in practice we still see historical division of departmental remits that perhaps limits the effectiveness of various initiatives. We also observe similar dichotomy among art professionals. Art businesses, critiques and academia are yet to build a mutually beneficial relationship where their expertise complement one another. Through dialogue, we would like to see businesses understanding that art, unlike other products, need long-term perspectives to blossom. Critiques and academia could also help to bridge the perceived gap between the pursuit of artistic excellence and commercial success for artists' benefits.

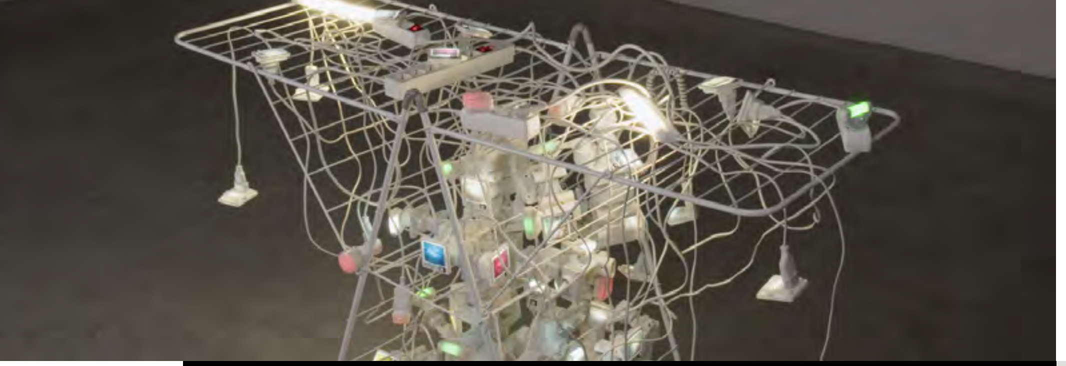
Josephine Yamada: A more expansive interpretation of the art sector has been suggested to address such dichotomy. Do you think adopting Culture and Creative Sector is a step in the right direction or do we need more concrete measures?

Taihei Shii
Expansive definition of the sector is a step in the right direction, especially when we want to foster more creative enterprises that combine artistic and technological skillsets to futureproof Japan. It's welcoming that many now turn their eyes to sectoral growth, but current debates are often skewed by expertise in specific fields and there is an urgent need for holistic understanding of the sector, its needs and possibilities to drive the debate. For example, the pandemic highlighted the urgent need to affect the commitment for supporting artists. Without an industry association or a mechanism for distributing government funding to individual artists, the rescue package could only reach cultural institutions despite the best intentions. To build such a mechanism requires a combination of expertise; clear view of the sector based on statistical information, solid planning to build consensus and technological expertise to bring ideas to shape.

Josephine: Alongside building the sound basis for sectoral growth, combatting the perception of art as unsafe market has become a priority. How has this perception impacted you as an art-centric business?

Taihei Shii
It made securing funding and partnerships challenging for us, particularly in Japan where venture capital firms have been traditionally risk averse. More recently there is a great interest in learning from overseas leading art markets and how technology can play a part in making the market safer. With this we see gradual increase in willingness to invest especially from top management, but the perception is certainly a limiting factor for many businesses especially in the financial sector.

The Cabinet Office, Ministry for Economy, Trade and Industry, Agency for Cultural Affairs, and the Municipal Government of Tokyo seem united in their desire to build resilience through the power of creativity.



We are seeking to raise awareness of the benefits to tracing provenance after sale.

As for other market participants, we are seeing mix results in demand for increased transparency. Artists are by far the largest user group (46.1%) of our blockchain-based registration system Startrail, followed by galleries (23.7%) and E-Commerce (7.9%). Collectors at 6.6% reveal their hesitation to storing information on blockchain in the fear of losing anonymity. Though we observe more welcoming attitude among younger generations of collectors, galleries are cautious in alienating clients through adoption as a result. We are seeking to raise awareness of the benefits to tracing provenance after sale. Galleries can track price appreciation after solid provenance and use this as a basis for determining prices at primary sales to earn collectors' confidence. For now, limiting the scope of information commonly shared or building a system dedicated to valuation specialists may offer a step forward to increased transparency and professionalism without compromising different user needs. Perhaps more so than increased transparency, enabling resale royalty represents the most attractive feature of blockchain in the current Japanese market in the absence of a statutory regime.

Josephine Yamada: In raising professionalism in the market, the wealth management community has a significant scope to contribute. Despite growing interests in offering art and collectibles services, what are the main hurdles for Japanese FSIs?

Taihei Shii
The art market for many in the financial sector is synonym to risks and uncertainty. This makes it challenging to secure internal consensus around service development, but the need to respond to client demands is pushing them to study how collectibles wealth management services are structured and delivered in more mature markets overseas. Private banks are seeking to identify reliable art experts to partner with, but specialized art advisory firms are difficult to find domestically. Family offices are still limited in number, but generational transfer of wealth is necessitating them to expand their focus to art, technology and philanthropy as younger clients seek fresh perspectives and global insights from their trusted advisors.

While much of the focus now is on localising overseas practices, FSIs have a key role to play in increasingly technologically driven landscape. For example, securities firms can leverage their expertise in structuring safe NFT art and trust banks will be crucial as digital assets become integral part of clients' wealth. More active participation from the wealth management community would be certainly welcomed.

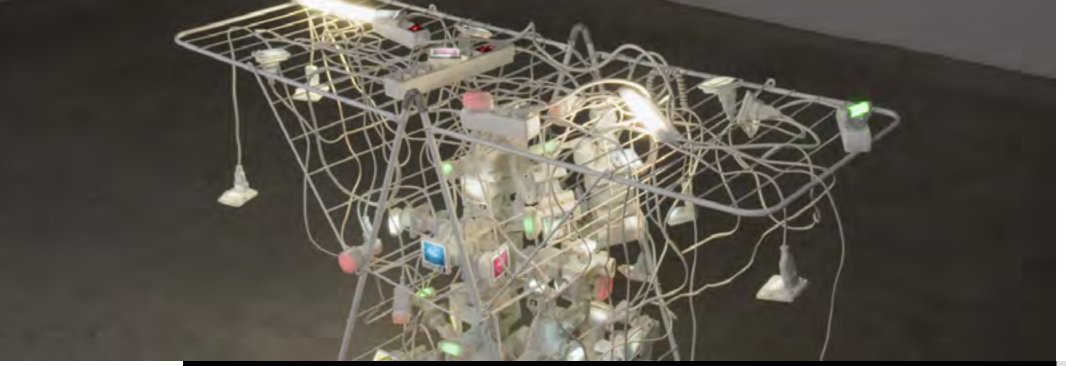
Josephine Yamada: While their motivations differ, different stakeholders from policymakers to FSIs and collectors are certainly united in their interests in blockchain technology. Are there any unresolved issues you are seeking to address?

Kensuke Ito
Reliability of data is of paramount importance to the success of blockchain-based platforms. There is a constant effort to arrive at best practices around ensuring the accuracy of input and addressing misalignment between the ownership of physical artwork and information stored on blockchain. Whether limiting entry to licensed users or linking them with off-chain storage, a careful balancing act is required to maintain the spirit of decentralization while holding participants accountable to the accuracy of information. At present we require our users to have their personal information linked to their Ethereum address via a KYC certification.

Interoperability between different blockchain project is another area we focus on. Especially for NFTs marketplaces, where rules around resale royalty payment are not standardised. While most of the current activities in the NFT sphere are in the primary market[12], ensuring smooth carryover of contractual agreements will become important as they move on to subsequent sales. Since facilitating royalty payment is one of the most urgent concerns in Japan, we released Startrail PEG free of charge to NFT marketplaces and infrastructure firms to provide a way to extend the original token contract without requiring changes or upgrades[13].

The pandemic necessitated a refocus from monetization to sector resilience, highlighting the need for uniting stakeholders including the wealth management community towards increased professionalization. As policymakers debate introducing resale royalty, régime des salariés intermittents du spectacle or 1% for arts, blockchain technology is gaining refocus for their potential to serve as social infrastructure.

12 Anders Petterson and James Cocksey, NFT Art Market Report, ArtTactic, 2021, p.10
13 Tomohiro Nakamura, "Overview and technical introduction of Startrail and Startbahn Cert.", Medium, 2021



Part 3. Data and technology ecosystem

"Collaboration between the owners and operators of emerging technologies and existing market stakeholders could revolutionize not only the way that the art world functions but, equally importantly, also how it is perceived by people less familiar with its workings and have built their views from the outside looking in. This would attract and reinforce the industry's bonds with a new generation, raise standards across the board, improve the market's reputation via transparency and social responsibility and, ultimately, usher a lot more liquidity into the marketplace." **Chris Bentley's article shares his views on the** real revolution gently fomenting in the art market's infrastructure that is generating more efficiency on p.277.

The art technology industry is maturing: the art and technology ecosystem has attracted more specialized players recently, who aim to address the various friction points faced by the art and finance industry. The digital transformation that is sweeping the art market is likely to drive more efficiency and growth.

Collaboration between the owners and operators of emerging technologies and existing market stakeholders could revolutionize not only the way that the art world functions but, equally importantly, also how it is perceived by people less familiar with its workings and have built their views from the outside looking in...

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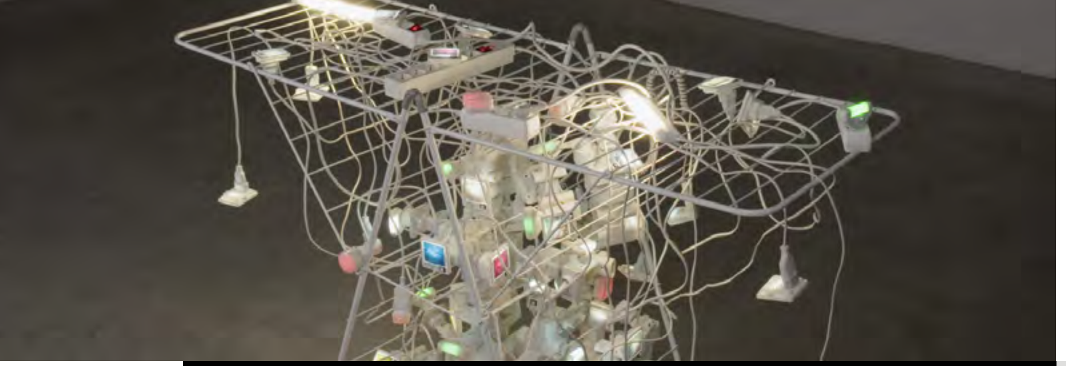


Chris Bentley
Head of Fine Art & Specie,
UK & Lloyd's, AXA XL

Expert voices

Cultural revolution

Art's emerging digital ecosystem

Despite the art world's longstanding resistance to the wholesale adoption of technology, the COVID-19 pandemic forced much of the art market to embrace the most well-known technological innovations of the last decade or two. However, over the last few years, a growing number and diversity of technology-driven start-ups had already begun to make incremental inroads into the centuries-old systems that govern the marketplace.

Are these changes beginning to accelerate, and will COVID-19's impact continue to hasten change? As evolving companies grow in relevance and confidence, are they creating truly new opportunities, or simply rehashing what we already had? Why is change in the art market so slow compared with other industries, with so few useful ideas and products gaining commercially viable traction? Forget non-fungible tokens for a second (if you can)—maybe the real revolution brewing is the one that has been gently fomenting in the art market's infrastructure instead?

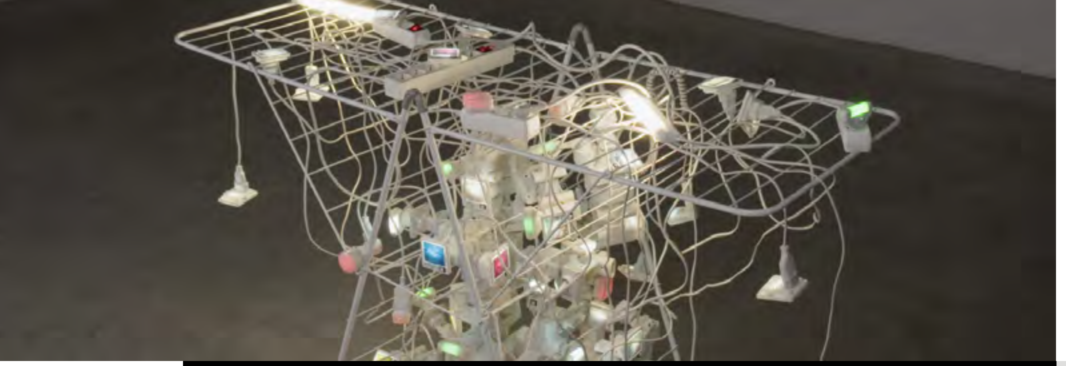
Similar to many industries, those making a living from their connoisseurship are more than ever aware that they will need to adapt significantly over the coming months and years. It will not be long before artificial intelligence (AI), already in the early stages of development, will be able to value and authenticate artworks better than a human can[14].

The technology used to identify fakes and forgeries also continues to advance, in an inexorable arms race with ever-more sophisticated forgers. Add to this the many "fingerprinting" technologies in development around the world, which would allow due diligence records (e.g., provenance information) in the cloud or on a distributed ledger to be irrevocably attached to a physical artwork.

It seems unlikely that the traditional art specialist will be the sole keeper of the keys for much longer, which is extremely relevant given that issues like attribution, provenance and authenticity are often areas of major contention. This development will help generate greater efficiency in a market that has always relied heavily on agents and middlepersons. It will also democratize the art market's parallel service industries in ways that suit both consumers (in providing access they may not otherwise have had) and suppliers (in ensuring they can access the best and most appropriate jobs without unnecessary friction).

So, perhaps what may first appear as a threat to the status quo could be the best way of preserving what should be preserved—cultural objects, and a global market with a strong reputation built on well-founded confidence and increasing transparency. The art market has had its fair share of scandals over many decades. So, is this not an opportunity to throw off these shackles and remove, once and for all, what could be viewed as the single largest barrier to its continued growth?

14 Joanna Chi, "Pricing My Art... With AI?," Medium, 26 September 2020



In addition to the previously mentioned activities, it should not be long, for example, before the technology-based businesses entering the art market can prevent the illegal export of artworks and impede the fencing of stolen works. Artwork owners and custodians should also be able to proactively manage risk in the future; for example, by routinely identifying the need for pre-emptive conservation, or improving logistics chains by analyzing data to identify weaknesses in routes and processes. Many such developments feed into another topic that has risen in people's consciousness over recent years—sustainability in the art world, particularly the air miles clocked up by some and the resulting carbon footprint.

As well as strengthening the confidence of collectors, dealers and institutions to safely buy, lend and borrow artworks, these developments can, if properly grasped and embraced, attract further institutional investment at a time when capital inflow in the art world has noticeably slowed down. Surely this is the ultimate reward, even for players who may be forced to make (temporary) sacrifices?

If most of these new business models are successfully implemented, then perhaps collectors and registrars will in the future be able to access a fully functional dashboard, allowing them to arrange to revalue, insure, transport and exhibit the same artwork with a few clicks, regardless of their location. Although these dashboards could be difficult to build due to the collaboration required, this innovation may attract a significant new generation of art market participants of all stripes, from the young hobbyist collector to the largest institutional investor[15].

Perhaps the most important barrier to such widespread adoption of these technologies is simply a practical one—that these "nodes" are being developed without a central system to which the emerging technologies can attach.

And if this is the most significant barrier, data security concerns must come in a close second and require more effort to overcome. Even if the data can be secured with sufficient protection and regular reviews, some still prefer quill, ink and landlines over smartphones and cyberspace for their perceived reliability and greater privacy. Such people will have far to travel psychologically before they can feel comfortable with an art market whose business is conducted substantially online.

In the end, I suspect that even the most committed traditionalists and those with the biggest concerns (reasonable ones, I may add) can come around with the proper engagement and reassurance—especially with the strong incentive of straightforward access to these useful and relevant innovations.

This pandemic, which has affected everyone's lives so deeply has, in my view, undoubtedly accelerated technological change in the art world. It does feel as if a tipping point has been reached at last. Many of the chief barriers that blocked this evolution appear to be disappearing, or that the spell has been broken at least. And even if the art-tech companies that have sprung up or risen in prominence over the last 18 months are largely solving old problems in new ways, this does not mean that they will not bring considerable added value to the art world—far from it.

In short, increasing collaboration between the owners and operators of these emerging technologies and existing market stakeholders could revolutionize not only the way that the art world functions, but, equally importantly, also how it is perceived by people less familiar with its workings and have built their views from the outside looking in.

This would attract and reinforce the industry's bonds with a new generation, raise standards across the board, improve the market's reputation via transparency and social responsibility and, ultimately, usher much more liquidity into the marketplace. Given how valuable these goals are to almost all art market stakeholders, it seems only a matter of time before this vision of the future is upon us.

Perhaps the most important barrier to such widespread adoption of these technologies is simply a practical one—that these "nodes" are being developed without a central system to which the emerging technologies can attach.

15 Scott Reyburn, "As the Art World Goes Online, a Generation Gap Opens," The New York Times, 8 June 2020

Risk Management & Regulation

08

Passerelle
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Highlights

The art market in need of rapid modernization
after 10 years of analysis, it is disconcerting that most stakeholders surveyed this year believe the art market's business processes still need modernizing, despite the acceleration of digital transformation, the growing role of technology and the increasing adoption of online markets. Although there are signs that certain problem areas are being addressed, some challenges remain. Lack of transparency, fear of price manipulation and anti-competitive behavior still linger among wealth managers' biggest concerns, alongside specific risks regarding authenticity and lack of provenance.

More government regulation may be required
although self-regulation remains the art market's preferred approach to establish trust and credibility, it is unsurprising that more art market shareholders believe increased government regulation may now be required, as self-regulation has proven less effective. Significantly more collectors (47%) indicated their preference for government regulation this year, up from 22% in 2019, with 36% of art professionals saying the same (compared with 28% in 2019). And, 44% of wealth managers this year believe government regulation would help restore trust in the art market (only slightly below 46% in 2019).

Most wealth managers and art market stakeholders see transparency and regulation increasing in the art market in the next five years
one ray of hope is that 67% of wealth managers expect the art market to become more transparent and regulated over the next five years, compared with 55% of collectors and 67% of art professionals who said the same. Younger collectors seem less convinced of the speed of change, with 50% saying it will take more than five years and 7% saying that regulation and transparency are unlikely to happen at all.

Wealth managers could play a key role in creating a more trustworthy art market: what role can wealth managers play in developing more transparency and creating an appropriate legal and regulatory framework around art and collectibles? Involving this stakeholder group from the outset will allow them to shape the future of the art and finance industry together with other art market players. Without wealth managers' valuable input, this process could take even longer.

Transparency is the key to unlocking future growth in the art and finance industry and art market as a whole
83% of wealth managers said lack of transparency was a key factor that undermined trust in the art market (compared with 77% in 2019). Both art collectors (74%) and art professionals (79%) also identified this as a major challenge. Transparency concerns ranked even higher among younger collectors, with 86% saying this was one of the top challenges in today's art market.

New transparency requirements for offshore entities
new tax and anti-money laundering (AML) laws and regulations to improve transparency will affect collectors using offshore entities to buy, sell and hold art. Even if there are legitimate reasons for setting up an offshore entity, it is increasingly difficult to find banks willing to onboard these types of entities because they are flagged as a higher risk than normal, especially regarding AML, FATCA/CRS, and DAC6/MDR rules.

Money laundering remains a key concern despite new regulations
68% of wealth managers remain concerned about money laundering risks in the art market (down from 76% in 2019). The recent introduction of AML regulations in the European Union and the United States seems to have stemmed some wealth managers' fears. Both art collectors (65%) and art professionals (63%) continue to see money laundering as a great threat to the art market's reputation going forward (compared with 59% and 65% respectively in 2019). The United Nations Office on Drugs and Crime estimated that GBP2.3 billion of the global art market could be linked to money laundering or other financial crimes annually.[1]

Building trust in art market data paramount for further development of the art and finance industry going forward
the importance of trust in art market data is also essential for the future development of the art and finance industry, as it is the foundation of a robust valuation and risk management infrastructure around art and collectibles. However, trust in art market data remains low, particularly among wealth managers; therefore, this is an area that must be addressed. As all industries move towards an increasingly data-driven business model, it is critical that the art market does not fall behind. Reducing information asymmetries and boosting transparency are critical to support the sector's growth and aid the onboarding of new collectors.

1 HM Treasury, National risk assessment of money laundering and terrorist financing 2020, December 2020, p.141.

Introduction

The risk management and regulation of art and collectibles transactions and ownership have grown in importance since our last survey in 2019. With new AML regulations coming into force in the United Kingdom, the European Union and the United States in the past two years, transitioning to this new regulatory environment presents new challenges and opportunities for the art market.

This section is divided into the following parts:

1. **Survey findings 2021**
   here, we explore what art and finance stakeholders (wealth managers, art professionals and collectors) view as the biggest threats to the art market's reputation this year, and how regulation and risk management can mitigate these risks.
2. **Regulation—a focus on AML effort**
   this section features specialist contributions from Deloitte US, Deloitte Germany and Deloitte Luxembourg, as well as Bonhams.
3. **Risk management, legal and regulatory developments**
   here, we explore the rapidly evolving legal and regulatory environment around art and collectibles, including the emergence of digital collectibles (such as non-fungible tokens, or NFTs), with contributions from Deloitte Italy and Megan Noh, Co-chair of Pryor Cashman LLP's Art Law Group.

Despite the intensifying debate on the need to modernize the art market's business practices in recent years, very limited progress has been made so far. While the digital transformation of the art market has accelerated, including the growing role of technology and online markets covered in Section 7 of this report, most wealth managers, collectors and art professionals believe the art market's business practices still need updating.

Lack of transparency, fear of price manipulation and anti-competitive behavior still linger among wealth managers' biggest concerns, alongside specific risks associated with authenticity and lack of provenance. In this year's report, 83% of art professionals said the art market must continue modernizing its business practices (up from 80% in 2019 and 74% in 2017), indicating they believe the art market still has some way to go before it is fit for purpose. Most collectors (75%) and wealth managers (69%) also believe there is room for further modernization.

83% of art professionals said the art market must continue modernizing its business practices.

Volupta
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In this year's risk management and regulation section, we focus on the new transparency requirements in the European Union; legal issues concerning the digitalization of art collections and the use of new technologies; consignor protections; updates on AML regulations; and the legal aspects associated with NFTs.

Pascal Noel (Director, Deloitte Monaco), takes a closer look at the new transparency requirements for offshore entities. This is a follow-up and update to his article in the last edition of the Art & Finance Report 2019 as well as his contributions on this topic in the Art & Finance conferences in 2019 and 2020. The message is clear, investors using offshore entities, should anticipate change and seek professional advice on this ever-evolving subject.

In this year's report, 83% of art professionals said the art market must continue modernizing its business practices (up from 80% in 2019 and 74% in 2017), indicating they believe the art market still has some way to go before it is fit for purpose.

Vista Interior
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Pascal Noël
Director, Deloitte Monaco

Expert voices

Transparency in the art market

Are exchanges of information improving the situation?

During the last Art and Finance Conference—held remotely of course—there were interesting debates on the new tax and anti-money laundering laws and regulations aimed at improving transparency and the contributions to national budget that were severely impacted by the COVID-19 pandemic. These new transparency rules should allow tax authorities—and indeed, the general public— better access to financial and beneficial ownership information. But how effective are these new laws? Will they in fact prevent the setup or the use of offshore entities, which are appreciated for the confidentiality they offer when acquiring art pieces?

Offshore entities used in the art market are traditionally located in jurisdictions that are not imposing income tax or indirect taxes; that do not require local presence, but only a local representative; that provide some kind of anonymity to its beneficial owners; and that provides flexibility to move the assets outside the country without any formality. If collecting is mainly driven by passion, changes in regulation could affect the way those collections are held and/or structured.

The main regulatory changes collectors and their trusted advisors should monitor:

- **A new international environment**
  Political changes in the US have allowed reactivating a multilateral approach to tackle harmful tax competition. The recent political agreement impacting the taxation of multinational groups (MNCs) with the adoption of a minimum tax rate of 15%, may force many low tax jurisdictions to review their laws if they want to remain attractive.
- **The substance of companies is becoming a must**
  Since 2019, complying with OECD substance requirements has forced 12 jurisdictions applying no or nominal income tax to significantly increase the substance level of local entities involved in activities such as distribution, financing, holding, shipping, fund management, headquarters etc. These jurisdictions (including the BVIs, Cayman, Bahamas, and the Channel Islands) entered this year in the second phase of the regulation and they need to check that the level of substance of local entities by the end of 2020 was sufficient. If not, they must inform the country of the direct shareholder, ultimate parent entity, or ultimate beneficial owners (UBOs) of the lack of local substance. Countries receiving this information will, in turn, potentially tax those entities, considering they are effectively managed in their jurisdiction. It is too early to judge the effectiveness of this approach, but the EU commission is already considering adopting similar minimum substance rules in a Directive applicable to all EU Member States. Countries like the Netherlands, Luxembourg, Ireland, Cyprus, and Malta will probably be the most affected by such a Directive.
- **Public reporting**
  The EU and the US are trying to restrict the use of offshore entities by MNCs, by providing the public with information that was, since 2016, only shared between tax authorities. Public country-by-country reporting will need to be introduced and will need to identify in which jurisdictions MNCs are implemented and the level of substance they maintained. The report will also inform, by jurisdiction, about the effective tax rate of the various group entities. However, the effective date of implementation of such rules still needs to be confirmed.

- **Register of beneficial owners**
  International transparency rules do not only require that the information on UBOs be made available to local authorities to facilitate the fight against money laundering or tax evasion. Information on UBOs should also be made available to the public, usually at the level of a register of beneficial owners. In 2020, more than 80 jurisdictions had laws in place requiring the identification of UBOs, but public access to this information is generally not possible in most non-EU countries. Many countries restrict the access to the register to persons justifying the reasons for accessing the information, like professionals subject to AML laws. UK overseas territories (such as the BVIs, Cayman, Bermuda, Anguilla, Gibraltar, Turks and Caicos….) and UK Crown dependencies (Jersey, Guernsey, Isle of Man) also committed to the implementation of a public register, but only as from 2024 onwards.

  - **Blacklisting process**
    Countries refusing to adopt international standards take the risk of being blacklisted by the Financial Action Task Force (FATF), the OECD, or the EU. The criteria used by the EU for blacklisting countries include:

  - The results of the OECD Peer Reviews regarding transparency and exchange of information (minimum rating required "largely compliant"); and

- Application of the OECD BEPS minimum standards, the absence of preferential tax regimes, or the signature of the Multilateral Convention on Administrative Assistance (MCAA). 9 countries are currently listed, including Panama. This list is updated twice a year and may soon integrate new members, because of the upcoming OECD Peer reviews, or following the request of the EU Parliament to include EU countries in the review process.

- **Extension of exchange of information**
  The automatic exchange of information between tax authorities on a multilateral basis is the new standard. At OECD level, Mandatory Disclosure Rules (MDR) is the new instrument used to exchange information reported by intermediaries (tax advisers, lawyers, company service providers, banks, etc.) on potential abuses in the disclosure of financial accounts held abroad or on arrangements aimed at creating a non-transparent beneficial ownership chain.

In the EU, MDR is replaced by DAC 6, the Directive on administrative cooperation, which in addition covers the disclosure of all aggressive tax structures. Due to the COVID-19 crisis, the initial reporting by advisers was postponed from July 2020 to January 2021 in most EU jurisdictions, with exchanges between Member States beginning in April 2021. Following Brexit, UK and Gibraltar have moved from DAC 6 to MDR reporting, a model already adopted by the Channel Islands and Mexico. The OECD is pushing for the adoption of MDR by all non-EU countries applying the Common Reporting Standard (CRS) for the reporting of financial accounts.

- **Effectiveness of the CRS**
  CRS is probably the standard which is the most impacted by new measures aiming to ensure that the participating countries (111 in June 2021) have identified all their reporting financial institutions (FI), have controlled the application of due diligence on clients and UBOs, and have properly identified all reportable accounts. In 2020, the OECD started its review of the effectiveness of CRS implementation, making recommendations that need to be followed by the jurisdiction wanting to avoid a bad rating. All CRS jurisdictions will need to use a risk-based approach in order to identify the local FI at risk that should be subject to an audit of their procedures and of their documentation. The results of the Peer Reviews should be published by the OECD in 2022.

- **Tax identification numbers (TIN)**
  In most countries, FIs are also acting as agent of the US tax authorities (IRS) in application of the FATCA regulations and of the agreements reached between their country of residence and the US (IGA). Under the IGA, local tax authorities have the responsibility to ensure that local FI have properly implemented FATCA and have identified their US accounts and recalcitrant account holders. FATCA audits will generally be performed at the same time than CRS audits. FIs failing to provide the TIN of their US clients are now at risk of losing their FATCA registration. The consequence is the application of a punitive withholding tax (30%) on US source income derived by their clients, associated with a significant reputational risk.

Even if there are many legitimate reasons justifying the setup of an offshore entity, it is proving more and more difficult to find banks that are ready to onboard these types of entities, which are flagged as presenting a higher risk than normal, especially regarding the application of AML, FATCA/CRS, or DAC6/ MDR rules.

Investors using such entities should anticipate that:

1. The confidentiality provided by offshore entities will disappear over the coming years with the development of public register of UBOs;
2. The need for substance and the costs associated with the management of the entities will significantly increase;
3. The need to provide FIs with justification regarding tax residency, and TINs of the entity and of its beneficial owners, anticipating the reinforcement of compliance measures that FIs must implement in all CRS-participating countries; and
4. The exchange of information between authorities will become more and more effective, and that the jurisdictions that were not always ready to absorb and use the huge quantity of data provided by the other CRS-participating countries, are now improving.

In light of these developments, art owners should consult their advisers to anticipate the potential impact of new rules on their individual situation. They should also appoint a Trust or company service provider who understands the new environment and are ready to provide the additional compliance services.

In addition to the opportunities offered by these new technologies, recent transparency rules, and the additional updated regulations, these could also be the keys to gain the attraction from an increased number of financial advisors and fresh clients that the art market is looking for.

Part 1. Survey findings 2021

Key threats to the reputation of the art market

Figure 106. Wealth managers: which of the following issues do you feel are the most threatening/damaging to the reputation of the art market?
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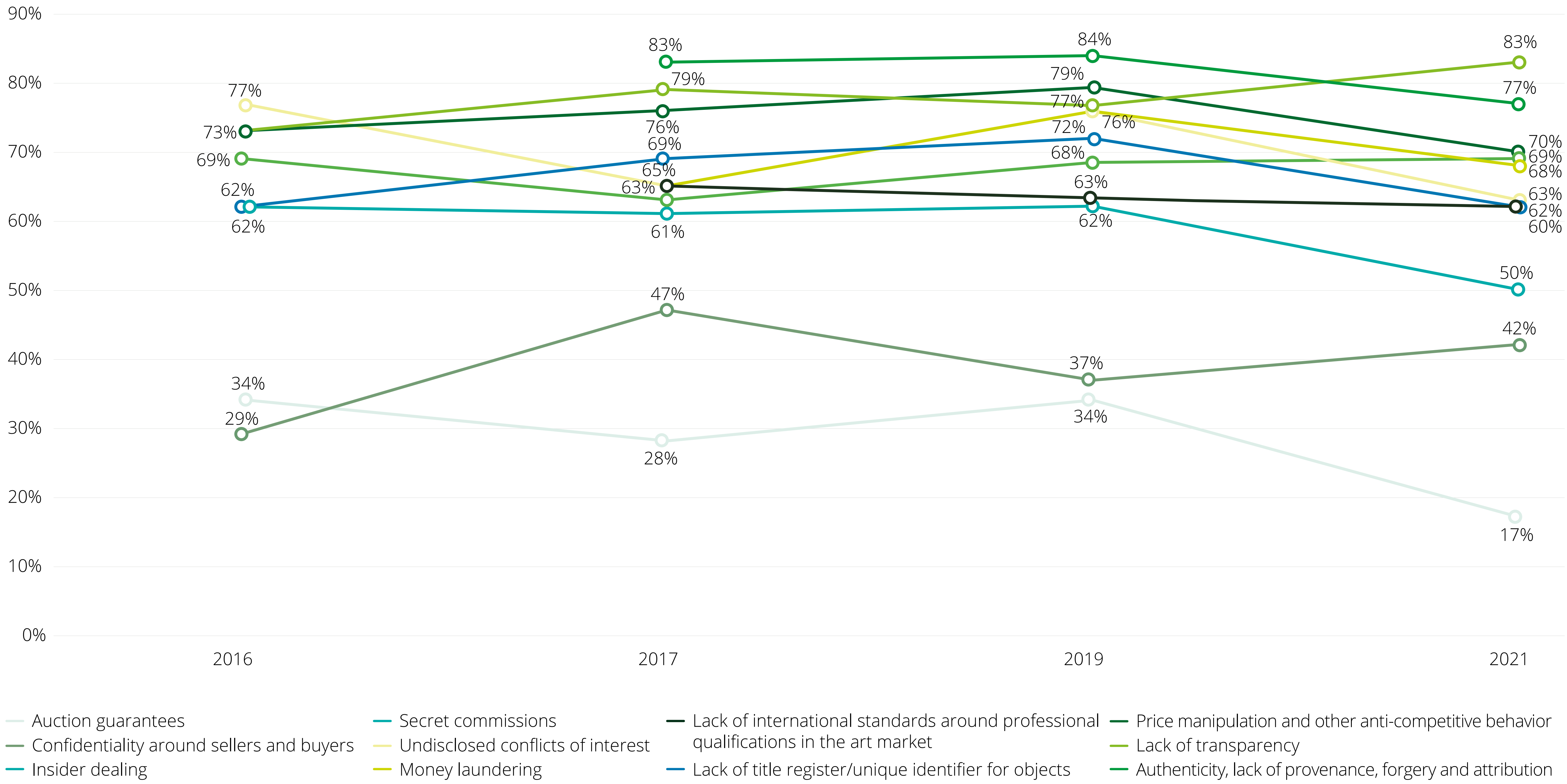

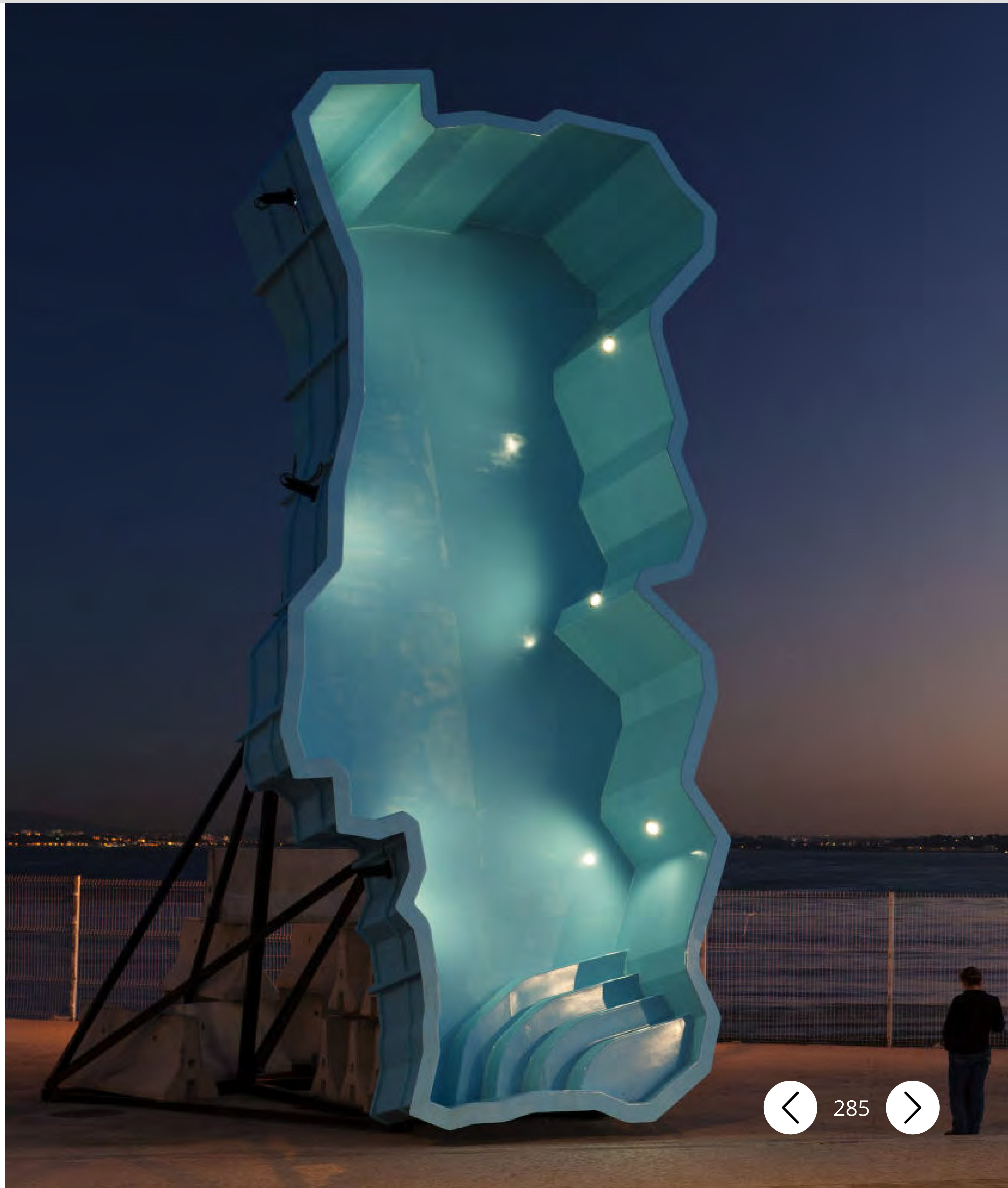

Portugal a Banhos
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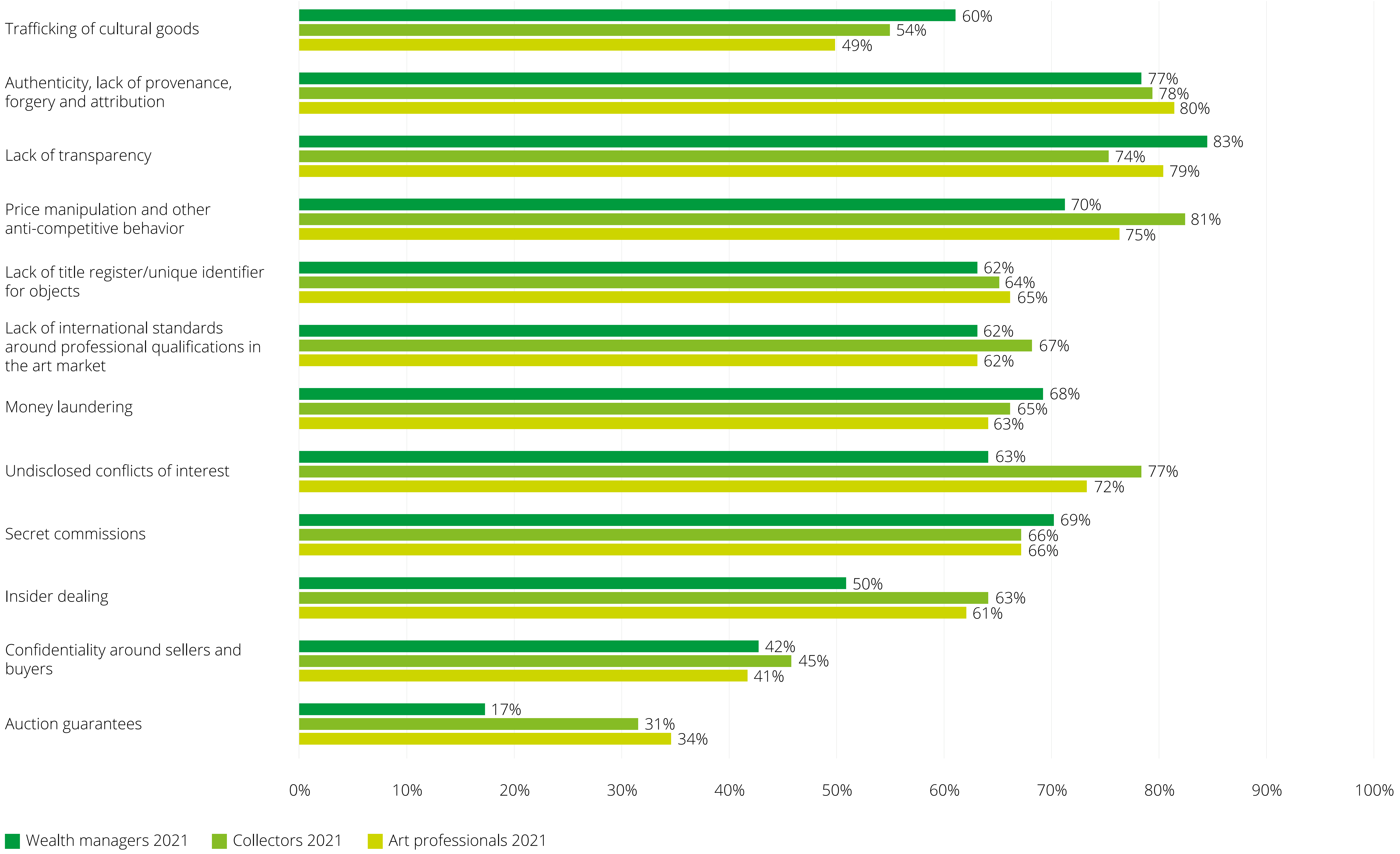
Figure 107. Stakeholder Comparison: Which of the following issues do you feel are the most threatening/damaging to the reputation of the art market?



83% of wealth managers said lack of transparency was a key factor that undermined trust in the art market (compared with 77% in 2019).

Wealth managers and art market stakeholders remain seriously concerned about threats to the art market's reputation.

There is a real consensus among stakeholders that the art market still has some way to go to increase trust. Although there are signs that certain areas are being addressed, in many cases the threats have amplified, such as the art market's continued opaqueness. While the art market has increased its transparency on the back of the digital transformation catalyzed by the COVID-19 pandemic, our findings suggest there is still much room for improvement.

Lack of transparency

83% of wealth managers said lack of transparency was a key factor that undermined trust in the art market (compared with 77% in 2019). Both art collectors (74%) and art professionals (79%) also identified this as a key challenge. Lack of transparency ranked even higher among younger collectors, with 86% identifying it as a major challenge in today's art market. However, this could be about to change, as the COVID-19 pandemic forced the art market to go largely digital, boosting its transparency as a result. Increased price transparency in the online art market and the rise in interest around fractional ownership, NFTs and tokenization could signal the beginning of a more open and transparent market model.

Price manipulation

70% of wealth managers expressed concern about the perceived threat of price manipulation in the art market (down from 79% in 2019), with 81% of collectors and 70% of art professionals saying the same (compared with 75% for both in 2019). The mistrust of art market data that is covered later in this section could be closely associated with this particular concern.

Undisclosed conflicts of interest

63% of wealth managers were concerned about conflicts of interest in the art market (down from 76% in 2019). Both collectors (77%, up from 69% in 2019) and art professionals (72%, compared with 71% in 2019) also saw this as a grave concern. The blurred lines between advisors, dealers, brokers and valuers mean a clearer division of roles may be required to address this issue. Of the wealth managers surveyed this year, 69% identified secret commissions as a major threat to the art market, compared to 68% in 2019, and 66% of art collectors and art professionals expressed the same concern.

Authenticity and provenance

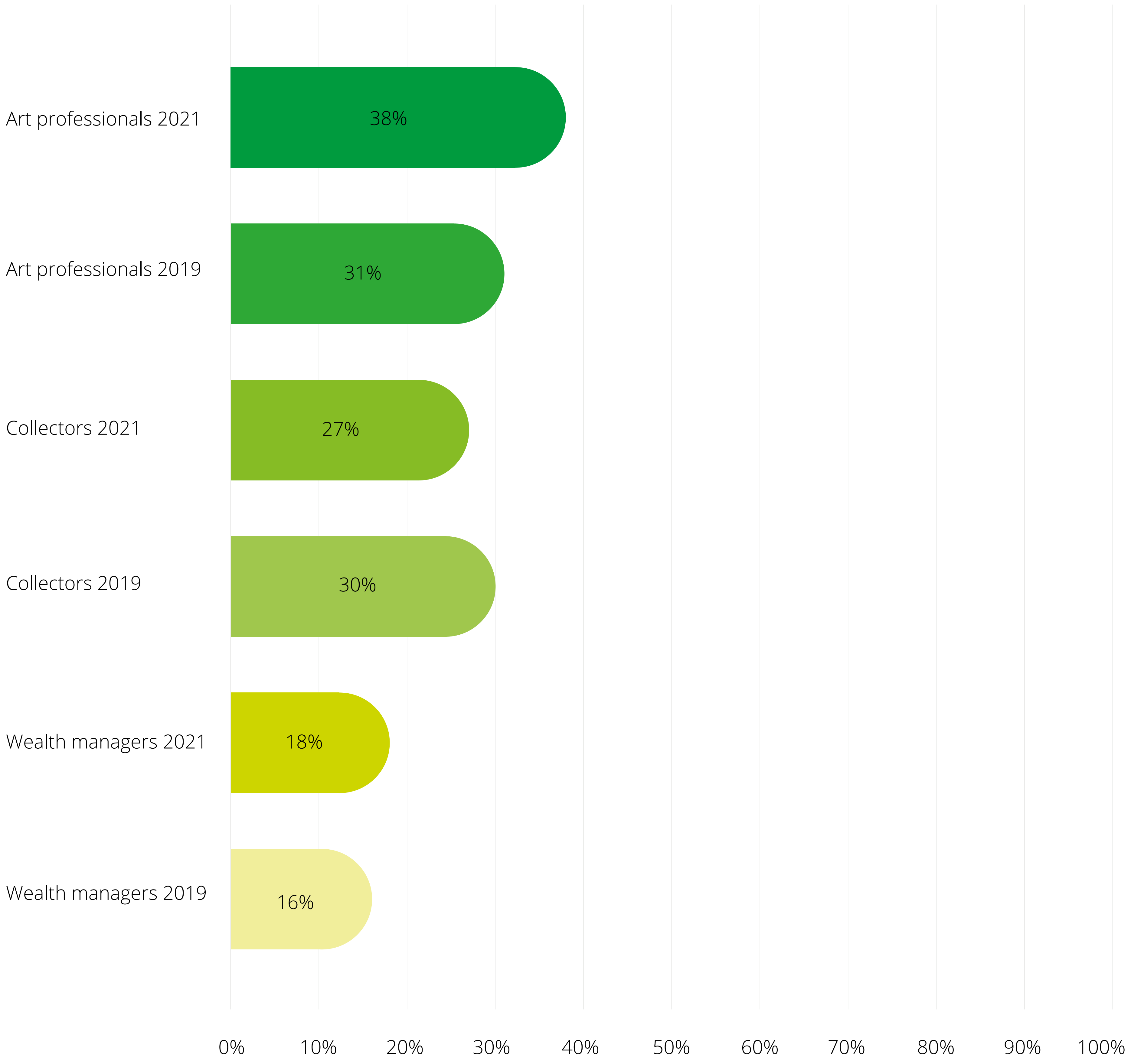
77% of wealth managers believed authenticity, lack of provenance and the risk of forgeries and misattribution were the greatest threats to the art market's reputation this year (down from 84% in 2019), with 78% of art collectors and 80% of art professionals saying the same. With art values at a historic high, so is the perceived risk of offering art-related wealth management services in a market fraught with authenticity issues. However, there have been significant technological advances in this area—including forensic science and DNA technology, as well as the use of blockchain as an artwork provenance tracking tool and title register—which could help address many of today's concerns. See Section 7 for more information on these developments.

Money laundering

68% of wealth managers remain concerned about the risk of money laundering in the art market (down from 76% in 2019). The recent introduction of EU and US AML regulations seems to have stemmed some wealth managers' fears. Both art collectors (65%) and art professionals (63%) continue to see money laundering as a substantial threat to the art market's reputation going forward (compared with 59% and 65% respectively in 2019).

Small World
©Unidade Infinita Projectos - 2001

Figure 108. What level of trust do you have in the art market data (qualitative & quantitative) currently available (% saying high and very high)?
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021



Data and trust

Building trust in art market data is essential for the further development of the art and finance industry.
As all industries move towards an increasingly data-driven business model, it is critical that the art market does not fall behind. Reducing information asymmetries and boosting transparency is critical to support the sector's growth and aid the onboarding of new collectors. Trust in art market data is also an essential foundation for building a robust valuation and risk management infrastructure around art and collectibles.

However, trust in art market data remains low, particularly among wealth managers. While this distrust may be triggered by the perception of price opacity, price manipulation and conflicts of interest (see the major threats to the reputation of the art market on figure 106 on p.285), it is obvious this area needs addressing.

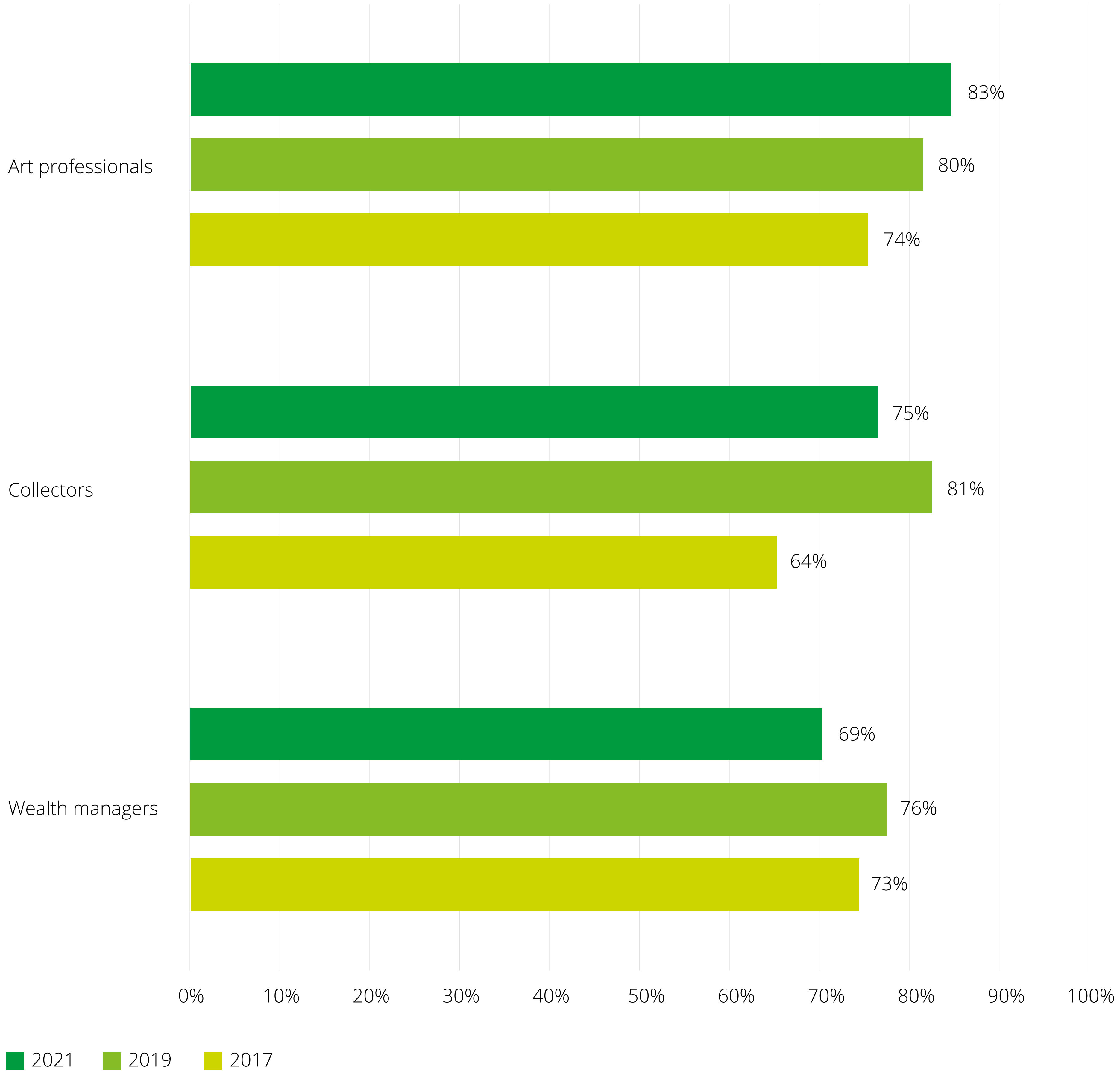
In this year's survey, most collectors, art professionals and wealth managers expressed a low-to-moderate trust in art market data. There are indications this trust is growing among some stakeholders, with 38% of art professionals saying they have a high level of trust in art market data (compared with 31% in 2019). Collectors were more cautious this year, with 27% expressing a high level of trust compared with 30% in 2019. Wealth managers remain the most skeptical, with only 18% having a high degree of trust in art market data (compared with 16% in 2019).

The art market and its professionals play a key role in building this trust, and both collectors and art professionals believe wealth managers should proactively embed art market data and research services into their wealth management offering, as a way to increase trust in art market research.

Regulation: government versus self-regulation

Most wealth managers and art market stakeholders believe the art industry is ripe for modernizing their business practices
69% of wealth managers believed the art industry must adapt to the new environment and update their business practices to meet market needs. Both collectors (75%) and art professionals (83%) also believed the industry needs to modernize its existing ways of conducting business.

Figure 109. Does the art market / art industry need to modernize its business practises? (% saying yes)



Spot Me

Attitudes are changing towards government regulation in the art market

Figure 110. Art professionals: Which regulatory approach do you favour when it comes to establish trust and credibility in the art market?

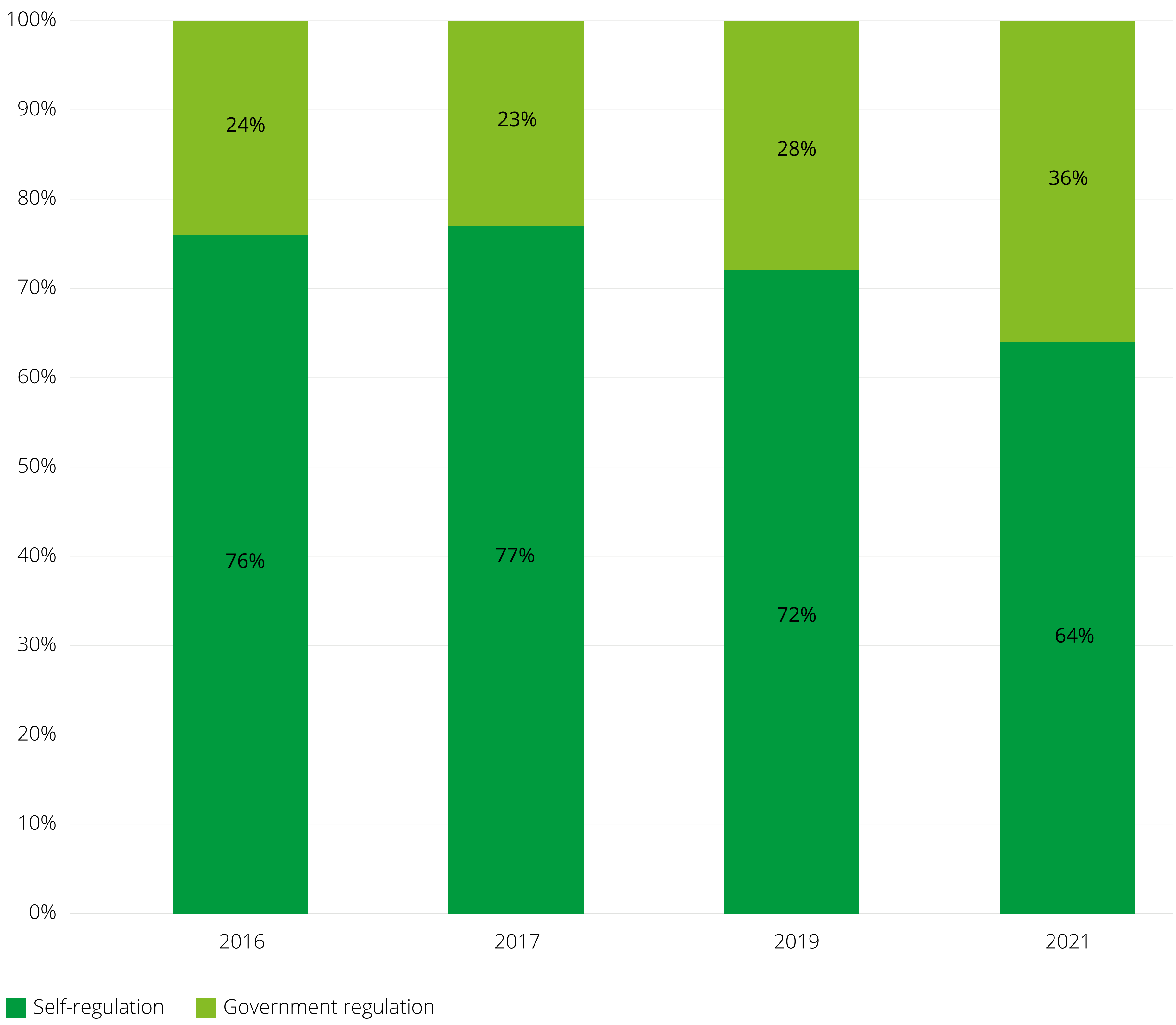


Figure 111. Collectors: Which regulatory approach do you favour when it comes to establish trust and credibility in the art market?

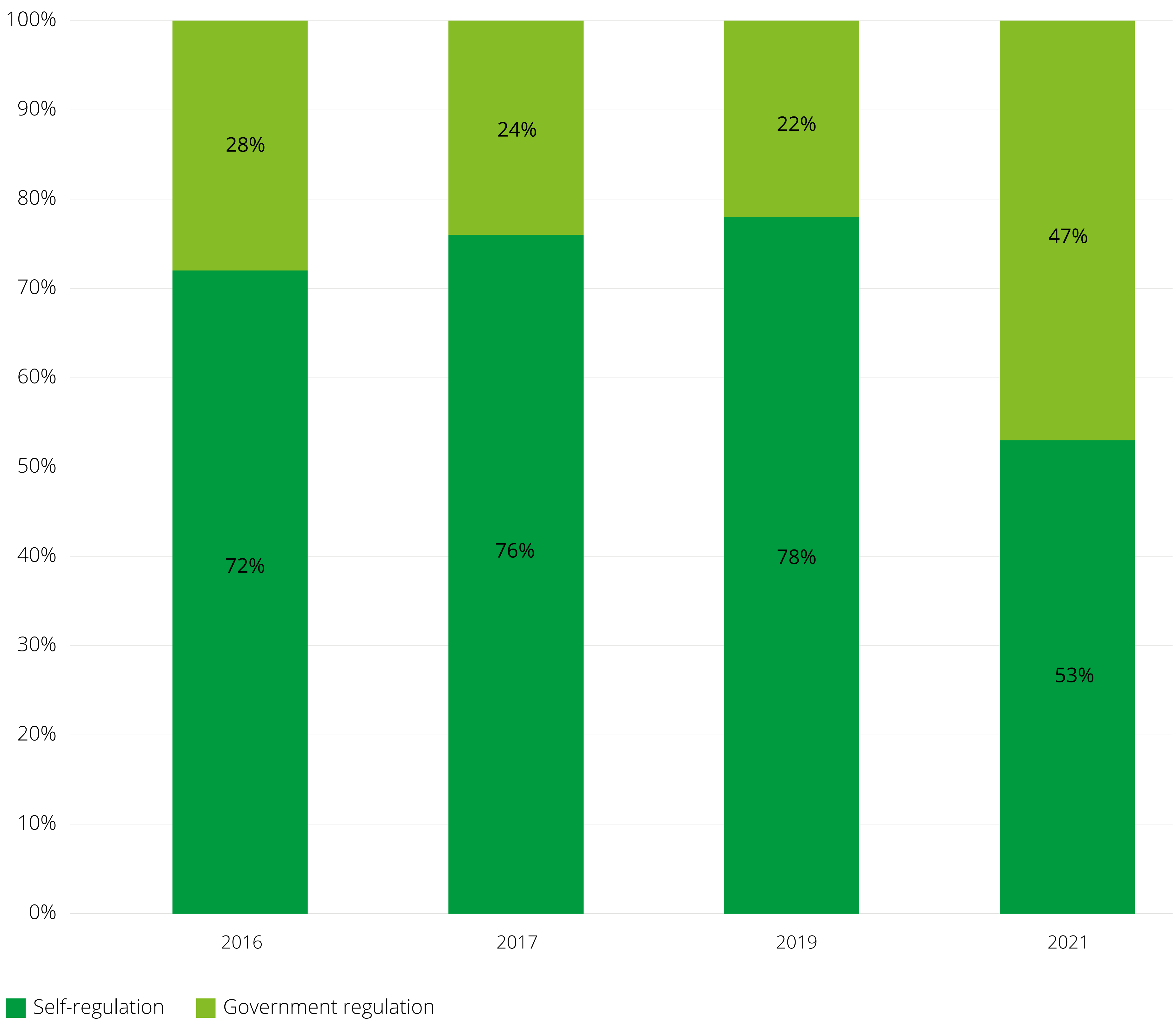
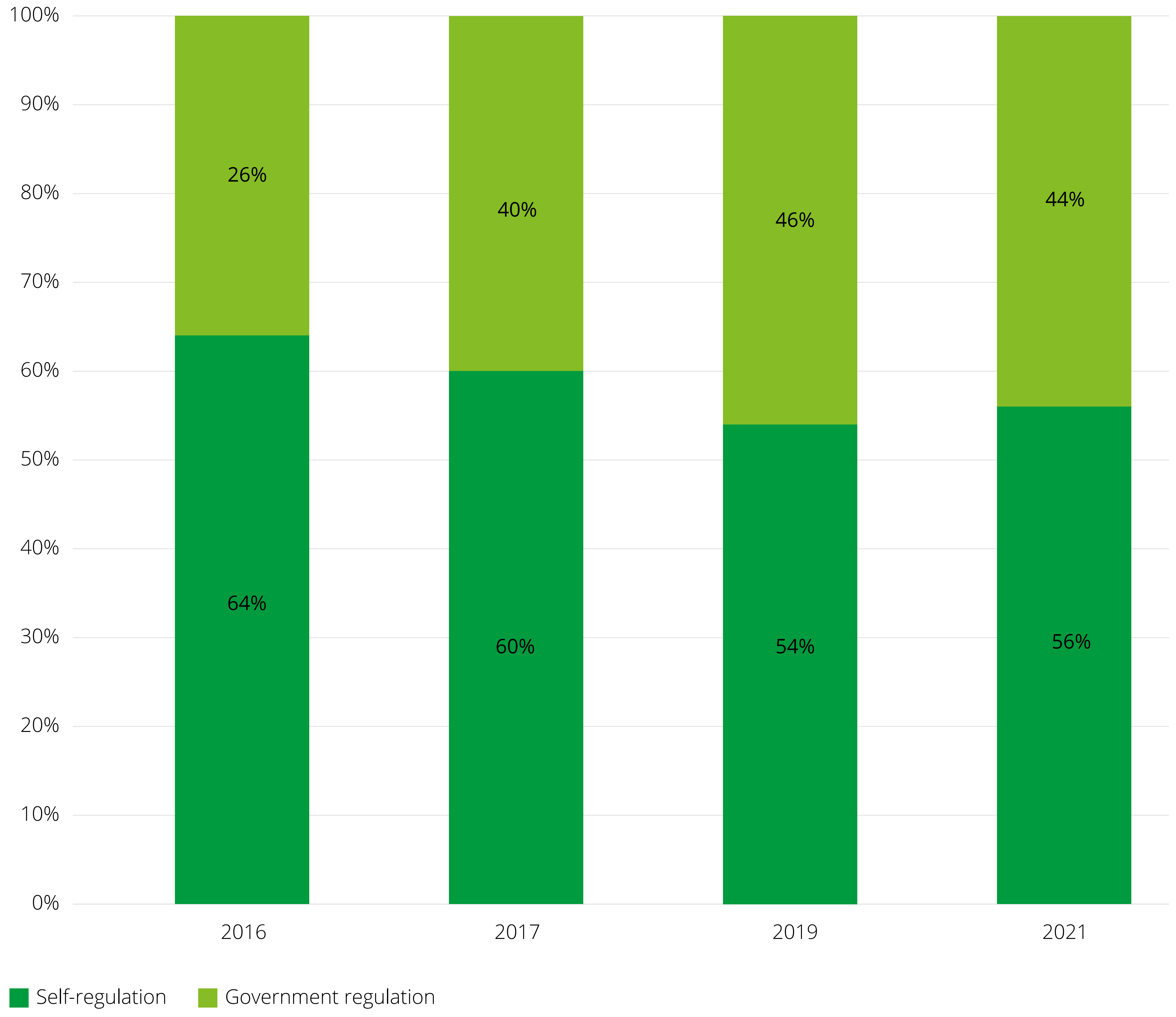


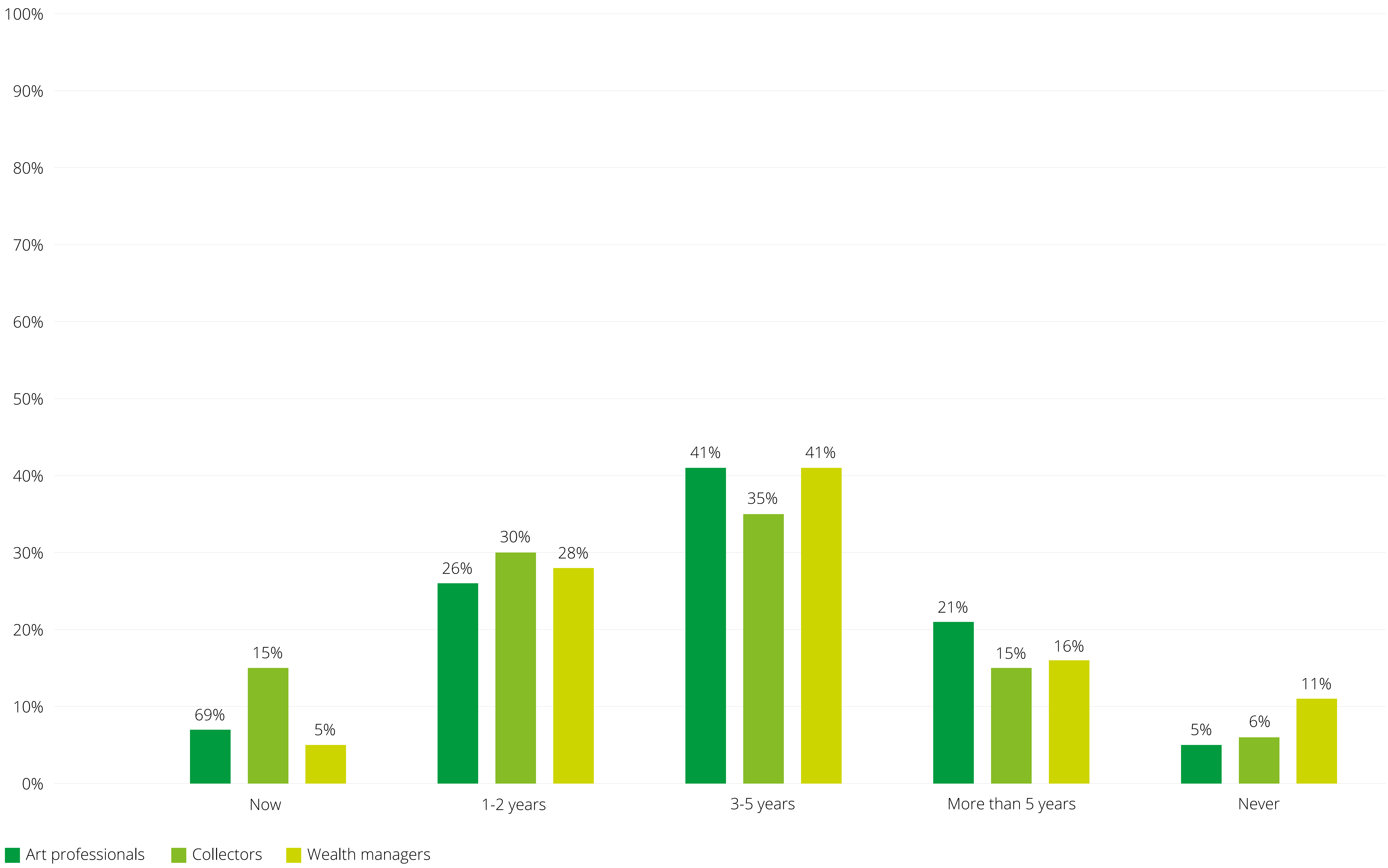
Figure 112. Wealth managers: Which regulatory approach do you favour when it comes to establish trust and credibility in the art market?



Increasing appetite for more government regulation

Although self-regulation remains the art market's preferred approach to establish trust and credibility, it is unsurprising that more art market stakeholders believe increased government regulation may now be required, as self-regulation has proven less effective so far. Significantly more collectors (47%) indicated their preference for government regulation, up from 22% in 2019, with 36% of art professionals saying the same (compared with 28% in 2019). And, 44% of wealth managers this year believe government regulation would help restore trust in the art market (only slightly below 46% in 2019).

Figure 113. In your view, when do you think we can see an acceleration in adoption of more transparency and regulation in the art market?
Source: Deloitte Luxembourg and ArtTactic Art & Finance Report 2021



Most wealth managers and art market stakeholders see transparency and regulation increasing in the next five years

67% of wealth managers expect the art market to become more transparent and regulated over the next five years, compared with 55% of collectors and 67% of art professionals who said the same. One-third (33%) of wealth managers believe this will take longer than five years or not happen at all, compared with 45% of collectors and 33% of art professionals. Younger collectors seem less convinced about the speed of change, with 50% saying it will take more than five years and 7% saying that regulation and transparency are unlikely to happen at all. Despite the hesitancy among younger age groups, these findings suggest that change is on the horizon. Judging by the speed of the transformation triggered by the COVID-19 pandemic on the global art market industry and existing business models, we will likely see an increasing acceleration of change over the coming years.

The question is, what role can wealth managers play in developing more transparency and creating an appropriate legal and regulatory framework around art and collectibles? Involving this stakeholder group from the outset will allow them to shape the future of the art and finance industry together with other art market players. Without wealth managers' valuable input, this process could take even longer.

Part 2. Regulation—a focus on AML efforts

An HM Treasury publication[2] "National risk assessment of money laundering and terrorist financing 2020" states, "According to the United Nations Office on Drugs and Crime, £2.3 billion of the global art market could be linked to money laundering or other financial crime annually.[3] While we are unable to assess the full extent of money laundering through the art market in the UK, the size of the sector, combined with a previous lack of consistent regulation, means the global art market has been an attractive option for criminals to launder money.[4]"

AML regulation is not only here to stay but it will likely continue to expand and develop. The European art market is subject to the Fifth Anti-Money Laundering Directive (AMLD5) as well as the United Kingdom, which adopted similar rules just before its exit from the European Union. On 1 January 2021, the US House and Senate voted to extend the 1970 Bank Secrecy Act to the art market, specifically to persons engaged in the antiquities trade.

As the European Union, the United Kingdom and the United States represent the biggest art trading zones in the world, and as the art market is truly international, these AML rules could have significant implications for many art collectors, art galleries and auction houses around the world.

We extensively covered AML in our previous edition of the Art & Finance report in 2019. In this edition, we have three contributions. The first article focuses on AML in the US and other art markets. Insights into recent developments are provided by Patricia Pernes, US Counsel at Bonham's, and Michael Shepard, Deloitte's Global Financial Crime leader and a Deloitte Risk & Financial Advisory principal in Deloitte Transactions and Business Analytics LLP, in their contribution on p.294.

This is followed up by the article on p.297 "Bridging provenance research and AML compliance" from Victoria Louise Steinwachs, Manager in the German Deloitte Forensic practice and part of the Corporate Intelligence Team in Berlin. Before joining Deloitte, Victoria gained many years of experience in provenance research while working for the international auction house Sotheby's in London, as well as for the so-called "Gurlitt Provenance Research Project", funded by the Federal Government Commissioner for Culture and the Media.

Finally, Maxime Heckel, Partner at Deloitte Luxembourg and Astrid Brandy, Senior Manager at Deloitte Luxembourg examine outsourcing as a possible route for art market stakeholders to meet their new AML obligations in their article on p.299.

The European art market is subject to the Fifth Anti-Money Laundering Directive (AMLD5) as well as the United Kingdom, which adopted similar rules just before its exit from the European Union.

Volupta
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2 HM Treasury, National risk assessment of money laundering and terrorist financing 2020, December 2020, p.141, paragraph 17.12.
3 International Monetary Fund, 'The Art of money Laundering', September 2019.
4 Ibid.

Adriano Picinati di Torcello
Global Art & Finance Coordinator at Deloitte Luxembourg

Michael Shepard
Deloitte's Global Financial Crime Leader

Patricia Pernes
US General Counsel, Bonhams

Expert voices

Airing the laundry

Direct and indirect anti-money laundering regulation of art markets

Adriano Picinati di Torcello (APT): We have been tracking the evolving AML regulatory landscape affecting the global art market. What is the state of play and is it too soon to ask: 'what's next'?

Patricia Pernes & Michael Shepard
Over the past few years, the art market has garnered significant attention from governments, regulators and law enforcement because of its perceived susceptibility to being used to evade economic trade sanctions and for money laundering. In the European Union and the UK the art industry became subject to AML and customer due diligence requirements through the EU 5th AML Directive. Following the issuance in July 2020 of a detailed report entitled *The Art Industry and US Policies that Undermine Sanctions*, by the US Senate Permanent Subcommittee on Investigations (a Committee that has traditionally been at the forefront of exposing financial crime schemes and lax regulation) the US Congress passed the Anti- Money Laundering Act of 2020. The Act will expand AML requirements to "persons engaged in the trade of antiquities". We cannot accurately predict at this time how broad the future regulatory definition will be, but one can assume that it will be consistent with or at least take on some of the characteristics of the EU requirements and at least cover transactions above a certain value threshold, if the objective is truly to mitigate financial crime risks.

On September 24th of this year, US financial crime regulator FinCEN solicited public comment on the implementation of the Anti-Money Laundering Act of 2020 as to the antiquities trade.

For the purpose of crafting regulations, FinCEN invited commentary on a list of factors, including "[h]ow is an antiquity distinct from a work of art?" Comments must be submitted to FinCEN by October 25, 2021 (following the publication date of this *Deloitte Art & Finance Report),* and although this current comment period applies only to the antiquities trade, in 2022 the broader art market may undergo the same process.

APT: What is your view of the impact of AML/CTF legislation on the way business is done in the art sector? To what extent do you feel that the way the industry operates will be affected by relevant obligations?

Patricia Pernes & Michael Shepard
Activities that may have gone unquestioned before, such as undisclosed principals, third-party payments or proceeding with a transaction without inquiring about the other parties involved, are now potential red flags that call for additional diligence and potential reporting. But there is a two-way street, and if the engine of the art market is indeed information mongering, anonymity lost is information gained.

And while AML/CTF legislation certainly raises the bar, the art market has for decades been (both directly and indirectly) subject to significant legal and regulatory developments that have affected the way the industry operates, including in the areas of border and trade controls, enforcement relating to cultural property and endangered species materials, sales and use tax, reporting requirements of cash payments exceeding

US$10,000, just to name a few.

In each instance, the industry adjusted; a decade ago it may have been taboo to disclose introductory commissions, now it's common practice. The impact of AML/CTF legislation will be similarly absorbed and integrated, with the requisite adjustments to operational processes and procedures.

APT: Provenance has long been a challenge in the sector, which has developed sophisticated tools to minimize connected risks. Are new AML/CTF obligations supporting the clear establishment of provenance? If so, with what potential industry outcomes for the future?

Patricia Pernes & Michael Shepard
In most instances, provenance traces back much further than the scope of AML/CTF obligations on an individual transaction basis.

One possible outcome of the new regime is an industry-wide move toward the disclosure of principals to transactions. However, while a buyer would know the identity of the seller (and vice-versa), the breadcrumb trail may very well stop there; the anonymity previously afforded by transacting through an agent can be achieved through confidentiality and nondisclosure agreements. Agents in turn may require non-circumvention agreements to protect their business positions.

The required processes map out the risks as we understand them to be, and are designed to identify suspicious activity and preclude illicit transactions, or compel reporting when these occur.

APT: Partly in connection with the above, and now that AML/CTF processes have become strict requirements in certain jurisdictions, is there a clearer sense of the risks to which the industry is exposed?

Patricia Pernes & Michael Shepard
The required processes map out the risks as we understand them to be, and are designed to identify suspicious activity and preclude illicit transactions or compel reporting when these occur. There are still elements within the art industry that question its propensity or exposure to money laundering and terrorist financing risks. A clearer sense of the risks will develop over time, through, among other things, the application of the AML/CTF due diligence and reporting framework and subsequent determination of the frequency and nature of the risk issues and suspicious activity identified.

This will in turn further inform regulatory guidance. For instance, since the implementation of the EU 5th AML Directive, local regulators have actively considered the 'what's next'. The UK regulator for the sector, HMRC, has recently issued an update to its guidance, focused specifically on money laundering risks. This is indicative of a drive to embed good practices by encouraging a better understanding of relevant risks. We can expect the next iteration of the UK's National Risk Assessment to have taken full stock of the industry's assessment of its risk exposure; other jurisdictions will follow suit. There will be more 'knowns' and opportunity to refine control frameworks on the strength of this improved knowledge. The hope of course is that regulation and self-regulation will, in and of itself, eliminate the risks by making the transactional process - and thus the industry as a whole - inherently inhospitable to bad actors.

APT: Is prevention by way of self-regulation the best medicine? Do the benefits outweigh the cost?

Patricia Pernes& Michael Shepard
Solely relying on self-regulation does not seem to be a viable option anymore, as legislatures, governing bodies and agencies in multiple jurisdictions are regulating the industry. Developing and properly executing risk-based AML/CTF policies, procedures and controls will mitigate risk exposure. Delivering comprehensive training to staff and testing the execution of relevant program controls is an integral aspect of this.

APT: KYC often relies on strict documentary requirements which, while expected in sectors such as retail or business banking, are less common and thus more controversial in captive regulated markets. Is the art sector encountering cultural resistance to implementing certain measures, or are we living in an age in which such measures are now generally expected?

Patricia Pernes & Michael Shepard
We are living in an age in which certain due diligence measures are generally expected in various aspects of everyday life. Overall, the art industry and its culture have adapted, and the documentary requirements have broadly been accepted as the status quo. Regulated parties, especially international actors with operations in multiple global art market hubs like New York, London, Geneva, Paris and Hong Kong, all generally responded by implementing additional requirements worldwide at about the same time, which contributed to setting a new tone. They continue to play a significant role in shaping this aspect of industry by mandating transacting parties to follow relevant requirements. The UK's HMRC recently confirmed that Art Market Participants (AMPs) should not only refuse to do business with an AMP that is not appropriately registered with HMRC for AML/CTF supervision but should consider reporting it to the National Crime Agency and HMRC. Non-compliance may be regarded as suspicious, not merely a sign of cultural resistance.

Art market participants in jurisdictions without AML/CTF regulations may have a higher risk profile if they lack relevant controls, particularly around KYC and identification of beneficial ownership.

APT: To what extent is scrutiny and regulation of the art market aimed at preventing financial crimes also affecting other industries? Or are recent coordinated efforts to lift the veil of financial secrecy resulting in art coming under the magnifying glass?

Patricia Pernes & Michael Shepard
While funds most frequently flow through banks, the view now is that the financial services industry cannot be the lone sector assisting law enforcement in tackling financial crime and terrorist financing. All industries can be used to launder money to some extent.

Like dealers in precious metals and stones before it, the art industry has been identified by law enforcement and regulators as one of the industries that is exposed to money laundering and terrorist financing risks. The recent US Senate report assessed the art-buying activities of certain US-sanctioned individuals and highlighted how the abuse of corporate structures in offshore jurisdictions can be used to obfuscate sources of funds and true ownership of artwork. While regulatory mandates and implementation of risk-based AML/CTF programs in and of themselves will not bar bad actors from attempting to use the art industry for illicit purposes, properly executed compliance programs will help mitigate risk and detect threats and bad actors. Learning from the results will be key to future program enhancements. It will also help art professionals to steer clear of unwittingly being used for nefarious financial crime purposes, which may itself, depending on the facts and circumstances, constitute a crime, such as 'wilful blindness'.

APT: The art world is now divided into regulated, semi-regulated, and non-regulated jurisdictions for AML/CTF, with corresponding differences relating to transparency of beneficial ownership and source of wealth/funds. What challenges does this present for organisations with a global reach?

Patricia Pernes & Michael Shepard
Art market participants in jurisdictions without AML/CTF regulations have a higher risk profile if they lack relevant controls, particularly around KYC and identification of beneficial ownership. Additional controls are recommended when transacting with such jurisdictions. For example, in the UK, AMPs are required to assess jurisdictional risk on the basis of multiple factors; HMRC specifically references levels of bribery and corruption, capital flight, conflict zones, organized criminal activity, and comparably weaker AML/CTF measures. Appropriate risk assessment and tailored due diligence is key.

APT: Can there be a one-size fits all solution to meet 5th Directive and FinCEN (using the current financial institution) requirements?

Patricia Pernes & Michael Shepard
Art market participants that operate in multiple jurisdictions should develop minimum global AML/CTF program standards to be applied to all transactions, in all locations. If a particular jurisdiction is subject to a higher regulatory standard in any specific area, that standard or requirement should certainly be applied in the jurisdiction that requires it.

APT: Covid-19 changed the way sales are made, including by accelerating the adoption of online platforms for the purchase and sale of art. The UK's National Risk Assessment recognizes this as a risk, in part because buyer and seller information can be more easily disguised or withheld. What is your view?

Patricia Pernes & Michael Shepard
The key is to have the appropriate risk-based policies, procedures, and controls in place, and necessarily follow these. Risk-based due diligence processes and requirements may entail additional steps where in-person interaction would typically be part of the process, such as when working with a new client. Addressing this may be as simple as connecting via video call instead of emails, or may entail more robust checks. The shift to online transactions has in some respects facilitated good practices, including through the adoption of technology platforms that require information and document submissions prior to account activation.

Victoria Louise Steinwachs
Manager, Deloitte Wirtschaftsprüfungsgesellschaft GmbH

Expert voices

Combating Financial Crime within the Art Trade

Bridging Provenance Research and AML Compliance

Financial crime risks within the art trade
Falsifying an entire art collection, as in the forgery scandal surrounding Wolfgang Beltracchi and the alleged Jägers Collection, may be an extreme example, but there is no doubt that art and the art market are by nature attractive targets of crime and criminals. While we know that the trade in stolen art and cultural goods is used to finance terrorist activities and that secret hiding places for such contraband could be found in poorly regulated free trade zones (FTZs), perhaps the most problematic issue in the art market is its traditional emphasis on privacy and anonymity. The 2020 national risk assessment (NRA) of money laundering and terrorist financing states that the art market is particularly vulnerable to money laundering due to its international character, the highly volatile art market prices and the ability to conceal the true beneficial owner of an artwork and the source of the funds used to acquire it.[5] In a recently published guidance on understanding money laundering risks and taking action for art market participants (AMPs), HM Revenue & Customs (HMRC) further pointed out that art, due to its size, can be transported with ease across borders, making the trade in art more attractive to criminals.[6] Cultural goods such as antiquities and archaeological artefacts are also at high risk of illegal excavation and smuggling. Since illicit trafficking in these items has already entered the realm of terrorism and ever-greater fortunes are being invested in art, international payment flows in the art market are becoming increasingly complex and opaque.

Regulating the art trade – where do we stand?
To address this risk, the European Union (EU) and the United Kingdom (UK) implemented the Fifth Anti-Money Laundering Directive (AMLD5) in January 2020, which brings AMPs into the regulated sector for anti-money laundering (AML) purposes when the value of the goods traded is EUR 10,000 or more, regardless of the payment method. As of May 2021, 70% of EU member states have fully transposed the new directive.[7] The United States (US) passed its own Anti-Money Laundering Act of 2020 (AMLA) in January 2021, which requires antique dealers to follow standards imposed by the Bank Secrecy Act (BSA). Similar to the regulations in the EU and the UK, dealers are now subject to AML and customer due diligence in the US as well.

Insofar as AML compliance is a rather novel concept in the art trade, it is no surprise that the new legal provisions in place in Europe and the UK raise a number of practical issues – especially since there is no “one size fits it all” standardized due diligence process for the art market. Smaller dealers in particular feel that the new regulations are too difficult and expensive to implement, and that the overall process is too burdensome relative to the size of their business. However, if applied correctly, this new set of controls can actually help AMPs build trust with their clients and protect their own businesses from financial and reputational risk.

In this environment, art collectors will also be required to provide more transparency in support of the global efforts to reduce the risk of money laundering and terrorist financing in the art trade. Both sides need to ensure that they know who is on the other side of the deal, which is where provenance (ownership history) comes into play. Both provenance research and AML compliance rely on detailed documentation and help assess the risk of a business deal in terms of the customer, product and country of origin, with the aim of exposing illicit transactions.

5 HM Treasury, National risk assessment of money laundering and terrorist financing 2020, December 2020, p. 140.
6 HM Revenue & Customs, Guidance: Understanding money laundering risks and taking action for art market participants, June 2021.
7 European Commission, Anti-money laundering directive V (AMLD V) - transposition status, June 2020.

However, AML regulations focus mainly on the buying and selling process – in other words, the origin of the money used in the transaction – but do not take into account art-related specifics such as the ownership history. So, let's say there is a collector interested in buying a work of art, and their trusted gallery owner takes the necessary measures to prevent money laundering. What happens when the work turns out to be the product of looting, bribery or even forgery, even though nothing suspicious was found by the gallerist? This example shows that despite careful implementation of the new requirements, there may still be a residual risk. One way to avoid such pitfalls is to carefully trace and verify the ownership history of an artwork.

Provenance research – what is to be considered

Works of art are often put on the market with incomplete provenance or only a vague ownership history, such as "Private collection Italy". Many buyers are therefore unaware where the object comes from, who is selling it to them or who owned the work in the past. Many collectors purchase artwork in good faith, assuming that someone along the line must have conducted the appropriate research for it to be freely traded on the market. A museum, for example, may be persuaded to gloss over dubious provenance in order to possess an extraordinary object, which on closer inspection is too good to be true and turns out to be a fake or a looted artefact. In July 2021, for example, the National Gallery of Australia announced it was returning 16 objects from its Asian collection to India, their country of origin.[8] The museum had reportedly acquired these artefacts from New York art dealer Subhash Kapoor, whom the US Immigration and Customs Enforcement (ICE) agency described as one of the world's "most prolific commodities smugglers".[9] The National Gallery launched its Asian Art Provenance Project[10] in 2014 and has since deaccessioned and repatriated numerous objects based on the research into their provenance.

Filling in provenance gaps can take a lot of time and ultimately depends on the information available. We must also accept that not every work will have a traceable provenance. However, anyone active in the art sector should understand how important it is to have the full history and ownership details of an artwork to determine both its authenticity as well as its legal title. An artwork with good provenance and a complete or at least almost complete set of supporting documentation (including invoices, inventory records, historical photographs, archival material and any papers documenting the biography of a work of art) will enhance its value, while unclear titles and gaps in provenance, for example during World War II, may raise questions and perhaps even restitution claims. These, in turn, could lead to a reduction in the artwork's value, loss of ownership or reputational damage. The same applies to art that has flawless provenance, but can be traced back to a dubious owner.

We must keep in mind that provenance information can also be falsified, as was the case with the artefacts traded by Subhash Kapoor, and collectors should therefore look closely at the information publicly available. Ideally, provenance documentation will contain verifiable facts about the ownership history from the time the artist produced it to the present. How was the object transferred from one owner to another, i.e., through a dealer, auction or inheritance? What about the exhibition history: Who lent it to which museum? Also of interest are queries about the country of origin and how the object in question survived during wartime. Was it stolen or looted? Can the seller prove a clean title, i.e., do they legally own the work?

A good starting point for anyone interested in provenance research is the Provenance Guide published by the International Foundation for Art Research (IFAR).[11] The guide includes links to important archives, image databases, dealer and sales records as well as other web resources for art theft such as INTERPOL's database on stolen artworks[12] and the Art Loss Register,[13] a private fee-based international organization offering services in the location and recovery of stolen or looted works of art. Another digitized resource is the Lost Art Database,[14] administered by the German Lost Art Foundation (Deutsches Zentrum Kulturgutverluste),[15] in Magdeburg, Germany, which serves as the national and international contact partner for all matters pertaining to the illegal seizure of cultural assets in Germany in the 20th century. With steady growth in the number of sources publicly available, those mentioned here should be seen purely as examples.

What's Next?

As is the case in other regulated sectors, we can expect criminals to adapt their behaviour to circumvent these new regulations. At the very least, however, the new policies, procedures and controls – when properly implemented by all AMPs – will help mitigate risks. Assessing an AMP's exposure to the risk of dealing in illegally obtained art plays a crucial role in designing the right controls. We recommend a tailored risk assessment including proper provenance research of the objects being traded, not only to better understand the exposure of AMPs to higher risk products, such as antiques, but also to determine the best way to minimize the risk of looted objects being sold to an unwitting buyer. As part of this process, the assessment of an AMP's records and market experience can help provide a more general understanding of their exposure to art-related criminal risk in several regulated sectors.

We expect to see an increase in law enforcement activity and investigations in the art market. It would therefore be prudent for any AMP subject to these new guidelines to invest time and effort in thorough due diligence and documentation. By doing so, they will ensure that their own business practices comply with the new regulations, and that they are able to quickly provide comprehensive documentation on a particular transaction in the event of a sudden investigation by regulators.

8 Elisabeth Fortescue, "National Gallery of Australia to return 13 stolen objects to India that it bought from disgraced art dealer Subhash Kapoor", The Art Newspaper, July 29, 2021.
9 U.S. Immigration and Customs Enforcement, "ICE seizes statues allegedly linked to Subhash Kapoor, valued at $5 million", press release, December 4, 2012.
10 National Gallery of Australia, "Asian Art Provenance Project", accessed July 30, 2021.
11 International Foundation of Art Research, "Provenance Guide", accessed July 30, 2021.
12 INTERPOL, "Stolen Works of Art Database", accessed July 30, 2021.
13 The Art Loss Register, accessed July 30, 2021.
14 The Lost Art Database, accessed July 30, 2021.
15 German Lost Art Foundation, accessed July 30, 2021.

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Expert voices

What if...

Financial institutions could monetize their experience in anti-money laundering while easing and securing art professionals' path towards compliance?

The pages of the Deloitte Art & Finance Report show how numerous, fertile, and diverse connections between the art market and the financial services industry (FSI) have become. Renaissance bankers set the tone, building such relationships by sponsoring promising artists. When talking about investment strategy, about advising collectors, about institutional investors' ESG strategy promoting arts, culture and education, or about works and collections tokenization, the initiatives are only proliferating.

However, now that the art market is becoming subject to anti-money laundering and counter-terrorism financing (AML/CTF) obligations comparable to the ones the FSI has invested years to comply with, collaborations in this area seem quite shy. Why restrain the alliances with the investment and finance area when we can advantageously extend them to the compliance field, where the FSI's experience could help art market professionals (AMPs) overcome the regulatory challenges posed by their AML/CTF obligations?

The onset of a cultural change with the deployment of the Fifth Anti-Money Laundering Directive (AMLD5) in the art market

Do you remember the first time your banker began asking 'indiscreet' questions? Requests for information such as; "Please send us a copy of your identification document", "How much do you make for a living?", "Where does your money come from?", or "Could you please list the persons who ultimately own your company?".

Well, from now on, art professionals[16] must ask their customers the same types of questions before they process a transaction. They are no longer allowed to complete an operation (e.g., the sale or purchase of an artwork to or from a collector or another art professional) before obtaining a Know Your Customer (KYC) questionnaire and assessing the level of money laundering or terrorism financing (ML/TF) risk the collector may represent[17]. For collectors, this implies cooperating with their trusted gallerist or auction house to swiftly share the requested information and documents, so they can smooth the transaction process rather than try to bypass the art dealer's obligations.

16 "art market participant" means a firm or sole practitioner who:
(i) by way of business trades in, or acts as an intermediary in the sale or purchase of, works of art and the value of the transaction, or a series of linked transactions, amounts to 10,000 euros or more; or
(ii) is the operator of a freeport when it, or any other firm or sole practitioner, by way of business stores works of art in the freeport and the value of the works of art so stored for a person, or a series of linked persons, amounts to 10,000 euros or more;"
17 See Section 6 of the Art and Finance Report 2019 for further information of the due diligence process art professionals have to lead, and the article "Combating financial crime within the art trade" of the present report for a view on the state of play on the market in the evolving regulatory context.

Alongside the well-known risks of theft, art trafficking, looting, or forgery that directly affect the existence or value of an art piece, criminals may also see the art market as an opportunity to discreetly launder illicit proceeds, evade taxes, or even fund illegal activities.

This major step towards greater transparency aims to shed light on the art market, which is often perceived as obscure and opaque, to limit the risk of it being used as a playground for the laundering of illicit proceeds, the investment of corruption proceeds, the evasion of tax, and other financial crimes. Despite the sound objective, this change comes with many challenges for the impacted professionals.

The art market's vulnerability to money laundering makes the task necessary, but complex

Alongside the well-known risks of theft, art trafficking, looting, or forgery that directly affect the existence or value of an art piece, criminals may also see the art market as an opportunity to discreetly launder illicit proceeds, evade taxes, or even fund illegal activities. The characteristics that can make the art market particularly attractive to criminals include:

- Its secretive culture: the common use of proxies, trusted intermediaries, and third-party advisors, which allow for both the buyer and seller to remain anonymous all along the transaction process;
- The amounts of money at stake and the lack of information regarding their origin and destination;
- The transportability of the works: the materialization of considerable amounts of money into high-value artwork that can easily be transported and transferred; and
- The international network: the frequency of cross-border operations and the common use of offshore structures, accounts, and freeports, which are out of reach or sight of usual financial crime surveillance and detection means, including sanction regimes.

This all contributes to the art market's intrinsic attractiveness to ill-intentioned investors, therefore increasing its inherent ML/TF risk and the complexity for art professionals to detect potential risk indicators.

How the steep learning curve towards compliance could be softened by relying on the financial industry's experience

The learning curve, to reach compliance, and maintain it, is steep and costly. It took years to implement robust and steady AML processes in the financial industry. And still, such processes require constant care, adjustment, and monitoring. So far, compliance activities are often perceived by the industry as a cost and a limitation of profit margins. What if such an impact could be limited for art professionals?

What if the banking industry could offer AML/CTF services to customers qualifying as art participants? A bank, for instance, could work as an external AML service provider for art professionals, assisting them with:

- Collection of relevant information from the collectors or their proxies;
- Checking of mandatory documentation;
- Screening of names against official watchlists;
- Risk assessment of the transaction from an AML/CTF standpoint; and
- Tracking of the due diligence process and reporting.

This way, the responsibility to approve or refuse the transaction with the considered collector would be based on the expert analysis provided through the bank's intermediation, as opposed to being left to the gallerist or the auction house.

Such methods supported by qualitative, user-friendly web interfaces and phone apps, could allow a swift and secured processing of the transaction from an AML point of view. Of course the principle could also be extended to art works provenance tracing, or to any financial or advisory service a bank could deliver to art professionals under the umbrella of a single and readily accessible interface and service offering.

Example of possible outsourced KYC operating model

Bank's interface with art professionals

1 Collector

Provides requested information and documentation
The operational team collects and records the mandatory KYC information and documentation from the art professional's counterparties.

2 Operational support team

Documents the file through a common interface
Whether the collection of relevant information and documents is performed by the bank's teams or by external service providers, one screen gathers the KYC file and other relevant information such as work provenance.

3 Gallerist

Consults the common interface to decide upon case
The art professional consults the result of the risk analysis and makes the decision to accept the transaction or to reject the business relationship with the considered seller or buyer.

Due diligence on form

Collector's profile

First Name
....
Last Name
....
Date of birth
../../....

· Identification document
· Power of attorney
· Ownership structure

Download

Artwork provenance

Artwork title
....
Artist
....
Provenance
....
Appraisals ....
History of location:

KYC solution provider

· Screening result
· Risk score computation
· Documentation storage
· Audit track
· ...

Provenance tracing solution

· Artwork registry
· Documentation sharing
· Audit track
· ...

Ongoing monitoring and due diligence
The operational team can be contacted by the gallerist on an ad hoc basis to review screening alerts, perform ongoing due diligence, provide reporting etc...

An open path for outsourcing under the AML regulatory framework
In the European Union for instance, the modalities of due diligence activities outsourcing are described in a dedicated section of the AML Directive[18]. Under this framework, the obliged entities may rely on third parties to meet the customer due diligence requirements, if provided so by the local transpositions of the Directive. The main conditions of selection of the provider include the need to comply with the Directive's due diligence and record keeping requirements, and to be supervised by competent authorities[19] with regard to AML/CTF compliance.

Outsourcing KYC activities is becoming more frequent for the FSI—relying on expert solution providers and teams to support or handle parts of the due diligence process, building highly secured operating models, setting collaborative hubs to mutualize the efforts, are now solid options to limit the costs and maintain overtime or improve the overall quality of the due diligence.

What's in it for financial institutions?
- Monetization of AML/CTF services and amortization of investment in KYC solutions;
- Capture and retention of a lasting art professionals customer base; and
- Enrichment of the digital service offering.

What's in it for art professionals?
- Benefit from expert services and economies of scale, instead of facing the cost of implementation of AML solutions and processes alone;
- Minimized administrative burden, and accessible ad hoc advice and operational support all along the due diligence process; and
- Readily accessible information on the level of completion of due diligence obligations.

What's in it for collectors?
- Smoother buying and selling process, based on harmonized and rationalized procedures;
- Less back and forth exchanges to complete KYC files; and
- Safer environment to conduct business and to indulge in their passion for art.

18 See Directive (EU) 2015/849, Chapter II, Section 4, as amended by Directive (EU) 2018/843.
19 See Directive (EU) 2015/849, Chapter VI, Section 2, as amended by Directive (EU) 2018/843.

Part 3. Risk management, legal and regulatory developments

This part features three articles covering specific topics related to recent risk management, legal and regulatory developments.

Risk management: insurability and valuation of NFTs

The following article complements the content on NFTs covered in Section 1 p.61-63, Section 3 p.150, Section 7 p.258 & 271

Tolerância Zero
Luís Vasconcelos/Courtesy Unidade Infinita Projectos - 1999

Megan E. Noh
Partner - Co-chair, Art Law

Expert voices

Brave new media

Collector risks in relation to the insurability and valuation of NFTs

As high net worth collectors consider diversifying their art collections to include non-fungible tokens (NFTs) associated with digital artworks, there is little doubt that risk mitigation and potential leverage opportunities for this rapidly-expanding asset class will be top-of-mind.

To get a sense of this developing landscape, **Megan Noh**, Co-chair of Pryor Cashman LLP's Art Law Group and counsel to many sophisticated collectors spoke with **Ankur Kacker**, Senior Vice President of Specie & Digital Assets at Marsh, the largest global insurance broker and a leader in the fine art, jewelry, and specie categories; **Drew Watson**, Art Services Specialist at Bank of America Private Bank, which provides advisory and credit facility services to collectors; and **Claudia Hess**, CEO of Hess Art Advisory and a certified member of the Appraisers Association of America.

Megan Noh (MN)
Established collectors are accustomed to the availability of comprehensive insurance policies which address risks associated with traditional artworks such as paintings and sculptures. What risks are insurable in the context of NFTs, and what is not covered?

Ankur Kacker (AK)
Traditional fine art policies have all been for "all risks" of physical loss or damage. This is because insurers are able to determine risks which they may face in the physical art world. However, in the NFT or cryptocurrency world, it's not currently possible for insurers to do this, and therefore relevant policies provide "named peril" cover, including infidelity and third-party physical attacks on locations where the assets are stored.

In simplest terms, the product available to insure an NFT—meaning the token itself—will recognize as an insured "loss" a situation where an NFT owner has lost access to their token. A number of traditional exclusions apply, such as insurers being unable to cover "systematic" risks (in the context of NFTs, this would include risks associated with the failure of the blockchain or smart contract). Any risk which is too remote may also be excluded. For example, if a policyholder's customer is compelled under duress to send transactional instructions which the policyholder acts upon, the underwriter is unlikely to provide cover for loss resulting from the resulting diversion of the token to a bad actor's digital wallet.

MN
Some collectors have been surprised to learn that an NFT does not typically contain the digital artwork with which it's associated, but rather references that content, which is often stored in another location. Assuming that the token and referenced artwork are part of a package being acquired (which is not the case for all NFT sales), can collectors insure the digital artwork component?

AK
With respect to a digital artwork that is referenced by the token, but is separately stored, the market remains untested as to whether intellectual property insurance or cyber insurance could respond to a loss event.

MN
What criteria are underwriters taking into consideration in evaluating the availability of coverage, and how can policy-holders collaborate with the underwriter in minimizing risk?

AK
As this is a new space for the insurance market, insurers are being careful and selective both about the clients and the insured assets. Regarding the former, insurers are looking for best-in-class insureds with whom they can build relationships, establish a detailed mutual understanding of what the relevant policy covers, and from whom they can also learn about their business and/or investment in this asset class.

With respect to the latter, importantly, at this early stage in the development of NFT insurance products, insurers are unable to provide coverage unless the NFTs are stored with reputable third-party custodians. This is due to the high risk of moral hazard, and the fact that there is no global standard for NFT storage. As the industry matures, insurers are likely to be responsive to developments in security and storage protocols.

MN
What is the process for assigning a scheduled insurance value to an NFT?

AK
Valuation is extremely important in the insurance process, however at this stage there is no universally-recognized accreditation for third-party valuation of NFTs. Therefore, insurers can either rely on the purchase price of the NFT and provide insurance for the same—as is often done for newly-purchased traditional-media artworks—or they can agree to a different basis of valuation and charge the premium on that basis. There is no certainty that the value of the NFT will remain stable. Therefore, having an agreed-value policy can have its own pros and cons, whereas insuring an NFT based on purchase price is much more straightforward.

MN
Exploring a different question around tying value to NFTs, can this asset type be accepted by Bank of America to secure a credit facility?

Drew Watson (DW): Not at this time. Our loans focus on assets for which there is a stable secondary market track record and global depth of bidding. As the NFT market continues to develop, we'll be looking for confirmation that NFTs can sustain value independently of movement in cryptocurrencies, and also staying alert to regulatory developments. Another important area to be fleshed out through actual precedent is the ability of lenders to perfect security interests in NFTs used as loan collateral.

MN
For clients with diverse portfolios, how can Bank of America's Art Services team engage with the increasing curiosity in acquiring digital art cryptoassets?

DW: Bank of America understands that collectors buy art for intellectual, aesthetic, and social reasons (in addition to serving investment or other financial objectives), and we want to support our clients' collecting interests over the long-term. For that reason, we will continue to monitor the NFT space and learn more about the history, technology, and aesthetics driving value here—applying the same lens we use to assess other client acquisitions.

MN
Discussions with both insurance and banking professionals highlight the importance of developing reliable valuations for these assets. Has a professional consensus developed as to the appropriate methodology for Fair Market Value (FMV) appraisal of NFTs?

Claudia Hess (CH)
Not yet... we are in a similar place with NFTs as we were around 15 years ago when I was on the cutting edge of appraising 'new media' works and comparable sales were more scarce. In time, I'm expecting the secondary market for NFTs to expand and stabilize. However, the bottom line is that the IRS wants qualified appraisers to generate qualified appraisals. When we examine the definition of FMV, there is no restriction that appropriate comparables must come from the secondary market. Therefore, when performing such an appraisal, I would determine the correct market level (which is where my expertise is critical), and combine it with value attributes for that kind of work to generate an appraisal report that is compliant with the Uniform Standards of Professional Appraisal Practice.

MN
What would be appropriate value attributes for artworks associated with or linked to NFTs?

CH
For NFTs, in addition to the tried-and-true measurements of **quality** that we employ for traditional art, key value attributes may include the artist's:

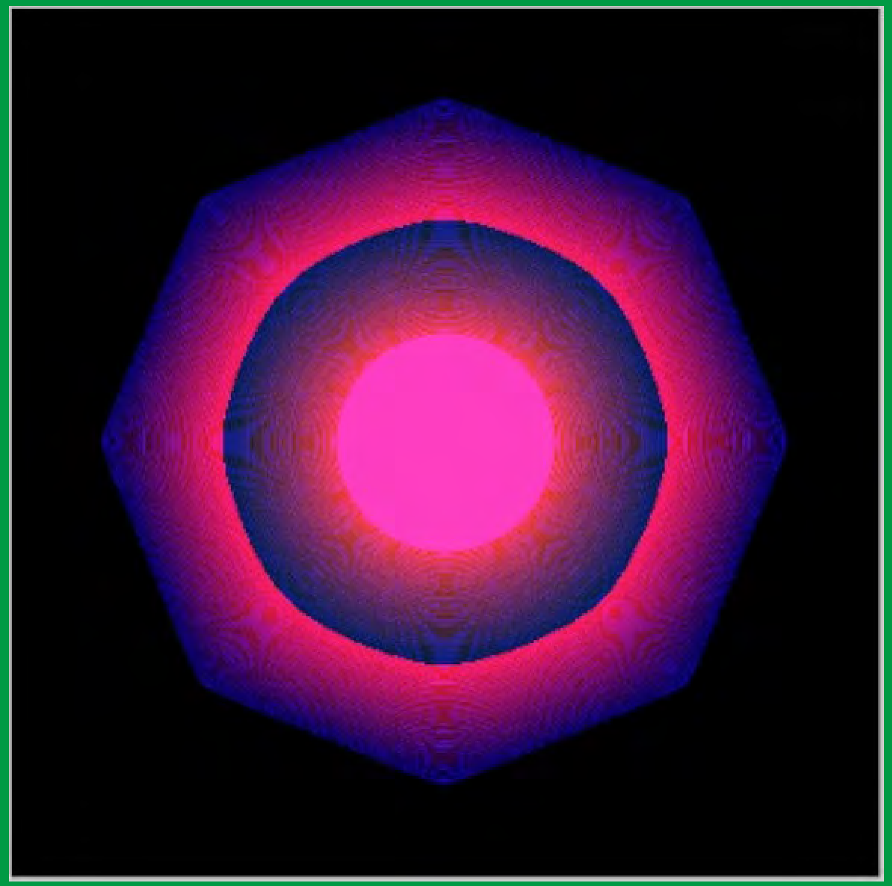
- **Role in the creation of this market** (works by pioneers in this realm could be considered more valuable, but not necessarily);
- Status as established or recognized on **social media;**
- Ability to drive sales; and
- Gallery and museum representation.

There is also market pushback with respect to the environmental costs of minting NFTs and the blockchains used to store and trade them, and that may continue to develop as a factor driving (or diminishing) value, as will the restrictions or permissions created by the smart contracts surrounding individual NFTs. A deep understanding of these kinds of works, their place in a rapidly evolving market, and their historical underpinnings is crucial.

We're now working with a larger and more complicated data set to determine FMV as of an effective date. But while value attributes may be different and more complex for these kinds of works, the basic rigor of collecting data and making comparisons to determine value remains the same.

As the comments from these industry professionals reveal, collectors entering the NFT space must be aware that insurance products, collateralization, and valuation are all nascent and likely to substantially evolve in coming years. In addition, critical legal questions—regarding taxation of cryptocurrency and tokens, appropriate anti-money-laundering and related diligence protocols, and applicability of securities regulations and copyright law—currently remain unanswered.

While it is an exciting time to be exploring investment in a new asset class, collectors should proceed with caution and an understanding that, in addition to the risk of unfavorable regulatory intervention, the security and fidelity risks to this property cannot currently be mitigated in the same manner as for traditional-media artworks, nor can digital works be as easily leveraged for liquidity needs. In this "brave new world" of rapidly-trading tokenized artworks, collectors will accordingly benefit from working with trusted professionals who can advise as to developments in their respective advisory disciplines.



Quantum, © Kevin McCoy, all rights reserved.

Originally minted on 3 May 2014 on the Namecoin blockchain, this work by pioneering media artist Kevin McCoy was the first to be associated with a blockchain certificate of ownership. It was preserved in 2021 on an ERC-721 non-fungible token minted by the artist, which was sold in Sotheby's Natively Digital auction on 10 June 2020 for US$1.47M.

Risk management: legal aspects related to the consignment of artworks in the United States

The following article complements the content on art and wealth protection covered in Section 3 p.129.

Plastic Party

Megan E. Noh
Partner - Co-chair, Art Law

Expert voices

Mitigating bankruptcy risk to artwork consignments in the United States

The onset of the global COVID-19 pandemic in early 2020 prompted significant change in the art market, including an abrupt shift to digital-only forms of engagement following the cancellation of in-person art fairs, gallery exhibitions and auctions. Compared with other sectors, the art market is seen as opaque; art transactions are often conducted privately and/or informally by commercial players, of which some of the largest and most influential are privately-held rather than publicly-traded.

Market uncertainty from pandemic-induced disruptions was exacerbated in March 2020, when news broke that prominent auction platform Paddle8 had sought Chapter 11 bankruptcy protection. This was compounded further in May 2020, when an independent audit of another leading auction house noted "substantial doubt" about the company's ability to continue as a going concern.

Against this backdrop, sophisticated consignors sought greater clarity on the potential impact of bankruptcy on their artwork consignments.

This was particularly the case for consignors with fiduciary obligations, such as trustees, executors, family office heads, and private bank art advisors.

In the United States, one of bankruptcy law's fundamental aims is to protect creditors from interests in a debtor's property that could not reasonably have been known to them: so-called "secret liens." If a consignor has not placed a consignee's creditors on notice of the former's interest in the consigned property and the consignee seeks bankruptcy protection, the consigned property may be deemed part of the bankruptcy estate. In this scenario, the consignor effectively loses title thereto and may be relegated to general creditor status, potentially limiting the consignor's recovery to a pro-rata distribution (typically at a pennies-onthe-dollar rate) following the liquidation of the bankruptcy estate assets.

The risk of this worst-case scenario can be mitigated under certain circumstances. **Fiduciary consignors are arguably obligated to explore common-law, statutory, and contractual protections for their consigned property,** the availability of which depends on several factors, including the type of consignor, the type of consignee, and the location of the consignment.

Common-law protections

- US bankruptcy courts apply state law to determine the nature and extent of a debtor's interest in property. Some states have developed relevant common law precedents pertaining specifically to auction consignments.
- For example, New York common law imposes an agent-principal relationship between auctioneers and their consignors, which continues through the property's sale until the auctioneer has remitted the net proceeds due to the consignor.[20] Under this precedent, if an auctioneer does not segregate consignor proceeds, the consignor may benefit from the court's imposition of a constructive trust on these funds. Similarly, an auctioneer's agency may be presumed under New Jersey law, resulting in sale proceeds being held in constructive trust for the consignor's benefit even when the parties' consignment contract is oral.[21]

20 In re Martin Fein & Co., 34 B.R. 333, 43 B.R. 623, 628 (Bankr. S.D.N.Y. 1983-1984).
21 McMakin v. Pine Bush Equip. Co., 242 B.R. 271, 277-78 (D.N.J. 1999).

- However, common-law precedent varies from state to state, and other precedents are less favorable to consignors than in New York and New Jersey. For example, bankruptcy courts applying Nebraska and Oregon law have found that the agent-principal relationship between an auctioneer and a consignor may end when the consigned property is sold, if the parties' written agreement does not require segregation of consignor proceeds.[22] In these cases, consignors are not entitled to constructive trusts and instead recover (if at all) alongside other general creditors.

Statutory protections

- For property consigned to certain art merchants, a consignor may be able to file a protective financing statement under Article 9 of the Uniform Commercial Code (the "UCC"). All 50 US states have adopted in some form this model act's provisions that apply to secured transactions involving personal property.
- When consigning artwork property to a gallery, a consignor should strongly consider filing a UCC-1 financing statement in the state where the gallery is formed.[23] The consignor may seek to ensure the priority of its interest by delivering the requisite notice to other relevant creditors before delivering the artwork into the custody of the gallery or its agents. Although there are relevant filing, notice and timing requirements, no contractual grant is needed to create such an Article 9 interest.
- By contrast, when the consignee is an auctioneer, the arrangement is expressly excluded from the relevant definition of "consignments" for which a financing statement is meant to be filed.
- Accordingly, auction consignors should consider the application of art-consignment-specific statutes. Over 30 states have enacted such laws, but they vary widely in terms of the type(s) of consignor to which they apply, and whether/how they supplant or modify a consignor's obligation to undertake UCC filings.
- In New York, the class of regulated "art merchants" expressly includes auctioneers. However, the class of consignors that benefit from the relevant statute is limited to artists consigning their own property. Such artworks and their proceeds are held in trust for the artist's benefit; as a result, the artist's interest is automatically protected from subordination to any claims of the consignee's creditors,[24] and the artist does not need to file a financing statement to notice this interest.
- However, for most fiduciary consignors, protections that benefit artist-consignors will not apply. States including Massachusetts and Michigan have enacted artwork consignment statutes that apply to a broader class of consignors. Other state laws, such as Florida's and New Jersey's, may require these consignors to notice the consignee's creditors by posting signage.[25] In other states, such as California and Washington, auctioneers have statutory obligations to undertake consignor trust accounting, or otherwise keep consignor funds separate from their own operational funds.[26]

Contractual protections

- If a consignor is not clearly entitled to file a UCC-1 financing statement under Section 9-102 and/or the consignment is not protected by applicable state statute—or if the consignment is to a foreign consignee in a jurisdiction without a comprehensive system for registering and/or noticing secured interests, such as the United Kingdom and certain European Union countries—the consignor should consider negotiating contractual protections.
- An auction consignor may consider requiring the auctioneer to acknowledge a precautionary purchase money security interest (PMSI) in the consigned property and the net proceeds due under the consignment agreement, under Section 9-103. Unlike the security interest recognized under Article 9 for consignors to non-auctioneer consignees, a transactional party can contractually grant a PMSI to recognize the other party's first-priority interest, including in non-consumer goods. Despite the lack of robust legal precedent on the treatment of precautionary PMSIs, 2020 and 2021 saw a marked increase in such filings, most undertaken by trust companies and other professional representatives of fiduciary consignors.
- Also, a consignor may seek to include provisions in the governing consignment agreement that confirms the consignee's express duty to hold and remit net proceeds as the consignor's agent, and/or reduces the period during which the consignee is permitted to hold these funds following a purchaser's payment.
- When doing business with gallery partners, a would-be consignor may prefer to structure the transaction as a sales agency rather than a consignment, which permits the gallery to broker sales **without** taking custody of the property.
- In addition, for consignments transacted as private sales, using a third-party escrow agent to receive and disburse sale proceeds may provide enhanced security.

Although the long-term impact of COVID-19 on the art market remains to be seen, the radical shifts of 2020 and 2021 do not appear to have triggered a wave of auction house or gallery bankruptcies. **Still, it is always prudent for fiduciaries to consider the impact of market conditions on their transactional risks and attempt to mitigate these risks in light of available legal and practical options.**

This will likely require fiduciaries to consult with transactional counsel experienced in navigating both the legal nuances that apply to different consignment contexts, and the art market's unique business norms and negotiation mechanics.

22 In re Rine & Rine Auctioneers, 74 F.3d 854, 859-60 and 74 F.3d 848 (8th Cir. 1996); In re Walker Indus. Auctioneers, 38 B.R. 8, 11-13 (Bankr. D. Or. 1983).
23 UCC-1 financing statements may also be filed to evidence certain arrangements that are not consignments, including (1) bailment of artwork for exhibition purposes, in which case the lender-bailor may notice its interest in the loaned work(s) as against the museum or other borrower-bailee's creditors, and (2) treatment of artwork as collateral securing a borrower's obligations to repay a credit facility extended by a bank or other lender.
24 NY ACA Section 12.01 1.(a)(ii)-(iii).
25 See Mass. Gen. Law Title XV, Ch. 104A, Section 4; Mich. Compiled Laws. Ann. Section 442.312; Fla. Stat. Ann. Section 686.502; N.J. Stat. Ann. Section 12A:2-330.
26 See Cal. Civ. Code, Title 2.95, Section 1812.600(j); Wash. Rev. Code, Title 18, Section 18.11.230.

Risk management: legal aspects related to the digitalization of art collections and the use of new technologies

The following article complements the content on collection management covered in Section 3 p.129, Section 7 p.261.

Wash and Go
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Expert voices

Collection management platforms

legal aspects concerning the digitalization of art collections and the use of new technologies

Art has crossed another boundary: it has become digital. Through digitalization, collectors can now experience new ways to enjoy their art collections, not only through the digital reproduction of their physical pieces of art, but also through the acquisition of the so called digital art, which has no physical counterpart to be hanged in the collector's living room.

For the purposes of our analysis, the role of platforms devoted to the management of art collections is twofold: on one hand, they allow private collectors to enjoy their collections irrespective to where they are safely kept. On the other hand, such platforms are a useful instrument to store documents that certify the authenticity of each piece of the collection, making them more accessible also to third interested parties, and allow to keep track of sales and rents. Those functions are carried out by leveraging on the potential of new technologies, such as Blockchain and augmented reality.

Each one of the above mentioned functions have legal aspects and issues that have to be taken into account.

Collection management platforms as repository of art works
It is not uncommon that collection management platforms are used by collectors as a repository for their works of art: this kind of use entails that the work of art is transformed in a digital form in order for it to be reproduced in the repository of the platform.

Under a legal standpoint, to reproduce a work of art through a digital medium, the author's authorization may be necessary. In fact, contemporary art being the work of a living artist or of an artist whose death occurred less than 70 years ago is protected by copyright. In order to reproduce a piece of art protected by copyright, the authorization of the right holder is needed. Thus, when digitalizing entire collections, it is very important to check whether by reproducing a series of artworks, any copyright infringement may occur, depending on the applicable law, based on the author's nationality and the country of origin of the work.

While it may be overlooked, it is worth mentioning that, in order to lawfully digitalize a work of art, the authorization of the current owner is as important as that of the artist.

The above is true assuming a static reproduction of the work of art on the pages of the collection management platform also in case such reproduction is made in the personal account of the art collector; but what if, in addition to be two-dimensionally reproduced on a web page, the art management platform allows reproduction of the work on a tri-dimensional fashion? Nowadays, several platforms use augmented reality to allow their users to enjoy art as if it were hung in their living room. Even though the process of "digitalization" of the physical work of art in its three-dimensional and two-dimensional form seems similar, this is not the case. While the reproduction of the work of art in a two-dimensional form is made, more often than not, by polishing a picture of the work of art taken with a smartphone or a camera, tri-dimensional reproduction is more complex.

Under a technical point of view, the creation of a tri-dimensional copy of a work of art requires for it to be reworked through a software that, at the bare minimum, add layers on the original picture. Such kind of reworks and reproduction may need specific authorization from the artist, given the intense editing process. This is particularly true when the copyright legislation applicable on the basis of the artist's nationality acknowledges protection to the moral rights of artists, such as in Italy or France.

Collection management platforms as database

Each work of art is accompanied by a number of documents that are needed to prove its authenticity; moreover, such documents allow owners to track its various changes of ownership, and leases to museums and art institutions. Collection management platforms often offer a useful tool to collect all such data and documents and to track further changes in ownership or leases. In this respect, Blockchain is often considered one of the most trustworthy technology to absolve this task. Indeed, any transaction that is recorded on a Blockchain receives a date and hour stamp and is immutable over time.

While Blockchain certainly is an interesting technology, which may serve the purpose of recording transactions of works of art, it is worth noting that, under a legal standpoint, Blockchain does not in any way warrants for the authenticity of the documents that are recorded on it. Therefore, Blockchain is not, in itself, able to certify the authenticity of the artwork. In this respect, as far as works protected by copyright are concerned, it is worth noting that the author is the only subject entitled by law to claim or deny the authenticity of his/her work of art.

What is certainly true is that art collection management platforms collect a huge amount of data of various type. In addition to personal data (on which please see below) of the current and prior owners, which are often well-known personalities, each work of art carries with it data concerning, for example, their value, the number of times that one specific artwork has been traded or leased, to which institution, for how long or where. Those kind of data, if properly collected and organised, could be protected in Europe under the EU Directive 96/9/EC. According to such Directive, "collection of independent works, data or other materials arranged in a systematic or methodical way"[27] can enjoy protection under copyright law, if arranged or selected in a way that shows the intellectual creation of its author, or through the sui generis right of the author of the database. Considering the case of art collection management platforms, it is more likely that the database eventually created by collecting and organising the data concerning the artworks managed through such platforms would be protected through the sui generis right, that rewards the investments made by the owner of the database in building and organising it. Protection granted by the sui generis right lasts for 15 years starting the 1st of January of the year following the date of completion of the database.

Collection management platforms and personal data

As mentioned in the previous paragraph, data collected and stored by art collection management platforms may be various in kind and nature. For sure, among such data, some of them can be qualified as "personal data" regulated under the Regulation (EU) 2016/679 ("GDPR"). In this respect, "personal data" are defined as that information relating to an identified or identifiable natural person[28]. In order to dutifully collect and process such personal data, collection management platforms need to properly assess and manage data protection risks, taking into account the nature and the specific circumstances of the processing of personal data, in order to identify the most appropriate security measures for the assessed risk.

In particular, it is important that the platforms are aware at all stages where those data are stored. Indeed, if the platform is cloud-based it is not unlikely that the data are, in whole or in part, stored in servers owned by the cloud provider that are not located in the EU but rather in the US. For data protection purposes, the US legislation on data protection is not considered by EU as granting the same level of protection and safeguard as the EU legislation, therefore specific information and consents have to be, respectively, provided to and acquired by the data subjects (i.e., the collection management platform's clients).

Many other steps may be appropriate and necessary to fully comply with GDPR, which should not be overlooked considering that EU legislation on data protection provides for significant fines - up to EUR 20 million or 4% of the previous year's total group annual turnover – in case of infringement.

While digitalization of artworks can open new possibilities for art collectors and enthusiasts and art collection management platforms can play a big role in it, it is important to remember that digitalization is not inconsequential under a legal perspective. Dealing with artists' intellectual property rights, collection management platforms should be particularly cautious in obtaining the necessary authorizations from all stakeholders, in addition to employ technological tools, being aware of either their potential and their risks. Towards their clients, collection management platforms should carefully consider the data they are collecting and how are they doing so in order to grant the best possible experience to their users, while complying with the applicable law.

27 Art. 1.2 of the Directive 96/9/EC
28 Art. 4.1 of the GDPR.

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