

Investment In The Fine Art Market Versus Traditional Investment

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Abstract

The market for Art has experienced a phenomenal growth since a decade and has catapulted in gathering attention of local and international collectors. The art market has always been a field of excellence, where the nuances of the arts can only be comprehended by the elite class of investors. Although both investment in assets may take place, investment in art and investment in traditional investment may vary. The differences between these two types of investment are explored in this paper.

Key words: Art Market, Traditional investment, Collectors, Investors, Passion

I. Introduction

Art is a luxury good and represents wealth which has an intrinsic value. Art combines both consumption and investment benefits in the long horizon. The demand for art is dynamic and is proportionate to the disposable income of the art investor. The market demand for art and the wealth of art collectors is positively correlated. "Utility derived from art is measured by the value of possession of art and the expected capital appreciation of holding it in long-term". (Benjamin, 2009). Thus, art is considered as more of a lucrative investment and an investment opportunity as compared to other fixed securities (Jianping and Michael, 2002), (Witkowska and Kompa, 2015).

Art economics

A study of art economics was first published by Baumol and Bowen in their 1969 publication, "Performing Arts: The Economic Dilemma". In their book, the authors analysed the state of the art of performance, the costs and revenues, the variables affecting demand and earnings, and the financial support that organizations might need.

Mark Blaug, in his 1976 book *The Economics of the Arts*, examines the shifts in the arts market age. In 1977, at the University of Akron, William Hendon and his colleagues founded *The Journal for Cultural Economics*, which eventually became an internationally recognized biennial conference (Edinburgh).

David Thorsby and Glen Withers published "The Economics of the Performing Arts" in the *Journal of Economic literature* in 1990. In 2006, David Thorsby published Victor A. Ginsburgh's *Handbook of the Economics of the Arts and Culture*, one of the most comprehensive materials, collecting articles on the economics of art. The literature on art economics expanded starting in 2000.

Ruth Towse published the *Cultural Economics Handbook* in 2011 and Iain Robertson and Derrick Chong published *Understanding International Art Markets and Management* in 2005.

Articles published by auction houses such as Christie's are documented, and Dr. Clare McAndrew, founder of *Arts Economics*, who publishes a yearly analysis of the art market in the *Art Basel Report*, performs a detailed analysis of the art market.

Arttactic analyses auction results and regularly publishes reports on the art market. Deloitte publishes the annual *Deloitte Art & Finance report*, which includes an analysis of the state of the art, general trends, art as well as investment, and other issues such as risk and regulations. The literature on

art and cultural economics has grown with the growth of the market over the last two decades.

II. Fine Art Market - Cliches

Artists and collectors or museums are the main players, the initiator, and the end users of the art market. There are also dealers, gallery owners, curators, art critics in the value chain, but, at the end of the day, market transactions are, on the one hand, the artist and, on the other, the collector, the museum or the investor. In the Renaissance, for example, the beneficiary-the patron, usually a church or a rich person, used to commission the artist, the patron paid for the materials (e.g. painting and dust colors) and, in addition, the artist's work was remunerated separately, depending on how famous the artist was. Transactions in the art market are now different from what they used to be a few centuries ago.

The artist has a number of ways to sell his paintings in our time: he can have his own website, his works of art can be sold through online art dealers (Saatchi Online, Artsy), the artist can be represented by a gallery or dealers, or by art fairs and festivals.

Primary Art market

Sales made by distributors and gallery owners represent the main art market, the market where the original works are first sold. Investing in the primary art market is comparable to investing/joint venture funds investing 'unicorns' in start-ups or potential companies. In addition to the due diligence process they conduct before entering a transaction, investors need to have passion and intuition.

Similarly, to anticipate fashion and trends in the future, collectors or investors in the art market must have knowledge of the art market as well as instinct. The main intention of investors is to discover the next famous artists in the early stages, such as Taleb's black swan [4].

Secondary Art Market

The secondary art market encompasses all subsequent sales of this artwork as it undergoes its journey through the auction house. The secondary market has more artist information, and the work begins to have a history, the auction houses are the main players in the sub-market. The auction is a market institution with an explicit set of rules defining the allocation of resources and prices based on market participants [5].

Art Market Size

The prevailing economic conditions have prompted investors to be interested in alternative forms of investment. The art market follows the major trends of the stock market, but it has its main features that in difficult times could make art more appealing to investors. Table 1 below depicts the impact of the financial crisis, with a significant decrease in 2009 [6].

Year	Year Value (\$m)	Volume (m)
2007	\$65,875	49.8
2008	\$62,020	43.7
2009	\$39,511	31
2010	\$57,025	35.1
2011	\$64,550	36.8
2012	\$56,698	35.5
2013	\$63,287	36.5
2014	\$68,237	38.8
2015	\$63,751	38.1
2016	\$56,948	36.1

2017	\$63,683	39
2018	\$67,653	39.8
2019	\$64,123	40.5
Growth 2018–2019	–5%	2%
Growth 2009–2019	62%	34%

Table 1: The Global Art Market: the value and volume of art transactions

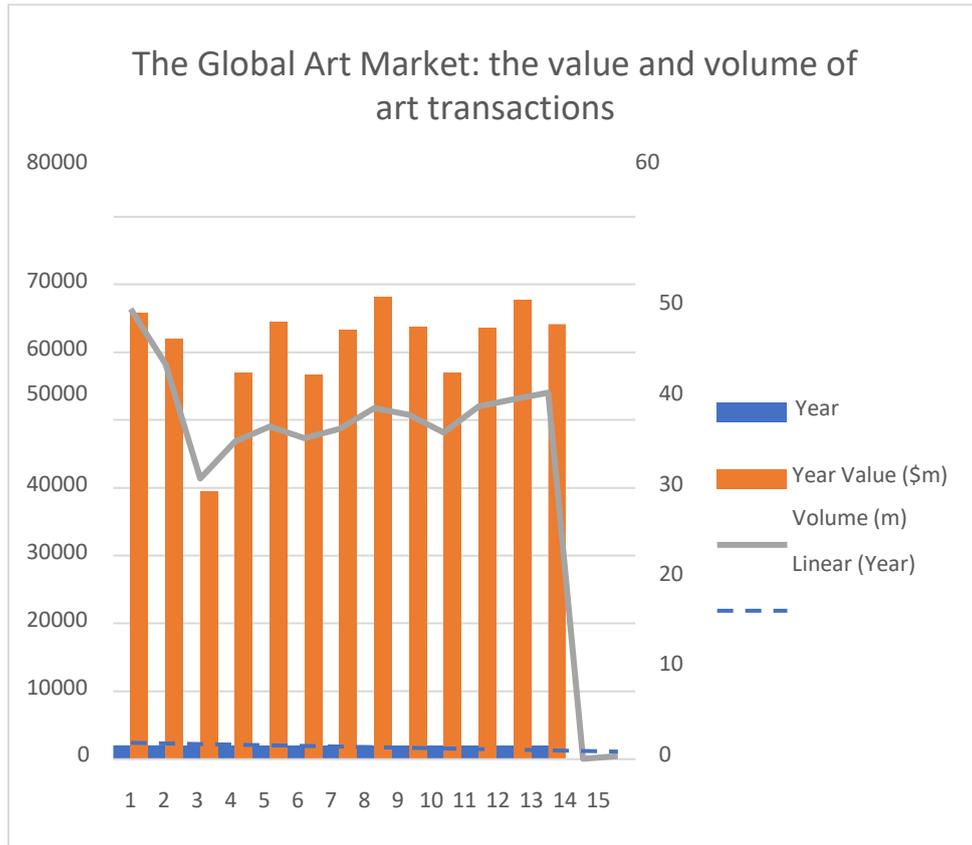


Chart 1: The Global Art Market: the value and volume of art transactions

III. Analysis

The analysis compares investments in the art market and securities investments. The starting point was from the moment of creation, continuing with the purpose, and a comparison of market differences.

Commencement moment

By the time the Romanesque cross was considered for sculpture, the Madonna of Cimabue had been long labelled an image. Such was not primarily a sculpture, even Pallas athena of Pheidias[9]. Art, as did James Rosenquist, is in fact done for no reason other than an artist's self-expression. [10]."

When the shareholders establish an abusive business, they generate a share. The shareholders can decide to go into public, increasing the value. Although the business is clearly distinct, if we consider

the passion of the founders and their efforts to build and develop the company, there might be similarities in creating the artwork. the company's business activities are strong and profitable enough to generate a greater return,

The main difference might be that the entrepreneur creates functional and useful products or services, while artists create works of art for their soul or minds, both artists and entrepreneurs are creative people and innovate and build new items. The use of the artwork is ornamental one or more, and in the respective times the use it was made by society. For artists to sell their work, they need to have a minimum understanding of the market today, "while not all entrepreneurs are artists, all artists are entrepreneurs"[11].

The intent, emotions, and message

A feeling or state is transferred to the viewer by the painting. If the viewer is on one side of the painting, they experience the artist's personal space: how much time and experimentation has gone into the colour. The work of art also has a decorative use for the owner of the piece of art; it is a source of aesthetic pleasure for them. We do not have the same information with respect to stocks traded in other markets.

Usually, investors have purchased the stock in our days and are monitoring the economic return of that stock on the computer or on the smartphone, the investor has no tangible stock value and has information from the press releases and annual reports on the company's activity. The visual aesthetic value of art is the monetary dividend for investors.

Exceptionality

he painting is unique, even though in more than one painting the artist created the same theme, they are not the same, they come to complete each other, and they form the message that the painter wanted to express. If we look at the entire Melancholy series, we can see that the artist conveyed his message better than if we only look at a piece of the work. Another example of the diversity in the types of art is Monet, who experimented with the colour of his water lilies to border on abstraction. Monet attempted to create a "a refuge of peaceful meditation in the centre of a flowering aquarium". The intent of Monet's Water Lilies (1914-26) was to convey the illusion of an endless whole, water without a horizon or bank. However, we need to examine and consider Monet's previous work to comprehend how he has achieved this stage of creative moment. To support my view, Picasso's series of bulls, Picasso created 11 lithographs depicting the animal in different stages of abstraction, eventually reaching the content of the bull through the simplicity of a few lines. If we just look at the outcome, we are unable to grasp the depth of the process and of the painter without considering the whole process through which the painter went to achieve this degree of simplicity. Lithography is used to print illustrations and prints, but drawing is the result of the creative process. Stocks are identical in price, representing equal shares of stock in a company. The stocks are perfectly substitutable, uniquely identical to each other. They are not hard-to-measure; their worth is generated through the company's economic operations. One firm can make various instruments such as bonds, preferred shares, but all instruments are interchangeable in their category and are just a way of investing for investors who want to diversify. The outcome of a week of trading in Sotheby's shares is an example given as evidence of the importance of volatility in the market. The total amount of shares traded at closing, all of which had values lying between the open and closing market rates.

Date Requested	Closing Price	Volume	Split Adjustment Factor	Open Price	Day High	Day Low
16-Sep-19	\$56.87	238,558	1:01	\$56.87	\$56.99	\$56.87
17-Sep-19	\$56.91	261,812	1:01	\$56.92	\$56.95	\$56.87
18-Sep-19	\$56.90	347,792	1:01	\$56.93	\$57.05	\$56.87
19-Sep-19	\$56.94	1,228,163	1:01	\$56.89	\$56.98	\$56.88

20-Sep-19	\$56.94	1,446,766	1:01	\$56.97	\$56.99	\$56.90
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Table 2: Sotheby's weekly historic stock search of September 16, 2019.

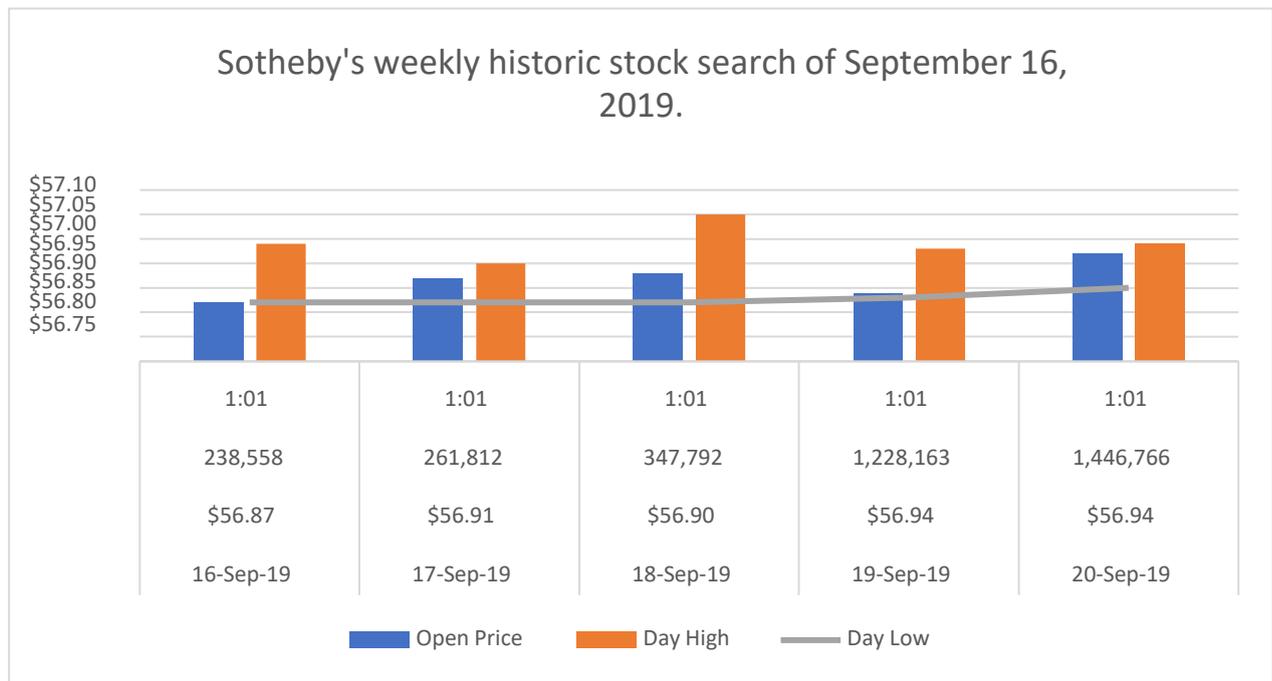


Chart2: Sotheby's weekly historic stock search of September 16, 2019.

Liquidity

The bonds and stocks are both traded on the stock exchange, with many transactions daily, and prices of the bonds and stocks changing daily for reference, see the amount of transactions on Sotheby's stock presented in Table 2. Artwork, on the other hand, are capable of being traded indefinitely, or even for a century. The world's most expensive painting, Salvator Mundi, sold for USD 450.3 million by Christie's in New York to the Abu Dhabi Department of Culture and Tourism, painted by Leonardo around 1450-1519. It was considered lost until it was discovered and restored in 2011-2012. It was then exposed in the National Gallery of London. The art market is not an active market, transactions do not take place as often as the stocks.

Transparency

Art is divided into two types of art: primary and secondary. Both are shipped and sold as artworks. Not all works of art are put on the market, and not all trades are made public. The most well-known auction houses are those that publicly broadcast the results of the auction while inadvertently limiting access to information about transactions in the art market. All trades on the stock exchange are indeed public, the price at which the stock is traded is known, and the price is publicly available. The financial participants on the stock exchange are required to follow the rules of the exchange and cannot raise the price of a security on the exchange by more than a certain amount in one day. One share of Sotheby's stock is worth between 56.87 and 57.05, and as shown in Table 2. The value of the share is known quickly. At the same time, the quality of the artwork is something that requires an expert grade. The market is less transparent, and there is less trust in the market.

Policies or lack of policies.

The securities industry is highly regulated, with complicated laws and regulations for each firm. The art market is thought to be unregulated, and transactions on the market are not reported, making it difficult to know if a market is good or not. The stock market has strict regulations regarding insider trading, and the potential consequences for those who break it. The art market lacks certain laws about insider

trading. Additionally, there are times when, in auctions, the artist is buying their work back in order to maintain the price, a practice that is legal, but the public is unaware that the bidder acquired the work. With the lack of transparency in the market, investors will make incorrect investment decisions. Investors who invest in art do not speculate on the success of a management team. The collector does not have to worry about purchasing something that may be fake but is aware of the genuineness of the piece.

Valuation

It is possible to differentiate between price and value. As Warren Buffet put it, "Price is what you pay, value is what you get." However, they are related to one another. For financial reporting, a company is valued based on a number of different methods. The fair value is determined based on the discounted future cash flows, or the value in use. If fair value less costs to sell is based on a similar market transaction, there will be many potential inaccuracies as to the future activity of the company (e.g., the growth rate, discount rate and the inflation rate, period of the business plan, etc.). Given all that complexity, the process still has value to the company. Publicly traded companies represent the type of company the buyer wants to buy and the type of the seller wants to sell. The Sotheby's values are reflected in Table 2.

How much a piece of work is valued, but not based on the anticipated increase in cash flow. It is difficult to estimate the worth of an artist's work. With a question of a stock we know, at least in principle, what the stock's 'pro rata' price should be—it is the stock's pro rata share of the stock's expected future earnings stream. However, it would be impossible to calculate the true equilibrium price in such cases. Even though the critics' claims may be based on a knowledge of values, they may be unaware of the true value of nothingness.

The future of an artwork is in the tastes and fashion of the future, which defy any predictions of the artwork. One example is Vermeer who disappeared from the public without a trace to be then rediscovered and considered the greatest artists of all time. El Greco is an example of a modern artist rediscovered. A famous painter whose value increased dramatically was Vincent van Gogh. He sold one painting before his death.

The art market is more volatile than the overall economy. The biggest risk in art-secured lending is to correct for value variability. Valuation is key when providing loans, so we rely on the knowledge of the expert to assess the value of a client's art. Even expert art critics can value individual artworks at a range of values. While we cannot control the stock market, we cannot explain the movements of the stock market.

- ✓ Future returns are not predictable. However, investors consider other objective and subjective factors as well as preferences and style when they make investment decisions. The rational factors of the work include its artist, work, and genre.
- ✓ Art market valuers evaluate the artist themselves: who they are, their fame and their role in the art market, the role in the history of the art market and the importance of the artistic group. The different types of artists can be categorized as follows:
 - ✓ These painters broke with tradition in painting revolutionary works. Artists include Francis Bacon, Max Beckmann, Paul Cezanne or Pablo Picasso.
 - ✓ The second type of modern artists are Picasso, Derain, or Duffy.
- ✓ These artists are in the third phase of abstract art movements. Often, they are confined to small audiences. This timeline well reflects typical developments in various fields of science study.
- ✓ The higher the price of the art piece, the more famous the artist. Also the more important the art movement, the higher the price. Through greater fame and prestige, markets are more susceptible to uprisings, driving prices up.

The artwork's characteristics are another category of objective factors that impact the value of art. In

reviewing the factors, the following was noted:

- ✓ The job's size. It is known that the value of art increases with the size of the work.

Prices tend to increase proportionately with the size of a good or service. After a certain point, prices increase with an inverse relationship to the size of the good or service.

- ✓ People who own small- to medium-sized pieces find it easier to display them in their home. This decreases the total number of pieces and allows them to be a smaller proportion of the collection. There are institutions that drive demand for large parts of work, but also have some pricing power.
- ✓ Medium of work of art. The price of oil paintings are more expensive than works of art on paper. Materials costs are higher for canvas and oil and durability is higher for oil, but effects vary between artists. If the artist's works become famous, then they would be the most expensive.
- ✓ The period in which the work was created. The artist's work can be divided into early, transitional, and mature stages. As time goes on, an artist's prices tend to increase, but due to the rarity of a famous artist's works, early works are sometimes prohibitively expensive.
- ✓ Prices may affect subjects. No rules can be laid down in this area. There are a variety of artists, regions, cultures, and artistic movements that devalue certain subjects. Historical portraits are known to be valued over unknown figures. The religious theme is known to have decreased in value.
- ✓ Recognition of type affects the price. It can be said that Theodor Pallady's work or Ciucurencu's work belongs to the masters. They are often more expensive when part of an artist's sacred style.
- ✓ The condition of the canvas will affect the price of the art. A canvas with many holes requires more restoration work, and these costs are deducted from the price of the art. However, this artwork has been restored to its original condition. Some collectors like this and are willing to pay a premium for it.
- ✓ Provenance is a key factor in determining the value of the artwork; signed works will be more expensive, and the history of previous owners is critical to knowing the price. The locations and times show up on our radar.
- ✓ Rarity in the work market may increase the price of the work. Inexpensive work may be more costly due to scarcity of the work.

The artist typically has few creative periods, and the paintings themselves generally rise in value as the artist reaches the latter stages of his or her life. The painting may have different value depending on when it was created. The artist's life-long work is made up of all the paintings he has painted. The artist may have several works in his repertoire, but the value of each is based on the entire catalogue. The artist's rare and valuable works increase in value if the artist was popular.

The company produces goods over time which are sold and used by its customers, the way in which this is done is reflected in the price of stocks (share/bonds). Several investors/traders' own shares in the same company. The paper does not claim the price depends on the public actions and the financial performance of the company. To explain the paintings, the paper went back to the historical facts. Decline in income (e.g., interest or dividend income)

It is a significant difference and one of its kind. Artworks generate only income from the capital growth. Investing in art is typically done with a longer time horizon but does not provide a dividend or interest income. Investing in securities generates a dividend in the case of securities, or a coupon income in the case of bonds. The utility of art is in aesthetic pleasure. Collection of art works will be expensive due to the costs of insurance, security and maintenance.

Regardless of the return, during the crash, investors in shares/bonds are much safer than those of works

of art. The value of an individual stock may be zero, while the value of art in the art world. Despite the financial crash, the value will be recovered in the following period and the art object may be sold for profit. In an economy with bad economic times, collectors have less pressure to sell.

When prices are rising, art as an investment option. The most well-known example is the Railpen (British Rail Pension Fund) which invested in artwork to protect itself against inflation. At that time, the inflation rate was 30% and the stock market was falling, and property was in decline. There were no inflation-proof instruments for the pension funds at that time. The fund was successfully hedged against inflation, and after a period of just over thirty years, the £40 million invested generated a return of 4% above inflation. After the US Government deregulated the Railpen art investment, Railpen chose to sell its investment in art. The Investment Manager also considered the opportunity cost of investing in various instruments, the difficulties involved in valuation, storage costs and insurance costs.

Accounting valuation

The value of a painting and/or artwork should be recorded in the balance sheet. The painting could be recorded in a different position in the balance sheet depending on its position in the market.

Art auctions - art as inventory

Sotheby's stated in its annual reports that it is difficult to assess the proper valuation. If the estimated realizable value of the property pledged as collateral for the loan is less than the corresponding loan balance, we record a loss to reflect our revised estimation of the realizable value. If the estimated realizable value of the property pledged as collateral for the loan is less than the corresponding loan balance, we assess whether it is necessary to record a loss in order to reduce the carrying value of the loan, taking into account the ability of the borrower to repay any shortfall between the value of the collateral and the amount of the loan. In estimating the current fair market value of artworks in inventory, consider the factors listed below: A the supply and demand of the artwork in the market at present, considering the current market conditions of the art, as well as changing trends in terms of what. Because the value of these bonds is hard to estimate in retrospect, our estimates may prove, with the benefit of hindsight, to be different from the value ultimately realized on sale.

Others similar companies

There is no clear definition of how to qualify a capital investment in art. Art is an asset because it has both the potential for future economic benefits and the benefits from past events. Without a standard or an interpretation, companies apply their judgment to develop and apply an accounting policy that results in information that is relevant and reliable. In making the asset/liability/revenue/expense judgment, IAS 8.11 requires management to use the definitions, recognition criteria and measurement concepts for assets, liabilities, revenues, and expenses. If art is acquired for another purpose, it is presented as Other long-term investments, Property, Plant and Equipment or Inventory.

The fact that works of art are not like any other type of asset does not mean that all investment advisers can sell these assets.[22]

Consolidated results

If a company is made up of various subsidiaries which are similarly managed, the financial results can be consolidated to produce consolidated financial statements, and these consolidated financial statements can be used to generate the same financial results that the different markets where the company is listed are presented.

IV. Conclusion

Investment in the art market is not transparent, lacks liquidity and valuation requires time and expertise. It is true that the art market has been growing, and more data is available to the public. Moreover, the art is not regulated by accounting standards, and can therefore be sold at auction without providing for

a regular depreciation. This makes it less difficult for new investors to understand the market. Valuation is hard because there are many factors that influence prices, but Sotheby's mention this in their annual financial statements, and JP Morgan mentions it in their interview with Deloitte Art and Finance. The lack of well-established accounting standards and the poor willingness to grant loans with art as collateral are the factors that limit investors' interest in investing in this market.

There are some clear differences between the art market and other markets. Investment in the art market requires special skills and knowledge and requires a passion for the decorative and aesthetic role of art. The dividend income of the artwork is the privilege of admiring the artwork.

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