

Art & Finance Report 2014.



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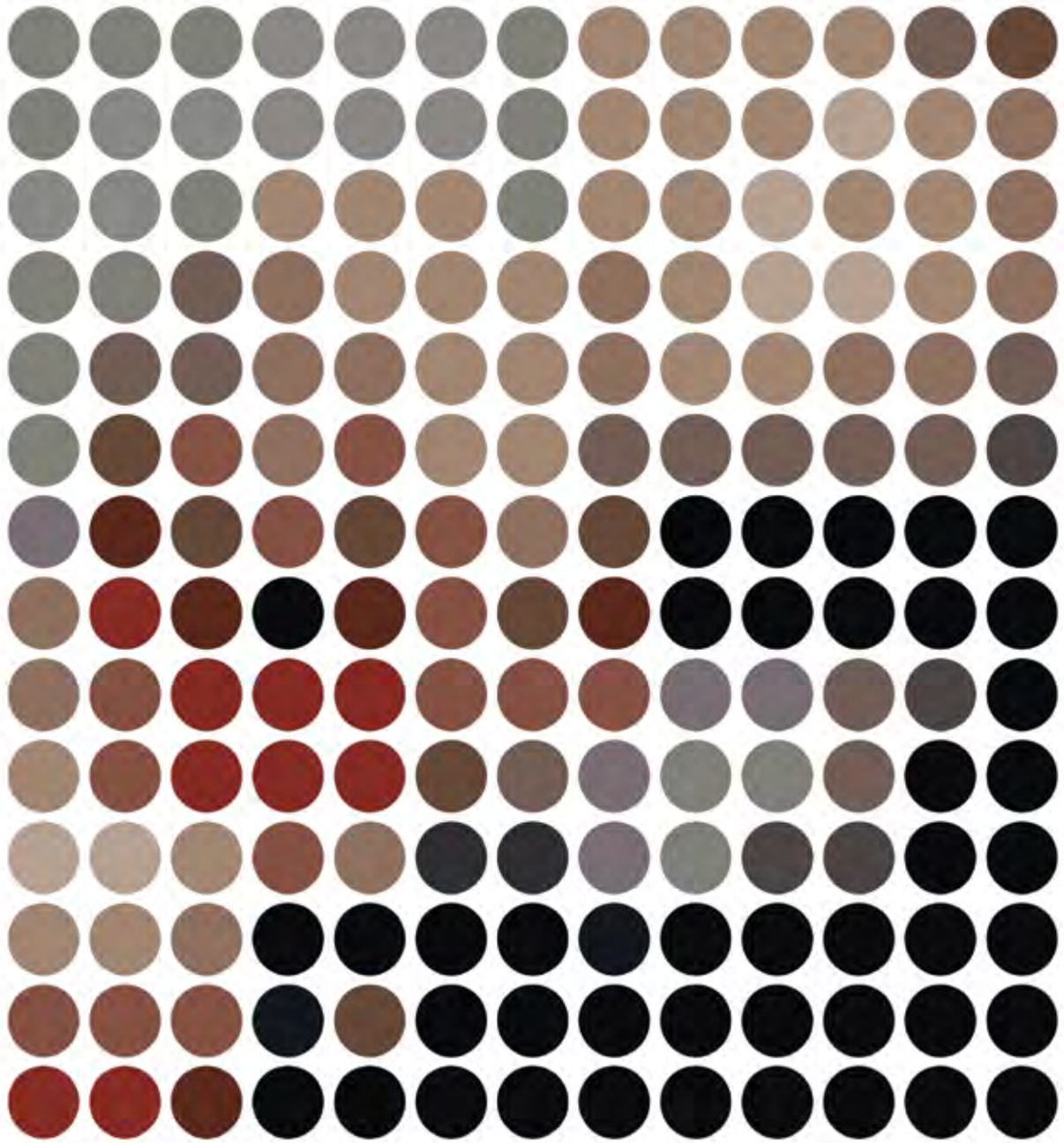
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Foreword



Adriano Picinati di Torcello
Director - Art & Finance
Initiative Coordinator
Deloitte Luxembourg



Anders Petterson
Managing Director
ArtTactic
London

Deloitte Luxembourg and ArtTactic are pleased to present the 3rd edition of the Art & Finance Report.

The two first editions of the Art & Finance Report (2011 and 2013) helped us to establish a forum and platform for monitoring emerging trends and attitudes around important issues related to the Art & Finance industry. In this year's report we have taken this one step further and invited 11 key opinion formers, representing major market stakeholders, to express their views on what they believe are opportunities and challenges for the Art & Finance industry, now and in the future.

As the Art & Finance industry is becoming increasingly global, we are also delighted to announce that what started as a local initiative in Luxembourg in 2011 has now become a truly global Deloitte initiative, and we are proud to announce new partnerships with Deloitte US, Deloitte China, Deloitte Singapore, Deloitte Italy, Deloitte Germany and Deloitte Austria.

Based on the overwhelmingly positive response and feedback from the wealth management community, art professionals and art collectors in producing this report, we are delighted to say that the report is more than just a companion on a journey: it is becoming a destination in itself, a virtual meeting point of diverging and converging opinions that we feel will become very valuable in shaping the future of the Art & Finance industry.

Once again, we would like to express our most sincere thanks to all the individuals and institutions that contributed to this report. Without their support, this report would not have been possible.

Deloitte US launches an Art & Finance practice

It is our pleasure to announce the establishment of our US Art & Finance Group. Located at the centre of high art and high finance at 30 Rockefeller Plaza in New York City, we have a diverse team of consulting, tax, and business intelligence professionals inspired by the new challenges and opportunities brought about by the rapid maturation of the international art market.

Our mission is simple: to deliver creative solutions to the individuals and institutions at the crossroads of business, finance and the arts. We offer collectors, art-related businesses and cultural institutions an entry into Deloitte's traditional tax, consulting, and business intelligence services and we help financial institutions incorporate fine art and collectibles into their advisory models.

Our team has a great passion for art, and we hold in high esteem the cultural subtleties that make up the art world's distinct eco-system. But we also see incredible opportunities for innovation and change. From the growth of art as a capital asset to new sources of market liquidity and growing demand for art banking, the worlds of art and finance continue to converge.

Together with Deloitte Luxembourg and our global network of specialists, we look forward to working with you. These are exciting times indeed.

Service area	Art & Finance overview	Core offerings	Clients
Consulting	We combine our knowledge of the art market with our experience of delivering strategy and operations advice to companies and governments around the world	<ul style="list-style-type: none"> - Strategy and operations - Digital strategy - Customer experience - Cost and revenue strategies - Education and learning 	<ul style="list-style-type: none"> - Private banks - Hedge funds - Art-related businesses - Museums - Cultural institutions - Public sector
Tax	We help clients structure and manage their art collections in a tax-efficient manner	<ul style="list-style-type: none"> - Gift and estate planning - Philanthropy and charitable planning - Import/export strategies - US sales & use tax - VAT and GST tax - Code 1031 exchanges 	<ul style="list-style-type: none"> - Family offices - Asset managers - Individual collectors - Galleries - Museums
Business Intelligence	We help art market professionals deal with the complex mix of counterparty, legal, and regulatory risks	<ul style="list-style-type: none"> - Anti-money laundering services - Provenance research - Fraud and investigations - Counterparty vetting - Forensics services - Know-your-customer (KYC) 	<ul style="list-style-type: none"> - Art secured lenders - Individual collectors - Auction houses - Freeports - Art funds



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Introduction

In last year's report we identified an increasing sense of convergence in motivations among key stakeholders in the art market and in the wealth management community regarding art as an asset class.

Based on the findings of this report, the wealth management industry is clearly taking a more strategic view on art as an asset class and how it might be used as a tool to build stronger and deeper relationships with clients, in an increasingly competitive marketplace.

This year's findings suggest that art buyers and collectors are increasingly acquiring art and collectibles from an investment viewpoint (76% said so this year, compared with 53% in 2012), which will most likely increase the need and demand for professional and wealth management services relating to the management and planning, preservation, leverage and enhancement of art and collectible assets.

It is particularly interesting to see that the wealth management community is already responding to this new demand, with 88% of the family offices and 64% of the private banks surveyed said that estate planning around art and collectibles is a strategic focus in the coming 12 months. This highlights that art related tax, estate and succession planning issues are increasingly becoming a hot agenda topic. Also, 50% of the family offices surveyed stated that one of the most important motivations for including art and collectibles in their service offering was due to the potential role it could play in a balanced portfolio and asset diversification strategy.

Methodology and limitations

Deloitte Luxembourg and ArtTactic conducted the research for this report between April and June 2014. We surveyed 35 private banks (up from 30 in 2012), mainly in Europe, and 14 family offices, mainly in the United States. The addition of family offices to the

overall sample was new this year, and reflects our belief that family offices will play an increasingly important role in the Art & Finance industry. Our report again focused on monitoring the perceptions, motivations and actions related to the development of art as an asset class within the global wealth management community. Due to the broadening of the sample by including 14 family offices, we have highlighted the specific findings of this group where we felt it had an impact on the interpretation of the overall findings.

As in the previous year, we also conducted research among other important stakeholders in the Art & Finance market, such as art collectors and art professionals (galleries, auction houses and art advisors). A total of 122 art professionals (up from 112 in 2012) and 90 major art collectors (up from 81 in 2012) from Europe, the United States, the Middle East, Latin America and Asia were surveyed on a variety of topics relating to art as an asset class, covering their motivations, current and future involvement, and the challenges and opportunities.

Section 1 of the report includes findings (market outlook for different art markets) based on qualitative art market confidence surveys that ArtTactic sent out to 360 international art collectors, art advisors, galleries and auction houses between May 2014 and July 2014. This section also includes auction data analysis of different modern and contemporary art markets, and is predominantly based on data from Sotheby's and Christie's, but will also occasionally include other auction houses where these represent a major share of the market.

In order to provide a market context for the survey findings, we have provided a broad, international overview of recent developments across various modern and contemporary art collecting categories. Most of the data is collected from Sotheby's and Christie's, as they cover the majority of the modern and contemporary art-collecting categories covered in this section, although certain regional markets such as China, India and Russia also include auction data from other leading auction houses. This year, we have added two new markets, South East Asia and Africa, to better reflect the increasingly global nature of the art market.

We have estimated the size of the global art fund industry, combining data and information from interviews with US and European art funds, as well as public records on art investment trusts and art funds in China. As more information has been released regarding the art trust market in China, we updated the figures for the period between 2011 and June 2014, which were significantly higher than the estimates we used in the previous two editions of the Art & Finance Report.

Like last year, we have also significantly expanded our coverage of the emergence of digital technology and the online art market, and the potential impact it could have on the Art & Finance industry in terms of addressing key challenges such as transparency, liquidity and valuation.

New this year is Section 5, which is dedicated to different legal issues that are already impacting the development of the Art & Finance industry and could have a significant effect going forward. We are delighted to have the contribution of leading lawyers in this field such as **Catherine Cathiard, Jean-Philippe Drescher, Karen Sanig, Steven Schindler and Pierre Valentin.**

We are also delighted to be able to publish a series of interviews with key figures in the Art & Finance industry, as well as venture capitalists and investors in the online art market and in technologies that can facilitate a more efficient and transparent art market. Interviewees include:

- **Hala Khayat**, Christie's specialist and Head of Modern and Contemporary Arab and Iranian Art sales
- **Georgina Hepbourne-Scott**, Art Management Division Head of the Stonehage Group
- **Paul Aitken**, CEO and founder of borro.com
- **Harco van den Oever**, founder of Overstone Art Services
- **Dr. Christian G. Nagel**, partner and co-founder of Earlybird Venture Capital
- **Christian Leybold**, General Partner at e-ventures

We also want to thank Chen Bao and Audrey Limier from Deloitte Luxembourg for their contribution on the Chinese and Brazilian art markets, as well Zhang Yi, an independent consultant on the Chinese art market. A special thank you also to Professors Michael Moses and Jianping Mei for their ongoing support.

Deloitte Luxembourg and ArtTactic recognise that the findings are indicative and acknowledge the limitations of these findings; however, we believe that the results reflect a broad representation of the perceptions and attitudes that exist in the global wealth management and art communities.

Key findings

Based on the findings of this third edition, although it is still relatively early days, we continue to see the gradual positive development of the Art & Finance industry, on the back of global art market growth and a global increase in wealth.

Art and wealth management is currently the area where we see the strongest interest, boosted by the rapid rise in the value of art and the increasing accumulation of art and collectible wealth.

The art investment fund market remains a niche sector of the Art & Finance industry, and although a few successful models have emerged, it is still too soon to talk about a fully-fledged art investment fund market. Based on the motivations of wealthy individuals for buying and investing in art, future art fund models might have to be adapted to create demand for these types of investment products.

Technology-driven and online art businesses have a clear potential to support the emergence of an Art & Finance industry, particularly through increased liquidity, lower transaction costs and more transparency. However, a better regulatory framework might be necessary to grow the Art & Finance market going forward.

Section 1: The art market

- **Wealth creation drives art market growth:** the growth in sales of art and collectibles has been fuelled by the globalisation of the art market and an exceptional increase in wealth, especially in new growth markets such as Asia, the Middle East and Latin America
- **An increasing number of UHNWIs are buying and investing in art and collectibles:** global art buying trends indicate a continuous accumulation of wealth in art and collectibles, and an opportunity for wealth managers to provide art and wealth management services, such as wealth protection, estate planning, leverage and value enhancement. According to a Barclays report¹ published in 2012, art and collectible holdings vary between region and type of assets, but on average represented 9% of the net assets of wealthy individuals
- **The first half of 2014 signals another record year for the art auction market:** this year is set to become another positive one for the art auction market, with the six-month auction figures from Christie's and Sotheby's already accounting for 88% of the 2013 total
- **There is a positive art market outlook for the first half of 2015:** the experts' outlook for the majority of the modern and contemporary art markets is neutral to positive for the next 12 months

¹ Barclays Wealth Insights report: Profit or Pleasure? (2012)

- **United States and Europe:** there is a positive outlook for art wealth management services in the United States and Europe, as art market values are moving towards an all-time high. Wealth managers expect their clients to increase their total wealth allocated to art, providing a fertile ground for Art & Finance-related services aimed at protecting, leveraging and enhancing art and collectibles wealth
- **China:** the Art & Finance industry in China is likely to grow as the Chinese government has adopted a proactive role in creating closer cooperation between the financial and cultural sectors
- **Middle East:** despite geopolitical uncertainty in the region, expansion in art and museum infrastructure, together with rapid growth in UHNWIs and their significant allocation of wealth to treasure assets, indicates that this region is likely to play an important part in the global and regional art and collectibles markets in the future
- **India:** the Indian art investment fund market took a hit in 2009, which significantly dented confidence in art as an asset class among Indian investors. However, the improved outlook for the Indian art market and an increase in prices for modern Indian art should lead collectors and investors to revisit this market in the near future
- **Latin America:** the Latin American art market remains the second most attractive market in which to buy art over the next 12 months according to the experts, and signals future growth in art and collectible assets and increasing opportunities for the emergence of an Art & Finance industry in this region
- **South East Asia:** rapid art market growth and regional growth in UHNWI population and wealth, combined with Singapore's position as a financial and art market hub, point to significant opportunities to grow an Art & Finance market in South East Asia
- **Russia:** auction sales of modern and contemporary Russian art in the first half of 2014 show signs of renewed confidence in this market and the advantages of art as a tangible and movable asset
- **Africa:** African art market and UHNWI growth have created a new generation of African collectors with an interest in art as an asset class and opens up the possibilities for a future Art & Finance industry as the African art market matures



Section 2: Art and wealth management survey

- **As competition in the global wealth management industry increases**, there is an increasing focus on client-centric value propositions, including art-related services for UHNWIs, which could be one way to provide more client-centric services
- **The rapid rise in the value of art and the continued accumulation of wealth in art and collectibles mean that** wealth managers need to take a more holistic view of their clients' overall asset portfolio
- **Passion versus investment:** 76% of art collectors are buying art for collecting purposes, but with an investment view (up from 53% in 2012). This implies that the investment aspect of art is something that collectors are increasingly concerned about
- **Art and wealth management:** an increasing number of art professionals (76%) and art collectors (62%) think that art and collectibles should be integrated into the wealth management offering, while 53% of wealth managers and 57% family offices strongly believe there is a role for art in wealth management
- **Higher awareness of art as an asset class:** a higher proportion of wealth managers is monitoring developments linked to art as an asset class
- **The Deloitte/ArtTactic Art & Finance Future Indicator** has increased by 61% versus 2012 and now stands at 39, which signals that the wealth management community is taking a more strategic view with regard to art-related services in the next 12 months compared with 2012
- **Increasing demand for art-related services:** wealth managers say that their clients are increasingly asking for help with art-related issues, but wealth managers need to listen to their clients' needs to develop tailored art and wealth management offerings
- **Wealth managers can provide clients with exclusive access to the art world:** the social value (status and access) associated with buying art is a strong motivation for art collectors, and presents an opportunity for wealth managers to provide their clients with access to this exclusive 'club'
- **There will be a focus on art and wealth management in 2015:** wealth managers will focus on three art-related financial services in the next 12 months—art and estate planning, art and philanthropy and art secured lending
- **More banks are offering art secured lending:** 36% of the private banks surveyed said that they offer art secured lending and art financing services; this was up from previous years
- **Art insurance products could help expand the art secured lending market:** a range of new art insurance products could potentially help the art secured lending market to reach £15-20 billion per annum².
- **Family offices see art as a diversification tool:** family offices consider art and collectibles to have an important role in a balanced portfolio and asset diversification strategy
- **Lack of regulation remains a key obstacle:** the overriding challenge for the development of the Art & Finance industry remains the unregulated nature of the art market, combined with a lack of transparency and difficulties in sourcing and finding the right art-related expertise
- **Freeports as competence clusters for the Art & Finance market:** freeports specialising in tangible valuable goods offer the possibility for wealth managers to develop regional competence centres for these assets. This is especially the case with Luxembourg, Singapore and Switzerland

² Robertson Taylor W&P Longreach estimated today's art lending market to be in the region of £6 billion per annum, but with the potential to reach £15-£20 billion per annum.



Section 3: Art as an investment

- **The Mei Moses® World All Art Index (All Art-W)** reported a negative performance between 2012 and 2013
- **Ten-year art performance:** the compound annual return for the World All Art Index was 7% between 2003 and 2013, slightly below the S&P500 total return of 7.4%. Post-war and contemporary art as well as traditional Chinese works of art delivered compound annual returns of 10.5% and 14.9% respectively
- **The global art investment fund industry is concentrated in existing art funds that can demonstrate a track record.** The global art investment fund market was estimated (conservatively) to be worth US\$1.26 billion in the first half of 2014, down from US\$2.13 billion in 2012, driven by a significant unwinding of art investment funds and trusts in China. In 2014, an estimated 72 art funds and art investment trusts were in operation, and 55 of these were in China
- **Tougher regulations on art investment products:** France's AMF (French Financial Markets Authority) now regulates art funds, and the Chinese government has introduced stricter regulations on trusts
- **China's art investment boom slowed in 2013:** China's art fund and art investment trust market is rapidly slowing down, with an estimated \$169 million raised in 2013, compared with \$529 million in 2012. Stricter government regulations on the Chinese shadow-banking market has triggered a decline in art investment trusts
- **Confidence in the future of the art fund industry is mixed:** the majority of art professionals and art collectors believe the art fund industry will expand in the next two to three years, but wealth managers are still very cautious, as issues such as due diligence, lack of liquidity, valuation, lack of track records and an unregulated market have a negative effect on these types of investment products

Art and wealth management is currently the area where we see the strongest interest, boosted by the rapid rise in the value of art and the increasing accumulation of art and collectibles wealth

- **Art funds could become service platforms for the wealth management industry:** art investment funds have the potential to become one-stop art service platforms for the wealth management industry, offering vetted and tested expertise, transparent and professional reporting, and operation within a regulatory framework
- **Art collectors see the benefit of art investment funds as a diversification tool:** a large majority of collectors see the potential of art funds as a way of gaining broader exposure to the art market
- **Art professionals see art funds as potential 'door openers' for new art collectors and investors to enter the art market:** art professionals say that an art fund could provide access to experts and knowledge that buyers do not currently have

Section 4: The online art industry

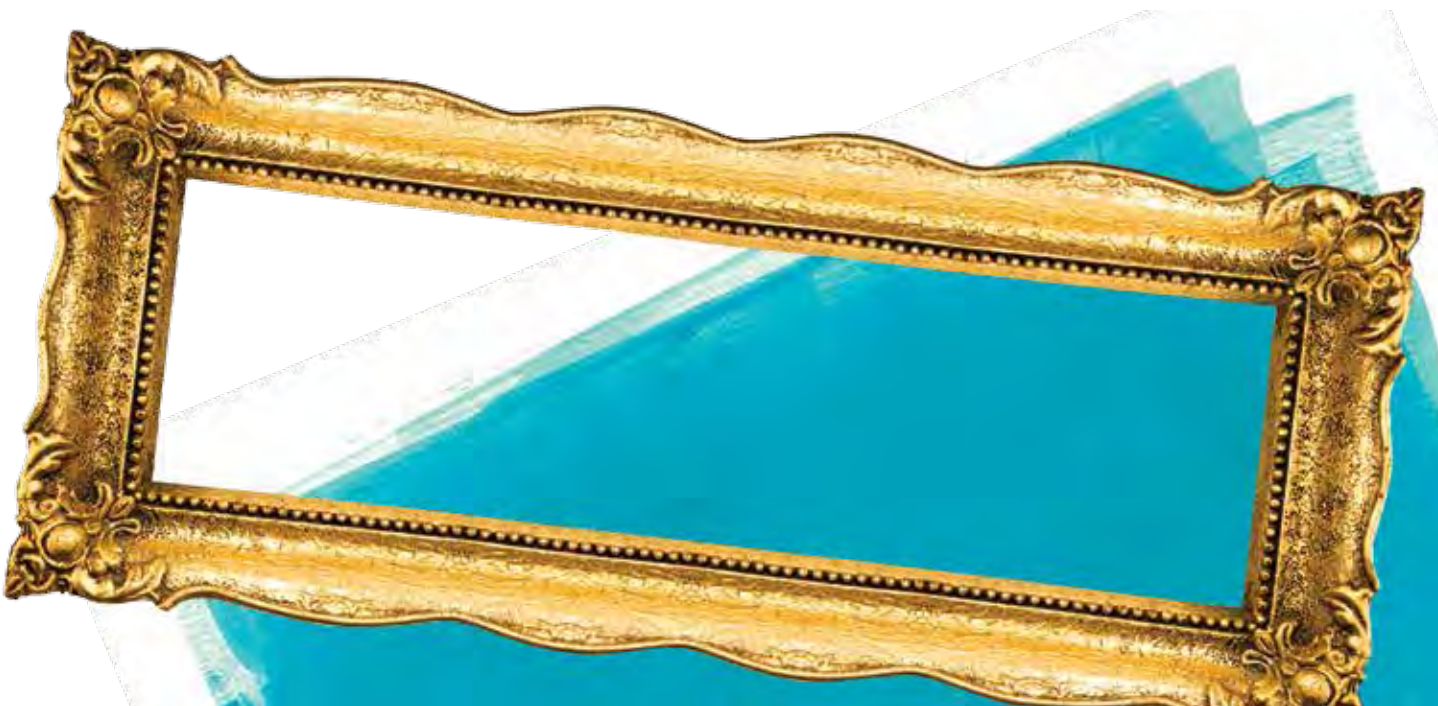
- **M&A activity is likely to pick up as the online industry matures:** with the number of online art marketplaces and auctions increasing, consolidation can be expected to take place in the future, opening up opportunities around art and corporate finance
- **Larger online art marketplaces are likely to increase liquidity,** broaden the collector base, reduce transaction costs and increase transparency, which could encourage more people to look at art as an asset class
- **Opportunities in data, research and analysis should arise** as the art market is increasingly looking for better tools to make informed decisions and help address some of the concerns that wealth managers have when it comes to transparency and the lack of information and research tools in the art market
- **Art professionals and collectors see opportunities for online art education:** 67% of collectors and 63% of art professionals see potential for businesses focusing on art education
- **Disintermediation shows untapped potential:** collectors and art professionals both indicated increased confidence in the future of consumer-to-consumer and dealer-to-dealer sales platforms for the online art industry
- **Online art and collectibles auctions expected to see rapid growth:** 77% of art collectors and 69% of art professionals believe that the online art auction market will become one of the winning business models

- **eBay is to enter the higher end of the art and collectibles market by partnering with Sotheby's:** a further boost to the online art auction market has come from e-commerce giant eBay, which announced in July 2014 that it has agreed to partner again with Sotheby's
- **Building trust:** developing online brands and companies that can instil a high degree of trust will be the key challenge for any online player in the art world

Technology-driven and online art businesses have a clear potential to support the emergence of an Art & Finance industry, particularly through increased liquidity, lower transaction costs and more transparency

Section 5: Legal aspects

- **Legal expectations of an asset class:** the art market falls short of meeting the legal expectations of an asset class, particularly in terms of regulatory structure, information availability and clear title
- **Fiduciary responsibilities of art advisors:** an art market downturn is likely to raise questions on the legally vague fiduciary responsibilities of new intermediaries, such as art advisors
- **The AMF (French Financial Markets Authority)** regulates art and collectible investment products to protect investors from misleading information
- **Auction guarantees** raise questions on transparency and market distortion
- **Authentication:** the absence of clear authentication processes and authentication bodies can make the verification of genuine art extremely difficult to establish
- **Protection for art authenticators** against lawsuits is necessary for the art market to operate properly. A bill was introduced recently in New York State to protect art authenticators against frivolous lawsuits brought against them for issuing opinions as to an artwork's authenticity
- **Due diligence and carefully drafted warranties** in sale and purchase agreements of artworks can offer some level of protection
- **Art secured lending and allowing the borrower to keep possession of artworks:** in the United States, lenders against art typically allow the borrower to keep possession of the art collateral as they register its security interest under the Uniform Commercial Code (UCC). Several continental European countries have also introduced a register of charges against chattels such as France, Spain and Belgium, but in most other European countries, the lender cannot register a charge against art assets, particularly if the borrower is a private collector
- **Insurance products are being developed** to protect the lender against the risks associated with leaving art collateral in the borrower's possession. Some of these insurance products are designed to give the lender the same protection as a validly perfected charge against the art collateral



Priorities

1. Freeports have the potential to become important hubs for the art and wealth management industry:

with the increasingly global nature of the art market and the art trade, the demand for storage facilities and duty-free zones is likely to increase. 28% of both the art collectors and art professionals surveyed said they had already used or had a relationship with a freeport provider, and 43% of the art professionals said that their clients were likely to use a freeport facility in the future, versus 42% of the art collectors who said they were likely to use such a facility.

The wealth management industry is waking up to the opportunities associated with freeports, with 41% of the private banks surveyed saying they were likely to create a new or expand on an existing art and collectibles service offer as a result of the creation of freeports. It is paramount that the freeport providers and wealth management community work closely together to build an attractive service offering that covers art lending, art advisory services, collection management and tax and legal services related to art and collectibles.

2. Wealth managers and art professionals can provide access to exclusive social networks:

the social value³ of buying art is a key aspect for art collectors. 61% said this was a key motivation, up from 60% in 2012, while an even higher 72% of art professionals believed this was a key motivation for their clients (up from 62% in 2012).

There is no doubt that the social value and status linked to art collecting is attractive for many HNWIs. Invitations to art fair VIP openings around the world and gallery and museum dinners for collectors and patrons provide members with an exclusive network, giving access to the artists themselves, but also to other business people and celebrities. Deutsche Bank's sponsorship of the Frieze art fair, the UBS sponsorship of Art Basel and Royal Bank of Canada's sponsorship of Masterpiece highlights the value that such events can bring to their clients, not for the financial benefits, but in terms of the emotional and social value these events provide.

The wealth management industry should strategically think about how to create and provide services that offer access to exclusive events and networks for their clients, and how to build partnerships with art professionals to deliver this.

For the art fund industry to evolve, a rethink of the current art fund model is probably required, which needs to incorporate the reasons why art investors buy art in the first place

³ We define social value as the status of belonging to an exclusive group of people and the status associated with buying and collecting art

3. The art fund industry may have to rethink its current model:

art funds have seen limited growth in recent years, and the survey shows that only 8% of wealth managers are currently offering clients advice on investing in art investment funds, down from 26% in 2012. On the other hand, art collectors do see the benefit of art investment funds as a diversification tool and a way of gaining broader exposure to the art market (67% of collectors surveyed said so in 2014). 61% of collectors also said that art funds could offer professional management with strong investment discipline and a focus on value.

Art professionals see art funds as potential ‘door openers’ for new art collectors/investors to enter the art market, and 68% of art professionals said that an art fund could provide access to experts and expertise that buyers do not currently have. There seems to be a mismatch between what clients/potential investors are looking for and what the art fund industry is offering. For the art fund industry to evolve, a rethink of the current art fund model is probably required, which needs to incorporate the reasons why art collectors buy art in the first place. With 78% of art collectors citing emotional factors as key to buying art, and 61% saying that the social value aspect is very important—future art fund models should more effectively incorporate these non-financial elements into their strategy. Art fund models built around a boutique-style art and wealth management offering could become a model for future art investment funds, and have the potential of becoming one-stop art service platforms for the wealth management industry. The art funds’ audited track records and regulatory compliance make them more suited to service an increasingly regulated financial industry.



4. Continuing to build closer relationships between art professionals and the wealth management community could be an effective way to grow the Art & Finance industry:

this was a trend we identified in the Art & Finance Report 2013, and remains a key priority for the Art & Finance market to develop further. There are already initiatives such as PAIAM (Professional Advisors to the International Art Market) in London, which opened its membership to international advisors in February 2013. PAIAM is a networking association for professionals supporting the global art industry in terms of legal, consulting, tax, financial, insurance, logistics, research, recruitment and communication services. A closer collaboration between different interest organisations in the Art & Finance industry is needed.

A certain level of regulation in the art market would not only be helpful for the Art & Finance industry, but also for the art market as a whole

5. The art market requires a better regulatory framework: in section five of this report, Steven Schindler makes the point that the art market currently falls short of meeting the legal expectations of an asset class, with clear weaknesses in terms of regulatory structure, information availability and clear title. He also raises another important issue regarding the legally vague fiduciary responsibilities of new intermediaries, such as art advisors. He expects—as more investments start to go wrong—that we will see cases brought to clarify the fiduciary responsibilities of art market intermediaries who don't necessarily represent only the buyer or only the seller. As regulation in the art market remains a considerable hurdle (83% of wealth managers surveyed said this was a key challenge), self-regulation remains key, and it is important that the wealth management industry and associations in the art market (representing appraisers, auctions, dealers, galleries and other professionals) work together more closely, so that the wealth management industry can leverage the skills and knowledge of qualified and vetted art professionals. A certain level of regulation in the art market would not only be helpful for the Art & Finance industry, but also for the art market as a whole.



6. Authenticity issues and defective title raise the need for an international art market register and traceability of artworks: existing problems associated with authenticity (see Steven Schindler and Karen Sanig, Section 5) are likely to become even more of a challenge in the art market in the future. Record prices may encourage criminal activity and result in an increase in fakes and forgeries. With many artist authentication bodies no longer providing authenticity certificates due to the risk of lawsuits, a neutral and credible art register that can trace the origin of artworks, supported by all the key players in the art market, such as auction houses, dealers, art historians, museums and artist foundations, should be a priority going forward. Without a concerted effort to protect the market against fakes, confidence in art as an asset class could evaporate.

7. New tools created by technology-driven companies and online marketplaces will play an increasingly important role in the Art & Finance industry: technology and the advent of an increasingly global art market present new opportunities for art and collectibles in a wealth management context. Firstly, online art businesses are perceived as important in broadening the existing collector base and improving market liquidity, transparency, education and the dissemination of market information. Secondly, online art businesses can help improve the valuation of art and collectibles. 78% of the wealth managers surveyed cite valuation as a key hurdle in providing art secured lending services. The advent of the digitisation of more art-related data and the ability of technology to process this data means that we are likely to see significant improvement in, and the potential standardisation of, valuation methods and processes in the future.



Section 1: The art market

Highlights

- **Wealth creation drives art market growth:** the growth in sales of art and collectibles has been fuelled by the globalisation of the art market and an exceptional increase in wealth, especially in new growth markets such as Asia, the Middle East and Latin America
- **An increasing number of UHNWIs are buying and investing in art and collectibles globally,** which presents an opportunity for wealth managers to develop regional and/or global Art & Finance strategies
- **Global art buying trends indicate a continued accumulation of wealth in art and collectibles** and an opportunity for wealth managers to provide art and wealth management services around wealth protection, estate planning, leverage and value enhancement. According to a Barclays report⁴ published in 2012, art and collectible holdings vary between region and asset type, but on average represented 9% of the net assets of wealthy individuals
- **The first half of 2014 signals another record year for the art auction market:** this year is set to become another positive year for the art market, with auction figures based on sales (for the first half of 2014) already amounting to US\$5.98 billion⁵, only 22% lower than the total figure for 2013, and still with the autumn season to come
- **The positive market trend of 2013 is likely to continue for the rest of 2014 and the first half of 2015,** as the experts' outlook for the majority of the modern and contemporary art markets is neutral to positive in the next 12 months. Auction sales of US and European, Chinese, South East Asian and Russian modern and contemporary art saw the strongest growth in 2013, and is likely to have a favourable impact on the development of Art & Finance in these markets
- **United States and Europe:** there is a positive outlook for art wealth management services in the United States and Europe as market values are moving towards an all-time high. Wealth managers expect their clients to increase their total wealth allocated to art, providing a fertile ground for Art & Finance-related services aimed at protecting, leveraging and enhancing art and collectible wealth
- **China:** the Art & Finance industry in China is likely to grow as the Chinese government has adopted a proactive role in creating closer cooperation between the financial and cultural sectors. The strong appetite for art as an investment among Chinese buyers is likely to continue to be a major motivation and a key dynamic in the Chinese art market going forward, and we expect significant financial innovation in the area of art and collectible assets in the future

The positive market trend of 2013 is likely to continue for the rest of 2014 and the first half of 2015, as the experts' outlook for the majority of the modern and contemporary art markets is neutral to positive in the next 12 months

⁴ Barclays Wealth Insights report: Profit or Pleasure? (2012)

⁵ Based on global sales by Sotheby's and Christie's of impressionist and modern art, contemporary art, Chinese art and Old Masters

- **Middle East:** geopolitical uncertainty in the region could weigh on the Middle Eastern art market outlook in the next 12 months. However, expansion in museum infrastructure and rapid growth in UHNWIs and their significant allocation to treasure assets indicate that this region is likely to play an important part in the global and regional art and collectibles markets in the future
- **India:** the Indian art investment fund market took a hit in 2009, which significantly dented confidence in art as an asset class among Indian investors. However, the improved outlook for the Indian art market and an increase in prices for modern Indian art should lead collectors and investors to revisit this market in the near future. The Indian art market is likely to need a further two to three years of stable growth before we see the emergence of an Art & Finance industry in India
- **Latin America:** the Latin American art market remains the second most attractive art market to invest in over the next 12 months according to market experts, and wealth managers say that a large majority of their clients in these regions will increase their holding of art in the future. This signals future growth in the market for art and collectible assets, and increasing opportunities for the emergence of an Art & Finance industry in this region

The first half of 2014 signals another record year for the art auction market

- **South-East Asia:** the outlook for the South-East Asian modern and contemporary art market is positive, with strong growth being recorded since 2009. Rapid regional growth in UHNWI numbers and wealth, combined with Singapore's position as a financial and art market hub, point to significant opportunities to grow an Art & Finance market in South East Asia
- **Russia:** auction sales of modern and contemporary Russian art in the first half of 2014 revealed signs of renewed confidence in this market. This is likely to highlight the advantages of art as a tangible and moveable asset, which could be attractive in light of the current geopolitical situation
- **Africa:** international and domestic sales of African modern and contemporary art have increased, fuelled particularly by rapid growth in the UHNWI population in Nigeria. This has created a new generation of African collectors with an interest in art as an asset class, and opens up the possibilities for a future Art & Finance industry as the art market matures

Global art collecting trends in 2014

This section aims to give a broad overview of some of the key art market and collecting trends, in order to provide greater context for the analysis and the survey findings presented later on in this report. In order to have a better grasp of the development and challenges of the global Art & Finance industry, we also need to improve our understanding of the dynamics of different global art markets, and how these may impact on the Art & Finance industry now and in the future. More market participation among HNWI, higher valuations and more risks associated with buying art and collectibles are important indicators for whether there is potential for an Art & Finance industry to develop in these markets.

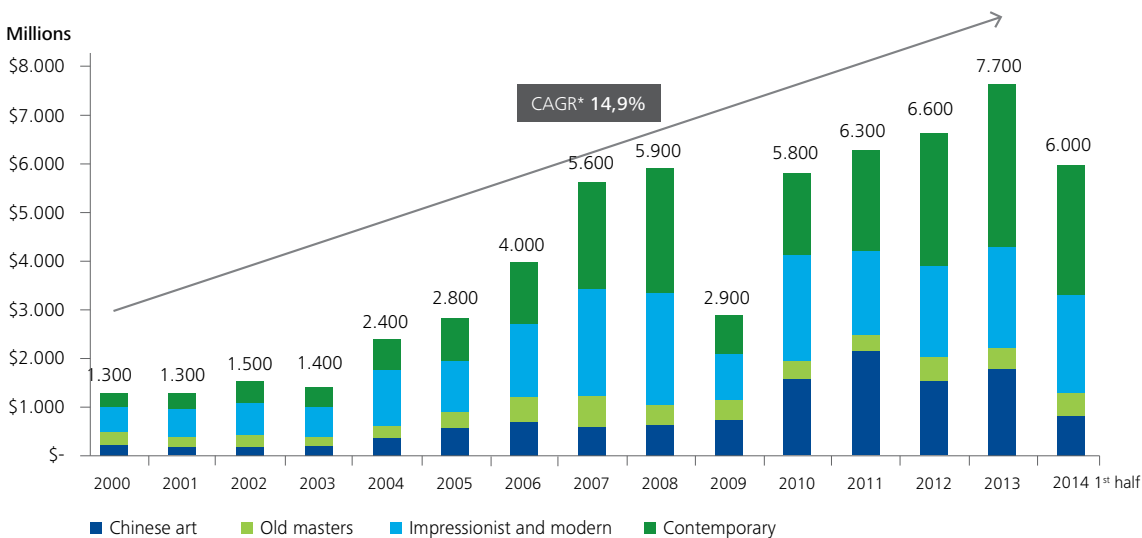
For clarity we have provided a brief background to some of the key global art auction categories, showing how these have evolved in the 2000 - 2014 period, and indicating where wealth is currently being invested. We have also taken a closer look at the world's second largest market, China, since this is a market that is likely to continue to grow and attract increasing wealth from the region, as investors look to diversify their capital into alternative assets such as art and collectibles.

The Art & Finance industry in China has also undergone rapid development in recent years, particularly in the area of art investment funds and trusts (see Section 3) and art lending (see Section 2). Finally, we have provided a broad analysis of modern and contemporary auction sales, collector perception and market outlook, combined with wealth indicators for a number of countries and regions. By combining these indicators we will get a better understanding of the regional and country-specific potential for an Art & Finance industry.

Global art auction sales set new records in 2013, with contemporary art again fuelling global sales growth

Total global auction sales at Sotheby's and Christie's in the Chinese art, Old Masters, impressionist and modern art and contemporary art segments grew by 15.6% in 2013 to US\$7.68 billion, up from US\$6.4 billion in 2012. All collecting categories, aside from Old Masters, registered a significant increase in 2013. Auction sales in the contemporary art segment increased by 24.2% to US\$3.39 billion, from US\$2.73 billion in 2012. The level of contemporary art sales is now 32.7% above the previous market peak in 2008.

Fig. 1 Christie's and Sotheby's: auction sales (in US\$) by category 2000-2014 (1st half)



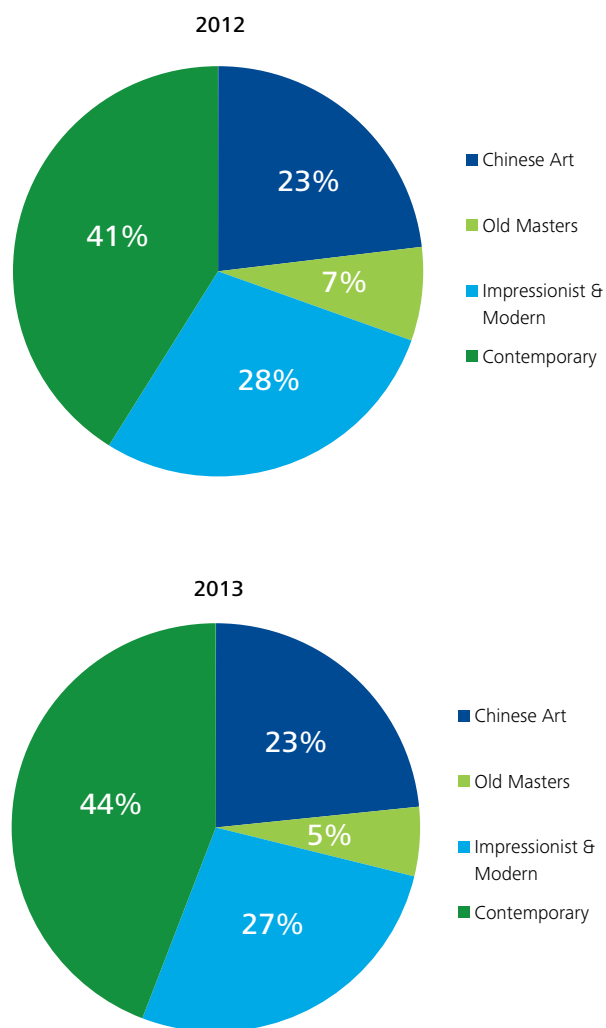
Source: ArtTactic

The impressionist and modern art market saw sales increase by 9.8% in 2013, to US\$2.07 billion, and this collecting category accounted for a 27% market share in 2013, down from 44% in 2003. Contemporary art has increased its market share to 44% in 2013, up from 28% in 2003, taking over the leadership position from the impressionist and modern art market. The overall Chinese art market also gained market share over the last ten years, with an increase from 14.6% in 2003 to 23% in 2013.

2014 is set to become another record year for the art market, with auction sales for the first half of the year reaching US\$5.98 billion, only 22% lower than the total figure for 2013, and still with the autumn season to come. The impressionist and modern market has been doing particularly well, with sales for the first half of 2014 just 4% below the annual total from the previous year.

In order to have a better grasp of the development and challenges of the global Art & Finance industry, we also need to improve our understanding of the dynamics of different global art markets, and how these may impact on the Art & Finance industry now and in the future

Fig. 2 Christie's and Sotheby's: auction sales by category—market share in 2012 versus 2013



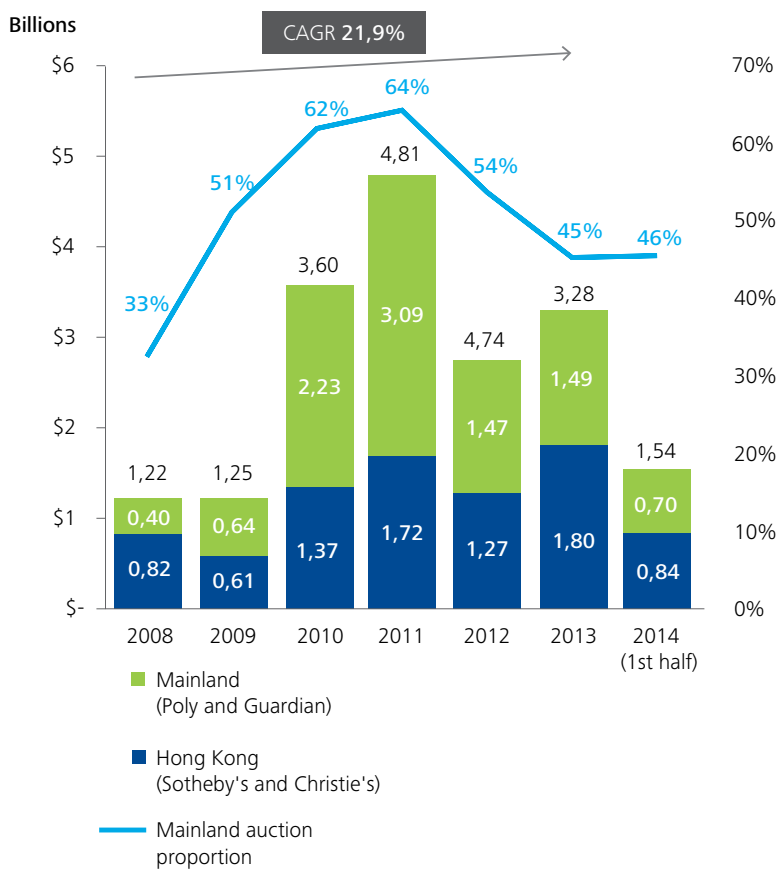
Source: ArtTactic

Chinese art regained market share from auction sales⁷ in 2013, but struggled to maintain momentum in the first half of 2014

Since the financial crisis in 2009, the Chinese art market has emerged as one of the fastest growing art markets in the world, and was ranked as the second biggest art market in 2013 by the annual TEFAF report⁸.

According to recent research by ArtTactic, Chinese auction sales (based on all Chinese art categories) regained market share in 2013, with a 19.6% rise in sales to US\$ 3.28 billion. This is the third highest annual sales total for this auction category, but is still 16.8% below the peak reached in 2011. However, the first six months of 2014 saw auction sales decline by 12.6%, based on the four largest auction houses (Sotheby's, Christie's, Poly Auction and China Guardian) compared with the second half of 2013.

Figure 3. Chinese art auction sales (in US\$)
(All Chinese art categories in US\$ 2008 - 2014 (1st half), based on Hong Kong (Christie's, Sotheby's) versus mainland China (Poly, China Guardian))



However, after a strong sales performance in autumn 2013, Sotheby's and Christie's in Hong Kong saw a 19.8% decrease in combined sales in spring 2014 (all Chinese art categories). Total sales for Sotheby's Hong Kong were US\$444.3 million (down 19% from six months ago), while Christie's Hong Kong achieved US\$391.8 million (21% lower than six months ago). Both Christie's and Sotheby's have established a mainland Chinese auction presence, with total sales of US\$38.3 million in the first half of 2014 (down from US\$55.3 million in autumn 2013).

The two main domestic Chinese auction houses⁹ performed better, with Guardian Beijing achieving \$360.3 million in total sales, which was 4% lower than its last autumn sales, but this remains half of the total it reached at the peak of the market in 2011. Poly Beijing reached a sales total of \$444.3 million (3% lower than the autumn 2013 total), on a par with Sotheby's Hong Kong. The two mainland auction houses have increased their market share to 49%, based on spring 2014 sales, up from 44% in autumn 2013. Poly and Guardian's Hong Kong auction sales (established in autumn 2012) came in at US\$188.8 million in spring 2014 (down from US\$193.5 million in autumn 2013).

⁷ This is based on all Chinese art categories sold through Sotheby's and Christie's in Hong Kong and Poly Auction and China Guardian in Mainland China (smaller auctions might be excluded)

⁸ Source: TEFAF Art Market Report 2014

⁹ For comparative reasons (with Sotheby's and Christie's) these auction sales are based on the May/June and November/December sales seasons only)

Global wealth creation fuels art market growth

In the last ten years, the global art market has grown from around US\$20 billion in 2003 to US\$63 billion¹⁰ in 2013, according to figures in the TEFAF Art Market Report 2014. Despite the financial crisis that started in 2008/2009, the global art market saw an increase in total art sales of 60% between 2009 and 2013.

The growth in the art market has coincided with its globalisation and an exceptional increase in wealth creation, especially in new growth markets such as Asia, the Middle East and Latin America. According to the annual World Wealth Report¹¹, the population of High Net Worth Individuals¹² (HNWIs) has increased from 7 million individuals in 2003 with total wealth of an estimated US\$27.2 trillion, to 13.7 million individuals in 2013 with total wealth of US\$52.6 trillion (an increase of 93.3% in total wealth). The Asia-Pacific region has seen particularly strong growth, from 1.57 million individuals in 2003 with total wealth of US\$5.7 trillion to 4.3 million individuals in 2013 with wealth of US\$14.2 trillion (up 149% in the last ten years).

In 2013, the world's Ultra-High Net Worth¹³ population reached an all-time high of 199,235 individuals and combined wealth of US\$27.8 trillion according to the Wealth-X and UBS World Ultra Wealth Report 2013. Growth in 2013 largely related to North America and Europe, with a net gain of nearly 10,000 UHNW individuals and a total increase in wealth of US\$1.5 trillion. However, the findings from the report suggest that this will change in the future, and forecasts suggest that more UHNW individuals and wealth will be created in Asia than in North America/Europe in the next five years.

The billionaire effect on the high end of the art market is also clear. According to the Wealth-X and UBS World Ultra Wealth Report 2013, the global population of billionaires was 2,170 in 2013 (up from 2,160 in 2012), with a total net worth of US\$6,516 billion (up by US\$326 billion from 2012, a 5% increase)¹⁴.

Based on research by Wealth-X, the average billionaire holds US\$31 million (or 0.5%) of his/her net worth in art, which means that total billionaire wealth allocated to art was an estimated US\$32.6 billion in 2013. The increase in the number of billionaires between 2012 and 2013 would imply that this group put an additional US\$1.63 billion of their total wealth into art.

With overall wealth on the rise and the UHNWI population growing, it is likely that more money will flow into the art and collectibles market, creating an opportunity that should be seized by the wealth management community.

The positive market trend of 2013 is likely to continue for the rest of 2014 and the first half of 2015, as the experts' outlook for the majority of the modern and contemporary art markets is neutral to positive in the next 12 months. Auction sales of US and European, Chinese, South East Asian and Russian modern and contemporary art saw the strongest growth in 2013, which is likely to have a favourable impact on the development of Art & Finance services in these markets.

¹⁰ Based on results reported in the TEFAF Art Market Report 2014 converted into US\$ based on an annual average exchange rate of USD/EUR 1.39 in 2009 and USD/EUR 1.33 in 2013

¹¹ The World Wealth Report is an annual publication produced by Cap Gemini and RBC Wealth Management

¹² The report categorises HNWI's into three discrete wealth bands: those with US\$1 million to US\$5 million in investable wealth (millionaires next door); those with US\$5 million to US\$30 million (mid-tier millionaires) and those with US\$30 million or more (Ultra-HNWIs)

¹³ US\$30 million or more (Ultra-HNWIs) of investable wealth

¹⁴ Source: Wealth-X and UBS World Ultra Wealth Report 2014, page 16
















Table 1: Regional market trends in modern and contemporary art and 2015 outlook

Geographical market	Wealth indicator ¹⁵ (% growth 2012 -2013)	Buying art indicator ¹⁶ (Net balance)	% of treasure assets ¹⁷	Auction sales trend 2012-2013
GLOBAL TREND	World forecast: +4% (US\$ wealth) +5.4% (population)	A majority of wealth managers believe their clients will continue to buy art in the future, with most of the regions showing a positive net balance	Despite significant regional differences in terms of % holding of treasure assets, many of the new growth markets offer potential for art and wealth management services	Although there are significant regional differences, global sales of modern and contemporary art were up in 2013 and first-half 2014, mainly driven by the increase in high end US and European auction sales
US and European contemporary¹⁹ art	+9% (US\$ wealth) +7.9% (population)	Europe: +46% United States: +34%	Europe: 6-14% United States: 9%	+24.2%
Chinese contemporary art	-4.1% (US\$ wealth) -5.1% (population)	+39%	17%	Hong Kong: +76% Mainland China: +59%
Middle East modern and contemporary art	+15.3% (US\$ wealth) +23.9% (population)	+58%	Qatar: 2% Saudi Arabia: 17% UAE: 18%	+85.5%
Indian modern and contemporary art	+1.6% (US\$ wealth) +1.1% (population)	Not available	3%	+63%
Latin American modern and contemporary art	-4.1% (US\$ wealth) -4.1% (population)	+86%	Mexico: 9% Brazil: 15%	-11%
South East Asian modern and contemporary art	Singapore: +3.8% (US\$ wealth) +3.2% (population) Indonesia: +10.2% (US\$ wealth) +8.3% (population) Thailand: +15.2% (US\$ wealth) +15.8% (population)	+33%	Singapore: 16%	+ 36%
Russian modern and contemporary art	+3.1% (US\$ wealth) +2.5% (population)	+57%	Not Available	+21%
Africa modern and contemporary art	Africa overall: +9.5% (US\$ wealth) +7.7% (population) Nigeria: +31.9% (US\$ wealth) +33.3% (population)	+39%	South Africa: 11%	+64%

¹⁵ Based on UHNWI figures from 2012 and 2013 from the Wealth-X and UBS World Ultra Wealth Report 2013

¹⁶ Based on The Wealth Report 2014 by Knight Frank, The 'net balance' is defined as the difference between the number of respondents indicating a positive movement in sentiment and those suggesting a negative movement, taking into account those with a neutral position. For example, if 60% of respondents indicated that their clients were planning to buy more art, 10% said their position would remain neutral regarding art buying and 30% said they were planning to buy less art, that would give a positive net balance of +30%

¹⁷ Barclays Wealth Insight report: Profit or Pleasure? (pages 10 and 11). Findings are from 2012

Confidence trend 2012-2013	Collector outlook 2015 ¹⁸	Art & Finance outlook	
Improved economic sentiment boosted confidence in the global art market. Geo-political uncertainty continued to impact on some art markets, notably in the Middle East	The majority of collectors maintain a neutral to positive outlook on the next 12 months, and take a particularly optimistic view of US and European, and Indian and South East Asian modern and contemporary art	The combination of significant growth in wealth and the development of new regional art markets increases the future potential of a global Art & Finance industry	
+18%	Collector poll on market direction:  UP: 62%  FLAT: 38%  DOWN: 0%	Record sales in New York in May 2014 have boosted confidence in the market	POSITIVE
+9%	Collector poll on market direction:  UP: 45%  FLAT: 52%  DOWN: 3%	The market rebounded in 2013, and although 45% of art collectors believe the market will go up in the next 12 months, 52% believe the market will consolidate around current levels	POSITIVE
+47%	Collector poll on market direction:  UP: 9%  FLAT: 50%  DOWN: 41%	Auction sales were up by 85.5% in 2013, but collectors are nervous about the geo-political situation in the region and its impact on the next 12 months	NEUTRAL/POSITIVE
+6%	Collector poll on market direction:  UP: 51%  FLAT: 46%  DOWN: 0%	Christie's launch of the new auction season in Mumbai has instilled new confidence in the market	NEUTRAL
+1%	Collector poll on market direction:  UP: 43%  FLAT: 39%  DOWN: 18	Slowing economic growth in Brazil and financial uncertainty in Argentina could impact on the art market in the next 12 months	NEUTRAL/POSITIVE
+12%	Collector poll on market direction:  UP: 59%  FLAT: 41%  DOWN: 0%	South East Asian auction sales in April/ May 2014 reached a new high for this market, with US\$31.1 million in total sales, an increase of 12% from the last record set in autumn 2013	POSITIVE
+8%	Collector poll on market direction:  UP: 33%  FLAT: 46%  DOWN: 21%	Recent sales in London show that demand for Russian art is increasing, especially from Russian clients	POSITIVE
+20%	Collector poll on market direction:  UP: 39%  FLAT: 40%  DOWN: 21%	Sales for Bonhams Africa in May 2014 raised US\$1.9 million, up 47% from 2013. The Nigerian art market is set to take on the more established South African art market in the next 12 months	POSITIVE

¹⁸ ArtTactic Confidence survey of 360 art collectors, art advisors, galleries and auction houses in July 2014

¹⁹ Same as post-war and contemporary. In a western auction context, modern art belongs to the impressionist and modern auction category, and is therefore not included

Trends in global auction sales of modern and contemporary art

Modern, post-war and contemporary art accounted for an estimated 81.2% of art auction sales in 2012-2013²⁰. Although we don't aim to give a complete overview of the global art market and its myriad collecting areas, we believe that overall trends emerging in the modern and contemporary art sector across different regions give a representative view of some of the key trends emerging in these art markets. We have also aimed to link the dynamics in the art market to wealth trends and current holdings of art and collectible assets, giving us a better understanding and potential connection between the global art market and world of finance.

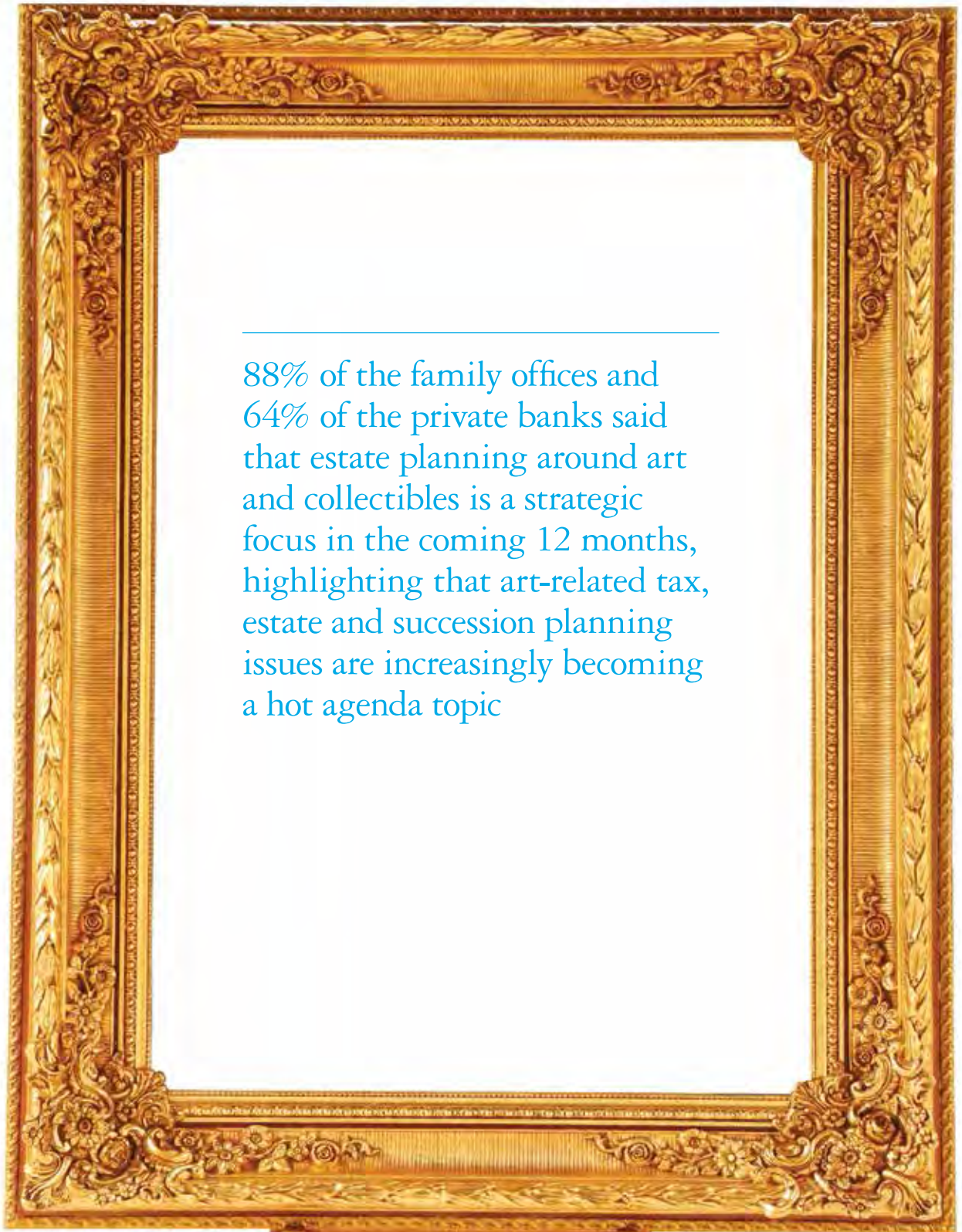
The following analysis focuses on modern and contemporary art by artist origin, focusing on the United States, Europe, China, India, the Middle East, Latin America, South East Asia, Russia and Africa. Rather than providing a comparative analysis between the different regional markets, the analysis will focus on the art market trends and wealth trends within each region to see how the two elements might be linked, and what this could tell us about the potential for an Art & Finance industry in each geographical area.

Art market analysis is not necessarily about auction sales data generated within the country or region itself. For instance, the Latin American modern and contemporary art market analysis is based on sales at Sotheby's, Christie's and Phillips in New York, but the majority of the buyers in these sales are of Latin American origin. The same goes for the Russian art market, where sales take place in London, but most buyers are from Russia or the CIS. The analysis is predominantly based on auction sales by Christie's and Sotheby's, although other auction houses are included as they represent a major share of the overall market for that particular modern and contemporary art segment. This is highlighted in each individual section.

For the United States and Europe, and China and Africa, we have used the contemporary art category to reflect the broad trends in the market. However, for markets related to Indian, Middle Eastern, Latin American and South East Asian artists we have included the modern art segment based on the auction category classification used by the main auction houses such as Sotheby's and Christie's.

We have also added wealth trends for each of the geographical markets, when available, drawing on results from research reports produced by Wealth-X and UBS, Knight Frank and GapGemini and RBC Wealth Management.

²⁰ Source: Artprice, 'Contemporary Art Market – The Artprice Annual Report 2013'



88% of the family offices and 64% of the private banks said that estate planning around art and collectibles is a strategic focus in the coming 12 months, highlighting that art-related tax, estate and succession planning issues are increasingly becoming a hot agenda topic



US and Europe

There is a positive outlook for art wealth management services in the United States and Europe, as market values are reaching an all-time high. Wealth managers expect their clients to increase their total wealth allocated to art, providing a fertile ground for Art & Finance-related services aimed at protecting, leveraging and enhancing art and collectible wealth.

Since the art market boom started in 2004, the auction sales of US and European post-war²¹ and contemporary art increased from US\$621 million to US\$3.39 billion in 2013 (or a total sales increase of 445%). Last year was a record year for the post-war and contemporary art market, with a 24.2% increase in auction sales. So far in 2014 (based on winter, spring and summer sales in London and New York in 2014), London is 30% ahead of the equivalent figure for 2013, and New York is 43% ahead, which bodes well for another record year in the contemporary art market.

However, growth could be slowing in the second half of 2014, according to an ArtTactic survey of art experts in July 2014. Although the majority of experts believe that the market direction will continue to be positive, a decrease in confidence in the last six months may herald a slowdown in the annual increase in market size following the unprecedented period of growth experienced since 2009.

Fig. 4 US and European post-war and contemporary art market (2000-2013)

Auction sales (in US\$) based on Christie's and Sotheby's

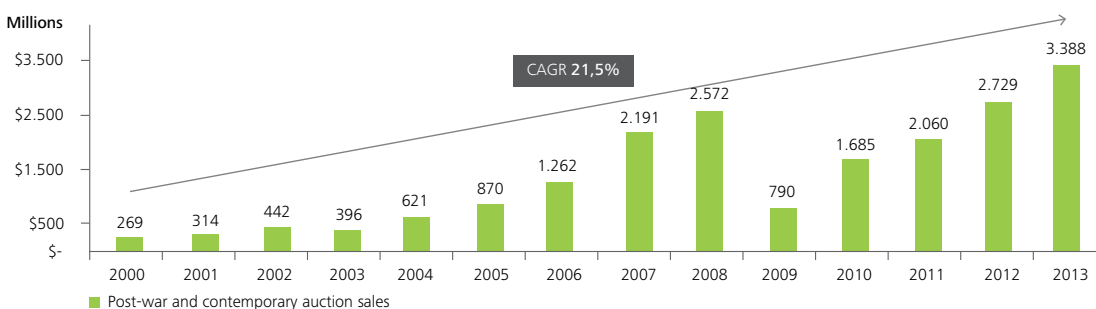
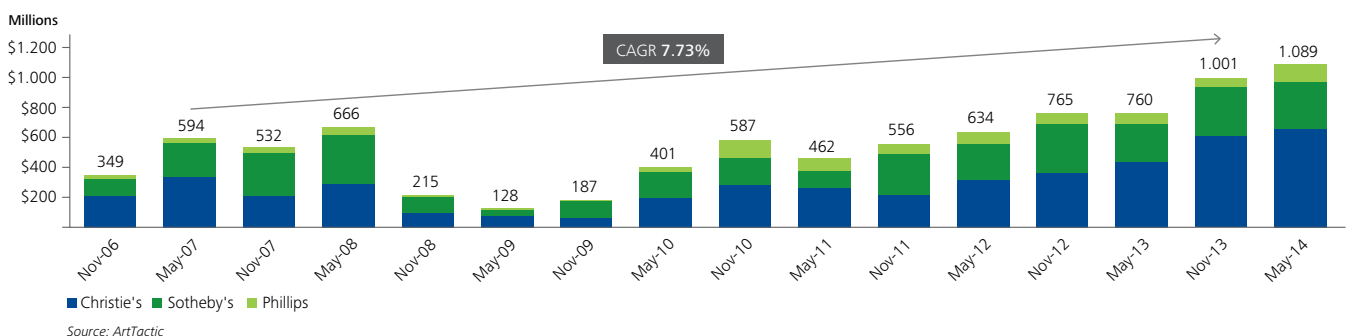


Fig. 5 New York post-war and contemporary evening sales

Auction sales (in US\$) based on Sotheby's/Christie's/Phillips



Christie's and Sotheby's compete for the top position in the contemporary art market

New York contemporary sales in May 2014 reached an all-time high for the three leading auction houses (Sotheby's, Christie's and Phillips), raising a total of US\$1,088,714,167 (excluding buyer's premium) against pre-sales estimates of US\$968,380,000 to US\$1,284,470,000.

This was the highest ever evening total for post-war and contemporary art, with total sales value up 43.3% from May 2013 and 8.7% from November 2013. Christie's has created a position in this market with a 60.3% market share based on the May 2014 contemporary evening sales. However, the July 2014 post-war and contemporary sales in London saw Sotheby's claw back market share, ending the London season with a 45% share of the evening sales against 50% for Christie's.

OUTLOOK

Market direction: 62% of experts²² believe the market will go up in the next six months (up from 54% in January 2014), while 38% (down from 46% in January 2014) believe that the contemporary art market will remain flat in the next six months.

Expert confidence: the United States and European ArtTactic Art Market Confidence Indicator is currently 5.8% higher than in July 2013 (although down 7.1% in the first six months of 2014). The result is the second highest reading since May 2007, and indicates that experts remain largely positive with regard to the contemporary art market in the next six months, despite a more cautious outlook.

Speculation risk: the 'speculation barometer' has increased by 12%. A total of 78% of the market experts surveyed by ArtTactic rated the speculation level at 7 or above (on a scale from 1 to 10, where 1 is very low speculation and 10 is very high speculation). Experts remain concerned that short-term investors and speculators are boosting art prices in the current market, particularly among some of the younger upcoming artists that have seen significant success at auction in 2013 and the first half of 2014.

Art buying trends: according to 'The Wealth Report 2014' by Knight Frank, a positive net balance of

46%²³ of the private bankers and wealth advisors surveyed²⁴ expect the popularity of art buying among their European UHNWI clients to increase. For North American UHNWI, a positive net balance of 34% of private bankers expect the popularity of art buying to rise.

Wealth outlook: according to the Wealth-X and UBS World Ultra Wealth Report 2013²⁵, the world's UHNW population reached an all-time high in 2012/2013. Growth was largely attributable to North America and Europe, with a combined net gain of nearly 10,000 UHNW individuals and a total increase in wealth of US\$1.5 trillion. According to Knight Frank's 'The Wealth Report 2014'²⁶, 67% of private bankers and wealth managers said they expected UHNWIs in North America to increase their wealth in 2014. An even higher percentage, (70%) said the same about European UHNWIs. This expected increase in wealth could have a significant impact on the art and collectibles market, as wealthy individuals (HNWIs and UHNWIs) in the United States currently hold an estimated 9% of their wealth in treasure assets such as fine art, jewellery and furniture, according to a Barclays report²⁷ published in 2012. This percentage varied between 6% and 14% across different European countries according to the same report.

21 For the United States and Europe we have used the Sotheby's and Christie's post-war and contemporary art category to analyse the trends in this market. We have not included modern art, as this belongs to another auction sales category (impressionist and modern art). For other regions we have used the modern and contemporary classification, again to reflect the definition of the sales categories used by the main auction houses

22 ArtTactic art market confidence surveys among 360 international art collectors, art advisors, galleries and auction houses between May 2014 and July 2014

23 The 'net balance' is defined as the difference between the number of respondents indicating a positive movement in sentiment and those suggesting a negative movement, taking into account those with a neutral position. For example, if 60% of respondents indicated that their clients were planning to buy more art, 10% said their position would remain neutral regarding art buying and 30% said they were planning to buy less art, that would give a positive net balance of +30%

24 Source: The Wealth Report 2014, and based on a attitudinal survey of almost 600 private banker and wealth managers

25 Wealth-X and UBS: World Ultra Wealth Report 2013

26 Knight Frank: The Wealth Report 2014

27 Barclays Wealth Insights report: Profit or Pleasure? (2012)



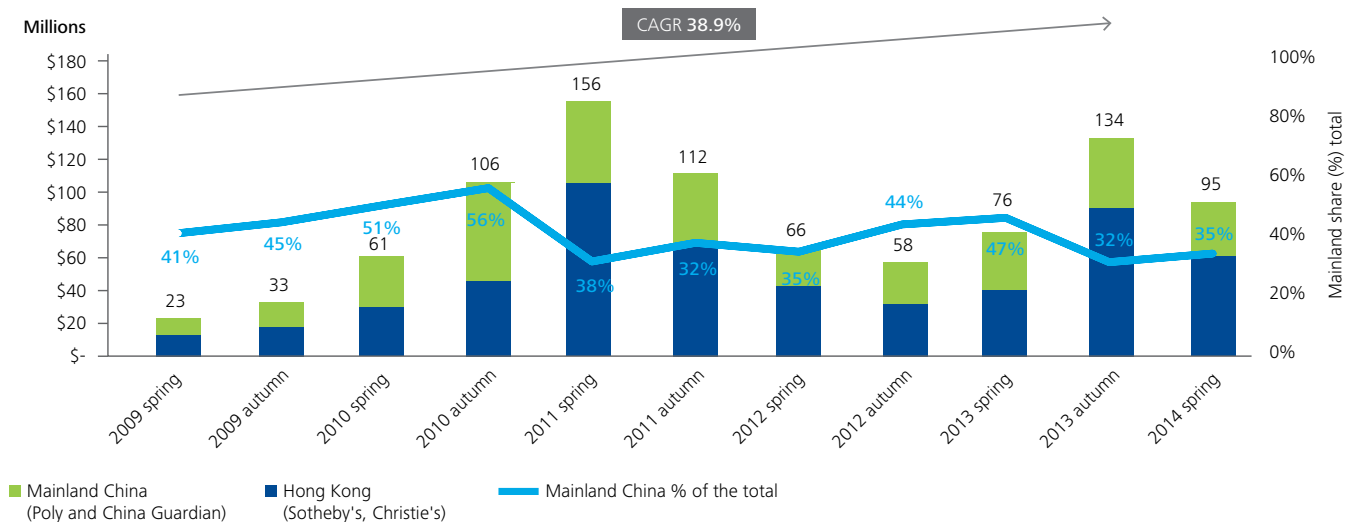
China

The Art & Finance industry in China is likely to grow as the Chinese government has adopted a proactive role in creating closer cooperation between finance and culture. The strong appetite for art as an investment among Chinese buyers is likely to continue to be a major motivation and a key dynamic in the Chinese art market going forward, and we expect significant financial innovation around art and collectible assets in the future.

After a strong performance in autumn 2013, which saw auction sales of contemporary Chinese art reaching US\$134 million (up 76% from spring 2013), the market was unable to sustain the growth momentum in this year's spring season in Hong Kong and Beijing. The sales total for all four auction houses (Sotheby's, Christie's, Poly and Guardian) decreased by 29% from autumn 2013. Sotheby's and Christie's both registered a 32% decrease in sales of contemporary Chinese art, while Poly and Guardian had mixed results. Poly posted a significant drop in sales of 43%, while Guardian Beijing increased its sales by 78%.

This season, Guardian paid more attention to Chinese contemporary art by introducing a number of themed sales such as 'Break Through: Chinese Avant-Garde Art in the 80s' and 'Look Inside: Reinventing Chinese Contemporary Art Since 2000'. Despite the slowdown experienced by Sotheby's and Christie's this season, the two international houses still have a 65% market share of the Chinese contemporary art market (down from 68% six months ago).

Fig. 6 Chinese contemporary art sales
Auction sales (in US\$) of Chinese contemporary art in Hong Kong and mainland China (Sotheby's, Christie's, Poly and Guardian)



Source: ArtTactic

Sotheby's and Christie's remain the dominant players at the top end of the Chinese contemporary art market, with the sale of 16 lots valued above US\$1 million (against 17 lots last autumn).

Poly and Guardian only sold three lots above the US\$1 million threshold (against nine last seasons). However, the two mainland auction houses have the largest share (52%) of the lower end of the market (US\$50,000 and below).

OUTLOOK

Market direction: experts²⁸ expect the rate of growth to slow down in 2014. 45% of experts believe that the Chinese contemporary art market will go up in the next six months, compared with 70% in December 2013; 52% believe that the market will remain flat (against 19% in December 2013) and the remaining 3% believe the market will come down (against 9% in December 2013).

Higher confidence in the Chinese contemporary art market: despite a slowdown in auction sales for contemporary Chinese art, the latest art market confidence survey in May 2014 showed that market confidence was up by 21% from the end of last year. The ArtTactic Art Market Confidence Indicator for China now stands at 75, up from 62 in December 2013.

The strong appetite for art as an investment among Chinese buyers is likely to continue to be a major motivation and a key dynamic in the Chinese contemporary art market going forward. A total of 78% of experts rated the speculation level above 7. The inflow of speculative and short-term investment capital from private and institutional investors is still of concern to the market, and might negatively impact the stability of the mainland Chinese art market going forward.

Increasing rivalry in the Hong Kong and mainland art markets: competition between the domestic Chinese auction houses such as Poly and Guardian and the international houses, Sotheby's and Christie's, is likely to intensify in 2014.

In September 2013, Christie's hosted its first auction in mainland China, while Sotheby's launched its Beijing branch through a joint venture with the state-owned Gehua group. In March 2014, the parent company of Poly Beijing and Poly Hong Kong, the Poly Culture Group, completed its listing on the Hong Kong stock market, bolstering its ambition of further international expansion.

Art buying trends: according to Knight Frank's 'The Wealth Report 2014', a positive net balance of 39% of private bankers and wealth advisors surveyed expect the popularity of art buying among their Asian UHNWI clients to increase.

Wealth outlook: Asia's UHNWI population and its total wealth is expected to overtake that of Europe by 2017, according to the Wealth-X and UBS 'World Ultra Wealth Report 2013'. Mainland China and Hong Kong account for the second highest population of UHNWIs after Japan, with US\$2.05 trillion in total wealth. According to the Knight Frank wealth manager survey²⁹, 55% are positive on the prospect of further wealth creation in 2014 and expect a 40% increase in the UHNWI population in the next ten years. The increase in wealth creation can be expected to have a positive impact on the art and collectibles market, particularly as wealthy individuals in China currently hold an estimated 17% of their total wealth in treasure assets (paintings, jewellery and precious metals), according to a report published by Barclays³⁰.

28 ArtTactic confidence survey among 360 art collectors, art advisors, galleries and auction houses in July 2014

29 Knight Frank: The Wealth Report 2014

30 Barclays Wealth Insights report: Profit or Pleasure? (2012)



Middle East³¹

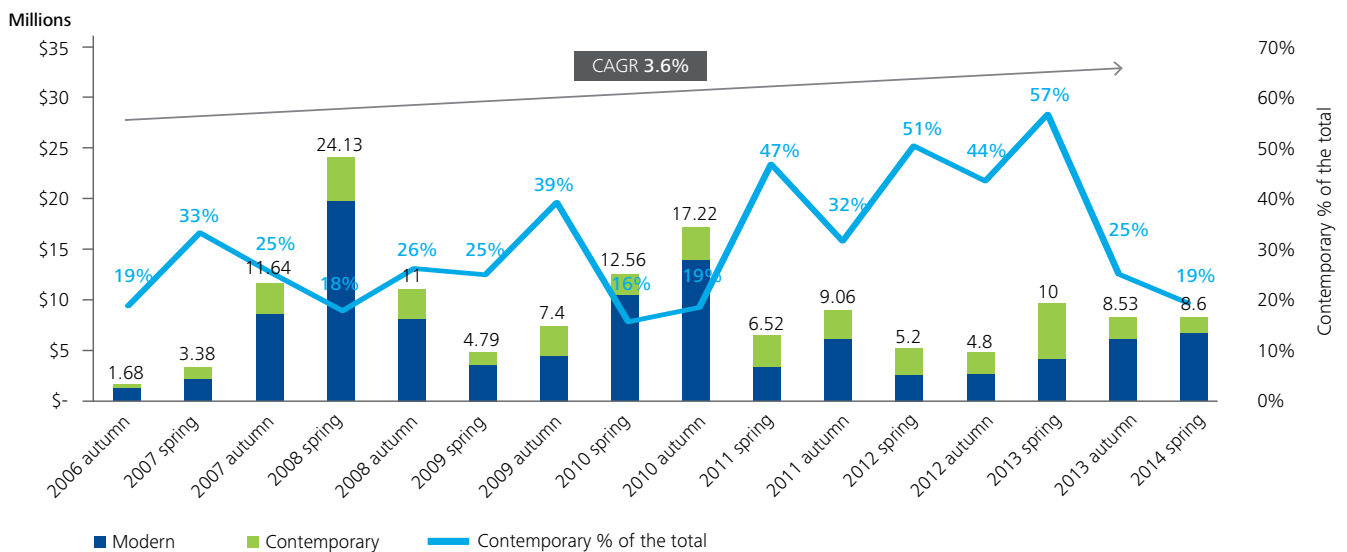
Geopolitical uncertainty in the region could weigh on the Middle Eastern art market outlook in the next 12 months. However, the expansion of museum infrastructure and rapid growth in UHNWIs and their significant allocation to treasure assets indicate that this region is likely to play an important part in the global and regional art and collectibles markets in the future.

Auction sales of modern and contemporary Middle Eastern³² art went up by 85.5% in 2013 to US\$18.5 million, from US\$10 million in 2012. This growth was driven by increased demand for Iranian, Egyptian, Lebanese and Turkish modern and contemporary artists.

The spring 2014 sales at Christie's Dubai came in marginally higher than the October sales in 2013, but were 14.1% lower than in spring 2013. However, this market shows an increasing level of confidence in both the modern and contemporary categories.

Low bought-in rates and an overall ArtTactic Auction Indicator of 61 (indicating that the majority of the lots sold above the average estimate) suggest that the final sales total exceeded market expectations, setting a positive tone for the market. In 2013, contemporary Middle Eastern art accounted for 42% of total auction sales, which was a much larger share of overall auction sales than what we see, for example, in the Indian art market at present.

Fig. 7 Middle East modern and contemporary art market (2006-2014 1st half)
Auction sales (in US\$) based on Christie's, Sotheby and Bonhams



Source: ArtTactic

However, the Middle Eastern art market is struggling to regain the momentum created in 2010, partly because of a lack of competition in the auction market. Christie's remains the leader in this market, with 15 consecutive auctions per season held in Dubai, accounting for 74% of the auction sales value in this collecting segment in 2013.

After several years of holding both Turkish and Middle Eastern modern and contemporary sales in London, Sotheby's shifted its sales to Doha in April 2013, after an 18-month absence.

See interview with Hala Khayat, the Christie's specialist and Head of Modern and Contemporary Arab and Iranian Art sales on page 52 on recent developments in the Middle Eastern art market.

OUTLOOK

Market direction: most experts³³ believe the market will remain at around current levels. While 9% of experts expect the Middle Eastern modern and contemporary art market to go up in the next six months, 50% believe that the market will remain flat and 41% believe the market could come down in the next 12 months.

Uncertain outlook for 2014: although sales almost doubled in 2013, a survey conducted by ArtTactic in July 2014 among international collectors showed that confidence in the Middle Eastern modern and contemporary art market was down 29% in the second half of 2013. Geopolitical uncertainty was cited as the most common reason for this view. However, confidence remains 4.6% above the 2012 reading, which suggests that the market might consolidate around last year's activity levels.

Iranian artists will continue to dominate the market: we expect Iranian artists to dominate the Middle Eastern auction market this year, and last year's performance by an older generation of artists such as Parviz Tanavoli and Mohammed Ehsai, as well as the younger contemporary artists such as Farhad Moshiri and Afshin Pirhashemi, is likely to instil further confidence among buyers.

Gulf buying likely to continue: the Gulf states, particularly Qatar, have been among the biggest buyers in the global art market in the last eight years. With the first phase of Saadiyat Island in Abu Dhabi scheduled for completion in 2015, we would expect buying activity to continue this year.

Art buying trend: according to Knight Frank's The Wealth report 2014, a positive net balance of 58% of private bankers and wealth advisors surveyed expect the popularity of art buying among their Middle Eastern UHNWI clients to increase.

Wealth outlook: according to the Wealth-X and UBS World Ultra Wealth Report 2013, the Middle Eastern UHNW population and wealth grew the fastest among all world regions, at a rate of 15.3% and 23.9% respectively in 2013. Saudi Arabia has the largest UHNW population and wealth at 1,360 individuals and US\$285 billion respectively, followed by the United Arab Emirates. Although the United Arab Emirates is behind Saudi Arabia in UHNW population and wealth, its UHNW population growth rate outpaced Saudi Arabia's at 20.7% according to the same report. With wealthy individuals in Saudi Arabia and the United Arab Emirates holding 17% and 18% of their total wealth in treasure assets (mainly jewellery, tapestry, furniture and precious metals) according to a Barclays report³⁴, collectors from this region can be expected to play an important part in the global art and collectibles market going forward.

31 We are using the definition of Christie's Dubai, which encompasses Arab, Iranian and Turkish modern and contemporary art

32 Based on the auction sales of Bonhams, Christie's and Sotheby's

33 ArtTactic confidence survey among 360 art collectors, art advisors, galleries and auction houses in July 2014

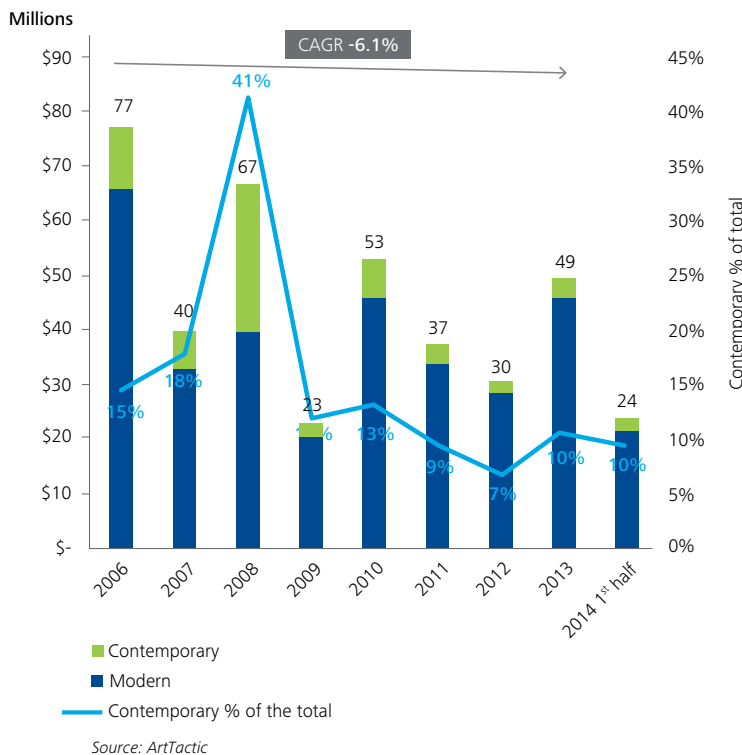
34 Barclays Wealth Insights report: Profit or Pleasure? (2012)



India

The Indian art investment fund market took a hit in 2009, which significantly dented the confidence in art as an asset class among Indian investors. However, the improved outlook for the Indian art market and an increase in prices for modern Indian art is likely to lead to collectors and investors revisiting this market in the near future. The Indian art market will probably need a further two to three years of stable growth before we see the emergence of an Art & Finance industry.

Fig. 8 Indian modern and contemporary art market (2006-2014 1st half)
Auction sales (in US\$) based on Christie's, Sotheby and Saffronart



Auction sales³⁵ of modern and contemporary Indian art was up by 62% in 2013 to US\$49.5 million from US\$30.4 million in 2012, and it looks like the market has reversed the negative trend in place since 2010. Christie's first auction in India ended 2013 on a positive note. The sale was a big success, raising a total of US\$15.45 million (including buyer's premium), almost doubling the pre-sale estimates.

Christie's remained the market leader in the Indian modern and contemporary art market in 2013, with a 49% market share based on the traditional March, June and September seasons. This was down from 58% in 2012, as Sotheby's increased its share from 15% in 2012 to 33% in 2013.

In 2013, the modern Indian art auction market accounted for 90.3% of the sales value, though contemporary Indian art represented only 9.7%. This is down significantly from the heyday of 2008, when contemporary Indian art generated 41% of the sales revenue. Although volumes of contemporary works being sold through the dedicated South Asian auction sales have dropped in recent years, many of the top Indian contemporary artists such as Bharti Kher, Subodh Gupta and Jitish Kallat are selling their work through the international contemporary art auctions in New York and London.

³⁵ Based on sales at Christie's, Sotheby's and Saffronart

OUTLOOK

Market direction: for the modern Indian art market, 63% of experts³⁶ believe the market will go up in the next six months (compared with 40% in November 2013), while 37% believe it will remain flat (60% in November 2013). For the contemporary Indian art market, 38% of experts believe the market will have a positive trend in the next six months (compared with 7% in November 2013). The majority, 55% of the experts, believe the market will remain flat (down from 72% in November 2013). Only 7% believe the contemporary art market will fall in the next six months (compared with 21% in November 2013).

Confidence in the Indian art market was up 42% in first half of 2014: the overall ArtTactic Art Market Confidence Indicator for India jumped 41.9% from the last reading in November 2013, and now stands at 74, the highest reading since October 2007. The increasing confidence comes on the back of a more positive outlook among experts for the Indian economy and a return of confidence to the contemporary Indian art market, which has struggled since the market downturn in 2009.

Market recovery: 46% of experts believe the Indian contemporary art market will bounce back and recover within the next two years. The remaining 54% of experts believe the market would need two to five years to fully recover to its former peak of 2007 and 2008.

Wealth outlook: according to the Wealth-X and UBS World Ultra Wealth Report 2013, India's UHNW population and wealth grew at 1.6% and 1.1% respectively in 2013. India has the third largest UHNW population in Asia (after Japan and China) with 7,850 individuals and total wealth of US\$935 billion. According to a wealth manager survey by Knight Frank³⁷, 70% expect a positive increase in wealth in India in 2014, and 37% believe there will be an increase in the total UHNWI population by 2023. Among wealthy individuals in India, an estimated 3% of total wealth³⁸ is held in treasure assets (mainly jewellery, furniture and classic cars). This percentage is much lower than most of the other countries in this report, and could explain why the Indian art market is lagging behind many of the other regional art markets.

³⁶ ArtTactic confidence survey of 360 art collectors, art advisors, galleries and auction houses in July 2014

³⁷ Knight Frank: The Wealth Report 2014

³⁸ Barclays Wealth Insights report: Profit or Pleasure? (2012)



Latin America

The Latin American art market remains the second most attractive art market to invest in over the next 12 months according to market experts. Wealth managers say that a large majority of their clients in this region will increase their holding of art in the future. This signals future growth in art and collectible assets and increasing opportunities for the emergence of an Art & Finance industry in this region.

The auction sales for modern and contemporary Latin American art in 2013 came in 14.1% lower than in 2012. Despite this, the result is still the second highest sale total since 2008. The sale of modern art continued to dominate the Latin American auction market, accounting for more than 94% of the sales total.

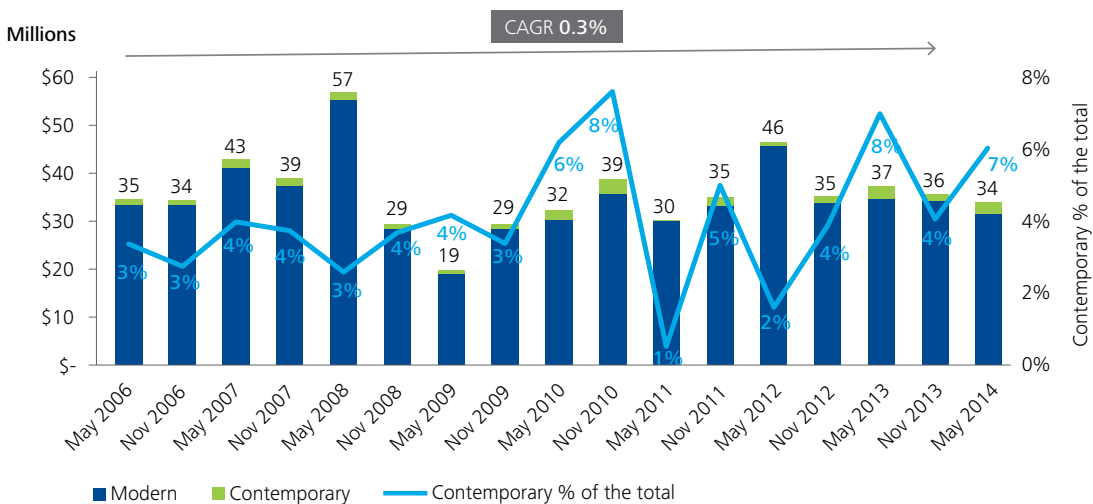
Although contemporary art only accounted for less than 5% of Sotheby's and Christie's sales, Phillips had a much larger selection of Latin American contemporary artworks, accounting for 22% of the 2013 sales total.

While both Sotheby's and Christie's saw their annual Latin American sales decrease last year, Phillips grew its sales of Latin American art by 62%, from US\$5.5 million in 2012 to US\$8.9 million in 2013. In May 2014, Phillips' market share was 13.5%, up from 11.4% in May 2013.

The November 2013 sales in New York saw attention shifting from Mexico back to Brazil. Brazilian artists accounted for 29% of overall auction sales in November 2013, as opposed to 14% in November 2012. Mexican artists accounted for 22% of overall sales in 2013, against Brazil's 21%.

Fig. 9 Latin American modern and contemporary art market (2006-2014 1st half)

Auction sales (in US\$) based on Christie's, Sotheby's and Phillips



Source: ArtTactic

OUTLOOK

Market direction: in ArtTactic's collector poll³⁹, 43% of respondents said that the Latin American market would go up in 2014 (down from 59% in 2013). A further 39% believe the market will remain around the current level, while 18% of experts think the market will go down in the next 12 months.

Potential remains strong: an ArtTactic survey conducted in July 2014 among international collectors established that the Latin American art market remains the second most attractive art market to invest in over the next 12 months.

Optimistic outlook for Brazilian modern artists: recent record prices set by Brazilian artists such as Lygia Clark and Sergio Camargo are likely to fuel further interest in Brazilian modern artists this year.

Art buying trend: according to Knight Frank's The Wealth Report 2014, a net positive balance of 86% of the private bankers and wealth advisors surveyed expect to see an increase in the popularity of art buying among their Latin American UHNWIs.

This is significantly higher than any other country or region, and signals a strong appetite for tangible collectible assets, particularly art.

Wealth outlook: according to the Wealth-X and UBS World Ultra Wealth Report 2013, Latin America was the only region to suffer a decline (-4.1%), with both its UHNW population and total wealth falling, by 600 individuals and US\$75 billion respectively.

The slowdown was particularly notable in Brazil, which saw a 13.5% drop in the UHNWI population and an 11% decrease in total wealth in 2013. With an estimated 15% of total wealth⁴⁰ held in treasure assets, the country's slower economic growth (estimated to be around 2%⁴¹ in 2014 and 2015) could have a negative impact on the Brazilian art market going forward. However, a survey by Knight Frank⁴² suggests that confidence in Latin America remains robust, with 48% of respondents predicting growth in the UHNWI population in 2014, while 40% took a neutral view.

³⁹ ArtTactic confidence survey of 360 art collectors, art advisors, galleries and auction houses in July 2014

⁴⁰ Barclays Wealth Insights report: Profit or Pleasure? (2012)

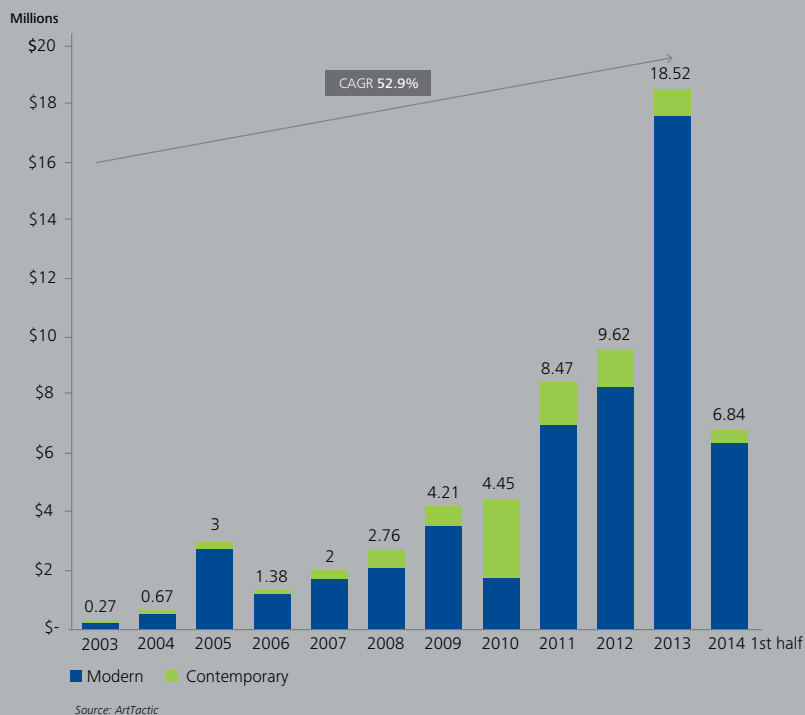
⁴¹ BBVA Research - <https://www.bbvarresearch.com/en/publicaciones/brazil-economic-outlook/>

⁴² Knight Frank: The Wealth Report 2014



Spotlight on Brazil's market

Fig. 10 Brazilian modern and contemporary art market (2003-2014 1st half)
Auction sales (in US\$) based on Christie's, Sotheby's and Phillips



Brazil's art market has been growing fast over the last five years. It has always been a well-established market—the Sao Paulo art biennial is the second oldest in the world after the Venice Biennale. Many of its galleries are barely more than ten years old (two-thirds of Brazil's galleries were created after 2000 and a quarter since 2010⁴³), but the market has been attracting more European and American buyers looking for lower prices for undervalued top quality artists. Although prices have increased in recent years, established modern Brazilian artists remain relatively 'cheap' in relation to many of the top modern artists in the Chinese, US and European markets.

Growth in the Brazilian art market has coincided with growth in its UHNWIs. The number of Brazilian UHNWIs increased by 71.1%, from 2,380 in 2009 to 4,072 in 2013⁴⁴. For many of these individuals, art is increasingly becoming a meaningful element of their total asset portfolios, comprising 16.9%⁴⁵ of their 'passion' investments. Traditional HNWIs are now requiring a higher level of personalisation and customised products and services⁴⁶, which presents new opportunities for the Brazilian wealth management sector or wealth managers working with Brazilian clients.

Another industry responding to the growth of the Brazilian art market is the fine art insurance industry. At the end of 2013, AXA Art partnered with SulAmérica, Brazil's largest independent insurer. The goal is to combine AXA Art's expertise and SulAmérica's distribution network to offer art insurance products and related services. Allianz had already entered the market, offering an 'all risks' policy, and local player Grupo BB & Mapfre saw the demand for its art insurance products double in 2012, confirming the growth of this market. Also, in July 2014, specialist global insurer Hiscox launched its first on-the-ground initiative in Brazil, aimed at expanding its London market business and extending its coverage of the fine art business.

The Brazilian art market still faces many challenges. In particular, the government's stop-and-go policies on liberalising the insurance market and the many barriers to entry for foreign companies illustrate the uncertainty of the regulatory environment. In spite of this, the art insurance market remains profitable and attractive, as prices are higher than in the international market due to a lack of competition.

43 According to a survey conducted in 2013 by the Latitude Project: a collaboration between the Brazilian Association of Contemporary Art and the government's Trade and Investment Promotion Agency (APEX)

44 According to the WealthInsight report: Ultra HNWIs in Brazil 2014

45 CapGemini and RBC World Wealth Report 2013

46 According to the McKinsey Global Private Banking Survey 2013 (see section entitled 'Latin America: Brazil and Mexico lead a fast-expanding market')

Brazil's art market has been growing fast over the last five years. It has always been a well-established market—the Sao Paulo art biennial is the second oldest in the world after the Venice Biennale.



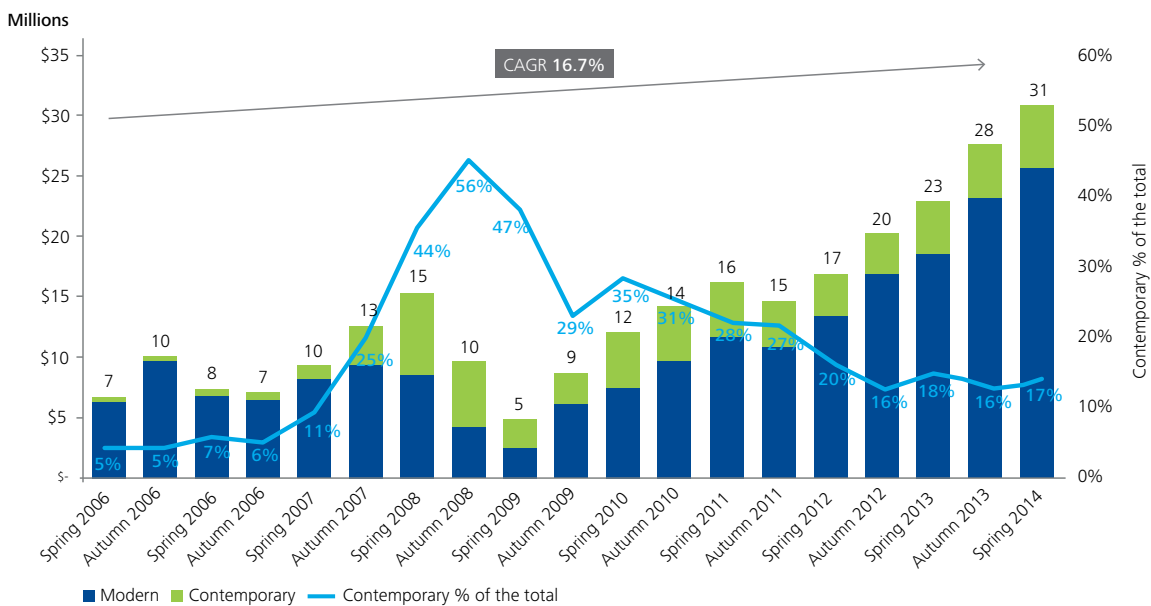
South-East Asia

There is a positive outlook for the South-East Asian modern and contemporary art market, following the strong growth registered since 2009. Rapid regional growth in the UHNWI population and wealth, combined with Singapore’s position as a financial and art market hub, point to significant opportunities to grow an Art & Finance market in South-East Asia.

South-East Asian auction sales at Sotheby’s and Christie’s raised a total of US\$50.8 million in 2013, up 36% from 2012, and up 62% versus 2011. The latest spring season of South-East Asian auction sales in April/ May 2014 reached a new high for this market, with US\$31.1 million in total sales, an increase of 12% on the last record set in autumn 2013. Modern art accounts for the lion’s share of the South-East Asian auction market, making up 83% of the 2013 sale total.

With the largest economy in South-East Asia and one of the strongest emerging markets, Indonesian artists have become a powerful force in the region. They accounted for the largest share of the South-East Asian art market at recent sales this spring: 54% of the sales value for both Sotheby’s and Christie’s auctions was for works by Indonesian artists, bringing in US\$11.7 million. This was followed by the Philippines (21%) and Singapore (16%).

Fig.11 South-East Asian modern and contemporary art market (2006 - 2014 1st half)
Auction sales (in US\$) based on Christie’s and Sotheby’s



Source: ArtTactic

OUTLOOK

Market direction: 59% of experts⁴⁷ believe the South-East Asian modern and contemporary art market will go up in the next 12 months, and a further 41% expect the market to remain around current levels in the next 12 months.

Singapore is investing in art infrastructure development: Singapore has invested significant amounts in art infrastructure, with the strategic aim of becoming the region's art market hub. With the South-East Asian art market growing, Singapore's position as a commercial and cultural hub is likely to strengthen going forward.

The Indonesian art market set to grow: while Singapore has the infrastructure, it is Indonesian artists who dominate the South-East Asian art market, with a 54% market share based on the 2013 sales results for Sotheby's and Christie's .

Art buying trend: according to Knight Frank's The Wealth report 2014, a net positive balance of 33% of private bankers and wealth advisors surveyed expect the popularity of art buying among their Australasian UHNWI clients to increase.

Wealth outlook: according to the Wealth-X and UBS World Ultra Wealth Report 2013, Singapore has most UHNWIs in South-East Asia, with a total population of 1,355 individuals with a total wealth of US\$160 billion (up 3.2% from 2012). This is followed by Indonesia (865 individuals with US\$130 billion in total wealth), which experienced stronger growth of 10.2% and 8.3% respectively in 2013. Other rapidly growing UHNWI markets are Thailand, with 15.2% growth in the UHNWI population and 15.8% growth in total wealth. According to Barclays' research⁴⁸, wealthy individuals in Singapore hold 16% of their total wealth in treasury assets (mainly jewellery, fine art and wine). With rapid growth in wealth creation in markets such as Thailand, Indonesia, Malaysia and the Philippines, we can expect this to have a positive impact on the art markets and its artists going forward.

⁴⁷ ArtTactic confidence survey of 360 art collectors, art advisors, galleries and auction houses in July 2014

⁴⁸ Barclays Wealth Insights report: Profit or Pleasure? (2012)



Russia

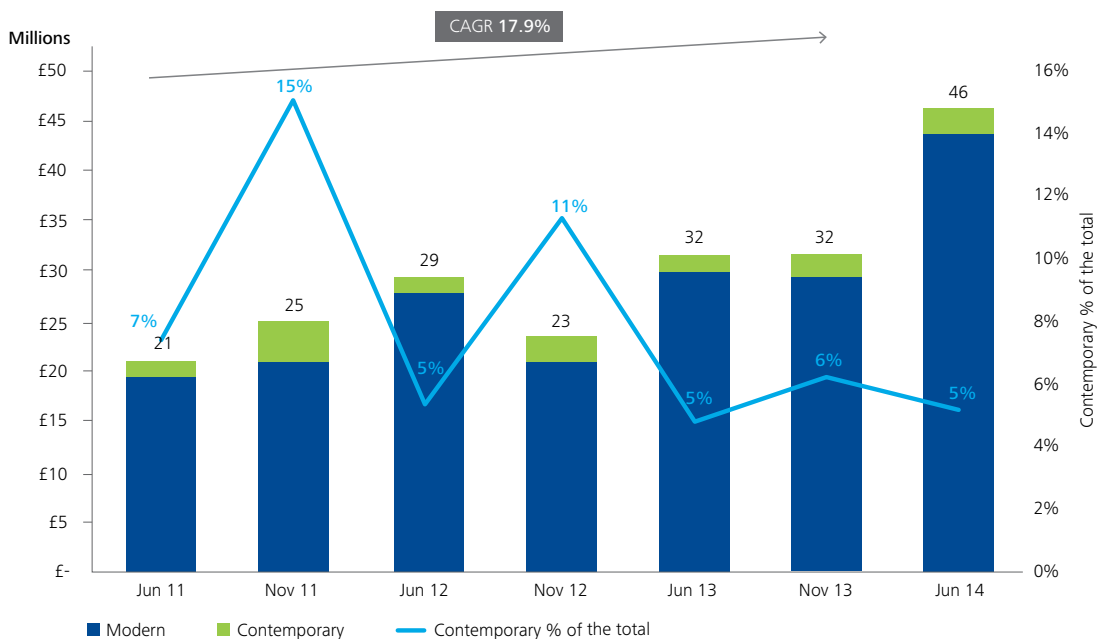
Auction sales of modern and contemporary Russian art in the first half of 2014 revealed signs of renewed confidence in this market. This is likely to highlight the advantages of art as a tangible and moveable asset for collectors.

Modern and contemporary Russian art auction sales rose by 21% between 2012 and 2013, signalling increasing confidence in the Russian art market. The positive tone in the market has continued in 2014, with the highest sales of modern and contemporary Russian art since 2008.

In June 2014, Sotheby's raised a total of £15.6 million from modern and contemporary Russian art, against £6.7 million for MacDougall's and £4.97 million for Christie's.

Sotheby's total was almost as big as the total auction sales for 2013 combined, which signals that the Russian art market could see a strong year in 2014. Notable prices were achieved by paintings by Russian artists such as Ilya Mashkov, Mikhail Nesterov, Nikolai Fechin, Natalia Goncharova and Lado Davidovich Gudishvili. However, contemporary Russian artists were almost entirely absent from the latest June sales, accounting for only 5% of the total Russian modern and contemporary art market.

Fig. 12 Russian modern and contemporary art market (2011 - 2014 1st half)
Auction sales (in GBP) based on Christie's, Sotheby and MacDougall's



Source: ArtTactic

OUTLOOK

Market direction: an ArtTactic art market poll conducted in July 2014 showed that 39% of respondents believe that the Russian art market will go up in the next 12 months (this is up from 29% in 2013). A further 40% believe the market will remain around the current levels and 21% think the market will go down in the next 12 months.

Increasing confidence among Russian buyers: recent sales show increasing participation and confidence among Russian buyers for high-end Russian avant-garde and modern Russian artworks. Christie's reported that 74% of the buyers at its auction were Russian, while for Sotheby's, 75% of the buyers were from Russia or the CIS. According to Sotheby's, about 40% of its works came from Russian sellers, with 60% from non-Russians.

Contemporary Russian art remains marginalised in the current art auction market, and the expectation that the Saatchi Gallery exhibition of Russian contemporary art in 2012 and 2013 would rejuvenate this market has so far failed to properly materialise.

Art buying trend: according to Knight Frank's The Wealth report 2014, a net positive balance of 57% of the private bankers and wealth advisors surveyed expect the popularity of art buying among their Russian/CIS UHNWI clients to increase.

Wealth outlook: according to the Wealth-X and UBS World Ultra Wealth Report 2013, Russia's UHNWI population is ranked ninth in Europe, with a total population of 1,180 individuals with a total wealth of US\$620 billion (up 3.1% from 2012). A survey carried out by Knight Frank⁴⁹ of private bankers and wealth managers found that 55% expected the UHNWI population in Russia to increase in 2014. It is also worth noting that the departure of many UHNWIs from Russia has boosted the number of UHNWIs in global cities such as London, New York and Dubai, which is likely to have a further positive impact on sales of Russian art in locations like London.



Africa

International and domestic sales of African modern and contemporary art is on the increase, fuelled by rapid growth in the UHNW population in Nigeria. This has created a new generation of African collectors with an interest in art as an asset class and opens up the possibilities for a future Art & Finance industry as the art market matures in the region.

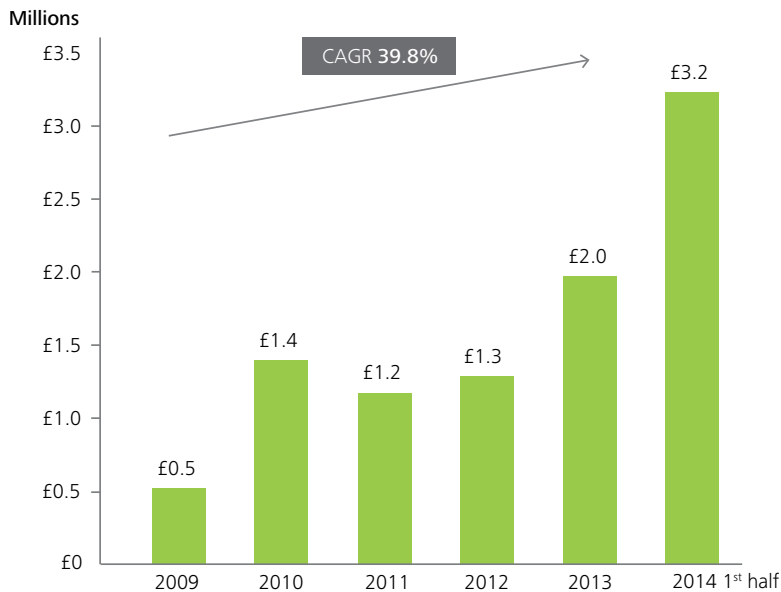
Bonhams is the only auction house with an annual sale dedicated to contemporary African art. The first auction was organised five years ago in London, and has seen strong growth since, with the recent sales in May 2014 raising £3.23 million, up 47% from 2013.

The Nigerian auction house, Art House Contemporary, registered a 25% increase in auction sales between 2008 and 2012, while 2013 was a record-breaking year, with US\$1.7million in overall auction sales (+21.8% versus 2012).

Meanwhile, African art is also attracting strong interest from museums, and last year's Venice Biennale had a record number of African pavilions. Angola took the award for best national pavilion, the first African country to ever win the prize. Tate Modern had the first major retrospective of Sudanese painter Ibrahim El-Salahi, as well as a special installation of the works of Meschac Gaba. El Anatsui also exhibited at the Brooklyn Museum of Art in New York last year.

Fig. 13 African contemporary art: Bonhams

Auction sales (in GBP) based on Bonhams' 'African Now' annual auction sales



Source: ArtTactic

OUTLOOK

Market direction: 33% of the experts surveyed believe the African modern and contemporary art market will go up in the next 12 months, 46% expect that the market will remain flat and 21% think the market will come down in the next 12 months.

Economic growth and wealth creation: growing wealth and rising interest in the rich history of the visual arts have seen fine art sales grow rapidly in Africa. The boom has been most pronounced in Nigeria and South Africa, the continent's two biggest economies, which between them account for half of Africa's billionaires. Increasingly, local rather than imported artworks adorn the walls of many of the local collectors.

Health warning: with the African art market still in its early stages of development, some experts worry that the large sums of money flooding into the region could lead to rapidly appreciating prices followed by market speculation and manipulation.

Art buying trend: according to Knight Frank's The Wealth Report 2014, a net positive balance of 39% of the private bankers and wealth advisors surveyed expect the popularity of art buying among their African UHNWI clients to increase.

Wealth outlook: according to the Wealth-X and UBS World Ultra Wealth Report 2013, Nigeria could have the largest UHNW population and wealth in Africa in 2014, overtaking South Africa. Nigeria accounted for 60% of the growth in Africa's UHNW population and 80% of the increase in the continent's UHNW wealth. At the same time, Nigerians are becoming Africa's most influential collectors of modern and contemporary art, and the market is starting to rival its more established South African counterpart.



Hala Khayat,
Christie's specialist and Head of
Modern and Contemporary Arab
and Iranian Art sales

Hala Khayat was appointed as a specialist for contemporary Middle Eastern and Iranian art, based in Christie's Dubai office, in 2007, and was promoted to Head of Sales in 2013. Hala Khayat has a BA in Fine Arts & Visual Communications from the University of Damascus, Syria, and an MA in Design Studies from Central St Martin's College of Art & Design, London. She has held a variety of roles in the world of art and journalism, including working as an art consultant for galleries in Damascus. She also lectures on the history of Arab art and the Middle Eastern art market. She has been resident in Dubai for the past ten years. She is intimately involved in consigning rare artworks, writing the catalogues for the Christie's twice yearly art auctions in Dubai, held in April and October. Her job includes evaluating, pricing and researching the artworks, producing condition reports, overseeing catalogue production and writing essays. She is also the Arabic spokesperson for Christie's in Middle East.

An informed view from the Middle East

For anyone interested in growth markets in the art world, an informed view of works of art from the Middle East is essential. There has been a long history of art in this region, stretching for more than a hundred years, from Persia to the Levant countries, Egypt and North Africa and more recently the Gulf region.

The art is very rich and unique in its inspiration with strong, local identities and a defined visual vocabulary. Since 2006, Christie's has sold more than US\$250 million-worth of art, watches and jewellery through our regular Dubai sales. In that time, we have adapted the sales to suit the needs of our clients. Our two most recent sale seasons have totalled more than US\$10 million, and the introduction of our first online only sale in the category in 2013 proved extremely popular with existing clients and introduced us to a significant number of new clients who had not bought with us previously. Also, in October of last year, we held our first Christie's Education event—a three-day course to introduce people to the international art market. A second edition will be held to coincide with our next sale season this October.

A very positive aspect of this market is the stability and steady growth it has enjoyed over the last ten years, most notably among international collectors. Christie's has been holding twice-yearly sales in this category in Dubai since 2006, which not only provides international reach for artists from the region, but also a regular opportunity for those interested in art to convene. The art market in the region is now well established, with two serious art fairs held in the United Arab Emirates twice in the yearly calendar, finishing this year in Abu Dhabi Art Fair with its 9th edition, and starting next year in the spring with Art Dubai, now in its 10th edition. A series of festivals, art events, biennales and art exhibitions spreading from Beirut, Sharjah and Cairo, all the way to Marrakesh, have all been set up and have thrived in this environment. It works because it is a collaboration with all those taking part—auction houses, collectors, gallerists and artists—working together to ensure the growth it enjoys is steady and sustainable.

Q: What is the current state of the Middle Eastern art market? How does the future look?

The future looks even more exciting. With the confirmation of the opening of a series of museums (in the UAE and Qatar), people from the region will finally be able to see and study works of art from their own region that are the narrative behind their own story. The most recent example of the important role institutions will have in the region is the amazing Mathaf Museum in Doha, which is the home to thousands of modern and contemporary works by Arab and some Iranian artists. These new museums will join the existing government-run museums and foundations in cities including Cairo, Alexandria, Damascus, Beirut and Baghdad.

In addition there are now some serious private initiatives supporting and encouraging artists in the region, such as Abraaj Capital—one of the most serious art prizes to be launched in Dubai.

It is also important to recognise the importance of art-specific publications for the region, which have raised awareness and become a useful resource for international collectors to follow and become better informed about Middle Eastern art. Christie's catalogues, written and researched by specialists in the field, are also considered to be a very valuable tool and are published in full online, which makes them very accessible.

Q: What factors will influence the future?

Artists are mirrors reflecting their surroundings. Today, a lot of the themes tackled by artists in the region are political—about war, human rights, religion, freedom and the role of women in society. Political stability in the whole region will definitely have a positive influence on the art produced in the future.

Q: If you can see the market growing, where do you think the growth will come from?

The world is becoming a smaller place, and looking to the future I have already witnessed the importance of technology, just in the last eight years since our first sale. First it was digital images, then the ease with which clients could view them, then the number of devices they could use to access the information

and finally, just last October, we held our first ever online-only sale in my category. This move proved to be extremely successful. We have seen collectors in faraway places, transacting online and buying works by Middle Eastern artists; they have embraced the ability to both bid through the internet via ChristiesLIVE and participate in the online-only sale, the first of which, as I said, was held in this category last year.

Another tool for us at Christie's is our catalogues, now also all published online. Using our worldwide collector base, we are able to reach collectors all over the world. While initially the majority of the works were bought by collectors in the region, we now have about equal buying from an ever-growing international collecting group. This adds real strength and depth to the market and each season the numbers participating increases. So we can see that growth comes from the local as well from the international communities.

Today more than ever, artists from the Middle East are represented at international fairs.

Q: Looking to the future and the next generation of artists... what would you recommend collectors to be watching out for? Any trends?

In growth markets, price points tend to be more affordable, and this helps to encourage the novice collector. Many of the works we offer start at around US\$2,000, still considered affordable in comparison to other markets. Generally, collectors from the Middle East are first motivated to collect art from their own countries. Then, as their collecting matures, they are happy to consider art from other nations.

This then acts as a springboard to the international art market and other categories. What begins as an act of patriotism becomes a growing passion to see art and appreciate the ideas and search for the true meanings within it. From here they begin to recognise common links with international artists. It is a gradual process, and becoming a true collector can take a lifetime.

Section 2: Art and wealth management survey

Highlights

- **The role of art and collectible assets in an increasingly competitive wealth industry:** with total wealth among Ultra-High Net Individuals (UHNWIs) reaching US\$ 27.8 trillion in 2013, competition in the private wealth industry is intensifying, and the wealth industry is increasingly focusing on client-centric value propositions, including art and collectibles-related services
- **Art increasingly accounts for a larger proportion of individual wealth:** wealth managers see the evident rise in art prices and values in both absolute terms and relative to their clients' overall portfolio (art in wealth portfolios is estimated at US\$ 1.5 trillion), as a strong argument for starting to offer services and products to help clients manage this new wealth
- **Increasing awareness of art as an asset class:** 53% of wealth managers had a high level of awareness of developments linked to art as an asset class, up from 43% in 2012 and 33% in 2011; this signals that increasing attention is being paid by the wealth management community to the art and collectibles market
- **The Deloitte/ArtTactic Art & Finance Future Indicator** has increased by 61% from 2012 and now stands at 39, which points to the wealth management community taking a more strategic view on art-related services in the next 12 months compared with 2012
- **Increasing demand for art-related services:** 38% of wealth managers (up from 33% in 2012 and 11% in 2011) say that their clients are increasingly requiring their wealth managers to help with art-related issues, but wealth managers need to listen to their clients' needs to develop their art and wealth management offering
- **Wealth managers can provide clients with exclusive access to the art world:** 72% of art professionals said that their clients' primary reason for buying art was related to the social and networking aspects that the art market offers and the status of being associated with buying art. There is a clear opportunity for wealth managers to provide their clients with access to this exclusive 'club'
- **The majority of collectors buy art for passion with an investment perspective:** 76% of art collectors are buying art for collecting purposes, but with an investment view (up from 53% in 2012). This implies that the investment aspects of art (its financial or economic value) is something that collectors are increasingly focusing on
- **Key art and wealth management priorities in the next 12 months:** wealth managers will focus on art and estate planning, art and philanthropy and art secured lending in the coming year
- **More banks are offering art secured lending:** 36% of the private banks surveyed said that they offer art lending and art financing services using art and collectibles as collateral; this is up from 27% in 2012 and 22% in 2011
- **New insurance products could help expand the art secured lending market:** a range of insurance products could potentially help the art secured lending market to reach £15-20 billion per annum⁴⁹
- **Family offices see art as a diversification tool:** 50% of the family offices surveyed said that one of the most important motivations for including art and collectibles in their service offering was because of the potential role it could play in a balanced portfolio and asset diversification strategy
- **Client entertainment remains important:** private banks and wealth managers continue to be avid supporters of art, mainly through corporate patronage and sponsorship. 41% of the private banks felt that client entertainment was one of the strongest arguments for including art in a wealth management context (this was up from 27% in 2012)
- **Lack of regulation remains a key obstacle:** the overriding challenge for the development of the Art & Finance industry remains the unregulated nature of the art market, combined with a lack of transparency and difficulties in sourcing and finding the right art-related expertise
- **Freeports as competence clusters for the Art & Finance market:** freeports specialising in tangible valuable goods offer the possibility for wealth managers to develop competence centres for these assets. This is especially the case with Luxembourg, Singapore and Switzerland

Art in a client-centric wealth management strategy

With total wealth among Ultra High Net Worth Individuals reaching US\$ 27.8 trillion⁵⁰ in 2013, competition in the private wealth industry⁵¹ is intensifying, as an increasing number of institutions are competing to service and manage the assets of relatively few, very wealthy individuals and families, including financial wealth linked to art and collectibles. Deloitte estimates that there are at least 400,000 art collectors in the top wealth segments (HNWIs and UHNWIs), with an estimated USD 1.5 trillion of wealth in art assets.

One of the key debates in the wealth industry at the moment is how wealth managers can build sustainable and better value-added relationships with their clients. One of the key strategies will be to develop client-specific value propositions, which will require more insight and understanding of the clients' diverse backgrounds, financial needs and investment behaviours. A more client-specific value proposition will force wealth managers to develop better knowledge of multiple markets and segments, and the wealth management survey findings in this report suggest that there are strong reasons and potential benefits for developing a specific value-proposition around art and collectibles, as part of a client-centric wealth management strategy.

The success of an art and collectibles-related value proposition will depend on wealth managers' ability to first of all understand the client's specific needs and then seamlessly put together multiple experts and third-party service functions to deliver the required product. As mentioned in last year's Art & Finance report, a closer relationship between the wealth management industry and the art professional community will be necessary in order to deliver a client-specific value proposition for art and collectibles.

One of the key debates in the wealth industry at the moment is how wealth managers can build sustainable and better value-added relationships with their clients

⁴⁹ Robertson Taylor W&P Longreach estimated today's art lending market to be in the region of £6 billion per annum, but with the potential to reach £15-£20 billion per annum.

⁵⁰ Wealth-X and UBS: World Ultra Wealth Report 2014

⁵¹ From page 2 of the Deloitte 2014 Private Wealth Outlook, 'Championing growth Redefining the roles and responsibilities of the evolving family office': The private wealth industry does not have one universally accepted definition. Broadly, it refers to the multitude of entities and institutions that serve the financial needs of high-net-worth individuals and families

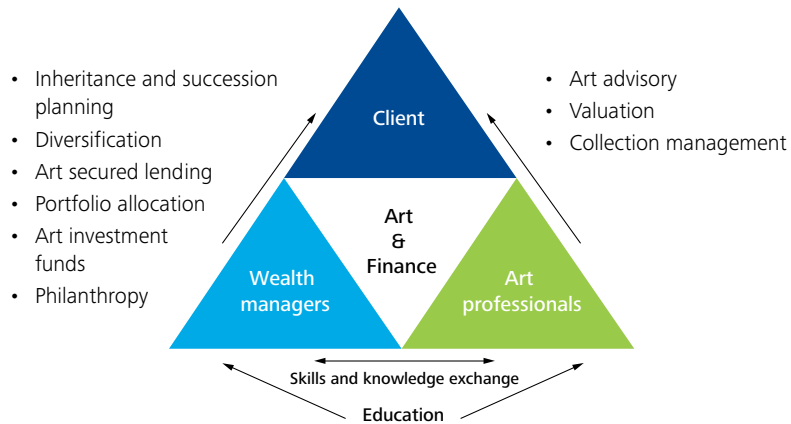


Stakeholder analysis: a comparative view

In this section we present the survey findings for private banks, family offices, art professionals and art collectors, from surveys conducted in May and June 2014 on issues related to art and wealth management. The aim was to gain a better understanding of the motivations, current involvement and challenges that each of these stakeholders are up against, and how an effective strategy can be developed to bring these stakeholders together, to help create a better foundation for the Art & Finance industry.

Overview of private banks, family offices, art professionals and collectors

The first part of the analysis aims to provide a combined view of the stakeholders involved in the Art & Finance industry. We hope this will bring together some of the key elements raised by each stakeholder group (private banks, family offices, art professionals and art collectors) and help us to identify the aspects in relation to which stakeholders' views are aligned and on which topics they differ, and the likely implications of this in the future.

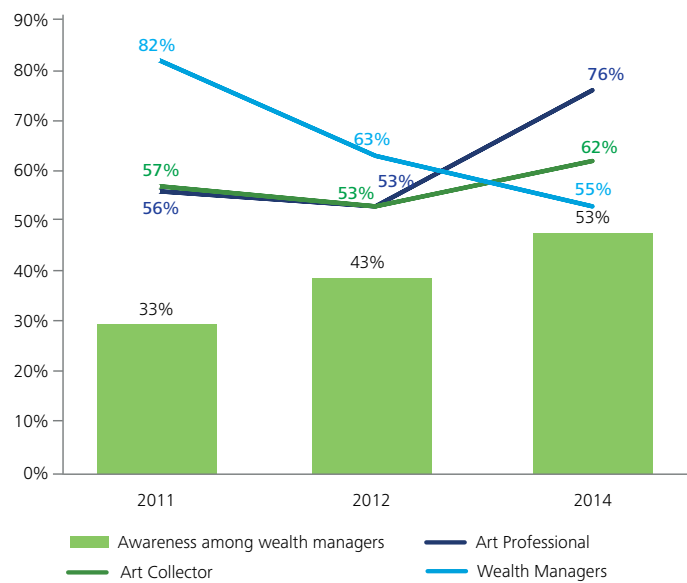


Perception: converging views on art as an asset class

While the wealth management community felt enthusiastic about the prospect of art in traditional wealth management in 2011, their enthusiasm seems to have been curbed by an increasing realisation (and awareness) of the complex nature of the unregulated art and collectibles market and its interaction with an increasingly regulated financial services industry⁵². In Section 5, some of these legal issues are discussed in more detail. However, as the Art & Finance industry gradually matures, a significant 53% of private banks and 57% of family offices believe that there is a role for art in traditional wealth management. It is also interesting to note that both the art collector (typically a wealthy client) and the art professional (typically a third-party service provider) are increasingly convinced about the advantages of art as an asset class and its role in traditional wealth management. A large majority, 76% of art professionals and 62% of collectors, believe that private wealth managers should incorporate art and collectibles into their service offering.

Collectors buy art for passion with an investment view: although only 9% of art professionals say their clients buy art and collectibles for investment purposes (only 3% of art collectors say they buy art for investment purposes only), 81% of art professionals believe that their clients are buying art for collecting purposes (up from 77% in 2012), but with an investment view. 76% of art collectors said the same (up from 53% in 2012). This implies that the investment aspect of art (its financial or economic value) is becoming increasingly important among buyers of art and collectibles.

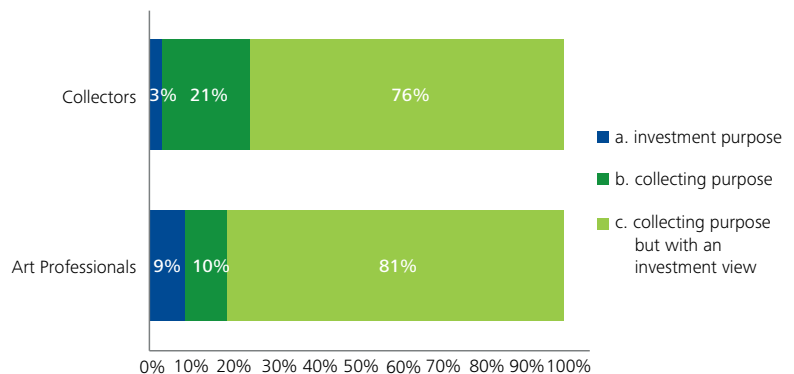
Fig. 14 Do you think that art and collectibles should be part of a wealth management offering?



Sample	2011	2012	2014
Private banks	19	30	35
Family offices	0	0	14
Art collectors	48	81	90
Art professionals	140	112	122

Source: Deloitte Luxembourg & ArtTactic Art & Finance Report 2014

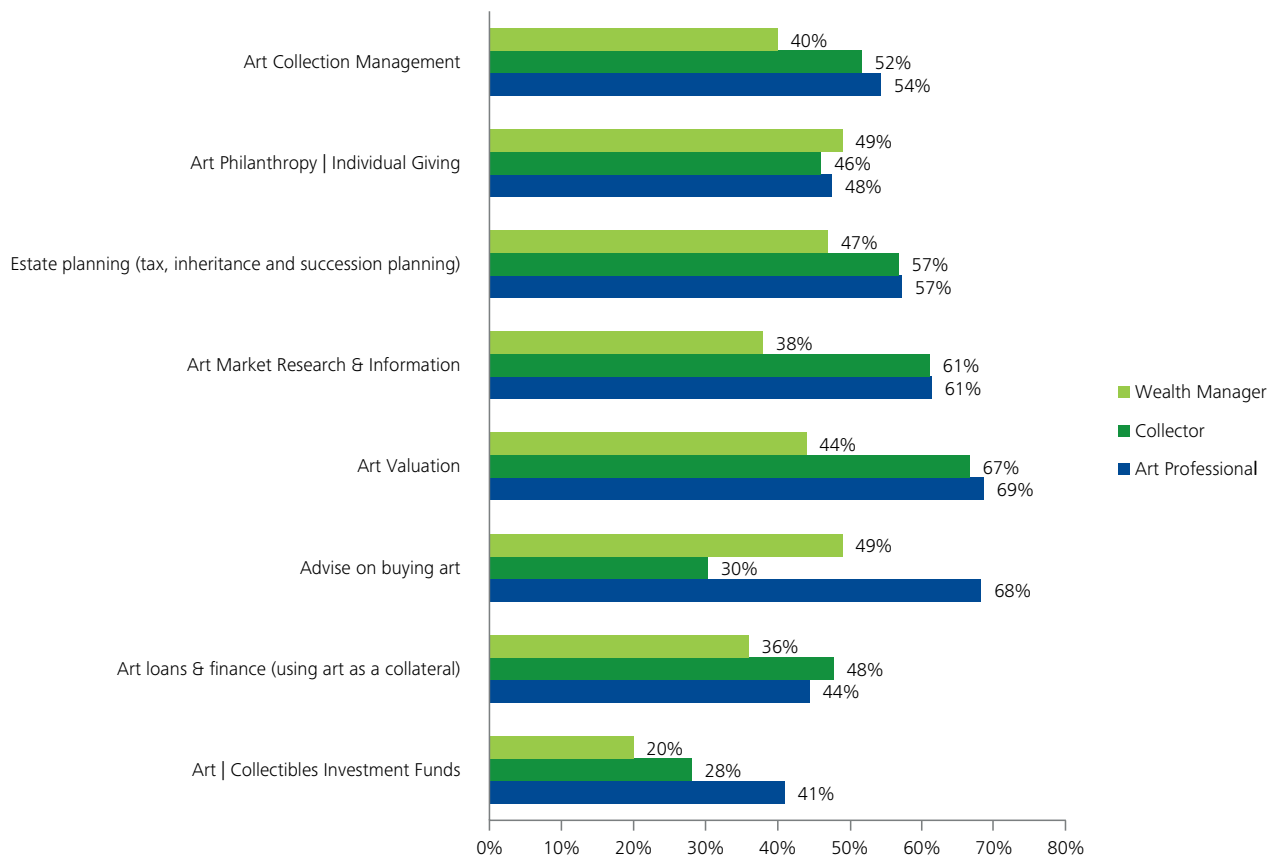
Fig. 15 Why are you/your clients buying art?



Source: Deloitte Luxembourg & ArtTactic Art & Finance Report 2014

⁵² We cannot ignore the fact that the decline also could be a result of the changes and growth in the sample. The first Art & Wealth management survey was conducted in 2011 and included 17 private banks from Luxembourg. In 2012, the sample was increased to 30 private banks, including banks from Poland and Spain. The latest survey included 35 banks, mainly in Europe, the United States and Asia (with no participation from Poland this year), and an additional 14 family offices in Europe and the United States

Fig. 16 Which of the following 'art and wealth management services' do you feel would be most relevant to your clients and/or the institution you represent?



Source: Deloitte Luxembourg & ArtTactic Art & Finance Report 2014

Current needs versus current offering

According to the above comparative analysis, there are a number of areas that need the focus of a wealth manager, while some areas are better left to others.

Art advisory best left to others: advice on buying art should not be a wealth manager’s main preoccupation; despite both wealth managers and art professionals listing this as one of the key services offered, it is among the lowest priorities on art collectors’ wishlists, with only 30% saying they wanted art advisory services from their bank. This could be due to the fact that most established art collectors already have a long-standing relationship with art advisors, galleries and auction houses.

Raising the credibility of valuation, art market research and information: both art collectors and art professionals strongly believe that valuation, research and information services should be offered by private banks or family offices. It is likely that the neutral position of the wealth manager would give more credibility to both art valuation and research. The increasing confidence in online art businesses providing valuation, research and information (see Section 4), could suggest that new tools might be available to the wealth management community in the near future, enabling it to address this particular market need.

Collection management and consolidated reporting:

both collectors and art professionals see collection management as an important aspect of a wealth manager's remit, and provides the wealth manager with an opportunity to integrate the client's art and collectible assets into an overall asset management and wealth reporting structure. 71% of family offices said that their clients wanted to include art and other collectible assets in their wealth reports, in order to have a consolidated view on their wealth. 52% of the private banks said the same.

Estate planning: it is evident from the sentiment of both art collectors (57%, up from 42% in 2012) and art professionals (57%, up from 32% in 2012) that issues related to estate planning are increasingly becoming a high priority. It is also good to see that 88% of family offices and 64% of private banks said that this would be a strategic focus in the coming 12 months. There seem to be an increasing recognition that wealth managers need to respond to their clients' growing estate planning needs in key areas related to art and collectibles, particularly with regard to valuation, taxation, inheritance and succession planning.

Art secured lending: in the Deloitte/ArtTactic survey of important art collectors and art professionals, 48% of collectors said they would be interested in using their art collection as collateral for a loan (this was up from 41% in 2012). Again, parts of the wealth management community seem to be responding, with 40% of private banks having said that this would be a strategic focus in the coming 12 months. This was up from 13% in 2012, and signals an increasing confidence in using art and collectibles as collateral for financing purposes.

The demand for art investment funds is likely to increase in the next two to three years:

41% of art professionals and 28% of art collectors feel that an art investment fund is a service that the wealth management industry should be able to offer. Although this is not a top priority at the moment, 68% of art professionals and 62% of art collectors believe the art fund industry will expand in the next two to three years, and it is important that the wealth management industry keeps abreast of developments in this market. 25% of family offices said they would increase their focus on art investment funds in the next 12 months, against 8% of private banks.

While the wealth management community felt enthusiastic about the prospect of art in traditional wealth management in 2011, their enthusiasm seem to have been curbed by an increasing realisation (and awareness) of the complex nature of the unregulated art and collectibles market and its interaction with an increasingly regulated financial services industry

General motivation and perception among wealth managers, art professionals and collectors

A. Private bank and family office survey findings

1. Awareness

Wealth managers are becoming increasingly aware of the development of art as an asset class: 53% of wealth managers (private banks and family offices) were aware/very aware of the developments linked to art as an asset class, up from 43% in 2012 and 33% in 2011, which suggests that increasing attention is being paid by the wealth management community to what is happening on the art market. 69% of the wealth managers said that their awareness has been heightened through increasing media interest (against 53% in 2012), and 60% said they had been exposed to the topic through conferences and seminars (against 57% in 2012).

Is there an argument for including art and collectibles in traditional wealth management?

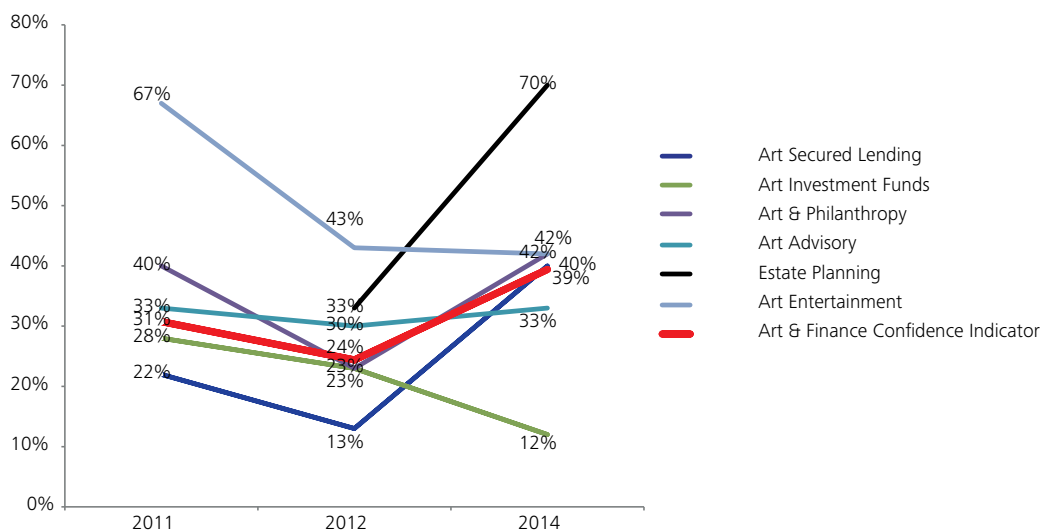
57% of the family offices and 53% of the private banks surveyed believe there is a strong case for including art and collectibles in traditional wealth management,

while 76% of art professionals and 62% of collectors believe that private wealth managers should incorporate art and collectibles into their service offering. This highlights the need and client demand, but also raises questions about the type of services that should be offered, and how.

2. Focus in 2015: the wealth industry is likely to focus more on art and wealth planning services in the next 12 months

With the global art market reaching US\$65 billion⁵³ in 2013, up 8% versus 2012, it is clear that art and collectibles have become an increasingly important part of the UHNWI's overall asset portfolio. The findings of this section indicate that the wealth management industry is taking a more strategic view on art as asset class and how it could be used as a strategic tool to build stronger and deeper relationships with clients, by focusing on both the financial aspects of art as well as the emotional and social characteristics associated with this asset class.

Fig. 17 Confidence—which services will you focus on in the next 12 months?



Source: Deloitte Luxembourg & ArtTactic Art & Finance Report 2014

Deloitte/ ArtTactic Art & Finance Future Indicator

The Deloitte/ArtTactic Art & Finance Future Indicator⁵⁴ has increased by 61% since 2012, and now stands at 39, which signals that the wealth management community is taking a more strategic view with regard to art-related services in the next 12 months than in 2012.

In particular, there are three art-related financial services that wealth managers will focus on in 2015: art and estate planning, art and philanthropy and art secured lending.

Art and estate planning: 70% of wealth managers (88% of family offices and 64% of private banks) said that this will be a strategic focus in the coming 12 months. There seems to be an increasing recognition that wealth managers need to respond to their clients' growing estate planning needs in key areas related to art and collectibles, particularly with regard to valuation, taxation, inheritance and succession planning, as well as charitable donations and philanthropy.

Going forward, it is not only individuals and families with valuable art or art collections that will need these services, but also the artists and their families. In 2010, artist-endowed⁵⁵ foundations in the United States reported aggregate assets of US\$3.48 billion, of which US\$1.99 billion (57%) were art-related assets (up 83% from 2005). Over the last several decades, the number of artists whose careers have thrived during their lifetimes has grown significantly, a shift that has allowed artists and their families more time, resources and flexibility to plan ahead. As the market for modern and contemporary art continues to expand, the number

of artist-endowed foundations is likely to increase, and the need for a new type of wealth management service for artists and their estate planning could be a growth opportunity for the wealth management industry in the near future.

Art and philanthropy: 42% of wealth managers (63% of family offices and 36% of private banks) said that this will be a strategic focus in the coming 12 months. Again, family offices seem to put more emphasis on philanthropy than the majority of private banks. The issue of art and philanthropy is something that has increased in importance in the last decade and is linked to the previous point on art and estate planning. The increasing value of art assets has meant that artist foundations⁵⁶ are playing an increasingly important role in terms of grant-making to the arts and other charitable causes, and major art collectors are also combining their passion for art and art collecting with a strong philanthropic agenda.

Art lending: 40% of private banks said that this will be a strategic focus in the coming 12 months. This was up from 13% in 2012, and signals an increasing confidence in using art and collectibles as collateral for financing purposes. The focus on these types of financial products is linked to stronger client demand for art-related financing. In the Deloitte/ArtTactic survey⁵⁷ of important art collectors and art professionals, 48% of the collectors surveyed said they would be interested in using their art collection as collateral for a loan (this was up from 41% in 2012). As family offices are not credit institutions, none of the family offices answered 'yes' to this question.

In particular, there are three art-related financial services that wealth managers will focus on in 2015: art and estate planning, art and philanthropy and art secured lending

⁵³ Source: TEFAF Report 2014

⁵⁴ The Deloitte/ArtTactic Art & Finance Future Indicator tracks wealth managers' strategic focus on Art & Finance-related services in the coming 12 months, based on six main activities: art secured lending, art investment funds, art and philanthropy, art advisory, art and estate planning and art entertainment. The Future Indicator is the average result of how wealth managers view their future focus in six of these underlying art-related services (i.e. 37 signals that 37% of the wealth managers will focus on these art services in the next 12 months)

⁵⁵ Sources: http://www.aspeninstitute.org/sites/default/files/content/docs/psi/AEF_V1.pdf

⁵⁶ Among recently deceased artists who set up foundations are Louise Bourgeois (the Easton Foundation) and Cy Twombly. Living artists who have set up foundations and are already making substantial gifts of money and artworks include painters Alex Katz, Ellsworth Kelly, LeRoy Neiman and Helen Frankenthaler

⁵⁷ A total of 122 art professionals and 90 important art collectors were surveyed on a variety of topics related to art as an asset class, their motivations and current and future involvement, and the challenges and opportunities

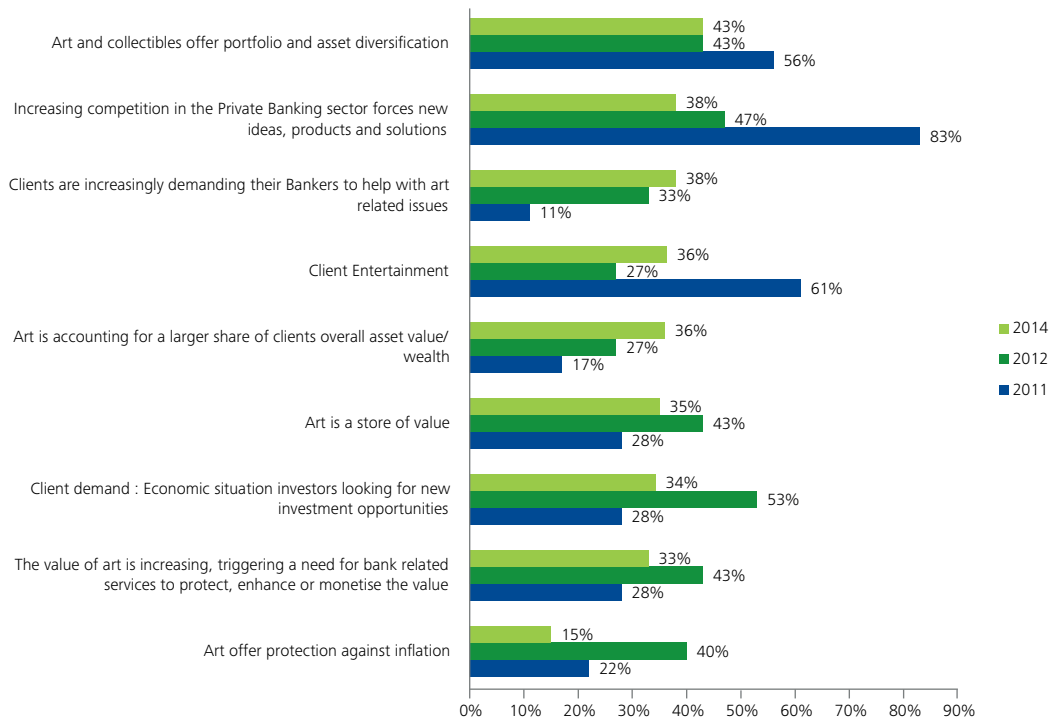
3. Motivations

There is no particular argument that stands out when it comes to motivations for including art and collectibles in a traditional wealth management practice. However, a number of motivations seem highly relevant, ranging from wealth protection, diversification and investment to entertainment. These are all aspects of art and collectibles that wealth managers should start to integrate into their discussion with their clients and prospects.

Family offices see art as a tool in a portfolio diversification strategy:

43% of wealth managers said that one of the most important motivations for including art and collectibles in their service offering was because of the potential role it could play in a balanced portfolio and asset diversification strategy. This percentage was higher among the family office representatives, where 50% of the respondents said diversification was one of the main motivations.

Fig. 18 What do you consider the strongest arguments for including art and collectibles in traditional wealth management/private banking?



2011 refers to the data collected in 2011 for the **Art & Finance Report 2011**
 2012 refers to the data collected in 2012 for the **Art & Finance Report 2013**
 2014 refers to the data collected in 2014 for the **Art & Finance Report 2014**

Source: Deloitte Luxembourg & ArtTactic Art & Finance Report 2014

Art is accounting for a larger share of overall

asset value: the value of art and collectibles has risen significantly in recent years, while at the same time, a larger amount of wealth has been allocated to this asset class. Wealth managers see the evident rise in values—in both absolute and relative terms to their clients' overall portfolio—as a strong argument for starting to offer services and products to help clients manage this new wealth. 31% of family offices and 38% of private banks said that this was one of the main reasons for including art in the traditional service offering (up from 27% in 2012, and 17% in 2011).

More demand for art-related services will force banks to build a strategy encompassing art and collectible assets:

38% of wealth managers said that their clients were increasingly requesting assistance with art-related issues (this is up from 33% in 2012 and 11% in 2011). The demand for these types of services seems to be stronger among family offices, with 54% saying that clients want them to help with art-related issues. We believe this factor is likely to become an important driver for wealth managers' increasing engagement with the art and collectibles market.

Client demand for art and collectibles is less

dependent on the economic situation: 39% of the wealth managers and 23% of family offices said the current economic situation encouraged clients to look at new investment opportunities such as art. This was down from 53% in 2012, and signals that the economic situation is a less important argument for investing in art compared with two years ago.

Art as a store of value: despite the economic recovery and bounce back of the performance of traditional investments, 38% of the family offices surveyed and 33% of the private banks said they view art as a 'store of value' (against 43% in 2012 and 28% in 2011).

Client entertainment remains important: although some of the financial characteristics of art and collectibles are attractive to the wealth management industry, the emotional and social aspects of art cannot be forgotten. Private banks and wealth managers continue to be avid supporters of the arts, mainly through corporate patronage and sponsorship. 41% of private banks felt that client entertainment was one of the strongest arguments for including art in a wealth management context (this was up from 27% in 2012), but only 25% of family offices felt the same.

Wealth managers see the evident rise in values—in both absolute and relative terms to their clients' overall portfolio—as a strong argument for starting to offer services and products to help clients manage this new wealth

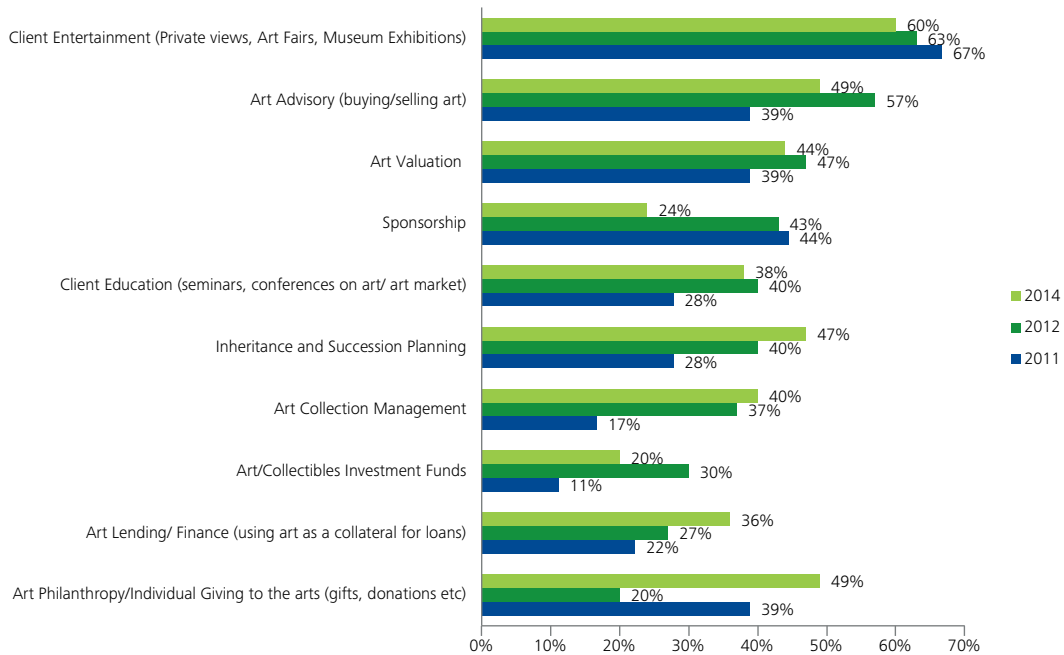
Current engagement

Current engagement: what type of art-related services do you currently offer?

73% of the wealth managers surveyed said they offered some kind of art-related service: a majority of the family offices (57%) and private banks (81%) surveyed offer some kind of service related to art and collectibles, including entertainment. This is up from 63% of the private banks surveyed in 2012.

More than 70% of the wealth managers surveyed said they had offered this service for more than three years, with 30% of wealth managers adding art-related services in the last one to three years. 38% of family offices had offered an art-related service for between one and three years, which suggests that these types of wealth management companies are increasingly taking an interest in art as an asset class and how best they can service their clients in this regard. Of the banks not yet offering art-related services, 40% said they were very likely to do so within the next two to three years.

Fig. 19 Which of the following services do you offer?
(% shown below are for combined internal and third-party services)



Source: Deloitte Luxembourg & ArtTactic Art & Finance Report 2014

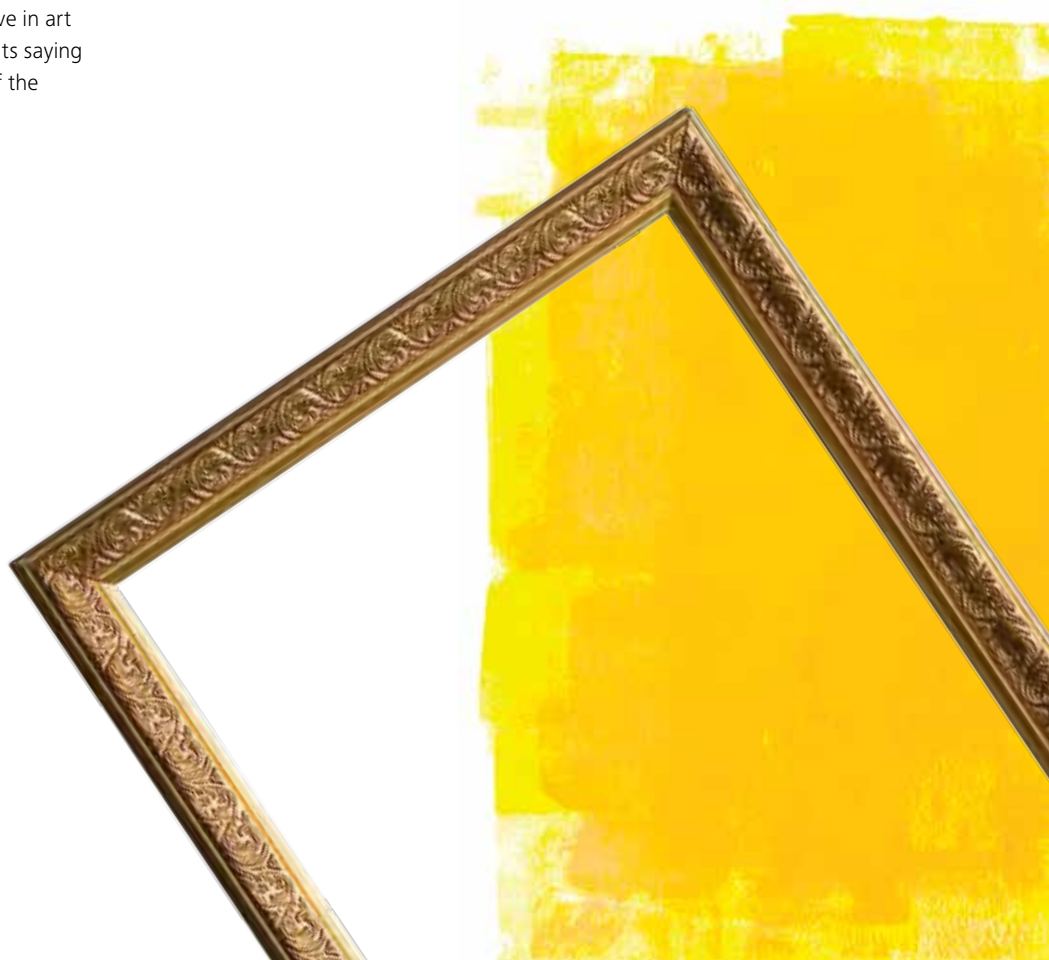
Services in the area of art protection are most likely to develop the fastest

Art and wealth planning is high on the list of services currently provided: most private banks (81%, up from 71% in 2012) are already offering art-related services. A smaller number, 57%, of family offices said they were offering art-related services. As in the last survey in 2012, client entertainment (private views, visits to exhibitions, etc.) remains the art-related service most commonly offered by private banks and wealth managers. However, it looks like the trend towards offering more specific art-related services, which started in 2012, has developed further since the last report.

One area that is worth paying attention to is the increasing portion of wealth managers that are providing inheritance and succession planning services—currently 61% of the private banks surveyed are offering this service (up from 40% in 2012, and 28% in 2011).

Among the family offices that said they offer art-related services, 56% said they offer advice on estate planning. However, family offices were much more active in art and philanthropy, with 78% of the respondents saying they offer this service, compared with 39% of the private banks (up from 20% in 2012).

One area that is worth paying attention to is the increasing portion of wealth managers that are providing inheritance and succession planning services—currently 61% of the private banks surveyed are offering this service (up from 40% in 2012, and 28% in 2011)



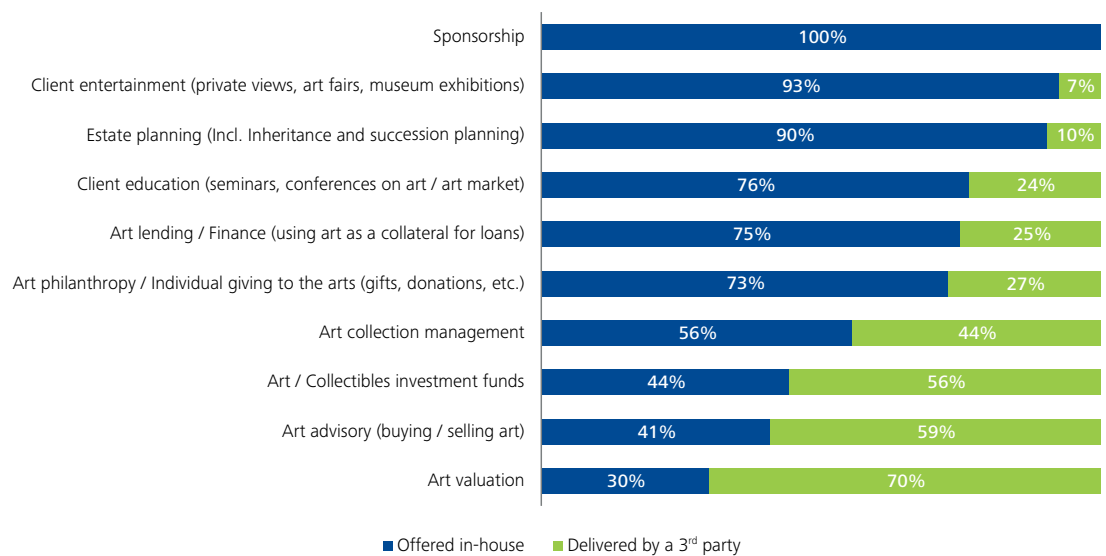
Art collection management: collection management services are more common among family offices, with 67% of the family offices surveyed saying they currently offer this service to their clients, compared with 17% of private banks.

Services related to the artworks are more likely to be provided by a third-party provider: art advisory services, valuation and appraisals are typically outsourced to third-party providers by most private banks and family offices. Services closely linked to the client relationship are more likely to be provided directly by the banks themselves.

There is clearly an opportunity for the art professional community to build strong relationships with the wealth management community, as 59% of art advisory work is outsourced (up from 47% in 2012), together with 70% of valuation and appraisal work (up from 64% in 2012).

Again, these findings suggest that the art and finance industries share a strong common interest in offering the best possible art wealth management service to their clients (often the same individuals). The future challenge remains how to create common platforms where the wealth management and art worlds can share their knowledge and expertise.

Fig. 20 Which art-related services do you offer in-house/via a third party?



Source: Deloitte Luxembourg & ArtTactic Art & Finance Report 2014

4. Challenges

The two main obstacles to the development of art wealth management services are likely to take a long time to overcome, and in the meantime they may hamper the development of art and wealth management-related services:

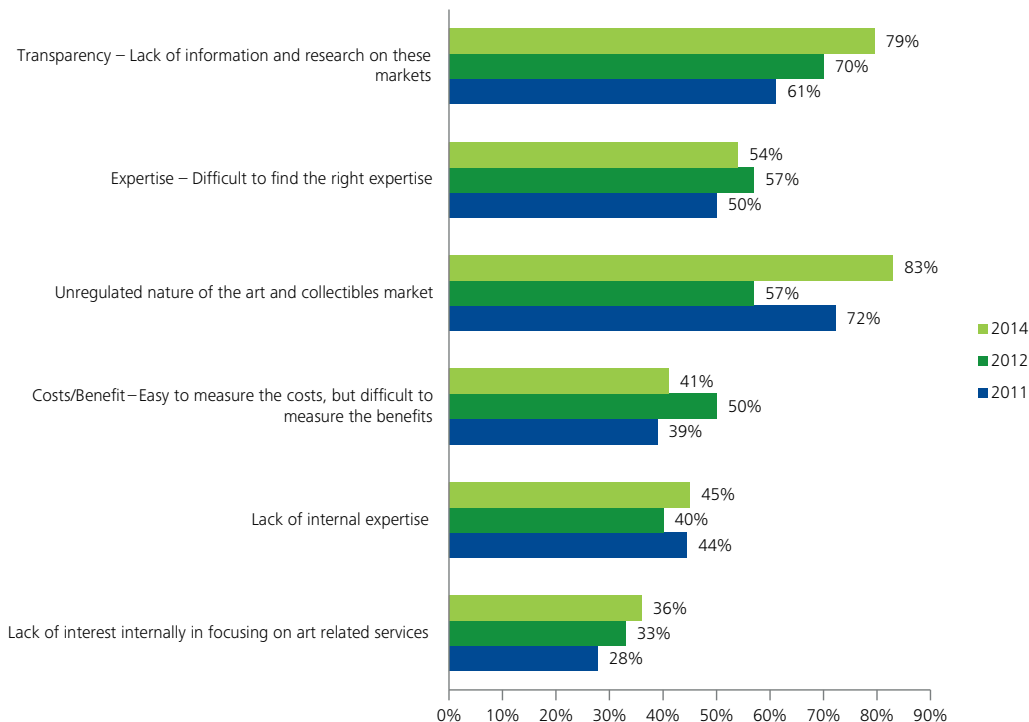
1) The unregulated nature of the art market remains a key concern: one of the key challenges for the wealth management industry is the unregulated nature of the art market. A total of 86% of the private banks and 77% of the family offices surveyed said this was the biggest challenge in dealing with art as an asset class, up from 57% in 2012. With the banking industry under greater scrutiny and subject to an increasing amount of industry regulation, the risks associated with dealing with a largely unregulated industry such as the art market are a major concern

2) Transparency and lack of information represent key challenges: 79% of the private banks and 77% of the family offices surveyed said that the lack of transparency in the art market is one of the main challenges they face when dealing with art. This was up from 70% in 2012 and 61% in 2011. The increase over the last three years is likely to be a consequence of greater engagement between the wealth management industry and the art market, rather than the art market becoming less transparent

In Section 5 these two issues are also discussed from a legal point of view.

The third biggest challenge is the sourcing of the right experts: for 54% of respondents, the biggest challenge of building an art-related service is the sourcing of expertise. The art market is notoriously difficult for outsiders to navigate, particularly as there are no or few regulations governing the providers of art services.

Fig. 21 What do you see as the biggest challenge in offering art-related services/products?



Source: Deloitte Luxembourg & ArtTactic Art & Finance Report 2014



Georgina Hepbourne-Scott,
Stonehage Group

Georgina heads the Art Management division of the Stonehage Group. She joined Stonehage in 2007 after previously working for Lord Foster at Foster + Partners and graduated from the University of St Andrews with a Masters in Art History. Georgina has a strong relationship with the leading auction houses and art dealers, as well as a broad network of galleries, regional auction houses, artists, conservators, advisers and insurers in Europe, the United States and South Africa. She attends relevant art educational events and, together with colleagues, travels to all major art fairs, keeping abreast of developments and trends in the art market. Georgina is a member of PAIAM and participates in training sessions on the art market within the art industry and for colleagues.

The role of art management in a family office

The rapid growth in art advisory and art management offerings in the past ten years reflects much increased interest in the art world, the dizzyingly high prices that (in particular in the contemporary market) are repeatedly achieved at auction, and the recognition that these assets need to be purchased and managed with care and expertise, like any other substantial asset.

As a multi-family office, and in our role as trustees to many art collectors, it is our responsibility to ensure we deliver a comprehensive fiduciary art management service. We fulfil the role of art gatekeepers, positioned between our clients and the largely unregulated art market.

Q: Why should a family office include art and collectibles in its wealth management service offering?

A family office is responsible for advising on a client's overall wealth. For trustees, there are further fiduciary obligations. Due to the rise of the current art market, art and collectibles now often constitute a growing proportion of a family's wealth. As such, their oversight must reflect this prominence and be subject to the same disciplines as other elements of the client's wealth.

Art and collectibles are subject to many risks, and careful fiduciary art management will help to mitigate these risks. In addition to the obvious risks of inadequate insurance (failing to keep pace with price appreciation), physical security, maintenance and transport, etc. there are, for example, major risks involved in the buying and selling process, with collectors often unaware of the depth of research required, the subtleties of the auction process, and the finer details which can be tuned to their advantage.

It is alarming to think how often collectors make an art purchase of several million pounds, on the back of a one-page invoice and in good faith. Just as investors will involve lawyers and advisers to carry out due diligence on significant investments, we highlight the importance of similar rigour with respect to the purchases of art. A recent example of a failure to establish true provenance and legal title is the case of the Monet, subsequently exposed as being allegedly stolen by an aide of Imelda Marcos, wife of the late Philippine dictator, and passed onto a London dealer without legal title.

As the market grows, with new collectors and advisers alike, it is all the more important to know who you are dealing with. As seen with the closure of the Knoedler Gallery, there were warning signs relating to the works sold to them by Ms Rosales. When it all seems too good to be true, it often is. As trustees, it is essential to review risks on a regular basis and identify the need for and seek the advice of specialists whenever necessary.

There are the financial, legal and tax risks arising from how the works are held, the location in which they are housed and the paperwork when they are transported from one jurisdiction to another, perhaps for exhibition purposes or from one home to another.

Works of art also need to be managed in the sense that their value can often be enhanced by intelligent strategies for lending them to exhibitions and galleries.

There is also the further risk of excessive concentration of value either in a single work or in a particular artist, which can often arise when that artist becomes much in demand. Family offices or trustees are obliged to consider the need to diversify and must consider the interests of all the beneficiaries and, where appropriate, the defined objectives of the trust in which the collection is held.

Q: What kind of services related to art and collectibles does Stonehage offer? Which model is favoured: in-house services or outsourcing?

Firstly, art does not fall within our investment management discipline; we do not advise our clients to invest in art. Rather, it is a lifestyle asset, albeit one that may turn out to be a very good investment. Given the crossover of expertise required, it is however important to have a combination of art, legal and financial skills in-house. Regardless, the greatest value is knowing when you need to bring in outside skills and who the best people are. We are proud to have a trusted network of specialists (art lawyers, appraisers, curators, conservators, etc.), which is constantly evolving.

We focus on the purpose and long-term goals of a collection—questions often evaded not only for art planning, but in many other areas of wealth. It is never too soon to address these.

Services that we provide include the structuring of collections, which requires careful thought about the future, taking into consideration each individual's vision; cataloguing and insurance; tax advice and valuations; cross-border movement and the potential pitfalls associated with it; loaning to leading exhibitions and museums to enhance the profile and value of works; assisting with both the buying and selling process; conservation; and logistics, including storage and installation. All these services benefit the future of the collection.

Q: What are the expectations of a family? What is the critical mass needed to offer art services?

Our fiduciary role ensures the art is managed in the interests of the family, as defined by the relevant deeds, settlements, or family agreements. Circumstances and visions evolve over time, therefore there must be regular reviews including the beneficiaries, trustees and advisers in order to adjust planning where necessary. This should not take away from the immediate enjoyment of the artwork. We help families focus on the future and establish who will be involved in the decision making. We understand the importance of involving the next generation, in order to increase the chances of passing on the family philosophy with respect to collecting, which is often associated with philanthropy. Careful planning can help avoid disputes further down the line, within the family or indeed with authorities.

Our art management service originated from the needs of specific clients whose collections had values well in excess of £100 million, but we work with both new and established collectors and our comprehensive service makes most sense for a collection worth in excess of £5 million. We also frequently advise clients on individual transactions, even where relatively modest sums are involved—it is all part of our family office service!

Q: How does a family office get remunerated for art wealth management services?

We offer advice and therefore charge time for this advice. Some clients prefer the certainty of a fixed fee where there is a more comprehensive service. We have a total non-conflict model; we are not art dealers. Our independence is one of our great strengths.

Q: How do you see the development of art services in wealth management, and why?

As art prices rise, and for as long as the art market remains unregulated, our services will remain increasingly in demand. More attention will need to be given to ownership structures and tax planning as governments keep a closer eye on art activities and also wish to benefit from rising values. Families and professional trustees require non-conflicted art gatekeepers and this need will grow.



Q: What would your recommendations be to other family offices and wealth managers for Art & Finance services?

Be careful not to over-reach yourselves or to think that because art management is a fashionable offering, every wealth manager must have one!

Our success to date is based on three main factors:

- 1) Our service evolved from the specific needs of Stonehage clients
- 2) For historical reasons we already had a large number of major collectors within our client base, so we had the clear and immediate potential for critical mass
- 3) While our in-house knowledge and expertise has grown massively over the last five years, we know our own limitations and continue to work with a variety of other professionals and experts, without ever seeking to displace them.

We have been fortunate that our model works for our clients and is financially viable, but others in different circumstances may find a different approach which works for them.

As art prices rise, and for as long as the art market remains unregulated, our services will remain increasingly in demand. More attention will need to be given to ownership structures and tax planning as governments keep a closer eye on art activities and also wish to benefit from rising values. Families and professional trustees require non-conflicted art gatekeepers and this need will grow



Art secured lending⁵⁸

As ultra high net worth individuals are allocating more of their total wealth to art and collectible assets—as demonstrated in Section 1 of this report—the need and demand for art secured lending is expected to grow. Art secured lending can be seen as an effective way of enabling art collectors to access the equity value in their artworks without having to sell them. Art lending makes it possible to redeploy their capital into new art acquisitions or attractive business opportunities, or to refinance existing loans.

Banks have previously been cautious when considering art collections as collateral for loans. This has largely been because of unwanted risks associated with these types of assets, such as defective title, authenticity risk and borrower infidelity risk, which could potentially leave the lender with a worthless asset or an asset to which it has no access. However, developments in the art insurance industry could protect the lenders from these types of risks and potentially open up the opportunity for a much larger art secured lending market in the future.

For recent legal developments in the art secured lending market, please see the interview with Pierre Valentin in Section 5 of the report.

Survey findings

As mentioned earlier in the report, art secured lending is one of the important strategic areas that private banks will be looking at in 2015.

More banks are offering art secured lending:

36% of the private banks surveyed said that they offer art lending and art financing services using art and collectibles as collateral, this is up from 27% in 2012 and 22% in 2011. This could suggest that private banks are getting more comfortable with the risks associated with lending against art, but could also be a result of increasing pressure from clients.

Client demand is on the increase: in the survey carried out among established art collectors, 48% said they would be interested in using their art collection as collateral for a loan, up from 41% in 2012). 58% of collectors and 66% of art professionals believe we will see a further increase in art owners using their art collections as collateral in the next two to three years.

Art secured lending can be seen as an effective way of enabling art collectors to access the equity value in their artworks without having to sell them

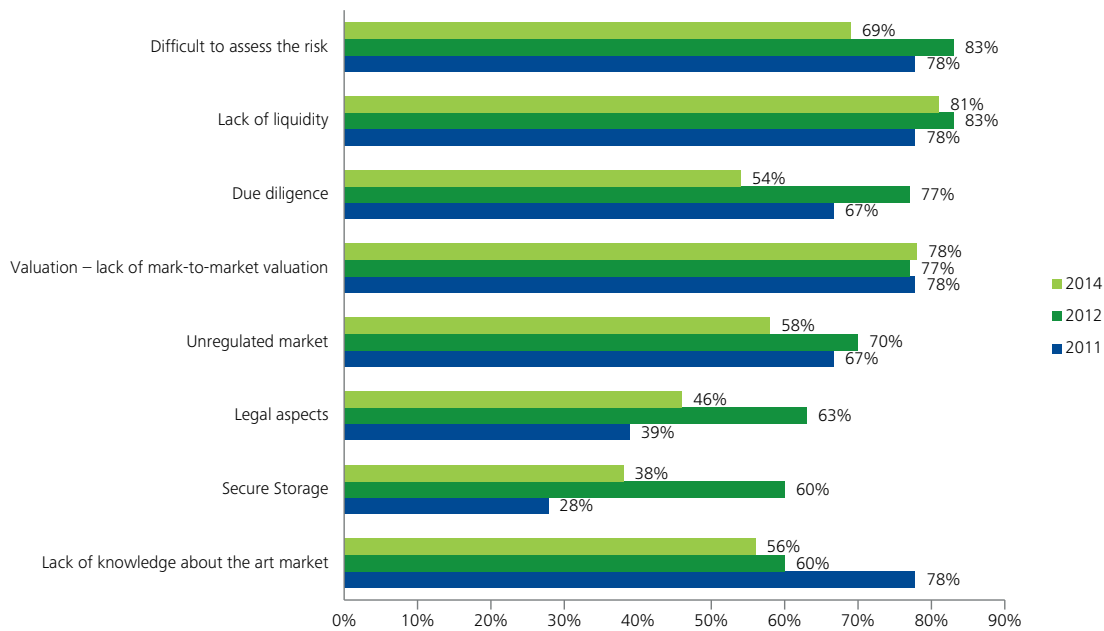
⁵⁸ There are two main forms of art secured lending: 1) recourse lending, where artworks form part of the collateral for a loan (traditional lending), and 2) non-recourse lending, where loans are offered against the security of a single artwork or an art collection (asset-based lending)

Collectors are looking for leverage when buying new art: 53% of collectors said that their motivation for using their art collection as collateral would be to buy more art (up from 39% in 2012), a further 38% (up from 18% in 2012) said they would use it to invest in other business activities and 9% said they would use it to refinance existing loans.

Liquidity and valuation risk remain the primary concerns for art lenders: the main concerns for private banks when considering lending against art remain broadly the same as in the 2012 survey. 81% of respondents said the lack of liquidity in the art market was their biggest hurdle (against 83% in 2012). This was closely followed by issues related to problems of valuation and the ability to provide a mark-to-market value on works of art (78% said this was the main hurdle, against 77% in 2012).

Improved knowledge about the art market increases wealth managers' understanding of risk: one notable change since the first survey in 2011 is that knowledge about the art market is clearly on the increase. 56% of respondents said that lack of knowledge about the art market was a key hurdle; however, this was down from 60% in 2012 and 78% in 2011. Difficulty in assessing risks was seen as one of the biggest hurdles in 2012, cited by 83% of wealth managers, but this had dropped to 69% in the latest survey. A similar trend was seen with regard to due diligence, with 77% saying that this was a major challenge in 2012, against a much lower 54% in 2014. This could be a sign that the resources invested in education and information, together with a closer relationship between the wealth management industry and the art market and art professionals, are starting to have an impact.

Fig. 22 What do you feel is the main hurdle for providing art lending/art as collateral to the bank's current clients?



Source: Deloitte Luxembourg & ArtTactic Art & Finance Report 2014

Recent developments in art secured lending

New insurance products

The insurance industry is launching new art lending insurance products: Hiscox recently announced the launch of their ‘Collateralised Art Protection’ insurance, which effectively covers the fidelity risk of the borrower. The insurance product will protect the lender against the borrower disappearing with the art or moving the art into a different legal jurisdiction where the loan agreement has no judicial force. The insurance also covers deliberate damage to an artwork that has been used as collateral for a loan. The key aspect of this insurance product is that it allows the art collection to remain in the possession of the borrower. The product is available to lenders anywhere in the world. Insurance broker, Robertson Taylor W&P Longreach, also recently announced a similar product in an exclusive agreement with five Lloyds underwriters, which allows £80 million of capacity for any one collateralised loan deal. Robertson Taylor W&P Longreach estimated today’s art lending market to be in the region of £6 billion per annum, but with the potential to reach £15-£20 billion per annum.

A new insurance product will protect the lender against the borrower disappearing with the art or moving the art into a different legal jurisdiction where the loan agreement has no judicial force

Business development:

- *Goldman Sachs*⁵⁹ has launched a new European lending unit for its private wealth management clients. The new lending business has a goal of building up a US\$5 billion loan book within the three next years, catering for the 1,700 wealthiest clients across Europe, the Middle East and Africa. It will comprise mostly secured loans for a wide variety of purposes including liquidity facilities, portfolio diversification, tax payments or luxury purchases such as yachts. Financing of art collections is currently offered by Goldman Sachs Wealth Management in the United States, and according to Bloomberg⁶⁰, Goldman Sachs Bank’s other consumer loans—a category that includes borrowings backed by art and excludes auto and student loans—more than doubled to US\$980 million at the end of 2013, from US\$464 million a year earlier
- *Falcon Group*, a leading global specialist financier launched Falcon Fine Art in 2014. Falcon Fine Art (FFA) is not a broker, and therefore finances clients using its own balance sheet. It also provides financial solutions purely on an asset-backed basis. It currently offers three categories of finance: liquidity—allowing a collector to leverage and monetise a work of art; bridge-to-sale, allowing a collector to monetise an artwork while awaiting its sale; and additional capital, allowing collectors to invest in additional works, while isolating their collecting from other business activities
- *Borro*[®], the personal asset lender, announced a new sale advance loan programme in October 2013, allowing borrowers to maximise both their immediate liquidity and final sale price
- *Citi Private Bank* has expanded its art advisory and art finance business in Asia and Latin America, hiring Edie Hu from Sotheby’s in Hong Kong, and Mary Kate O’Hare, previously a curator at the Newark Museum in New Jersey, for Latin America

⁵⁹ <http://www.ft.com/cms/s/0/a0f8ec30-0388-11e4-817f-00144feab7de.html#axzz381tAbIv5>

⁶⁰ <http://www.bloomberg.com/news/2014-05-06/goldman-sachs-supports-cohen-with-loan-backed-by-fine-art.html>

- *Willstone Management* secured a credit line in excess of US\$100 million from a pair of New York hedge funds specialising in debt and macro financing in October 2013, and is also seeking to raise up to €50 million from private investors in the UK and Europe
- *Right Capital*, a London-based art financing company entered the world of art finance in 2013 with a range of structured credit products specifically designed for dealers and art world professionals. Right Capital targets loans in the £0.5-5 million range. The company plans to open a second office in Luxembourg in September 2014
- *Privatbank Berlin* (formerly Bankhaus Dr. Masel) has launched new art secured lending service for wealthy borrowers in Germany and Europe. Lending products include short-term bridge financing, flexible lines of credit to up to 60 months and fixed borrowing at interest rates between 5% and 15%
- *Chinese banks* now offer art secured lending: in 2013, Minsheng Bank became the first bank to accept non-traditional assets such as wine, art, private jets, yachts, cars etc. as collateral for loans. Minsheng Bank is currently providing art secured lending services to its HNWIs clients in China





Paul Aitken,
CEO and founder of Borro®

Paul is the founder of borro.com. Prior to this, Paul founded and was the MD of Movota, a provider of mobile solutions to leading media companies, which he sold to Bertelsmann in 2005. In addition, Paul has extensive senior operations, supply chain, marketing and strategy experience in the retail and IT sectors from his time working with DSG International and RM plc. Paul also holds an MBA from IMD, Lausanne, Switzerland

Recent developments at Borro®

Q: Tell us about recent developments at Borro, for example, what will be the destination for the financing from the US\$112m funding round from Victoria Park Capital?

There have been lots of new developments at Borro recently. The biggest news is that we announced a new funding round of US\$112 million back in March, coming entirely from one backer that focuses on financial investments, Victoria Park Capital. The money will be used to continue to grow our business in the markets where we are active—the UK and the US—and specifically, to expand the pool of money that Borro has available to offer for financing.

Q: Any new products in the pipeline?

The Sales Advance Loan is one of our most recent product launches and has proved very successful. This product is aimed at clients who are going to sell an asset in the future, but are in need of liquidity immediately. We will lend them up to 70% of the value of the estimated sale value immediately, take possession of the asset and manage the complete sale process for them. This saves a huge amount of hassle for the client and frees up liquidity immediately, as opposed to waiting for what can sometimes be a lengthy sales process. We also have a world class team who will find the best auction to place the asset in, therefore achieving the best sale price possible.

An example of this is where a gentleman had inherited an Andy Warhol screen print which had gone unsold at auction two years previously. We gave him an advance on the estimated sale value and used our team of experts to place it in the best auction and achieve a sale. He built a conservatory with the advance while he waited for the sale to complete and then we returned the remainder when the sale was completed.

Q: Where do you see your growth markets in the next five years? You are developing your business in the United States and United Kingdom, do you have any plans for continental Europe or other geographical regions?

We continue to do very well in the UK market, where we continue to grow at about 60-70% a year. Having launched in the United States in 2012 in mid-town Manhattan, we definitely see this as a growth market, and it was an integral part of my first business plan five and a half years ago. The US market is about seven or eight times bigger than the UK market for this kind of lending and we are aiming to grow more than 100% over the next few years.

In addition to this we are opening an office in California, and are aiming to open offices in Chicago, Dallas and Miami in the next 18 months.

Q: Can you share with us some of the figures linked to Borro's growth in recent years?

We've done about £90 million of lending to date, and last month (June 2014) we did about £6 million of lending, which is up about 80% year on year. We expect, by the end of this year, to be close to double what we did last year in terms of loan value. From a revenue perspective we were just a shade over £10 million, and we expect to be around the £18 million mark by the end of this year. Much of this growth stems from relationships we have built with private banks and professional advisors who refer business to us.

We are also seeing an increase in our repeat rates, as well as our referral rates—people are referring others, which highlights our exceptional levels of customer service, something we pride ourselves on here at Borro.

Q: What is your typical client profile? What are their main motivations for using Borro?

We have a huge range of clients from professional sports players and city bankers to actors and landowners. In addition to this we are finding that our products resonate with people who are self-employed or have small businesses whose needs just aren't served by anyone else.

The advantage of it from our perspective is we are lending against the asset, so our diligence is on the asset rather than the individual. So there's no credit checks, there's minimal recall and it's very quick. A really good example of this was a lady who needed to raise £1.8 million very quickly for a property deal. She had some artwork as collateral and from our initial contact with her we had the funds in her account within 72 hours.

Q: Do you see peer-to-peer lending happening in the personal asset space, and if so, why?

The original idea for borro was to create a peer-to-peer asset lending platform. I quickly realised however that there would be major trust issues on both sides if we were to go down that path. As a consequence we have focused our energies on building trust with clients who hand over possession of their asset to us for the duration of the loan. We have made great progress in this regard, and as such the peer-to-peer option for our business is something that we could deliver against in the next 18 months.

We have a huge range of clients from professional sports players and city bankers to actors and landowners

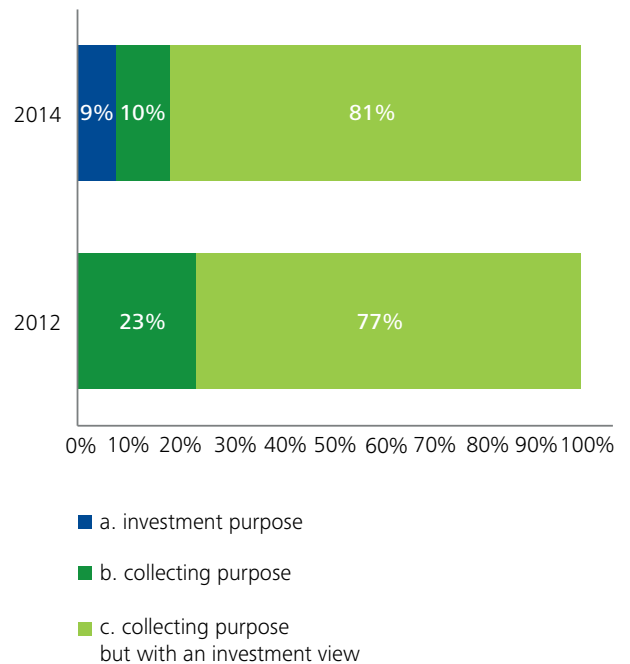
72% of the art professionals said that their clients' primary reason for buying art was related to the social and networking scene that the art market offers and the status of being associated with buying art (this was up from 59% in 2012)

B. Art Professionals⁶¹

Emotion versus investment

Emotion is key but investment matters: although only 9% of art professionals say their clients buy art and collectibles for investment purposes, a large majority, 81% of art professionals, believe that their clients are buying art for collecting purposes (up from 77% in 2012), but with an investment view. This implies that the investment aspect of art (its financial or economic value) is something that art advisors feel their clients are increasingly focusing on, a trend also reflected among collectors.

Fig. 23 Emotion versus investment: why do your clients buy art?



Source: Deloitte Luxembourg & ArtTactic Art & Finance Report 2014

⁶¹ The following survey results are based on the views of 122 art professionals based in Europe, the United States, the Middle East, Asia and Latin America

What specific factors motivate your clients to buy art?

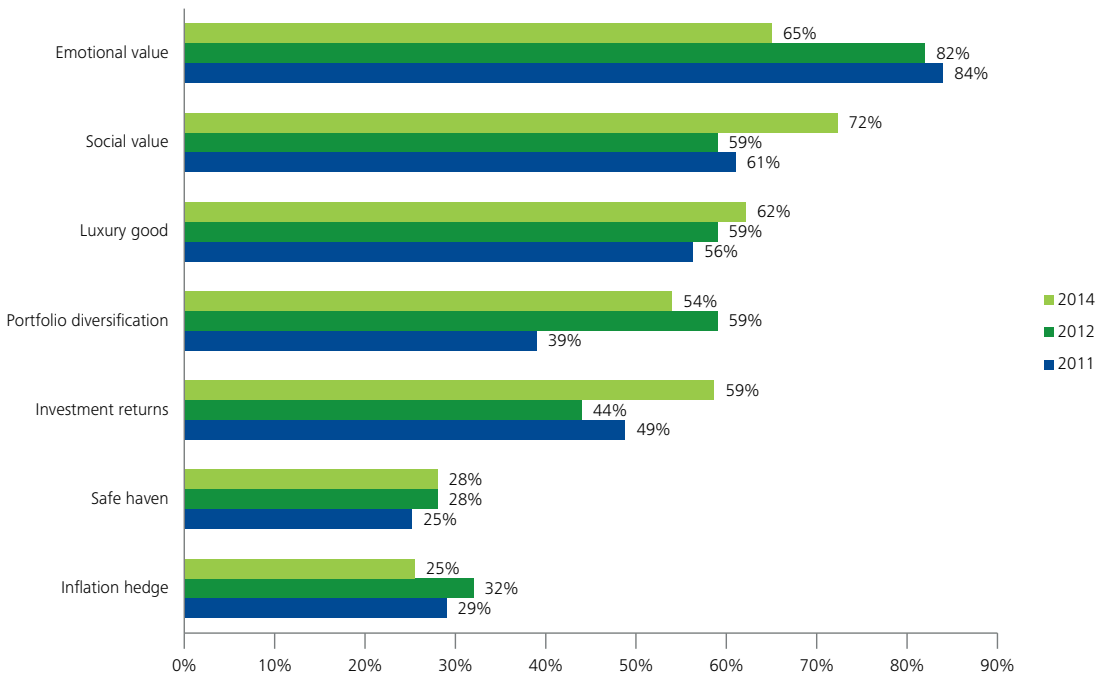
The social value associated with buying art takes centre stage according to art professionals:

while emotional value was the dominant motivation in 2012 (82% of the art professionals said so, compared with 65% in 2014), the social value (status, prestige and exclusive social network) associated with buying art is becoming a more important motivation among buyers according to their advisors. Although more art professionals and collectors higher than what collectors themselves stated this to be the prime motivation, it does bear out correspond with the observation that social value is the second strongest motivation among collectors (62% said so) after the emotional value associated with buying art, which 78% of the collectors said was the most important motivation.

72% of the art professionals said that their clients' primary reason for buying art was related to the social and networking scene that the art market offers and the status of being associated with buying art (this was up from 59% in 2012).

This also corresponds to the fact that more buyers are seeing art as the ultimate luxury good, with 62% of the art professionals saying that this was the case (against 59% in 2012). The perception of art as a luxury good might be hard to distinguish from the social value of art, but for the purpose of this study, luxury goods will be more associated with the 'brand' value that buying art works/artworks by certain artists gives, versus the social value (or status) associated with being an art collector and a key player in the art world or art market.

Fig. 24 Art professionals: which of the following motivations are most important in buying art?

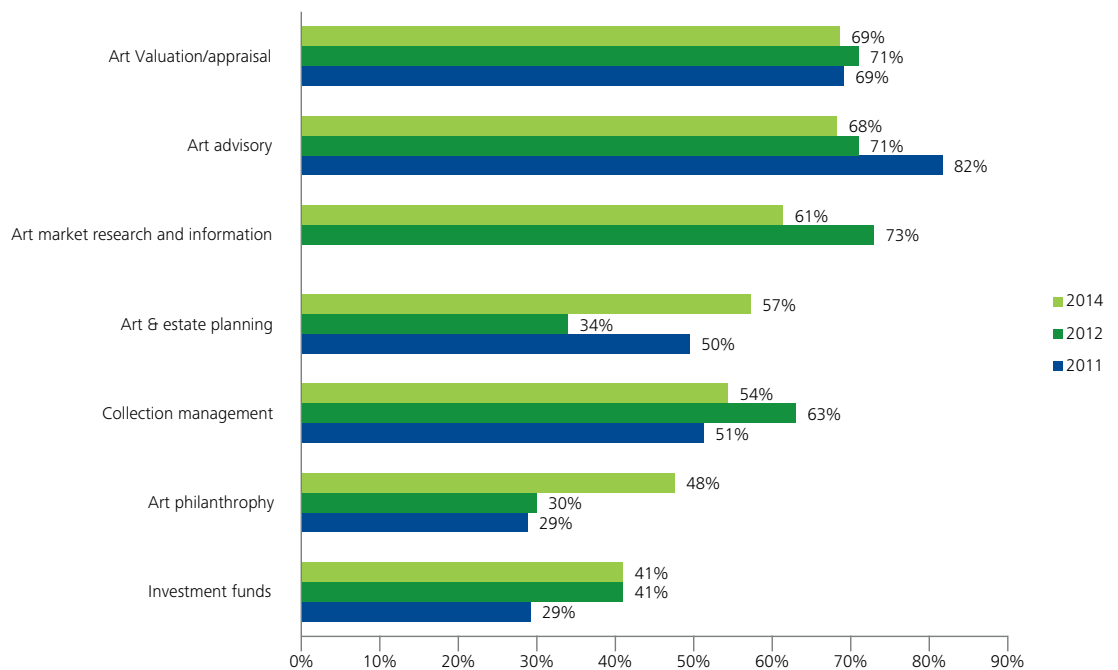


Source: Deloitte Luxembourg & ArtTactic Art & Finance Report 2014

The survey findings from this year suggest that there is a trend towards a new set of art wealth management services

The financial aspects of buying and holding art in a portfolio remain important: according to 59% of the art professionals surveyed, the potential investment returns on art is becoming an important reason why their clients are buying art. This was up from 44% in 2012, and signals that more buyers are engaged with the art market with a view to making a return on their investments. Portfolio diversification also remains an important reason for buying art, with 54% of art professionals saying that their clients were buying art for this reason (although this was down from 59% in 2012).

Fig. 25 What types of art wealth management services are most relevant to your clients?



Source: Deloitte Luxembourg & ArtTactic Art & Finance Report 2014

Art valuation and art advisory services are the 'glue' that connects the wealth management industry and the art professionals: art valuation and art advisory remain the two most important services, with 69% and 68%, respectively, saying that these are the services that their clients are seeking. This also corresponds to what the wealth managers are seeing as one of the main hurdles when offering art-related advice or services.

Estate planning, collection management and philanthropy could be an attractive entry point into the art market for traditional wealth managers: the survey findings from this year suggest that there is a trend towards a new set of art wealth management services. 57% of art professionals (up from 34% in 2012) felt that the wealth management industry could offer advice on art and estate planning, and a further 48% (up from 30% in 2012) said that services linked to art philanthropy (setting up foundations and charities) would greatly add value to their clients.

Art market research and information: 61% of art professionals said that art market research and information was highly relevant to their clients (down from 73% in 2012). 61% of collectors also said that market research and information is a product they would like to see wealth managers include in their service offering.

Art investment funds will continue to play an important role: 41% of art professionals feel that art investment funds remain an important investment product (this is the same level as in 2012) and an effective way for their clients to get access to the art market. Although the private banks and family offices surveyed said they were reducing their focus on art investment funds in the next 12 months, it is likely that art investment funds could play an important role in the art market for certain types of art investors who do not have the access and expertise themselves.





Harco Van Den Oever,
Founder of Overstone Art Services

Harco has a background in fine art and finance. He began his career in capital markets where he worked from 1989 to 1999 at Paribas, Bankers Trust and Credit Suisse First Boston, based in London, Hong Kong, Singapore and Sao Paolo, before co-founding a B2C financial services business in the UK. From 2001 to 2012, Harco moved to the fine art business becoming a senior executive with Christie's International as Continental European Head, European Client Development Head, member of the EMEA Executive Management Team and International Business Director of Impressionist and Modern Art. Harco has an MBA from the University of Hartford and is an INSEAD AMP alumnus where he is also a regular speaker. Harco founded Overstone Art Services in 2012.

Why using an art advisor

Q: Could you please present your company, your services and the type of clients you serve?

Overstone Art Services works with the wealth management industry, helping the likes of private banks and family offices with the management of art as an asset either for themselves or their clients. This ranges from the organisation of very selective art-related events in order to initiate a conversation about art with the wealth manager's clients, to art management, art brokerage and art-backed financing. Overstone Art Services does this on either a branded or white-labelled basis. The Overstone Art Services team combines deep experience in banking, art insurance, art law, art events and general art services.

Q: Could you please tell us what are the main motivations behind your clients' (financial institutions) need for your services? What do they want to achieve?

Wealth managers are facing a number of challenges, including low yields, increased competition and high compliance costs. As a result, they look for ways to enhance client interaction and diversification, while increasing revenues. In parallel, a generational shift is taking place where a new generation of collectors tend to look at their art with a more critical economic eye. This does not mean that they are not collecting for the pleasure of art itself, but they tend to be increasingly demanding as to the way their art is managed and its potential financial impact. Wealth managers are realising that they need to be able to respond to these needs to stay relevant across their clients asset classes.

With regard to art-backed financing, family offices and collectors, as borrowers, see an opportunity to leverage an existing collection easily by creating new liquidity. Wealth managers on the other side, as lenders, appreciate the yields and loan-to-value ratios offered by art backed loans.

Q: Could you please share with us your view on the evolution between art advisors and financial institutions?

This has been a very slow evolution. Art advisors have tended to be exactly that, advisors on what to purchase. There are very few art service businesses that understand both the needs of art collecting clients and those of the financial institutions serving them. As the long-term global value of art continues to increase and as collectors are becoming more aware of the financial needs and opportunities surrounding their collections, there will be an increasing need for a bridge between art and financial services.

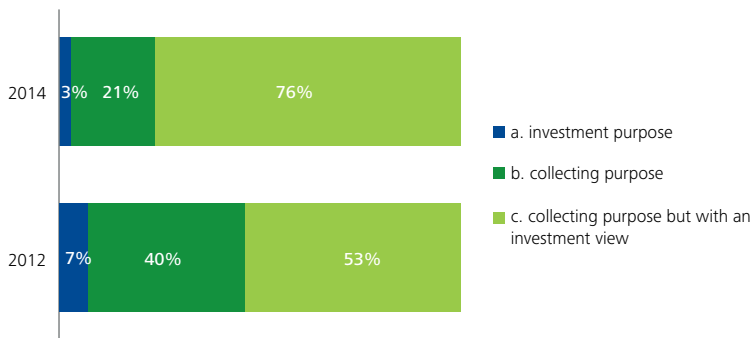
Q: What would be your recommendations to a financial institutions willing to offer art wealth management services?

Financial institutions aiming to interact with their clients in relation to their art assets need to see if this fits within their overall proposition, the make-up of their client base and the type of counterparty they want to be. This is best done with the help of a third-party provider who understands financial institutions from within as well as having deep knowledge and expertise in the art market.

Once an institution decides to offer art services and advisory to its clients, it needs to decide if it wants to outsource the function or build an in-house capability. The latter is complex as there are few individuals with an understanding of both industries to hire, and the integration of an art advisory team within a financial institution is not always straightforward due to different cultures. An alternative is to start with an outsourced capability and then bring it gradually in house as understanding, proof of concept and internal buy-in increases.

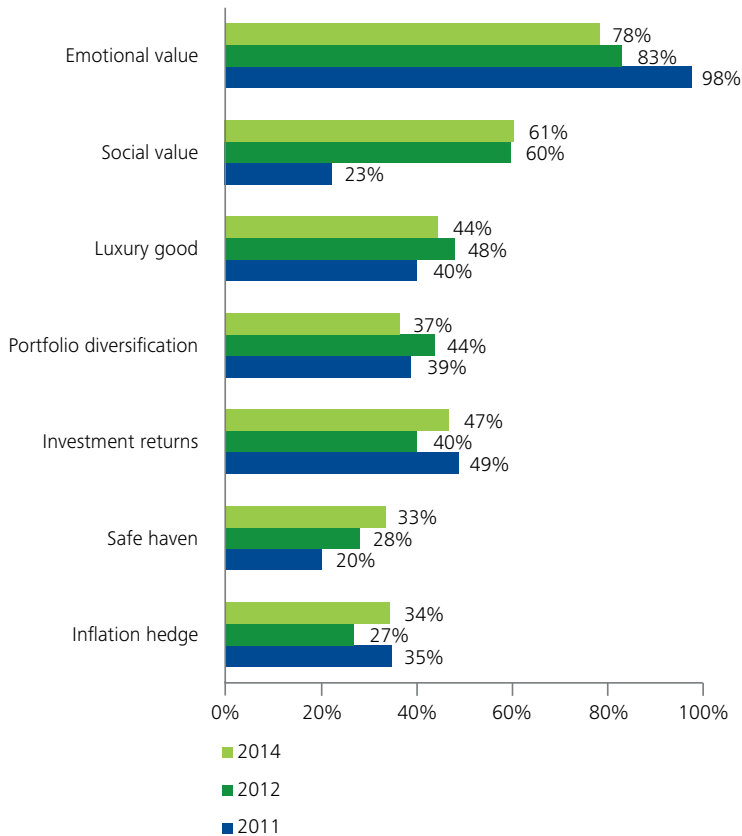
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Fig. 26 Emotion versus investment: why do you buy art?



Source: Deloitte Luxembourg & ArtTactic Art & Finance Report 2014

Fig. 27 Collectors: which of the following motivations are most important in buying art?



Source: Deloitte Luxembourg & ArtTactic Art & Finance Report 2014

C. Art collectors

Emotions versus investment

More collectors are buying art for passion with an investment perspective: only 3% of the collectors surveyed are buying art with a pure investment view, and only 21% are collecting for pure passion without an investment view. However, the large majority, 76%, are collecting art with an investment view (up from 53% in 2012). This could be an ideal type of client for the wealth management industry—not a speculator, but an individual who accumulates art wealth, and would like to enhance, protect and manage these assets. 62% of the collectors surveyed said they would like to see their wealth managers include art and collectibles in their service offering.

What motivates collectors to invest in art?

Emotional value remains a key motivation for art collectors, although the social value of buying art is becoming more important: as with the two previous Art & Finance surveys in 2011 and 2012, the emotional connection with art remains the dominant motivation for the majority of collectors. However since 2012, the collectors surveyed have registered a higher motivation for the social value that comes with collecting art. The exclusive social network and status associated with buying art is clearly drawing buyers to the art market. Art fairs and art exhibitions sponsored by major financial institutions are clearly important platforms in this regard.

What type of art-related services are collectors most interested in?

61% of collectors (against 53% in 2012) see art as an asset class. This suggests that we are likely to see an increasing demand for professional services linked to these assets. Below are some of the main trends with regard to services that the wealth management industry could offer its clients.

Art valuation, appraisal and research: 67% of collectors would like to have a service offering that covers art valuation and appraisal. This is followed by 61% who would like to have access to art market research and information.

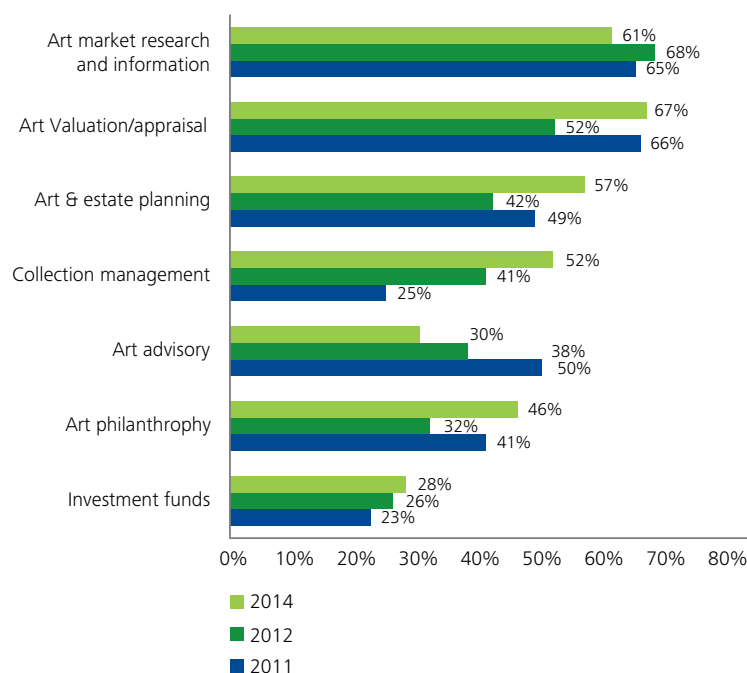
Art advisory is not a service priority: most collectors don't see art advisory as an essential wealth management service (only 30% said it was), most likely because they already receive these types of services from somewhere else. This could imply that wealth managers should focus on their core services, such as how to structure art wealth from an estate planning standpoint, including for philanthropic purposes.

Art and estate planning: this is one of the services that collectors are increasingly interested in. 57% of collectors said this service was highly relevant to them (up from 42% in 2012). It is evident that today's collectors are concerned about wealth preservation and planning for the future. This is also evident with regard to art philanthropy, which 46% of collectors said would be a highly relevant service for them (up from 32% in 2012).

Collection management: 53% of the collectors would like to see their wealth managers help in managing their art collection (this is up from 41% in 2012). As private banks are already managing client wealth and investment portfolios, it would be a natural step for banks and family offices to also include art in the future.

Art investment funds: although not a priority for a majority of clients, we are seeing a gradual increase in interest in art funds. Currently, 28% of collectors said they would like to see private banks offering such a product, up from 26% in 2012 and 23% in 2011.

Fig. 28 Collectors: which art wealth management services are most relevant to you?



Source: Deloitte Luxembourg & ArtTactic Art & Finance Report 2014

Freeports for valuable tangible assets

Most commonly, a freeport is referred to as a special customs area or small customs territory, in which customs regulations are generally less strict (or there are no customs duties and/or controls for transshipment). The world's largest freeports for the storage of valuable tangible goods such as precious metals, fine art, fine wine, etc. are situated in Geneva, Singapore and Luxembourg.

The Luxembourg Freeport will be launched on 17 September 2014. This high-tech facility is intended to become a hub at the heart of Europe for the storage, handling and trading of fine art, wine, precious metals and other collectibles. It will be the first of its kind in the European Union. The Luxembourg Freeport will actively contribute to the diversification of Luxembourg's art offering with the aim of becoming an 'art cluster' for artists, galleries, international sales and international art fairs. It will also provide one of Europe's largest wealth management communities with an opportunity to diversify its service offering by being able to focus on tangible valuable goods and help their UHNWIs with their art and collectible assets.

Survey findings of wealth managers, art collectors and art professionals

Current versus future use of freeports: 28% of both art collectors and art professionals said they already used or had a relationship with a freeport provider. 43% of art professionals said that their clients were likely to use a freeport facility in the future, versus 42% of art collectors who said they were likely to use such a facility.

Strong awareness of the new freeport in

Luxembourg among private banks: 90% of the private banks and 42% of the family offices surveyed were aware of the new freeport in Luxembourg⁶². This could be due to the fact that most of the family offices surveyed were based in the United States. 53% of art collectors and 54% of art professionals said they were aware of the new freeport.

Private banks could drive new business for

freeports: 57% of private banks would advise their existing clients to make use of a freeport facility, against 22% of the family offices. 37% of private banks also said they were likely to use the freeport facilities in terms of managing clients art and collectible assets, and 41% said they were likely to create a new or expand on an existing art and collectibles service offering as a result of freeports, of which 53% were private banks and family offices in Luxembourg.

⁶² The freeport in Luxembourg has opened 17 of September 2014

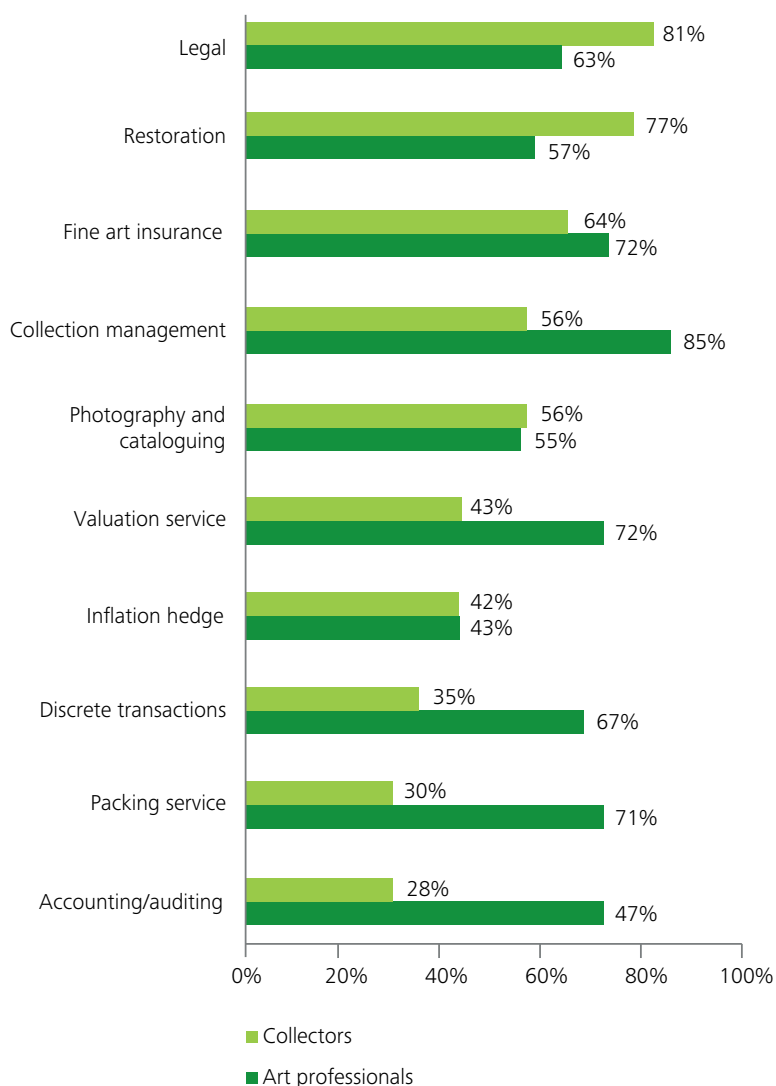
Increase in art lending: 30% of private banks said they were likely to offer art secured lending or increase their art lending business as a result of the new freeport and access to secure storage.

Both art professionals and art collectors have a variety of different views on the services they believe are integral to a freeport eco-system, though some are more obvious than others, such as logistical issues. However, a number of other professional services were identified as critical to the freeport model, and present new opportunities for these professionals to partner with the freeports to offer high value-added services.

Freeports focusing on tangible valuable goods offer the possibility for wealth managers to develop regional competence centres for tangible valuable assets. When dealing with UHNWIs, Luxembourg, Swiss or Singaporean wealth managers should consider incorporating this aspect into their wealth management strategy to create a competitive edge. Also, the development of a global network of freeports dedicated to valuable assets increases the opportunity for wealth managers to provide a global art and wealth management service offering.

Legal services seen as an important aspect of the freeport eco-system: 81% of the art collectors surveyed and 63% of the art professionals said that legal services were a critical part of the service offering connected to a freeport facility, and that such facilities present an opportunity for legal firms to develop a service offering related to the global freeport eco-system. Other services such as art restoration (77% of art collectors and 57% of art professionals said this was very important), fine art insurance (64% of art collectors and 72% of art professionals said this was very important). More than half of the respondents (56% of art collectors and 55% of art professionals) said that collection management is an aspect that should be offered as part of a freeport service or solution. Section 5 clearly illustrates the legal complexity of dealing with art.

Fig. 29 What type of additional services would be useful as part of the freeport eco-system?



Source: Deloitte Luxembourg & ArtTactic Art & Finance Report 2014



Jean-Philippe Drescher,
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Jean-Philippe is a member of the Luxembourg Bar and has extensive experience in cross-border structuring. He specialises in advising local banks on investment fund issues and provides, inter alia, corporate advice on large-scale cross-border transactions such as group restructurings, investments and M&A.

Prior to founding d.Law, Jean-Philippe was a partner with Deloitte Luxembourg. Jean-Philippe served as Chairman of the Committee for Financial Companies at the Luxembourg Institute for Directors (ILA), and is actively involved in the work for developing corporate governance recommendations and guidance for non-listed companies. Jean-Philippe holds a master's degree in business law from the University of Paris II-Assas (France).

Freeport and art secured lending in Luxembourg

Art secured lending is seen in the United States as an alternate means to unlock liquidity from an art collection for investment or personal finance purposes. In fact, the United States is an established and growing market where artworks are used as a less conventional form of collateral to secure the obligations under a loan taken out from a credit institution. The main reason for this success lies in the Uniform Commercial Code legislation (UCC) which benefits both the lender and the borrower, since the lender can perfect its security interest through registration where the borrower may keep possession of the art.

In Europe, though there is a higher ratio of asset rich/cash poor collectors than in the United States, art secured lending remains relatively undeveloped. Apart from the traditional hurdles that Continental European banks face when using art as collateral (risk assessment, illiquidity, due diligence, lack of mark-to-market valuations), the legal aspects are seen as obstructive for most of the wealth managers. Dispossession and secure storage are at the top of their list of requirements for this type of collateral.

Luxembourg can offer a series of answers to address the banker's main concerns. For example, the fiduciary transfer, whereby the lender takes title to the art collateral as a fiduciary and is contractually authorised to appropriate the collateral in the event of default, may be the right tool for a transfer of legal title without dispossession. On top of that, the new Luxembourg Freeport specialising in the storage of valuables can offer secure storage and is likely to become a major draw for bringing art and collectible assets to Luxembourg.

There is now a window of opportunity for art to become a viable option as collateral alongside the more traditional asset classes, especially at a time where people are seeking to monetise their assets.

News regarding Value Added Tax regime in Luxembourg

On 28 August 2014, a draft law (N°6713) modifying the amended law of 12 February 1979 with regard to value added tax was filed on the Chamber of deputies' website.

The modifications focus on:

- the scope of the application of the reduced VAT rate applicable to the import of art objects and antiques (currently 6% on the value of the artwork),
- some tax technical specificities relating to operations within the Free port (in French 'zone franche') completing the initial Law introducing the Free port regime on 28 July 2011 and also,
- the extension of the fiscal regime of the profit margin (in French 'marge bénéficiaire') to be applied to the deliveries of second-hand goods, art objects and antiques and more specifically within the context of public auction by 'Art professionals' who would choose (under certain conditions) to only apply VAT (currently 15%) on the difference between their sale price and their purchase price of an Artwork.

The corresponding Law should enter into force the 1st of January 2015.

There is now a window of opportunity for art to become a viable option as collateral alongside the more traditional asset classes, especially at a time where people are seeking to monetise their assets



Section 3: Art as an investment

Highlights

- **Mei Moses® World All Art Index (All Art-W)** reported a negative performance between 2012 and 2013
- **The most recent ten-year (2003-2013) compound annual return (CAR) for the World ALL Art Index for art was slightly below the S&P500 total return** of 7.4%, at 7%. However, post-war and contemporary and traditional Chinese works of art delivered compound annual returns of 10.5% and 14.9% respectively in the same period—ahead of US and European equities
- **The global art investment fund industry is concentrated in existing art funds that can demonstrate a track record:** the global art investment fund market was estimated conservatively to be worth US\$1.26 billion in the first half of 2014, down from US\$2.13 billion in 2012, driven by a significant unwinding of art investment funds and trusts in China. In 2014, an estimated 72 art funds and art investment trusts were in operation, and 55 of these were in China
- **Tougher regulations on art investment products:** the AMF in France now regulates art funds, and the Chinese government has introduced stricter regulations on trusts.
- **China's art investment boom slowed in 2013:** China's art fund and art investment trust market is rapidly winding down, with an estimated US\$169 million raised in 2013, compared with US\$529 million in 2012. Stricter government regulations on the Chinese shadow-banking market have triggered a slowdown in art investment trusts
- **Confidence in the future of the art fund industry is mixed:** the majority of art professionals and art collectors believe the art fund industry will expand in the next two to three years, but wealth managers are still very cautious owing to issues such as due diligence, lack of liquidity, valuation, lack of track records and an unregulated market
- **Existing art funds are increasing funds under management:** it is clear that those funds with a three to five year track record are finding it easier to attract investors in the current climate, while those with no track record are struggling to get investor attention. One of the major art fund groups accounts for more than 50% of the US and European total, with European art investment funds accounting for an estimated 68% of US and European AUM
- **Art funds could become service platforms for the wealth management industry:** art investment funds have the potential to become one-stop art service platforms for the wealth management industry
- **Art collectors see the benefit of art investment funds as a diversification tool:** 67% of collectors see the potential of art funds as a way of gaining broader exposure to the art market
- **Art professionals see art funds as potential 'door openers' for new art collectors and investors to enter the art market:** 68% of art professionals said that an art fund could provide access to experts and expertise that buyers don't currently have
- **Due diligence remains a key hurdle:** 82% of wealth managers said that due diligence and assessing the viability of art funds were important concerns when making decisions about art investment fund products

The performance of art as an asset class

The Mei Moses® World All Art Index declined by 2% in the first half of 2014

After 2011 saw an all-time year-end closing high for the Mei Moses® World All Art Index (All Art-W)⁶³, the index fell by 3.28% in 2012 and 1.3% in 2013, while the S&P Total Return Index was up 32.39%. However some collecting categories generated positive performance in 2013.

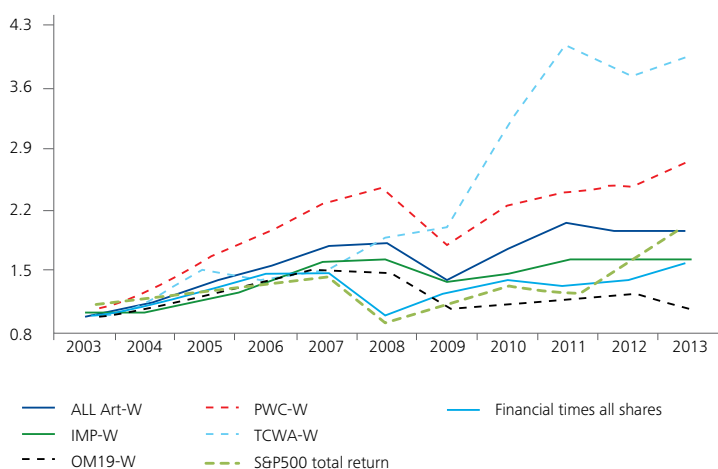
In the first half of 2014, the Mei Moses® World All Art Index continued to respond negatively to improving global economic conditions, declining by 2%⁶⁴, while the S&P Total Return Index was up 7.14%⁶⁵. However, a number of collecting categories continue to show positive performance. In the first half of 2014, traditional Chinese works of art were up 6.9%, impressionist and modern art posted an increase of 6.9% and Old Masters and 19th century works gained 5%, while post-war and contemporary art marked time.

Year-end 2013⁶⁶ performances of the collecting categories comprising the Mei Moses® World All Art index:

WORLD ALL ART INDEX (All Art-W)	⬇️	DOWN	-1.30%
WORLD TRADITIONAL CHINESE WORKS OF ART INDEX (TCWA-W)	⬆️	UP	6.70%
WORLD IMPRESSIONIST AND MODERN INDEX (IMP-W)	⬆️	UP	1.30%
WORLD POST-WAR AND CONTEMPORARY INDEX UP (PWC-W)	⬆️	UP	10.50%
WORLD OLD MASTER & 19 TH CENTURY INDEX (OM19-W)	⬇️	DOWN	-14.28%
NEW YORK-BASED LATIN AMERICAN INDEX	⬇️	DOWN	-15.70%
NEW YORK-BASED AMERICAN ART INDEX	⬇️	DOWN	12.40%
LONDON-BASED BRITISH WORKS OF ART INDEX	⬆️	UP	6.30%

The most recent ten-year (2003-2013) compound annual return (CAR) for the World ALL Art Index for art was 7%, slightly below the S&P500 Total Return Index of 7.4%. Post-war and contemporary and traditional Chinese works of art delivered compound annual returns of 10.5% and 14.9% respectively—a stronger performance than US and European equities in the last ten years.

Fig. 30 Mei Moses® family of world art indexes® since 2003
Mei Moses® world collecting category art indexes vs. S&P 500 total return and FTAS indexes since 2003®



63 The Mei Moses World All Art Index is from the Mei Moses® family of art indexes and is based on a proprietary database of repeat sale pairs created from transactions in the United States and Europe, recently added data from art transactions in China and historical information from THE EUROPEAN FINE ART DATABASE created by Prof Rachel Pownall

64 There are three regional indexes for American, Latin American in NY and British painting in London. There are also some sales, such as Russian art, that fall into several categories and are thus put in All Art, since these cannot be easily allocated. As post-war and contemporary (PWC) accounts for a larger share of the index and saw no change during 2013, the smaller regional indices may affect the overall result

65 Source: Bloomberg in USD for the period 31/12/2013 to 30/06/2014

66 Insights into art market financial performance through 2013 based on the Mei Moses® family of collecting category art indexes®

Table 2: Comparative performance 2000-2012

Mei Moses® world collecting category indexes (in US\$)

10 years	All Art	IMPMOD	OLM19C	Post war and contemporary	Trad. chinese	S&P total return
CAR	7.00%	5.10%	0.60%	10.5%	14.9%	7.40%
STDEV	13.10%	10.50%	14.50%	16.20%	22.80%	18.80%
CORR-S&P	-0.198	-0.099	-0.305	-0.061	-0.184	1.000

Risk and correlation

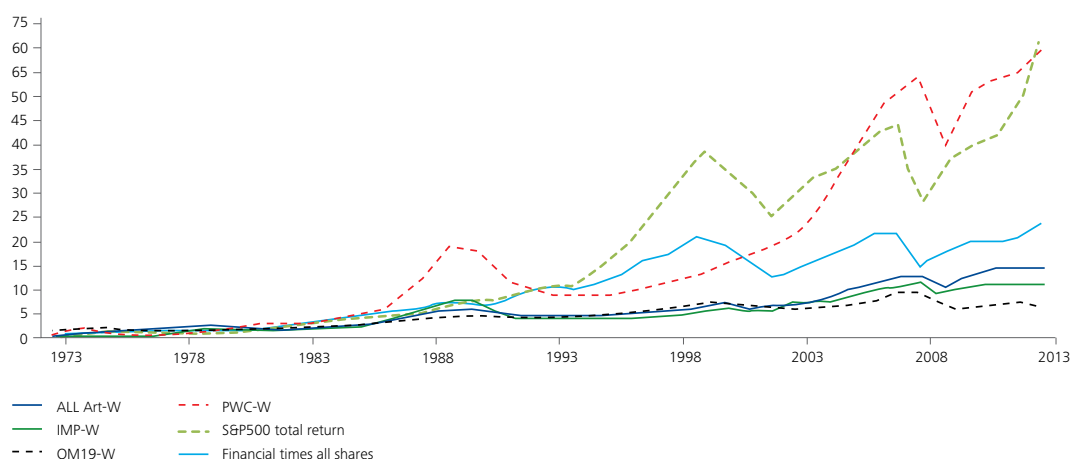
In addition to return, relative risk is another important measure of financial performance. The risk associated with traditional assets is reinforcing the opportunity to include art in an optimal portfolio allocation. It is clear from Table 2 that the S&P 500 Total Return Index has been more volatile than most of the art indices (except traditional Chinese) over the last ten years. The risk associated with each index is measured by the standard deviation of the changes in their annual returns.

The absolute risk associated with the Mei Moses® All Art Index is lower than that of the S&P 500 Total Return Index over the last ten years (13.1% versus 18.8% respectively).

According to Mei Moses®, the correlation of returns among assets is another measure used in financial decision making. The negative correlation factor between the annual percentage changes in the different art categories and stock indexes for the last ten years indicates that art may play a positive role in portfolio diversification.

Fig. 31 Mei Moses® family of world art indexes® since 1973

Mei Moses® world collecting category art indexes vs. S&P 500 total return and FTAS indexes since 1973®



For the last 40 years (1973-2013), the compound annual return (CAR) for the World All Art index was 6.9%, below the S&P's 10.9%. The S&P and post-war and contemporary art have very similar results, with a CAR of 10.9% and 10.8% respectively.

Table 3: Comparative performance

Mei Moses® world collecting category indexes (in US\$)

40 years	All Art	IMPMOD	OLM19C	Post war and contemporary	Trad. chinese	S&P total return
CAR	6.90%	6.20%	4.80%	10.8%	NA	10.90%
STDEV	15.70%	18.60%	15.10%	36.60%	NA	18.20%
CORR-S&P	-0.011	-0.036	0.074	-0.344	NA	1.000

Risk and correlation

From Table 3, we can see that the S&P 500 Total Return Index had a volatility comparable to most of the art indices, although post-war and contemporary have proven more volatile over a 40-year period. The absolute risk associated with the Mei Moses® All Art Index is slightly lower than that of the S&P 500 Total Return Index over the last 40 years (15.7% versus 18.2% respectively).

There is a low or negative correlation between the annual percentage changes in the art and stock indexes. The very low or negative correlation factor between the different art categories and stock indices for the last 40 years indicates that art may play a positive role in portfolio diversification.

Art investment: the art fund market

The art fund market is showing modest growth in the United States and Europe as existing art funds raise new capital

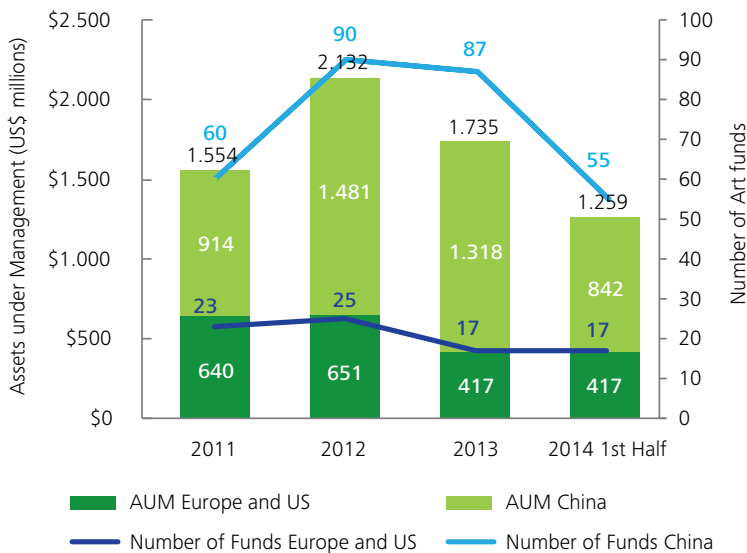
In the first half of 2014, the overall art fund market⁶⁷ was conservatively estimated at US\$1.26 billion⁶⁸, down from US\$2.13 billion in 2012. In the last report, we gave the 2012 figure as US\$1.62 billion, however, in 2013 more information was released regarding the extent of the art trust industry in China and the numbers in this section reflect re-adjustments of the figures for 2011-2014. In 2014, an estimated 72 art funds and art investment trusts were in operation, and 55 of these were in China.

The US and European art fund market remained relatively stable in 2014, with an estimated US\$417 million of assets under management⁶⁹. New capital has largely been raised on the back of existing art funds rather than an influx of new ones. It is clear that those funds with a three to five year track record are finding it easier to attract investors in the current climate, while those with no track record are struggling to get investor attention. To illustrate this point, The Fine Art Fund Group accounts for more than US\$250 million of the US\$ 417 million total, and European art investment funds account for an estimated 80.3% of US and European AUM.

Tougher regulation on transparency and marketing of art and collectible funds

European regulators are taking an increasing interest in unregulated non-traditional asset funds, with the AMF in France announcing that it will regulate investments in non-traditional assets as from March 2014. See Section 5 and the article by Catherine Cathiard for more information regarding these changes. In the UK, the Financial Conduct Authority (FCA) announced in 2013 that it will ban the promotion of unregulated collective investment schemes (UCIS) and certain close substitutes (together to be known as 'non-mainstream pooled investments' or NMPIs) to the vast majority of retail investors in the UK. The advent of stricter regulation could lead to a greater level of professionalisation among non-traditional asset funds, and increase the confidence among investors in these types of assets.

Fig. 32 Global art investment fund market 2011—2014 1st half
Estimated assets under management (AUM) in US\$



As more information has been released regarding the art trust market in China, we updated the figures for the period between 2011 and June 2014, which were significantly higher than the estimates we used in the previous two editions of the Art & Finance Report.

Source: Deloitte Luxembourg & ArtTactic Art & Finance Report 2014

⁶⁷ Measured in terms of assets under management (AUM)

⁶⁸ A conservative estimate of US\$417 million of this total is based on art investment funds in Europe and the United States that reported their AUM. The Chinese art fund and art investment trust market was worth an estimated US\$842 million in June 2014, based on publicly available information

⁶⁹ This is a conservative estimate and is based on art investment funds in Europe and the United States that reported their AUM. A number of art fund providers included in last year figures did not submit their AUM and are therefore not included in the above total. Fine wine and collectibles funds are also excluded, as are private, family wealth-oriented art funds that do not raise funds from external investors

The art investment fund and trust market has cooled following a clampdown by the Chinese government of the shadow banking system

After art funds and art trust products in China reached a peak in 2012, with an estimated total of assets under management (AUM) of US\$1.48 billion, the market cooled to an estimated US\$842 million in the first half of 2014. Of the art fund and art trust products launched in 2010-2012, 41% were expected to mature in 2013. The Chinese art investment fund and trust market raised an estimated US\$169 million in 2013, against US\$529 million in 2012, and US\$769 million in 2011. Based on the first half of 2014, an estimated US\$107 million of new funds was raised in the first half of 2014. The inflow of money into art funds and art trust products has been significantly reduced since 2011/2012, mainly as a result of stricter regulations on trusts⁷⁰ introduced by the Chinese government in 2014.

An overview of art and finance regulation in China

Over the last couple of years, with the fast development of the art market in China, the government has been conscious of the importance of implementing art specific legislation in order to achieve better regulation and decrease potential risks for art market operators and collectors/investors.

Back in 2010, nine ministries, including the Ministry of Finance and the Ministry of Culture, jointly issued '*Guidance on the financial support for the prosperity and development of the culture industry*'⁷¹ as a basis to expand and improve the financial services for the cultural industry. This guidance provided, among other things, recommendations on the development of credit products for the culture industry, a multi-level capital market and the insurance market.

Following the 1st Chinese Art Development Summit held in Beijing in December 2012, the Ministry of Culture began work, in March 2013, on the draft of the '*Management of Art Market Regulation*'⁷², aimed at improving the organisation of the art market and standardising operations involving art assets. This regulation will provide a clear management framework for art brokerage services, auction houses, exhibitions and selling, and art import and export activities, etc. While the issue of the authentication of art assets is still being debated, an official draft is not available yet.

In March 2014, the Ministry of Finance, in collaboration with the People's Bank of China (the country's central bank) and the Ministry of Culture, published a policy notice⁷³: '*Opinion regarding the promotion of further cooperation between finance and culture*'. It pointed out the importance of having a comprehensive understanding of the cooperation between finance and culture as a new trend for current economic and social development. In addition, the notice encouraged financial institutions to establish specific services dedicated to cultural industries with the support of professional financial and cultural teams. It also raised the need for innovative financial products and services that are in step with the development of the cultural industry, such as initiating the development of internet transaction services for art assets and payment and settlement systems, and exploring the solutions for custody of art assets. Finally, the notice emphasises the need to strengthen the implementation of organisational and supporting measures.

70 Art trusts are part of the unregulated Chinese shadow banking system, which has increasingly come under government scrutiny in the last 12 months. There are two kinds of art trust: one is used as a financing vehicle, and the other is an investment vehicle. In China, about 80% of art trusts were estimated to be of the financing vehicle type, where artworks were being used as collateral for other types of loans to the real estate industry, for example, or other types of businesses on which the government has imposed lending restrictions

71 Central People's Government of the People's Republic of China (http://www.gov.cn/gzdt/2010-04/08/content_1576191.htm)

72 Central People's Government of the People's Republic of China (http://www.gov.cn/gzdt/2013-03/15/content_2355205.htm)

73 The Ministry of Finance (http://www.mof.gov.cn/zhengwuxinxi/zhengcefabu/201403/t20140326_1059932.htm)

Although the regulation of the Art & Finance market is still at an early stage in China, great progress has been made over the last four years.

The different policy notices and opinions were listened to and followed by the stakeholders of the Chinese art market, and financial institutions have continued to propose more diverse culture and art-related products and services. In 2013, Minsheng Bank created a club for art collection and investment in order to provide art lending services to its HNWI clients, while in 2014, Weifang Bank announced its aim to build an art and finance database to shape the study of the art market towards a more quantitative approach.

In 2014, 98 companies obtained credit loans from more than 20 banks for culture and art projects for a total amount over RMB 150 billion⁷⁴. Undoubtedly, legislation specifically aimed at art and finance will help financial institutions to control their risks, bring more transparency to the art market and systematise best practice for a market that is still in expansion. Close collaboration between government and private sector experts might be necessary for this long legal journey to be successful.

Case studies: art investment funds

Below are two examples of art investment funds that are actively focusing on market transparency by making performance figures available to the public.

Table 4: Two examples of art investment funds—structure and performance

	Fine Art Invest Fund (PMG Fonds Management AG)	Tiroche Deleon Collection (Art Vantage PCC Limited)
Launch year	2010	2012
Term	Open-ended (quarterly redemptions)	10 years
Investment objective	Contemporary photography (1970 onwards)	Contemporary art from developing markets
Total return	32.69% (since 4Q 2011)	30.92%* (since Jan 2011)
Minimum subscription	€75,000	US\$500,000
AUM	US\$17.8 million (June 2014)	US\$20 million (July 2014)
Website	www.fineartinvestfund.com	www.tirochedeleon.com
Domicile of fund	Malta	Gibraltar

*30.92% is The Total return figure as of June 30 2014. This is counted from inception date of the collection which is Jan 2011. The private collection was converted to a fund on 1 March 2012 (and that is the inception date of the fund structure - which is 10 years).

'The Fine Art Invest Fund considers art a safe currency. A currency, whose intrinsic value increases, that can be handled worldwide and overcomes all national boundaries.'

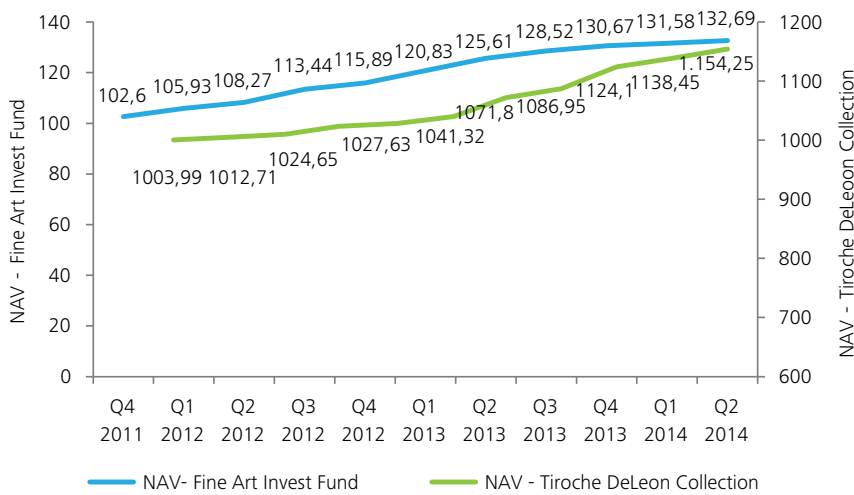
PFF—Fine Art Invest Fund, PMG Fonds Management AG

'Our objective is to bring a level of transparency and professionalism that will enable a broader range of investors to diversify into art investments.'

Tiroche DeLeon Collection, Art Vantage PCC Limited

Case study: art investment funds—historical net asset value (NAV) for the Fine Art Invest Fund⁷⁵ and Tiroche DeLeon Collection⁷⁶

Fig. 33 Illustration of the evolution of Net Asset Value* of two art funds



*Net asset value (NAV) represents a fund's per share market value

Survey findings⁷⁷: art investment funds

Wealth managers

The limited number of operational art investment funds is hampering confidence building in this type of investment. The recent survey shows that only 8% of wealth managers are currently offering clients advice on investing in art investment funds (none of the family offices surveyed offer this service); this was down from 26% in 2012. With regard to the future, again only 8% of the wealth managers said that they were likely to include art investment funds as part of the bank's product platform in next two years (this was down from 18% in 2012).

There is a lack of investor demand for art investment funds, but increasing confidence in the future of the art fund industry: 20% of wealth managers said they have seen an increase in demand for art investment funds in the last 12 months, compared with 30% in 2012. About 97% of the wealth managers said that less than 10% of their client base would consider investing in an art investment fund.

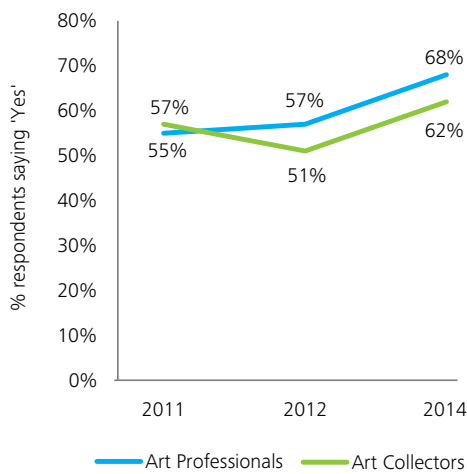
This corresponds with findings from the survey of art collectors, where a minority, 28%, would potentially consider investing in an art fund. However, both a majority of art professionals (68% up from 57% in 2012) and art collectors (62% up from 51% in 2012) continue to believe that the art fund industry will expand in the next two to three years, which suggests that a new type of art fund industry—targeted at a different type of investor—could emerge.

75 FAIF Performance Report—second quarter of 2014 (30.6.2014)

76 Source: <http://www.tirochedeleon.com/about/investors/> & <http://www.bloomberg.com/quote/ARTVANT:TL/chart>

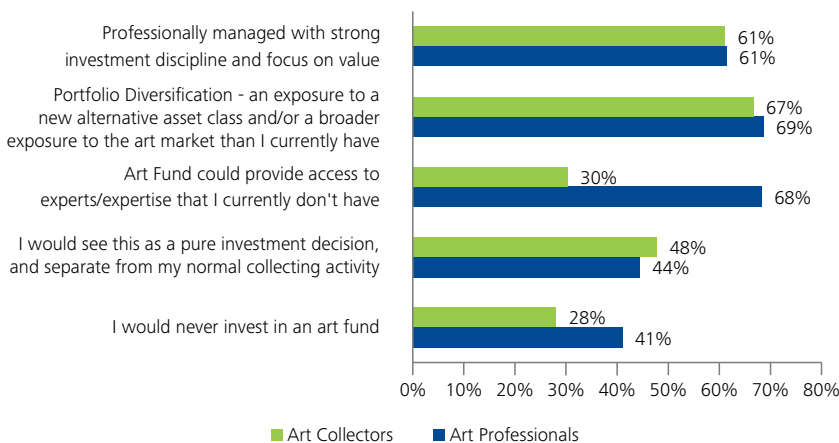
77 From Deloitte ArtTactic Art & Wealth Management Survey 2014

Fig. 34 Do you believe the art fund industry will expand in the next two to three years?



Source: Deloitte Luxembourg & ArtTactic Art & Finance Report 2014

Fig. 35 Art investment funds: which of the following statements do you agree/strongly agree with?



Source: Deloitte Luxembourg & ArtTactic Art & Finance Report 2014

New art fund art advisory models could become service platforms for the wealth management: a few of the operational art funds, such as the Fine Art Fund in London continue to add assets under management, and have seen an increase from US\$150 million in 2012 to US\$250 million in 2014. The art fund business has also evolved to include 'managed accounts', art advisory, co-investment arrangements, as well as traditional art investment funds. This boutique style set-up is likely to become a model for future art investment funds, and has the potential of becoming a one-stop art service platform for the wealth management industry. In general, an art fund's audited track record and regulatory compliance make it more suited to servicing an increasingly regulated financial industry.

Art collectors see the benefit of art investment funds as a diversification tool: 67% of collectors see the potential of art funds as a way of gaining broader exposure to the art market. A further 61% of the collectors surveyed said that art funds could offer 'professional management with strong investment discipline and a focus on value'.

Art professionals see art funds as potential 'door openers' for new art collectors/investors to enter the art market. 68% of art professionals said that an art fund could provide access to experts and expertise that the buyers don't currently have. 39% of art professionals would advise their clients to consider investing in an art fund; this percentage has remained constant since 2011, which is likely to relate to the stagnant nature of the art fund industry.

Challenges: what are the main challenges for the development of the art investment fund industry?

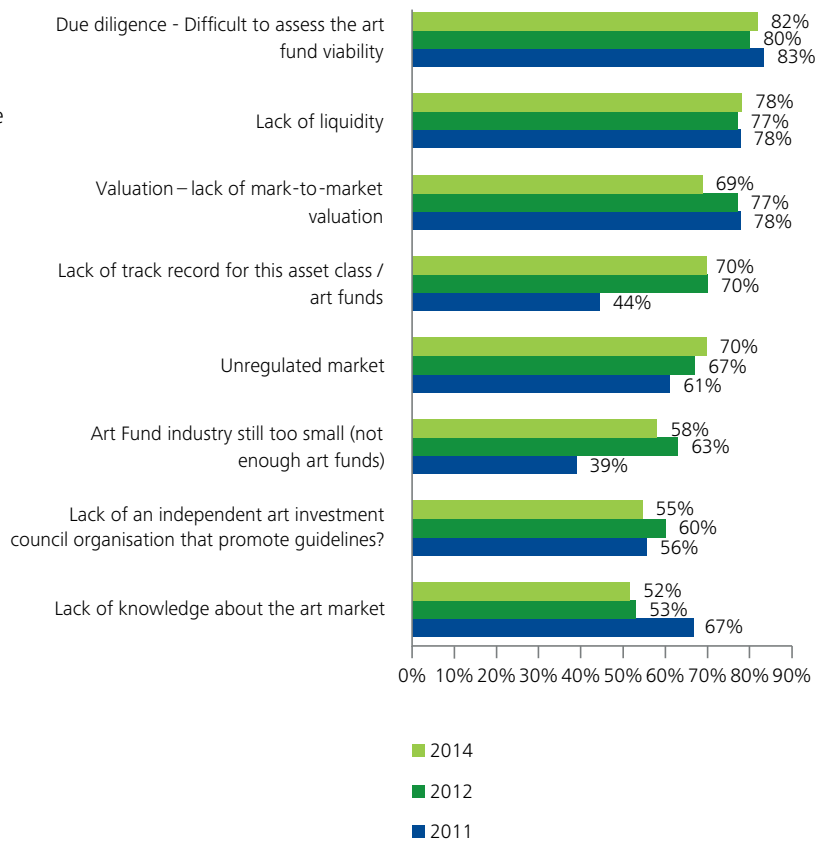
Due diligence remains a key hurdle: 82% of the wealth managers surveyed for this report said that due diligence and assessing the viability of art funds are among the biggest challenges (up from 80% in 2012). This challenge relates to the lack of track records for the art fund industry, which 70% said was a key challenge (the same as in 2012) and the unregulated nature of the market, which a further 70% of wealth managers said was a major obstacle (up from 67% in 2012).

Lack of liquidity and mark-to-market valuations:

78% of the wealth managers cited low liquidity (up from 77% in 2012) and a further 69% said the lack of mark-to-market valuations remained key challenges for the market (down from 77% in 2012). Despite some differences, the key challenges are similar to the 2012 and 2011 findings, which suggest that the art fund industry continues to struggle as a result of some fundamental obstacles linked to the immaturity of the industry and a lack of art funds with auditable track records.

Going forward, the performance and track record of a handful of art funds that will soon reach maturity, such as the Fine Art Fund Group’s first art fund set up in 2004, The Collector Fund (established in 2005), Artemundi Global Fund (set up in 2009) and the Art Photography Fund (set up in 2008), could instil new confidence in art as an investment and encourage new art funds to come to the market. However, the track record built up by the existing art funds gives these managers an advantage in raising further investments in the future.

Fig. 36 What do you feel are the main hurdles for incorporating art investment funds as part of the bank’s current client offering?



Source: Deloitte Luxembourg & ArtTactic Art & Finance Report 2014

Section 4: The online art industry

Highlights

Art & Finance and the impact of technology and the online art market:

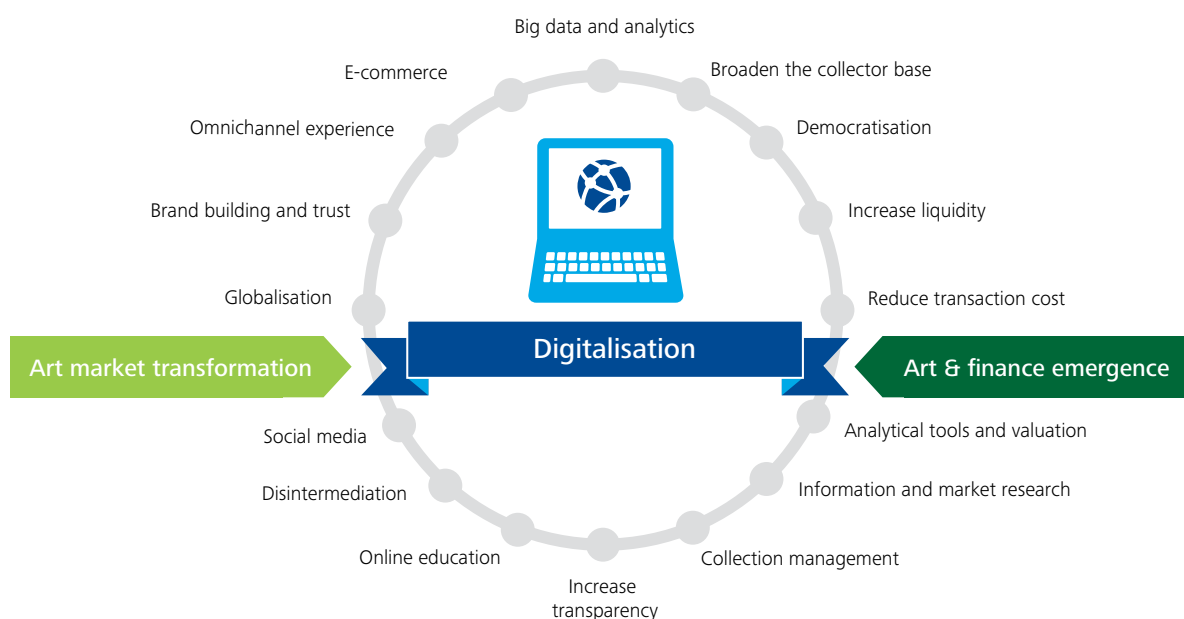
- **M&A activity is likely to pick up as the online industry matures:** with the number of online art marketplaces and auctions increasing, we are likely to see some consolidation taking place in the future, opening up opportunities around art and corporate finance
- **Larger online art marketplaces are likely to increase liquidity,** broaden the collector base, reduce transaction costs and increase transparency, which could encourage more people to look at art as an asset class
- **Opportunities should arise in data, research and analysis** as the art market is increasingly looking for better tools to make informed decisions and to help address some of the concerns that wealth managers have when it comes to transparency, valuation and the lack of information and research in the art market
- **Art professionals and collectors see opportunities for online art education:** 67% of collectors and 63% of art professionals see potential for businesses focusing on art education
- **Disintermediation shows untapped potential:** collectors and art professionals both indicated increased confidence in the future of consumer-to-consumer and dealer-to-dealer sales platforms for the online art industry
- **Online art and collectibles auctions expected to see rapid growth:** 77% of art collectors and 69% of art professionals believe that the online art auction market will become one of the winning business models
- **eBay is entering the higher end of the art and collectibles market by partnering with Sotheby's:** a further boost to the online art auction market has come from e-commerce giant eBay, which announced in July 2014 that it has agreed to partner again with Sotheby's
- **Building trust:** developing online brands and companies that can inspire a high degree of trust will be the key challenge for any online player in the art world

The relevance of the Art & Finance industry is strengthened by the development of the online art market. New technologies can improve transparency, valuation and risk monitoring in the art and collectibles market and are likely to facilitate further growth in Art & Finance-related activities, such as art secured lending and art investment funds.

The findings from this section show that the current focus in terms of investment trends in online art-related businesses is predominantly linked to the e-commerce aspect of selling art online. However, it is important to keep in mind that the online art market will struggle to grow without the help of other enabling online technologies that will provide information and price data, especially object-specific information such as electronic certificates of authenticity and condition reports, market research and analysis, as well as education. The management of the disparate information sources linked to individual artworks will also become important, which could signal growth in the industry linked to information aggregation and online art collection management tools.

In this section, we also draw inspiration from—and certain parallels with—a recent report by Deloitte titled *'Global Powers of Luxury Goods 2014—In the hands of the consumer'*, which looks at global trends in the luxury goods industry, including the impact of the internet. The art market should certainly take notice and learn from the lessons of the luxury goods industry, which is arguably ahead of the art market when it comes to its online evolution.

A. Global online art industry trends 2014 and survey findings on the outlook for the online industry



Global versus local: the globalisation of the art market has been accelerating in the last ten years, with significant growth in global art infrastructure investments such as museums, galleries, auction houses, art fairs, festivals and biennials. Art fairs have been particularly successful in bringing international art to new audiences and new markets.

With the maturation of e-commerce infrastructure and the emergence of online art marketplaces, the globalisation of the art market is now developing at an unprecedented pace. However, globalisation also presents unavoidable challenges, which the online art market will also have to face. Already, there are significant discrepancies among different geographical markets in terms of consumer protection when art is bought online.

Transacting across geographical markets with different legal jurisdictions presents risks associated with non-payment, defective title, condition and authenticity problems, and raises questions about rights and how to enforce them in the event of any of these issues arising. Complicated import, export and VAT duties make the movement of art far from frictionless. If we also add the specialist nature of packing, shipping and storing art, logistical challenges could make certain art transactions uneconomical. So while the art market might be perceived as the next market ready for disruption, it is the traditional galleries, dealers and auction houses that have the most knowledge in cross-border transactions and in handling often fragile artworks. Accordingly, online platforms or marketplaces that can plug experienced traditional art businesses seamlessly into the digital marketplace will be well positioned to benefit from, and participate in, the growth of online.

Brand building and trust in the online space:

reputation is arguably the most valuable commodity in the art world. How can traditional galleries and auction houses translate their existing reputation into a digital environment? And how can new art e-commerce platforms build a reputation and trust in a notoriously closed and relationship-driven art market. In a response to these challenges, the last 12 months have seen an proliferation of strategic partnerships between the 'new' and 'old' art world.

Omni-channel⁷⁸ approach to art buying: with online art e-commerce growing, there are increasing concerns among traditional bricks-and-mortar galleries, dealers and auction houses that their physical space will gradually become less relevant and by not embracing the online art market they also fail to cultivate a new group of art buyers and collectors. They need to work out how to adapt their existing business model and strategy to advances in technology and the advent of e-commerce. Those who actively embrace the online art market are likely to boost their existing business, as their online component becomes another aspect of the customer journey. According to a recent report by Hiscox⁷⁹, in the future, the question won't be about where the art sale takes place, but is more likely to concern how an online strategy could influence potential buyers to transact online or offline. According to the *'Global Powers of Luxury Goods 2014—In the hands of the consumer'* report by Deloitte, omni-channel shoppers spend 76% more than in-store only shoppers—and this trend is also likely to have an impact on the consumer habits of art buyers and collectors in the future.

Big data⁸⁰ and analytics can increase our understanding of client behaviour and how the art market works:

leading art market players are increasingly exploring new ways to develop insights across customers and markets. Seeking an information advantage is relatively new in the art market, and the ability for art industry players to incorporate new types of data from inside and outside their firms could produce new and interesting results. Big data allows firms to incorporate data from a wider pool of digitally available information that is now easier to access, manage and make sense of than ever before. The advent of the online art market is likely to increase the amount and availability of potentially useful information and help these companies compete in an increasingly consumer-empowered economy.

Social media is likely to play an increasingly important role in brand awareness and sales generation among the next generation of buyers:

it is quite telling how the traditional art world is embracing social media, when Sotheby's and Christie's are increasingly promoting individual auction lots coming up at future auctions via Instagram⁸¹ (often weeks in advance of the actual catalogue appearing). Traditional media advertising in the art world is increasingly being complemented by active usage of social media channels such as Twitter, Facebook, Instagram, Pinterest, Tumblr and ArtStack to reach new audiences.

Online education will increase awareness, interest and understanding: with the advent of media-rich and interactive online information platforms, both new and experienced art buyers and enthusiasts will increasingly educate themselves about art and the art market online. Both privately-run and public art institutions have taken massive strides recently in creating user-friendly digital archives of their collections and research material. Moreover, social media tools, such as ArtStack and Instagram, are becoming massive libraries for visual imagery and can provide invaluable insights into the evolution of an artist's practice and public interest in their work, particularly for practising contemporary artists. The Google Art Project, is another initiative that is opening up public online access to high-resolution images of artworks housed in the initiative's partner museums⁸², providing access to the art collection for those who might never have a chance to physically visit the museum itself. We are also likely to see an expansion in online art and art market-related courses going forward, provided by universities, public institutions, individuals and museums themselves. The Museum of Modern Art in New York (MoMA), Metropolitan and Guggenheim are all organising their own online art courses.

Both privately-run and public art institutions have taken massive strides recently in creating user-friendly digital archives of their collections and research material



⁷⁸ *Omni-channel is a term often used in the context of multi-channel retailing, but emphasises a more seamless approach to the consumer experience through all available shopping channels, i.e. mobile internet devices, computers, brick-and-mortar, television, radio, direct mail, catalogues and so on*

⁷⁹ *Hiscox Online Art Trade Report 2014*

⁸⁰ *Big data is a blanket term for any collection of data sets so large and complex that it becomes difficult to process using on-hand data management tools or traditional data processing applications*

⁸¹ *Sotheby's and Christie's had 31,300 and 41,200 followers as of 25 July 2014*

⁸² *On 3 April 2012, Google announced a major expansion to the Art Project with the signature of partnership agreements with 151 museums in 40 countries*

Survey findings on the outlook for the online industry

Despite certain reservations, online optimism remains strong: 53% of collectors (down from 65% in 2012) and 69% of art professionals (up from 62% in 2012) remain optimistic about the importance of online art businesses in the next two to three years. Although there are reservations concerning the future success of specific business models, the overall market perception is a positive one. This is also reflected by the increasing amount of investment flowing into new online businesses.

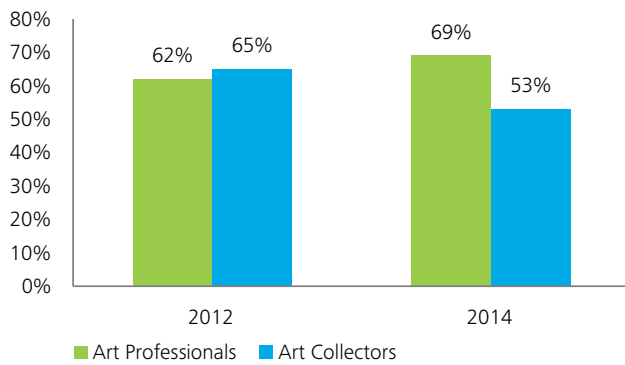
Although there are reservations concerning the future success of specific business models, the overall market perception is a positive one

The online art market is a supplement rather than a substitute: as was observed in the Hiscox Online Art Trade Report 2013, the online market is likely to lead to an evolution, not revolution for traditional market players. Though optimistic about the future importance of online art businesses to the market, the majority of both art collectors (70%) and art professionals (65%) do not see traditional operators in the art market being replaced by online business models. This is a positive sign, especially when viewed in the light of the overall industry and collector optimism about online art businesses. It is a sign that the art industry is learning how to integrate and exploit the benefits of digital services without undermining their traditional revenue streams and business models.

Collectors and art professionals question the sustainability of the current boom in online businesses: although 44% of collectors and 47% of art professionals believe that the current boom in online art ventures is sustainable, a significant 38% of collectors believe it is not, compared with 23% for art professionals. A further 18% of collectors are unsure, compared with 29% of art professionals. This is likely a reflection of overcrowding, with an increasing number of online marketplaces utilising similar business models in a relatively narrow segment of the art market. The threat of eBay and Amazon having entered the market is also likely to weigh on the sustainability of the current boom.

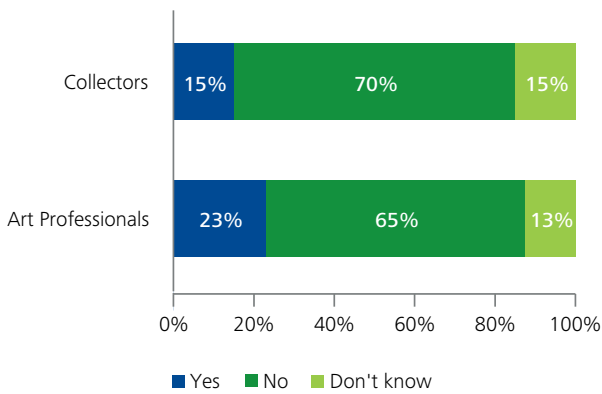


Fig. 37 How important do you think that online art businesses will be in the next two to three years?



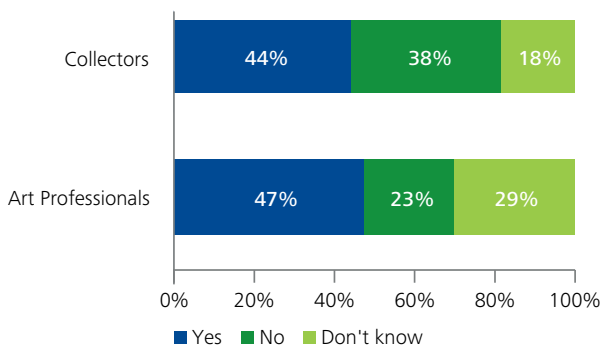
Source: Deloitte Luxembourg & ArtTactic Art & Finance Report 2014

Fig. 38 Do you think that the traditional operators in the art market could be replaced by new online ventures, similar to what we have seen in the music, film and book industries?



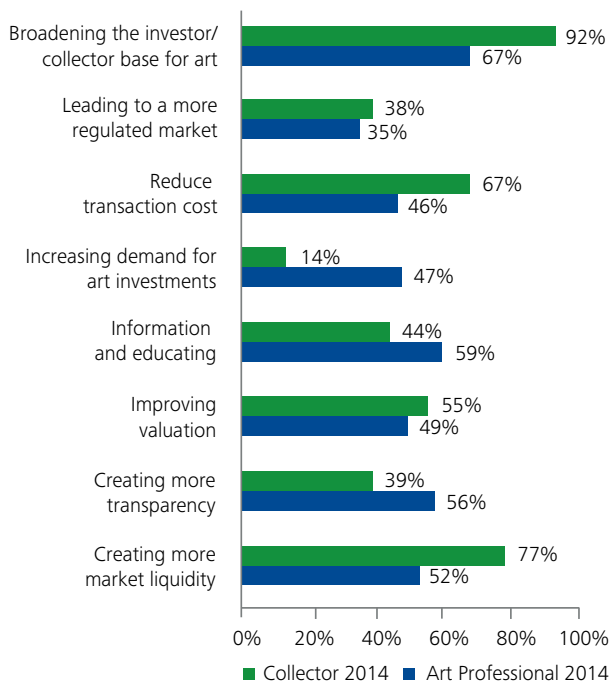
Source: Deloitte Luxembourg & ArtTactic Art & Finance Report 2014

Fig. 39 Is the current boom in online art ventures/businesses sustainable in your view?



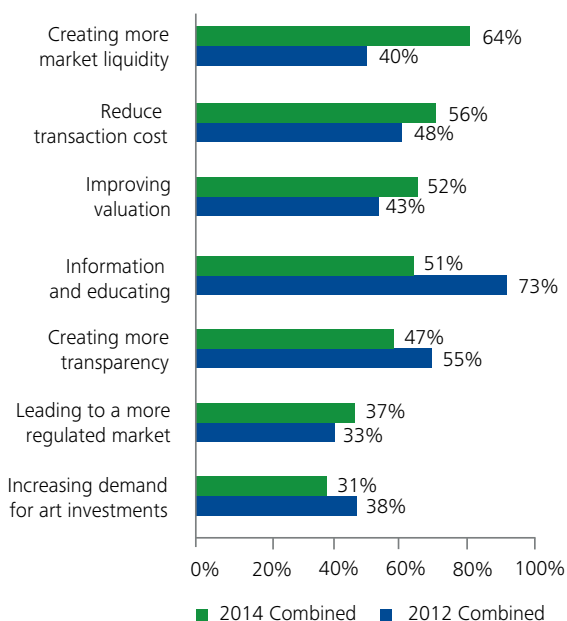
Source: Deloitte Luxembourg & ArtTactic Art & Finance Report 2014

Fig. 40 How important do you believe online art businesses and new technology will be in the following factors?



Source: Deloitte Luxembourg & ArtTactic Art & Finance Report 2014

Fig. 41 How important do you believe online art businesses and new technology will be in the following factors? (art professionals and art collectors combined in 2012 versus 2014)



Source: Deloitte Luxembourg & ArtTactic Art & Finance Report 2014

B. Survey findings: the online art industry and its potential impact on the Art & Finance market

Online art businesses are crucial in democratising and broadening the existing collector base, which is likely to lead to improved market liquidity:

92% of art collectors and 67% of art professionals said that online art businesses have the potential to broaden the collector and investor base for art, which in turn could lead to improved overall market liquidity as more participants enter the art market (the majority, 77% of art collectors and 52% of art professionals said this would be a likely outcome). This could be significant for the wealth management industry, as 81% of wealth managers said that liquidity was a key impediment to providing art secured lending services, and 78% said that this was also one of the key challenges with the art investment fund industry.

Online art businesses can help improve the valuation of art and collectibles: with 78% of wealth managers citing valuation as a key hurdle in providing art secured lending services and 69% saying this is a key challenge for the art investment fund market, it looks like there is significant room for online art businesses to improve this. 55% of art collectors and 49% of art professionals believe that new technology and online art businesses have the potential to improve valuation of art and collectibles. The advent of the widespread digitisation of data (see Big Data trends above) and the ability of technology to process this data means that we are likely to see significant improvements and potential standardisation around valuation methods and processes. This is unlikely to replace the connoisseurship approach to valuation and appraisal, but will be an additional tool with which to meet the demands of a data-driven wealth management industry.

There is a marked disagreement between art professionals and collectors over what effect online will have on investment demand. Only 13% of collectors believe that online art businesses will have an important role in increasing demand for art investments—while 47% of art professionals believe this to be the case. This represents a dramatic change from 2012, when 43% of collectors believed online art businesses would increase art investment demand, versus only 33% of art professionals who felt the same. This is likely a result of the increasing realisation among collectors that much of the trade in blue-chip works is not captured by online databases and that most of the items traded through online platforms are low- to medium-priced art and collectibles and rarely include market mature investment-grade art.

Online art businesses are likely to drive down transaction costs as competition increases: 67% of collectors and 46% of art professionals said that online sales platforms are likely to drive down overall transaction costs in the art market. With auction sales commissions as high as 25%⁸³, there is plenty of room for online sales platforms and marketplaces with a lower overhead structure to reduce transaction costs. For example, a peer-to-peer platform, such as ArtVatic, which charges only 3% commission from both the buyers and the seller, is well positioned to capitalise on a lower cost of doing business by implementing lower client service fees.

Only 13% of collectors believe that online art businesses will have an important role in increasing demand for art investments—while 47% of art professionals believe this to be the case

Art professionals and collectors are divided over importance of online in creating more art market transparency: 56% of art professionals believe the online art market will increase market transparency (up from 51% in 2012). However, only 35% of art collectors believe the online art market will create more transparency (this was down from 59% in 2012). This is likely a reflection of the fact that although online platforms are increasing market liquidity at the lower- and mid-range of the art and collectibles market, transactions at the higher end of the market are still done primarily via private channels. In addition, auction results from many of the online auctions and marketplaces are often not accessible to the public, presenting yet another hurdle to transparency. The immaturity of the online art industry also means that current players remain guarded about their performance to date, and hence are hesitant in sharing sales results; however, we expect this to change as the online art market matures. With 79% of wealth managers citing that lack of transparency as one of the key challenges in offering art-related services, it is clear that there are plenty of opportunities for the online art market to help in this regard.

Online information and education are seen as important for the Art & Finance industry—but less so than in 2012. Art professionals are still optimistic (59% said that they believed that these businesses will have an important impact on the Art & Finance industry, compared with 44% of collectors). The rapid growth of digital academic resources (digitisation of museum archives and online catalogues raisonnés), dedicated art news sites, price databases, art indices and analytical tools are likely to strengthen the information infrastructure required to make intelligent and informed decisions around art and collectible assets. However, such resources will augment, not replace, the importance of educated advice from industry professionals. Wealth managers could benefit from working more closely with online information and education providers to integrate these services into their existing offering. 61% of collectors and art professionals felt that art market research and information should be a service provided by the wealth management community to their clients.

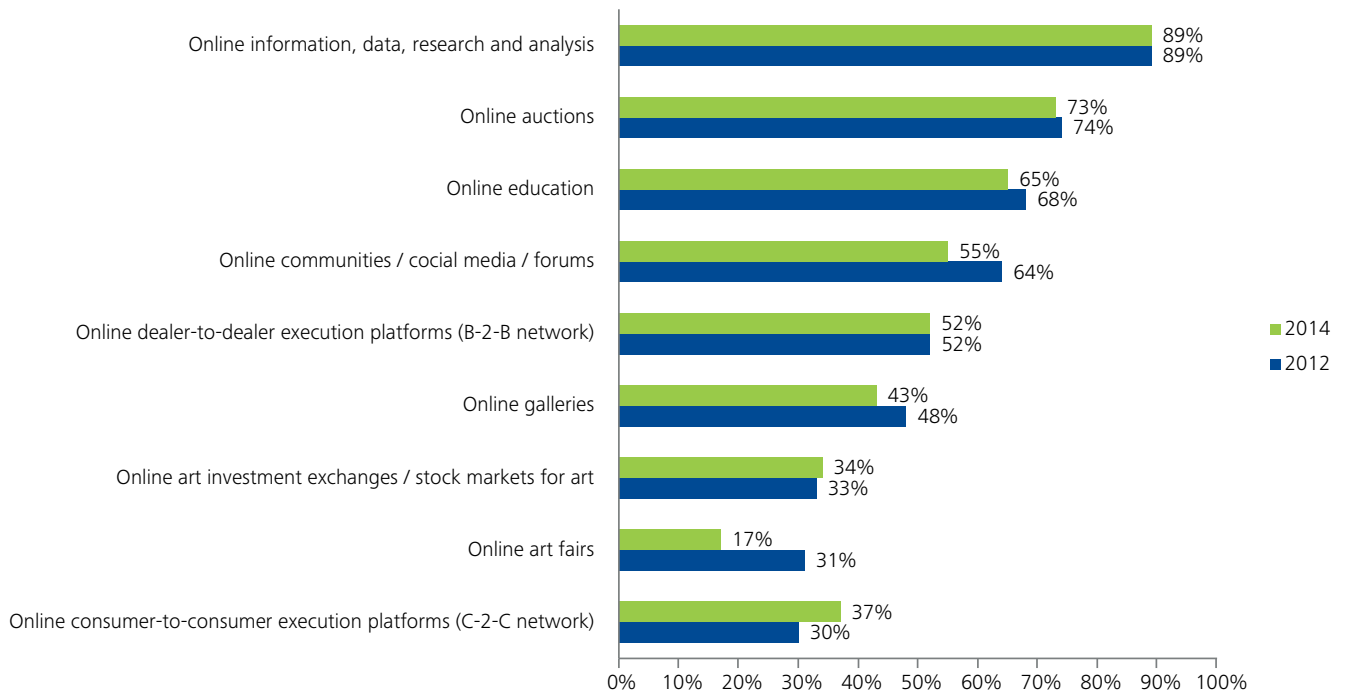
⁸³ Buyer's premium paid for works of art sold for less than \$100,000 at Sotheby's, Christie's and Phillips

C. Online art business models: what type of online businesses do you believe will succeed in the future?

Opportunities in data, research and analysis should arise as the art market is increasingly looking for better tools to make informed decisions: both art collectors and art professionals see a strong future for online businesses that facilitate access to information and data, research and analysis: 89% (the same result as in 2012) said that they believed these business models would succeed in the future. Collectors in particular are even more confident about the future of such online data, analysis and content businesses, with 92% saying this part of the online art industry will succeed (up from 83% in 2012).

However, new business models need to be adopted, since most of the information- and content-driven business models are becoming increasingly difficult to monetise, as users expect to access data and information for free. This is already happening in the art auction database market, where this data is increasingly becoming a free commodity. Artnet and Artprice have been among the dominant players in this field, offering access to data and past sales prices through different levels of subscriptions. However, Artinfo and other information platforms such as Invaluable and the-salesroom are offering access to past auction data for free or for a low entry price. Companies such as Tutela Capital provide instant valuations of paintings using statistical models, which is likely to prove a complementary service to more traditional form of appraisal and valuation.

Fig. 42 Which online business models do you believe will succeed in the future?



Source: Deloitte Luxembourg & ArtTactic Art & Finance Report 2014

Online art and collectibles auctions are expected to grow in the e-commerce race: 77% of art collectors and 69% of art professionals believe that the online art auction market will become a successful business model, compared with 39% and 47% who think the same about the online gallery model. The emergence of online auction houses such as Auctionata, as well as auction aggregators such as Invaluable, the-Saleroom and Liveauctioneers, is evidence that the online consumer shows a strong preference for online art and collectibles auctions. This could be because of the price/demand transparency that an online auction process provides, in addition to the opportunity to find bargains and undervalued art.

Art professionals and collectors see opportunities for online art education: 67% of collectors and 63% of art professionals see potential for businesses focusing on art education. With the advent of MOOCs⁸⁴, such as Coursera, Udemy, edX, Udacity, as well as online courses offered by art museums such as MoMA in New York and specialist art-education providers such as Sotheby's Institute of Art, a wide range of art-related courses are already available online.

Disintermediation shows untapped potential: collectors and art professionals both indicated increased confidence in the future of C2C (consumer-to-consumer) sales platforms for the online art industry (37% in 2014, compared with 30% in 2012). It is notable that this area has received relatively little attention from entrepreneurs or traditional market players. This is possibly due to the fact that the C2C model risks undermining the dealer/gallery-collector relationship on which the art market is largely based, and also requires a significant amount of trust between buyers and sellers. ArtViatic (founded in 2012) is currently the market leader in C2C high-end art sales (works valued above €150,000), with sales of €12 million registered in 2013.

There should also be scope for further peer-to-peer markets to appear at the mid- to lower-end⁸⁵ of the art market. eBay is the dominant C2C player in art and collectibles valued below US\$100, but with the advent of new partnerships with Sotheby's and Invaluable, it is showing an ambition to capture a larger part of the higher value art and collectibles market.

Art professionals are showing particular interest in the future of online dealer-to-dealer (B2B) platforms for exchanging inventory. Much like the C2C arena, there is relatively little market competition for B2B platforms, yet a discernible industry interest in the future success of such platforms (49% of respondents believed these businesses would be successful going forward, up from 46% in 2012). Weng Fine Art (founded in 1994), a B2B art seller, recently announced its plan to establish WFA Online AG, a new subsidiary which is to be 100% dedicated to selling contemporary art online. Another B2B model to come to the market is provided by ArtBanc, which works with professional advisors to private collectors and estates enabling them to sell artworks through its electronic sales system—the ArtBanc Trading Platform. Again, this is likely to be the result of entrenched market practices for dealer-to-dealer trading, which has traditionally been done through established personal relationships. As auction houses are moving from wholesale outlets to retail platforms, dealers are finding it increasingly difficult to source stock at attractive prices. The B2B model can offer an efficient solution to product scarcity and sourcing inefficiencies.

⁸⁴ A 'massive open online course' or MOOC is a model for delivering learning content online to any interested party, with no limit on attendance

⁸⁵ eBay is the dominant player in art and collectibles valued below \$100

Examples of online art industry business models:

1. Online art marketplaces

Among the most common online business models are online marketplaces such as Artfinder, Artsy, Artspace, SaatchiArt and 1stdibs.com. The online marketplace model acts as an intermediary between the traditional art world (artists, galleries and dealers) and the growing population of online consumers of art. Recent research published by Hiscox⁸⁶ said that 40% of existing art buyers had bought art online through a click-and-buy platform and that the online art market could grow to US\$3.76 billion by 2018, which clearly highlights the potential of the online art market.

2. Online auctions

Another area that is receiving significant investment attention is online auction platforms. Auctionata, which streams live auctions from its custom built studio, has received US\$50 million in funding in only two years since its inception, and has impressed investors with its rapid sales growth. Artnet and Artprice have also launched their own online auction platforms, and are shifting their business models from focusing on content and advertising to e-commerce. Among the traditional players, Christie's has launched its own online-only auction sales platform, which generated US\$20.8 million in 2013, while Sotheby's announced a tie-up with eBay in July 2014. Among the long-established online auction houses are Saffronart (India) and Heffel.com (Canada), which have been in operation since 1999/2000.

Other fast-growing online auction models include the auction aggregators (or auction marketplaces) such as the UK-based the-saleroom.com, which hosted 3,147 live online auctions and sales worth over £74 million in 2013. In the United States, Invaluable.com (which announced strategic partnership with eBay in May 2014), announced record-breaking fourth-quarter 2013 results with a 102% increase in gross merchandise sales over the same period of 2012. The third key player, LiveAuctioneers.com, recorded its best year ever in 2013, with gross online sales of US\$222.5 million.



3. Collection management tools

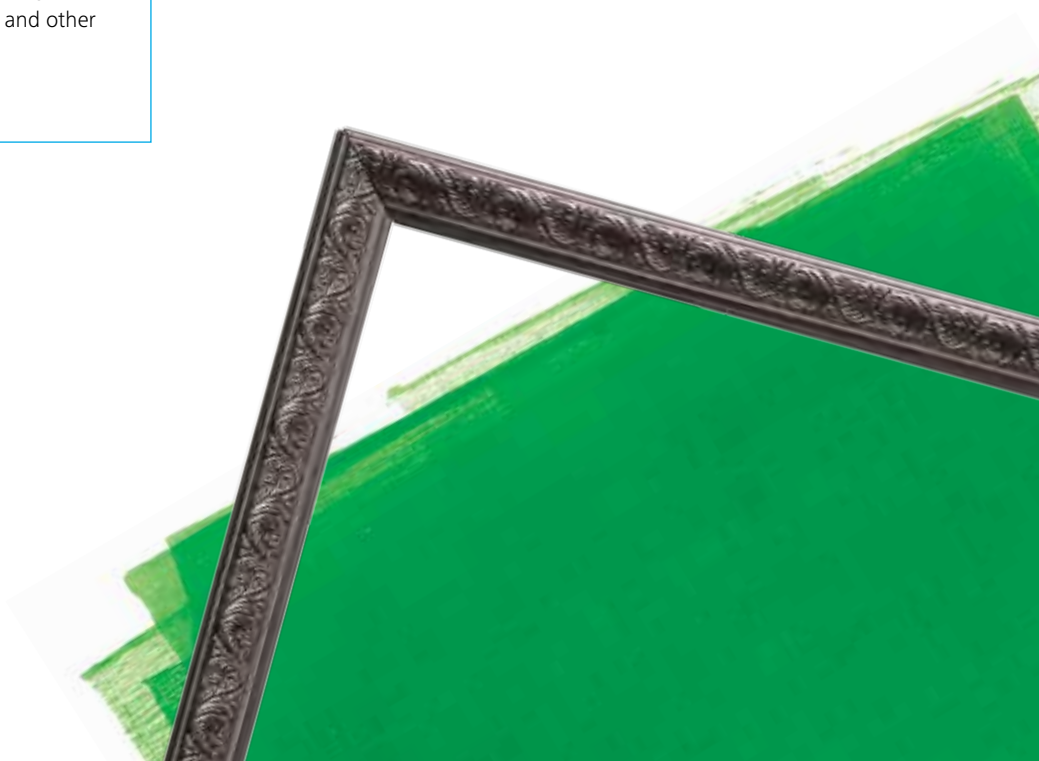
ArtBinder, an inventory and collection management tool for galleries and dealers, has raised US\$3.17 million in Series A funding led by Index Ventures and joined by a number of individual investors including former Etsy Chief Operating Officer Adam Freed, and art collector and investor Maria Baibakova. Another cloud-based collection management company, Collectrium, also raised a new round of investments in 2014 to grow its business. This signals that art service or support-related business models are also starting to gain traction as the online art market continues to grow.

Other players in this space include Tröv, operated and managed exclusively by Pall Mall Art Advisors, which creates applications that help people collect and benefit from information about everything they own. Tröv is privately funded and headquartered in the San Francisco Bay Area, with offices throughout the United States.

The UK-based ArtBanc provides a collections management system and related services to collectors, family offices and other institutional users. The ArtBanc system is capable of tracking fractional ownership interests and ownership by multiple forms of legal entities such as trusts, estates, partnerships and other ownership forms.

4. Online platforms for art secured lending

Borro, an online platform that lets people borrow cash and put up luxury watches, art and other fine goods as collateral, announced a new funding round of US\$112 million in March 2014, coming entirely from one backer that focuses on finance investments, Victory Park Capital. Prior to the most recent round of investment, Borro, which has been around since 2007, had raised just over US\$40 million from investors that include Canaan Partners, Eden Ventures, European Founders Fund, Augmentum and Ribbit Capital. With the growth in peer-to-peer lending, we are also likely to see growth in the peer-to-peer market for asset-based loans related to art and collectibles.





Dr. Christian G. Nagel,
Partner and Co-Founder,
Earlybird Venture Capital

Dr. Christian Nagel is a co-founder and partner of Earlybird. Christian has more than 20 years of entrepreneurial and investment experience. He was Chairman of the Board of Tipp24 AG (Prime Standard Frankfurt Exchange: TIM) and Interhyp AG (Prime Standard Frankfurt Exchange: IYP), which returned more than 50x the original Earlybird investment. Until the trade sale to SMSC (NASDAQ: SMSC) he also served on the board of BridgeCo AG. He is currently on the boards of Auctionata (Berlin), LiquidM (San Francisco/Berlin), Number26 (Berlin), Smava (Berlin), Ubitricity (Berlin) and Versus (Berlin). Prior to founding Earlybird in 1997, Christian, together with a group of investors, acquired various companies from the Treuhandanstalt (the former East German state holding company) and gained operational experience. He was a shareholder and Executive Director of HNP Präzisionsteile GmbH & Co. KG, SMB Industrieholding GmbH, DH Industrieholding Hohenthurm GmbH and a number of other subsidiaries of these holding companies.

Earlybird Venture Capital & the art market

Q: When Earlybird makes an investment what typical industry/market/ business model characteristics are you looking for?

Typically we invest in the first institutional round (A), something between €1 million and €3 million. We also do some seed and recently more B and C rounds up to €15 million in total. We look for innovative/ breakthrough business models with the potential to become global category leader in a market.

Q: Why have you invested in Auctionata? Why are you confident in its business model?

For exactly this reason: they are disrupting the art market and have the potential to become THE global marketplace for fine arts and antiques. There is quite some technology involved to make the live auction a great user experience on all kinds of mobile devices and available bandwidths. This, combined with deep auction expertise (Dorotheum) and a crowd-sourced expert network, makes it unique and hard to crack.

Q: Why did you decide to look at the art market? What are the disruptive forces in this industry?

The art market hasn't changed for decades. Small local auction houses give a bad user experience, no transparency, low liquidity etc. Sotheby's and Christie's are not available for most people and even their customers are used to the internet and smartphones and would like more transparency, competition and liquidity.

Q: Are there any precedents (in other industries) that tell you that the art market might be heading the same direction?

A couple of years ago no one would have realistically thought about buying shoes or glasses online—now this is standard. The same goes for the banking industry, where every line of business is now being challenged by new concepts.

Q: Where do you see the biggest opportunities in the art market?

The biggest opportunities are in transparency in reach, which can only be reached by an internet-based platform. The art market is huge, growing and geographically diverse, with two incumbents dominating the top segment and fast pick-up in China/South America as buyer and sourcing markets. This opens up opportunities for disruptive business models.

Q: What do you see as the biggest challenges?

The biggest challenges are building trust and relationships. In the art market especially that's a big challenge, as you have to trust the experts with regard to expertise and price. Today, this is mainly done through brands, Sotheby's/Christie's etc. The challenge is to detach from brands and trust individuals or systematic approaches like a crowd-based expert network—the wisdom of the crowd—which is stronger than individuals but nowadays not common in the art market.

Q: What do you think are the implications of big online players such as Amazon entering the online art market?

They may enter the market but will face the same challenges. The trend is more towards a dedicated vertical platform with a focus on one market segment rather than a supermarket where you are offered everything. Fine arts at eBay has never taken off, although in theory they had the necessary global liquidity. The art market is so individual it can only successfully be disrupted by specialists.

Q: What are your recommendations to online art business start-ups?

Monetisation without being involved in the transactional side of the business is tough. Pure content-based models are challenging as no one is willing to pay for it. Globalisation is key—local markets are so diverse that only global approaches can create sizeable opportunities.

The art market is so individual it can only successfully be disrupted by specialists



Christian Leybold,
General Partner,
e.ventures

Christian joined the firm in the San Francisco office in March 2003. He has since moved back to Europe where is working out of the Hamburg and Berlin offices, heading up European Internet Consumer investments. He holds a Master of Science in Electrical and Computer Engineering from the University of Illinois at Urbana-Champaign, and previously worked with management consulting firms in Paris and Berlin. Christian also held various research positions at the Daimler Chrysler Research Centre India in Bangalore and the Coordinated Science Laboratory at the University of Illinois. Christian is frequently quoted in the media as an expert on venture capital by key publications such as Spiegel Online and FAZ.

e.ventures & the art market

Q: Briefly, what type of business models/industries/sectors do you or your fund(s) normally focus on?

For the last 15 years, we have been investing in consumer internet and software companies. Currently, new marketplace models enabled by technology are disrupting a number of sectors.

Q: When and why did you decide to look at the art market?

We had been following the art market for a number of years, because we felt that luxury and art would be some of the last markets to really move online. However, it is clear that this is now happening, with all the more momentum, and a tremendous shift is occurring.

Q: Tell us briefly about your portfolio of art-related companies

We are investors in Auctionata, which has rapidly become the leader in bringing live auctions to the internet. We are also shareholders of Saatchi Art, which is providing an expertly curated online environment for artists from around the world to exhibit and sell their work.

Q: Is this a traditional market ready to be disrupted? Which parts of the market, and why?

We generally believe that online players that can offer worldwide reach and introduce transparency to the market will disrupt any traditional offline markets that are controlled by a small number of 'gatekeepers'. We also believe that there is tremendous opportunity and growth potential in making art more accessible and 'democratising' the market through the internet as a borderless platform, which lowers the barriers to purchasing for collectors and enthusiasts anywhere in the world.

Q: From an investor's perspective, where do you see the biggest opportunities in the art market?

We believe that the best opportunities will not be defined by market segment, geography or the like. The internet allows for business model innovations that can completely alter the cost structure, customer reach or value proposition of a business, and we cannot even foresee all those innovations today. In a similar way to how the CD has revolutionised the high-quality listening experience for music, high-resolutions screens, large bandwidths and portable devices form an environment that will allow us to access, enjoy and purchase art in a way not known before. Watching a live auction with a high-definition stream on Auctionata is a good example of how you can feel like you are inside the auction room, while sipping a coffee in your Eames chair.

Q: And what do you see as the biggest challenges?

The art world is based in large part on trust and relationships. Porting those two elements online is something that would have been impossible a few years ago, but the best of the online players today have proved that collectors are willing to spend hundreds of thousands of dollars on a piece of art with the click of a button and without ever having touched it before. Building brands and institutions that carry the weight to instil this kind of trust will be the key challenge for any player in the art world.

The art world is based in large part on trust and relationships. Porting those two elements online is something that would have been impossible a few years ago, but the best of the online players today have proved that collectors are willing to spend hundreds of thousands of dollars on a piece of art with the click of a button and without ever having touched it before



D. Art and corporate finance and strategic partnerships

The online art market has provided another strand to the definition of the Art & Finance industry, namely the increasing investment and corporate finance activity taking place with regards to art and technology and the growing online art market. This section looks at some of the recent activities and also includes interviews with two of the leading early-stage venture capital firms in the market.

Whilst the first generation of online art business models largely focused on bringing auction price data online (databases), information and content (Artprice, Artnet, Mutualart and Artinfo), the second generation of online art businesses are more focused on the e-commerce aspect of the art market. In this section we have looked at some of the most common models, and also some recent venture capital investments in these businesses.

So far there has been relatively modest M&A activity in the online art market, with Blacklot acquired by Paddle8 in 2012 for an undisclosed sum. Paddle8 also acquired an option to buy a 3% stake in Artnet in 2013, after an attempted hostile takeover failed to materialise.

Table 5: Selected venture capital funding for online platforms in 2013/2014⁸⁷

Company name and years established	Business model	Recent round investors		
Artsy (5 yrs)	Gallery subscription information- and experience-driven	<ul style="list-style-type: none"> • Kevin Colleran • Kevin Collins • Slow Ventures 	<ul style="list-style-type: none"> • Larry Gagosian • Peter Thiel • Thrive Capital 	<ul style="list-style-type: none"> • Dasha Zhukova • Wendi Deng • Sky Dayton
Artspace (3 yrs)	Online gallery— Click to buy	<ul style="list-style-type: none"> • Canaan Partners 		
Paddle 8 (4 yrs)	Online auction— also servicing the charity sector	<ul style="list-style-type: none"> • Damien Hirst • Jay Jopling • Founder Collective 	<ul style="list-style-type: none"> • Redline Capital Management • Alexander Von Furstenberg 	<ul style="list-style-type: none"> • Mellon Family • Haystack • Mousse Partners • Winklevoss Capital
Auctionata (2 yrs)	Live online auction streaming and bidding	<ul style="list-style-type: none"> • e.ventures • TA Venture • HV Holtzbrinck Ventures 	<ul style="list-style-type: none"> • Earlybird Venture Capital • Bright Capital • Kite Ventures 	
Lofty (1 yr)	Online gallery— Click to buy	<ul style="list-style-type: none"> • Founders Fund • Fabrice Grinda 		
500px (5 yrs)	Online gallery (photography)—sharing- and discovery-driven e-commerce	<ul style="list-style-type: none"> • CAA Ventures • Dustin Plett 	<ul style="list-style-type: none"> • Rugged Ventures • ff Venture Capital 	<ul style="list-style-type: none"> • Harrison Metal • Andreessen Horowitz
Expertissim (6 yrs)	Online gallery— Click to buy	<ul style="list-style-type: none"> • CM-CIC Capital Privé, Ne 		
Artsper (1 yr)	Online gallery— Click to buy	<ul style="list-style-type: none"> • Angels, unknown 		

⁸⁷ All data sourced from Crunchbase.com, except Lofty, Expertissim and Artsper figures, taken from following sources respectively: <http://www.lofty.com/press/lofty-receives-3-million-infusion>, <http://www.unquote.com/unquote/news/1586555/france-nextstage-makes-eur-expertissim-investment>,

On the 14 of August, 2014, Phaidon released a press statement confirming Artspace's acceptance of its purchase offer⁸⁸. In the statement released by Phaidon confirming the acquisition of Artspace, the company noted that the purchase would allow Phaidon to expand its unfettered access to 'global art collectors' who are already 'active buyers' of its art and design books, as well as multimedia products⁸⁹. Furthermore, the release notes that Artspace will benefit from Phaidon's 'global distribution and retail presence, sales organisation, and relationships with artists and those in the design community'⁹⁰.

Another recent M&A development in the online art sector is that of the purchase of online art gallery Saatchi Art by Demand Media Inc., a web content, commerce and media company behind sites such as eHow and livestrong.com. On the 11 of August, 2014 the LA Times reported that Saatchi Art accepted a USD\$17 million purchase offer from Demand Media, \$5.7 million of which was in cash⁹¹. Demand media already owns online art, fashion, and home decor website Society6 and is looking to grow its portfolio of 'community driven' websites⁹².

As this year's survey results indicate, there is strong industry professional and collector optimism concerning businesses focusing on online information, data and research and analysis, with 89% believing this will be among the successful business models in the future. As online content businesses are often difficult to monetise, the current acquisition of e-commerce platforms by media companies and publishers, could be seen as a strategy to increasingly bundle information and research with online art transactions. High quality information can be used effectively to increase online buyer confidence and support online sales, and at the same time establish new channels for these media companies to sell information to customers who are more likely to pay for premium content.

For an illustration of some of the recent private equity investments, please refer to the table on the left

Amount raised in 2013/14	Total raised
US\$18.5M Series B	US\$25.9M
US\$8.5M Series B	US\$12.2M
US\$6M Series B, and US\$7M debt financing	US\$17M
US\$47M Series A&B Combined	US\$50M
US\$3M Series A	US\$3M
US\$8.8M Series A	US\$9.3M
€5M Series B	€6M
€305,000 Series A	€305,000

Sferiq, a Russian venture capital firm, has created a new category in the Investor Allstars awards this year – *the Sferiq Award for Digital Innovation in Art* (www.investorallstars.com).

88 <https://research.tdwaterhouse.ca/research/public/Markets/NewsArticle/1314-L2NOQK05Y-1>

89 <https://research.tdwaterhouse.ca/research/public/Markets/NewsArticle/1314-L2NOQK05Y-1>

90 <https://research.tdwaterhouse.ca/research/public/Markets/NewsArticle/1314-L2NOQK05Y-1>

91 <http://www.latimes.com/business/technology/la-fi-tn-demand-saatchi-art-20140811-story.html>

92 <http://www.latimes.com/business/technology/la-fi-tn-demand-saatchi-art-20140811-story.html>

New strategic partnerships

eBay is to enter the higher end of the art and collectibles market by partnering with Sotheby's

A further vote of confidence for online art auctions has come from e-commerce giant eBay, which recently announced that it has agreed to partner again with Sotheby's in order to live stream its auctions, with an initial focus on prints, 20th century design, jewellery, watches and wine. This is a renewal of a partnership that was first formed, and quickly abandoned, in 2002-2003, when neither party felt the approach was working for them; however, significant evolutions in technology and online consumer shopping habits mean the market looks as though it is finally ready to accommodate this model of doing business.

The data is also pointing in the right direction, with Sotheby's reporting that the number of lots sold online through its BIDnow system increased by 36% in 2013. Sotheby's main rival, Christie's, is also showing positive online results, with a 77% revenue increase in 2013.

eBay to partner with Invaluable.com

In May 2014, eBay and Invaluable, the auction marketplace, announced a partnership for the sale of fine art and collectibles. Invaluable is now a market leader in the online sale of fine art and collectibles, and has experienced record growth in recent years, along with recently closing a series D funding round of US\$33.75 million led by Insight Venture Partners. eBay has been selling art and collectibles since its inception, but has always lacked the specialist expertise required to deal efficiently in fine art and high end collectibles. Partnering with Invaluable will allow eBay to offer works that have been vetted by industry experts, and to use Invaluable's specialised online auction system, which currently lists works from over 2,000 international auction houses. In return, Invaluable will gain access to eBay's 145 million active customer base, positioning it to improve on its already impressive 80% growth in buyer transactions in 2013.

Invaluable has also recently partnered with China-based Epailive, an online auction platform for fine art and antiques, with over 100,000 users in China. Both Invaluable and Epailive currently work with international auction houses, but will benefit from reaching a more international clientele, in the same way that Sotheby's and Invaluable are also benefiting from their partnerships with eBay. This rapid growth in new partnerships is reflective of a shift towards client diversification and platform consolidation, which should allow for a more efficient marketplace moving forward.

Section 5: Legal trends

Highlights

- **The art market is falling short of meeting the legal expectations of an asset class**, particularly in terms of regulatory structure, information availability and clear title. Another key issue is the legally vague fiduciary responsibilities of new intermediaries, such as art advisors
- **The AMF (French Financial Markets Authority) regulates art investment fund products to protect investors**. Recent cases have caused the AMF to impose stricter regulation on the marketing and transparency of investment products linked to art and collectibles, with the aim of ensuring that investors understand the risks attached to the investment
- **Auction guarantees raises questions on transparency and market distortion**. Third-party guarantees, which apply most often to the most valuable works sold at auction, can be considered a form of market distortion. There is real concern about the costs passed on to buyers at auction with respect to third-party guarantee arrangements and the significant buyer's premium every buyer must pay on top of the purchase price
- **Rising values generate new risks in an unregulated art market**. Record prices for art have generated record years for art lawyers and litigators, with much of their work arising out of attribution and authenticity issues
- **The absence of clear authentication processes and authentication bodies can make the verification of genuine art extremely hard to establish**. Recent art market cases have included the German 'Jaegers Collection' forgery ring where auction houses, private collectors and scholars alike were duped over a period of two decades
- **Protection for art authenticators against lawsuits**. An important bill was recently introduced in New York State to protect art authenticators against frivolous lawsuits. Art appraisers and authenticators face significant legal risks in offering opinions as to authenticity, or simply questioning assumptions about provenance, authorship and dating
- **Due diligence and carefully drafted warranties in sale and purchase agreements of artworks** can afford some level of protection to the unsuspecting investor in today's art market

- **Art secured lending and allowing the borrower to keep possession of the art work**: in the United States, lenders against art typically allow the borrower to keep possession of the art collateral as they register its security interest under the Uniform Commercial Code (UCC). Several continental European countries have also introduced a register of charges against chattels such as France, Spain and Belgium, but in most other European countries, the lender cannot register a charge against art assets, particularly if the borrower is a private collector
- **Insurance products are being developed** to protect the lender against the risks associated with leaving the art collateral in the borrower's possession. Some of these insurance products are designed to give the lender the same protection as a validly perfected charge against the art collateral

Introduction

Since we launched the first Art & Finance report in 2011, the key challenges mentioned by wealth managers in including art and collectibles in a traditional wealth management context have been linked to the unregulated marketplace, difficulties finding qualified expertise and lack of transparency, factors that have become even more important for wealth managers in recent years. But what exactly are these issues? Through the contributions below, we aim to provide an overview of some of the key legal aspects that lawyers are working on in relation to the Art & Finance industry and how they see these factors affecting the market going forward.

Firstly, **Steven Schindler** gives his view on some of the key recent legal developments, mainly from a US perspective, although most of the issues have a global relevance. This is followed by **Karen Sanig**, who discusses the increasing challenges linked to attribution and authenticity, two very relevant areas for Art & Finance, and the fundamental factor in the value of an artwork. **Pierre Valentin** discusses the recent development of art secured lending and the country-specific issues related to leaving artworks in the possession of the borrower. Finally, **Catherine Cathiard** discusses the recent developments in the French regulation of investments in art and collectible items.



Steven Schindler,
Founding partner, Schindler
Cohen & Hochman LLP

Steven Schindler is a founding partner of Schindler Cohen & Hochman LLP, a premier litigation and art law boutique located in New York City. Mr. Schindler represents clients in state and federal courts and arbitrations throughout the United States, and works closely with foreign law firms in complex transnational litigation. Mr. Schindler also advises art galleries, collectors and artists on the sale and acquisition of art, relationships with auction houses, and has litigated cases involving the authenticity, title, provenance and appraisals of art. Mr. Schindler is on the faculty of the Sotheby's Institute of Art where he lectures on art law, and he serves on the Art Law Committee of The Bar Association of the City of New York, as well as on the board of Artists Space, an organisation dedicated to the support of emerging artists. Mr. Schindler, who also heads SC&H's Art Law Group, was recently featured and quoted in an article on the practice of art law in the *Fordham Lawyer Magazine*, spring 2014 edition.

Most significant recent legal developments in the art world

Q: What have been the most significant legal developments in the art world this past year that investors should know about?

There have been developments in a few different areas. An artist resale royalty bill was reintroduced in the US Congress following a report issued by the Copyright Office in support of limited artist resale royalties in the United States. The proposed bill does not follow the report and is, in fact, more limited than the Copyright Office recommendations. There is very little chance it will get through Congress; nevertheless, there is increasing public awareness and discussion around the benefits and burdens of a resale royalty system and who bears the costs.

In New York State, an important bill was introduced to protect art authenticators against frivolous lawsuits brought against them for issuing opinions as to an artwork's authenticity. The plethora of these types of lawsuits targeting art authenticators has had a chilling effect on the ability of experts to do their work and assist courts in fact finding. Even though the existing precedents are favourable to authenticators, mounting a legal defence can be prohibitively costly. This bill seeks to level the playing field by imposing higher pleading burdens on plaintiffs and allowing authenticators who prevail to recover their legal fees.

Several other lawsuits continue to raise an ongoing issue in the art world related to how much diligence buyers must undertake before purchasing a valuable piece of art.

In New York State, an important bill was introduced to protect art authenticators against frivolous lawsuits brought against them for issuing opinions as to an artwork's authenticity

The many Knoedler Gallery cases (about the large number of forged artworks sold through the oldest and most respected gallery in New York), for example, rest largely on the question of whether the purchasers of forged artworks can argue they 'reasonably relied' on the Gallery's representations as to authenticity without conducting extensive diligence.

Another recent case from the federal district court in New York, *ACA Galleries Inc. v. Kinney*, anomalously held that professional buyers may even have a responsibility to hire experts before purchasing a work of art or they will be blocked from fraud and mutual mistake claims.

There has also been some high profile litigation in the antiquities and looted art context—for example, a federal lawsuit seeking forfeiture of a 10th-century sandstone statue, allegedly looted from the Koh Ker temple complex in Cambodia in the 1970s and illegally imported into the United States. This statue had been up for auction at Sotheby's but was removed when the lawsuit was initiated. Eventually Sotheby's agreed to return the statue to Cambodia and the seller received no compensation for the forfeiture.

Q: To what extent does the post-crisis legal and regulatory framework for banks and financial institutions affect the art world?

Although observers have noted that the confluence of investment money from highly regulated securities markets with a relatively unregulated art market may move the art market towards more regulation, to date this has not happened. Increasingly, though, all players in the art market are realising that art is an extremely valuable asset class and they want to protect their fine arts investments as they would other valuable assets.

In the current climate this translates into a greater awareness of the need to ensure by private agreement all legal protections and avenues for recourse possible in the event the work is later found to be fake or otherwise not as originally represented, especially for art secured lenders and art bankers that are exposed to art's unique legal risks like authenticity, title, or control.

Q: In light of some recent public lawsuits, can you help us understand the legal considerations of art appraisals and authentication?

Art appraisers and authenticators face significant legal risks in offering opinions as to authenticity, or simply questioning assumptions about provenance, authorship and dating. For example, we have seen the art world's major authentication boards (the Warhol Foundation for example) call it quits because of the risks and expense involved in taking a public stance on authenticity.

Because there are such great assets at stake (art as a major investment vehicle not just an aesthetic collector item) collectors and owners or potential owners are directly affected by expert analysis of art authenticity. These opinions can rock art markets. We have seen defamation and interference with business dealing-type lawsuits against art appraisers and authenticators. We are also, in our own practice, seeing great hostility to art experts conducting scientific analysis because it seems to present a threat to the connoisseurship model that has dominated art authentication study for so long.

This is why the bill introduced in New York is so important. Those who offer expert opinions need to receive protection if they are to freely give such opinions and without those opinions courts will be relatively handicapped in evaluating authenticity and appraisal issues.

The best advice we can give to those offering any sort of expert opinion about authenticity is to have a solid engagement agreement with the client that indemnifies the expert against any future lawsuits related to his or her work and makes clear that the opinions rendered are just that, opinions.

Art appraisers and authenticators face significant legal risks in offering opinions as to authenticity, or simply questioning assumptions about provenance, authorship and dating

Q: Art funds, lenders and investors often need to transport art. What are the legal risks of buying, selling, transporting or lending art across borders?

Of course, it depends on what country you are in. Most European countries, for example, have export laws that regulate the export of art and cultural property. So if you are in Europe, you need to be keenly aware of those laws. The United States does not have such export laws and does not enforce the export laws of other countries, but is a signatory to the 1970 UNESCO Convention regarding the illicit transfer of cultural property, and under the 1983 US Property Implementation Act recognises some rights of other countries to claim their cultural property, while the US government has been increasingly aggressive in assisting other countries to repatriate antiquities that were improperly obtained.

This past year, Sotheby's was involved in the major lawsuit I mentioned above about the return of an ancient Cambodian statute to Cambodia. Sotheby's was of course just a third party to the dispute between the owner and the U.S. government but decided to litigate the issue to protect its market in these types of works. In all these cases, US courts actually look to the law of the country of origin in determining what must be repatriated, which adds complication to the responsibilities of US courts in these types of lawsuits. These considerations apply equally to lenders who typically look at these issues as part of their due diligence—in the same way they review issues of authenticity and title.

In addition, for dealers in antiquities, selling cultural property from countries with patrimony laws can land you in prison for violating the US National Stolen Property Act—as Fred Schultz found out when he was sentenced to three years for selling Egyptian antiquities. This criminalisation of our cultural property laws has been extremely controversial, particularly among the dealer community, and there has been a vocal movement to get the US Congress to enact legislation overruling judicial decisions affirming convictions of dealers who knowingly trade in stolen cultural property.

Q: To what extent does the neutrality of the auction house suffer as more works come to the auction block with anonymous third-party guarantees?

There have been debates about the transparency of auction house practices for some time and I do not think anyone is, at this point, under the impression that there is total transparency. For example, chandelier bidding (where the auctioneer acknowledges bids that do not exist to drive up the price) is still legal and common up to a pre-agreed upon reserve price. In addition, auction houses now typically provide financing to consignors. These loans, secured by the consigned works, give the auction house an additional stake in the work's sale at high prices. In New York City, at least, these practices are regulated and must be disclosed, along with the existence of reserve prices, in auction catalogues.

The concern with third-party guarantees, which apply most often to the most valuable works sold at auction, is that when a third party has assurance it can buy a work of art at a reserve price and no one else in the room knows that, the third-party guarantor can bid indiscriminately to drive the price up so high that no one else will be able to buy the work save the guarantor, who often receives a discount on the hammer price as an incentive to enter into the guarantee relationship with the auction house. The guarantor may also receive a financing fee from the auction house whether or not he or she is the winning bidder. This is a form of market distortion and there is real concern about the costs passed on to buyers at auction with respect to third-party guarantee arrangements and the significant buyer's premium every buyer must pay on top of the purchase price.

The auction houses, however, take the position that guarantors simply get a discount for being willing to put up a financing commitment before the value of a work is tested at auction. Without guarantors, some sellers might hold back important and valuable works for fear they would not sell and the risk the reputation of the piece will be harmed. It is important to note that auction houses in New York City must disclose when a work is being sold with a guarantee and also when the guarantor is bidding at auction.

Q: Are there legal barriers to art expanding as an alternative asset class?

The most immediate barrier is simply that the art market still falls short in meeting the legal expectations of the investing class in terms of regulatory structure, information availability and clear title. Another key issue, which I expect will become more apparent once we see a market correction, is the legally vague fiduciary responsibilities of new intermediaries like art advisors. As more investments go wrong, I expect we'll see cases brought forth to clarify the fiduciary responsibilities of art market intermediaries who don't necessarily represent purely the buyer or seller.

Although observers have noted that the confluence of investment money from highly regulated securities markets with a relatively unregulated art market may move the art market towards more regulation, to date this has not happened



Karen Sanig,
Head of Art Law,
Mishcon de Reya, Solicitors

Karen founded Mishcon de Reya's Art Law group in 1995 in response to a growing demand from clients for a specialist approach to providing advice in this niche sector. Clients Karen represents across the globe include artists and their estates, collectors, dealers, art charities, auctions houses, galleries, museums and governments. She advises on a wide range of art-related matters, such as the sale and purchase of art, disputes over attribution, authenticity and ownership, the export of cultural heritage property, the return of looted cultural property and taking security over art.

Attribution and authenticity The quagmire

A strange thing is happening to the art market: prices are continuing to rise at spectacularly elevated levels. There is much conjecture as to the reason for this booming market at a time when instability, high taxes, low interest rates and crackdowns on banking secrecy reign in the financial markets.

The US\$744 million worth of art sold at Christie's May 2014 post-war and contemporary sale set a new record for a single sale. Works by well-known names abounded, such as Warhol, Basquiat and Rothko. Joan Mitchell's 1960 painting '*Untitled*' set a new world record for a female artist at US\$11.9 million. This was previously held by impressionist Berthe Morisot, whose '*Après le Déjeuner*' sold for US\$10.9 million in London 2013.

There has never been one clear means of denoting attribution in relation to art. Auction catalogues and other sales literature have traditionally used a kind of code which can be deciphered by those experienced in the buying, selling or appraising of art

With extreme prices come great risks in this largely unregulated market. Recent years have also seen a bumper crop of litigation, much of which has arisen out of the vexed issues of attribution and authenticity of artworks. Sometimes the identity of an artist and his style have helped to mask whether a forged work is fake. In other cases, there is a genuine change in art historical views given new material which comes to light. Established practices, like having a 'good eye' coupled with new scientific advances, have added to the complexity of determining accurately who has in fact created a work of art.

There has never been one clear means of denoting attribution in relation to art. Auction catalogues and other sales literature have traditionally used a kind of code which can be deciphered by those experienced in the buying, selling or appraising of art. A work which is accepted as an autograph work of an old master, for example can be described variously, as 'by Rembrandt', 'Rembrandt' or 'by the hand of Rembrandt'. The latter may also mean that it was only partially painted by Rembrandt, but if enough of it was painted by the artist for it to be accepted as an autograph work then it is deemed to be by the artist himself. Confusingly, a work not accepted to be by the artist himself can be referred to as 'after Rembrandt' or 'in the school of Rembrandt'.

There are other permutations—too numerous to mention—but which are equally obscure. Such descriptions do not necessarily cause alarm bells to go off for the inexperienced investor in art until it is too late. Auction house terms and conditions do often specify that a bidder should make their own enquiries prior to purchase. Purchasers often fail to read them.

'*Caveat emptor*' (buyer beware), is a maxim which still resonates loudly in the art market. The recent case of *Avrora Fine Arts Investments v Christie Manson and Woods Ltd* (2012) EWCH 2198 (CH) concerned the sale of a painting attributed to the Russian artist, Kustodiev. Following the sale, the purchaser was led to believe that it was not an authentic work by Kustodiev. The buyer sued the auction house several years after he made the purchase. The court decided on the strength of expert evidence that the buyer was correct and ordered the sales contract to be set aside. The evidence before the court included scientific testing of the paint of the alleged Kustodiev to verify its date.

Recent years have also seen a bumper crop of litigation, much of which has arisen out of the vexed issues of attribution and authenticity of artworks

The judge appeared to prefer the evidence of the specialist Russian experts who used their art historical knowledge to compare this work with other examples they had seen. Their conclusion was that it was not a genuine work by Kustodiev. The judge agreed. The sales contract was set aside. Christies was not held to be liable because its robust terms and conditions excluded any liability for negligence and misrepresentation. The court deemed this exclusion to be reasonable. It declined to order Christie's to pay damages for alleged negligence in attributing the painting to Kustodiev or for allegedly misrepresenting that it had reasonable grounds for its opinion regarding authorship of the work.

Living artists sometimes seek to distance themselves from a body of work. One example is the artist known as Banksy

Sellers must be on their guard too. In 1994, 'Salome with the Head of St John the Baptist' was attributed to the school of Titian and sold for £8,000 by Christie's, London. It was later revealed to be a lost masterpiece by Titian, once owned by Charles I. In 2009, it was offered for sale at Sotheby's New York with an estimate of US\$2,600,000-US\$4,000,000.

The true identity of the creators of contemporary art ought to be easier to determine than those of Old Masters. Either the artists are still alive, and as such ought to be able to verify their works personally, or else works were created within living memory of experts. Unfortunately, matters are not always straightforward. Living artists sometimes seek to distance themselves from a body of work. One example is the artist known as Banksy. In recent years, the Banksy authentication body, 'Pest Control', has refused to authenticate certain works of street art. In some cases these are works which Banksy's contemporaries claim to have seen him create.

This highlights an additional layer of mire in the form of authentication bodies and their practices. The Warhol foundation in the United States has recently had to disband because of the number of lawsuits it faced following authentication of artworks or failing to authenticate them. The methods deployed by authentication committees vary from artist to artist, from artist's estate to estate and from jurisdiction to jurisdiction. A Chagall painting, for example, that is newly discovered as original by UK experts, can be rejected by the Chagall committee in France. Presentation of such a work to the committee may lead to it being destroyed pursuant to French law—as happened recently.

Often heirs of an artist will set up their own authentication bodies. However, they may not always have the legal rights to determine whether and how artworks can be reproduced. In France, for example, these rights—known as '*droits moraux*'—do not pass automatically on death with inheritance rights, which do pass automatically to certain family members. This can create a kind of two-tier authentication process. Reproduced artworks, for example, authenticated by one set of experts as genuine may not be legitimised by the owners of the legal rights. Certain reproductions of Giacometti sculptures have been the subject of legal controversy in France for this reason.

While fakes and forgeries abound, the absence of clear authentication processes can make the acquisition of genuine art extremely difficult. Recent art market horrors have included the German 'Jaegers collection' forgery ring, where auction houses, private collectors and scholars alike were duped over a period of two decades.



The producers of fake modernist paintings managed to successfully sell works imitating such artists as Max Ernst, Kees Van Dongen and Fernand Leger. Their fraud was a skilful combination of forged paintings and provenance. They have received jail sentences in Germany, but no doubt many of their works remain undetected across the world. The United States has seen the closing of the well-known New York Knoedler gallery over the exposure of the allegedly fake Rothko, which sold for US\$8.3 million, and a law suit which followed, involving the US\$17million dollar sale of an allegedly fake Jackson Pollack to the financier Pierre Lagrange.

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Vigilant scrutiny of artworks by experienced experts, coupled with carefully drafted warranties in sale and purchase agreements, can afford some level of protection to the unsuspecting investor in today's art market. Irrespective of this, mud does not always stick. The same work may pass through various sales, public and private before any problem surfaces—even though there have been several hints at a problem along the way. The issues of attribution and authenticity might have slowed down the surge in sales given the sums of money concerned, but this does not currently appear to be the case. Perhaps therefore, after all, Pablo Picasso was right when he stated: *'art is a lie that makes us realise truth'*.



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Pierre Valentin is a solicitor. He specialises in art law. For the last 20 years, he has advised art collectors, art market professionals, artists and their estates and museums and galleries on all legal issues arising when buying and selling art and managing art collections. He is a partner of Constantine Cannon LLP, a London and New York boutique law firm. His work includes fraud and dispute resolution, restitution and repatriation, private treaty sales, consignments to auction, tax solutions involving art, import and export, raising capital against art and art investment funds. Prior to joining Constantine Cannon, Pierre was a Senior Director and Associate General Counsel at Sotheby's. He is a trustee of the World Monuments Fund in Britain and of the Artists' Collecting Society. He teaches art law at a postgraduate level at the Sotheby's Institute, the London School of Economics and Christie's Education. Pierre is fluent in French, Italian and Spanish.

Art finance Can the borrower keep possession of the art collateral?

One of the first questions an art collector looking to borrow against his collection will ask is whether he will be allowed to keep possession of the art collateral while the loan is outstanding.

In Europe, banks and other specialist providers of loans against art, antiques and collectible items often have no choice but to take possession of the collateral in order to perfect their security interest. This is the case where the law of the country where the collateral is physically located when the charge is granted affords the lender no option but to take possession of the art collateral in order to put third parties on notice that the lender has a charge on the art.

Several continental European countries have introduced a register of charges against chattels

By contrast, in the United States, lenders against art typically allow the borrower to keep possession of the art collateral. The lender registers its security interest under the Uniform Commercial Code (UCC), thereby putting third parties on notice that the collateral is encumbered.

Registration has the effect of perfecting the lender's security interest, by giving it priority over the claims of other creditors (assuming that no other creditor has a prior valid security interest in the collateral). Special rules apply in the event of the borrower's insolvency. Possession may still be required by the lender to mitigate risk, but not to perfect its security interest.

In England, the lender can register a charge over art collateral belonging to an English company. The charge will be registered by the lender at Companies House. The information on the register is publicly available. By registering its charge, the lender is deemed to have put third parties on notice of its charge against the art assets. However, if the borrower is a private individual, the lender cannot register a charge against art assets like in the United States. Registration is only available in the form of a 'bill of sale', a system introduced in the 19th century to protect widows and orphans from devious moneylenders. This system is antiquated and ill-suited to 21st century lending. In the absence of registration, a lender lending to an art collector against art assets in the UK often has no choice but to take a pledge on the art. A pledge is perfected by physical delivery of the art to the lender or the lender's agent.

Several continental European countries have introduced a register of charges against chattels. The register of charges follows the model of a register of mortgages over real estate.

In Europe, banks and other specialist providers of loans against art, antiques and collectible items often have no choice but to take possession of the collateral in order to perfect their security interest

The information on the register is publicly available. Once the charge is registered, other creditors of the borrower are deemed on notice that the asset is subject to a charge, and the first registered charge will normally take precedence over charges registered subsequently (there are exceptions in the event of the borrower's insolvency).

In 2006, France introduced a register of pledges over chattels. The French Civil Code now allows a lender against art to perfect a pledge by public registration if the art is owned by a private individual. By registering its security interest, the lender's charge over the art takes precedence over the rights of the borrower's other creditors (assuming no other creditor has registered a prior pledge, or perfected a pledge by taking physical delivery). There is no requirement to transfer possession of the art to the lender. Registration is deemed to put the borrower's other creditors on notice that the art is subject to the lender's security interest. Note that in the event of the borrower's insolvency, the lender's rights may be subject to priority rights of certain types of creditors.

Following on from the French model, Belgium has modified the rules of the Belgian Civil Code relating to pledges of chattels by introducing the concept of pledge without dispossession. This type of pledge is perfected by registration in a register of pledges (*Registre des gages*). In other words, a pledge duly registered in the register of pledges will give the pledgee priority over the pledgor's other creditors upon registration (assuming no other creditor has registered a prior pledge or perfected a pledge by taking physical delivery). The lender will no longer need possession of the collateral in order to perfect its security interest. As is the case in France, the traditional pledge, perfected by the delivery of the collateral to the lender, remains an option.

Registration has the effect of perfecting the lender's security interest, by giving it priority over the claims of other creditors (assuming that no other creditor has a prior valid security interest in the collateral)

In Spain, the lender against art can take either a regular pledge (perfected by delivery) or a pledge without dispossession. The pledge must be granted in the form of a public deed and, in the case of a pledge without dispossession, it must be registered in the Spanish register of moveable property (*Registro de bienes muebles*) in order to give the lender priority over the borrower's other creditors (subject to any prior valid security interests). Registration attracts stamp duty, the amount of which varies depending on the region where the charge is registered.

In most other European countries, the lender cannot register a charge against art assets, particularly if the borrower is a private collector. In Switzerland, for example, the traditional pledge (perfected by delivery of the collateral to the lender), is the norm.

In Luxembourg, the traditional pledge is one option. There are other options, such a transfer of title in the art collateral to the lender by way of security, and a fiduciary transfer whereby the lender takes title to the art collateral as a fiduciary and is contractually authorised to appropriate the collateral in the event of default. A transfer of ownership of the collateral to the lender is, in theory, also an option in other countries. However, there are issues associated with such a transfer. The passing of ownership may trigger tax liabilities both when ownership passes to the lender and when, upon repayment of the loan, ownership is transferred back to the borrower. Moreover, regulated lenders may not be able, or willing, to hold title of art assets on their balance sheet, even for a limited period of time.

Insurance products are being developed to protect the lender against the risks associated with leaving the art collateral in the borrower's possession. Some of these insurance products are designed to give the lender the same protection as a validly perfected charge against the art collateral. If, unbeknown to the lender, the borrower grants a charge against the art collateral to someone else, or absconds with the art, or refuses to deliver it up in an event of default, the insurers will indemnify the lender for its loss. These insurance policies are not standardised and the language of the policy should be scrutinised carefully by the lender to ensure that it addresses risk in a manner acceptable to the lender.

Possession of the art can be a significant issue for lender and borrower. Note that the test is not the nationality or residence of the borrower, but the physical location of the art collateral when the charge is perfected. Countries allowing charges against art without dispossession have an advantage over countries that don't, although it must be said that conservative lenders may well insist on possession even if the law allows them to perfect their charge over the assets without it.

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The evolution of French regulations on investments in art and collectors' items

Together with wine, horses, agricultural land, jewellery and precious metals, works of art and collectors' items fall into the category of 'other goods' under French law, which are sometimes also classed as 'atypical products'.

Often accompanied by a promise of high returns, these investments seem attractive. However, they expose investors to risks of capital losses, which led to the introduction of legislation in 1983 to regulate the activity of 'intermediaries of other goods' (Art. L. 550-1 to L. 550-8 of the French Monetary and Financial Code), placing such intermediaries under the supervision of the French Financial Markets Authority (*Autorité des Marchés Financiers*; AMF) (Art. L. 621-9 II, 8° of the French Monetary and Financial Code).



Law no. 2014-344 of 17 March 2014 (Art. 110) on consumer protection, also known as the '*Loi Hamon*', sought to reinforce the protection of investors in 'other goods'. In their communication materials of a promotional nature, the intermediaries of other goods are obliged to respect similar publication principles to those which apply to promotional material for financial products: content must be precise, clear and not misleading, so that the risks related to the investment can be easily understood.

The AMF therefore verifies, a posteriori, that the information provided by intermediaries is balanced, describing all of the risks attached to the investment. If this is not the case, the AMF can impose disciplinary sanctions on intermediaries that do not respect the provisions applicable to them, as well as regulate their promotional material by publishing a website alert or by joint action with the French Competition Authority to seek a court injunction.

In the recent Marble Art Invest case, the AMF imposed large fines (up to €1 million) on a number of intermediaries that offered a '*portfolio diversification product through investment in art*' promising a return of 4% per quarter on the resale of artworks, which garnered some €15 million from investors.

On the matter of investments in works of art or collectors' items, when a potential return or a sale on term is invoked, private collectors are required to ensure that the intermediary has obtained all the required authorisations, and that the risks of the investment have been clearly stated.

This reform should help limit the risks of investments in works of art and collectors' items, and reassure investors seeking to diversify their portfolio in order to escape from the uncertainties of the financial markets by investing in art.

The AMF therefore verifies, a posteriori, that the information provided by intermediaries is balanced, describing all of the risks attached to the investment



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