Understanding International Art Markets and Management

Edited by Iain Robertson

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Understanding International Art Markets and Management focuses on the visual art market – sculpture, paintings, drawings, prints – and examines the major transitions that have affected this market.

Exploring factors such as new tax initiatives, art being increasingly viewed as an alternative form of investment, the constraints placed on the market by public sector museums and galleries, and the huge amounts of money being spent on art, this text answers fundamental questions such as: Why is the art market dominated by America and Western Europe? Is art a good investment? In addition, it provides an insight into hot topics such as the illicit art trade, supply and demand in the Old Master picture market, and art crime.

This text takes an international perspective and merges theory with practice to enable the reader to understand the challenges and issues that those involved in art markets and management face today.

Analysing the decisions and actions of major art market 'players' – dealers, auctioneers, collectors, artists, investors – this text will be essential reading for all those studying and involved in art markets and management.

Iain Robertson is Senior Lecturer in Arts and Economics at City University School of Arts, London, Head of Art Business Studies at Sotheby's Institute of Art, London, Advisor to the Asia Art Archive, Hong Kong, and an Asia Correspondent for the International Edition of *The Art Newspaper*.

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To my parents, Alec and Sylvia

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Foreword

There have been many changes in art markets in the last two decades. Prices of many works of art have altered dramatically, but these are the stuff of headlines. Beyond the headlines there has been the appearance of a new generation of collectors, continuing sales by the inheritors of past collections, shifts in the commercial balance between sale-rooms and dealers, movements of trade to different countries as international demand or national taxation laws have exerted their influence, and long-running debates within government and museum circles about the role of museums in the management of their collections. It is therefore timely that a serious and authoritative book should appear dealing with these and other important themes.

Iain Robertson and his team of expert writers have compiled a text that will come to be considered a landmark in the field. I suspect that the book will be on the reading lists of all the arts management and business schools. Dealers, auctioneers, artists, museum professionals, private collectors and their agents will also want to study it.

The book aims to offer some refreshing and novel insights into the art market and its mechanisms. If, for example, you are interested in the debate about 'de-accessioning' by museums and whatever your views on the subject, you will want to read the discussion of it here. And is it always desirable that the governments of countries should actively prevent works of art from moving from one country to another, especially from richer countries to poorer ones? What is a reasonable position to take in this debate?

The book discusses at length the latest developments in art markets, such as the use of works of art as investment assets, new ways to tax works of art, and measures to combat the illicit trade in antiquities. The art trade emerges from the studies as a very complex market often driven by irrational decisions. It is a stimulating but risky market for its players, full of pleasing rewards and dangerous financial risks, and a potential minefield for amateurs.

Understanding International Art Markets and Management aims to unravel and de-mystify one of the last surviving unregulated international markets and to present a clear picture of its past and present state. I hope that readers will find it a valuable and stimulating source.

Sir Nicholas Goodison FBA, FSA

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I owe a special debt of thanks to Michael Quine Acting Head of the Department of Cultural Policy and Management, School of Arts, City University, who allowed me the time to research and write this book. My appreciation also goes to Francesca Heslop, the Commissioning Editor at Routledge, who saw the potential in such a book and guided me expertly through the publishing process. Thanks also to Sotheby's Press Office, Cass Business School library and the Bank of England for giving me all the information I needed.

1 Introduction

The economics of taste

Iain Robertson

> No arts; no letters; no Society; and which is worst of all continual fear and danger of violent death; And the life of man, solitary, poor, nasty, brutish, and short.
>
> (Thomas Hobbes, *Leviathan*, 1651, ch. 13, p. 62)

On 5 May 2004 at 7.25 p.m. New York time, in the space of five minutes Picasso's 'Boy with a Pipe' was hammered down to an anonymous bidder for $93 million, a price which rose to $104 million (£58 million) after Sotheby's added its colossal $11 million commission. A number of things can be said about this event. The first is that 'Boy with a Pipe' is now either the most or, in real terms, the third most expensive work of art ever sold at auction. The second is that the prices paid for art and antiques since the late 1980s are the highest ever. If the extravagant Duke of Saxony had been pitched against the Picasso buyer in a bidding battle of similar magnitude for Raphael's 'Sistine Madonna' (a painting the Duke acquired in 1754) he would have needed 163 times more cash. The third is that the capital returns on the Picasso have earned the vendor the equivalent of 64 per cent interest per annum over 54 years. The fourth is the morally suspect circumstances in which the work was sold, with the wife of its original owner, Mendelssohn-Barholdy, allegedly having sold the painting to a dealer against the wishes laid down by her deceased husband in his will. What does all this tell us about the art market, its past, present and future? Indeed, what is the art market? This book aims to give you the answers.

Art, some argue, stands between us and the bleak life vision encapsulated in Hobbes's epigraph to this chapter. Public sector curators, the descendants of Shaftesbury's leisured, landed class of gentlemen philosopher who achieved virtue through taste, are the self-appointed custodians of this 'treasure'. Yet, how disinterested, how unsullied by Hobbes's life are these connoisseurs of beauty? A profession by the early nineteenth century, connoisseurship imagined that it might reveal pictorial beauty through forensic analysis. Giovanni Morelli, the founding father, searched for the artist's signature brush mark in an inconsequential fragment or detail and his method informed

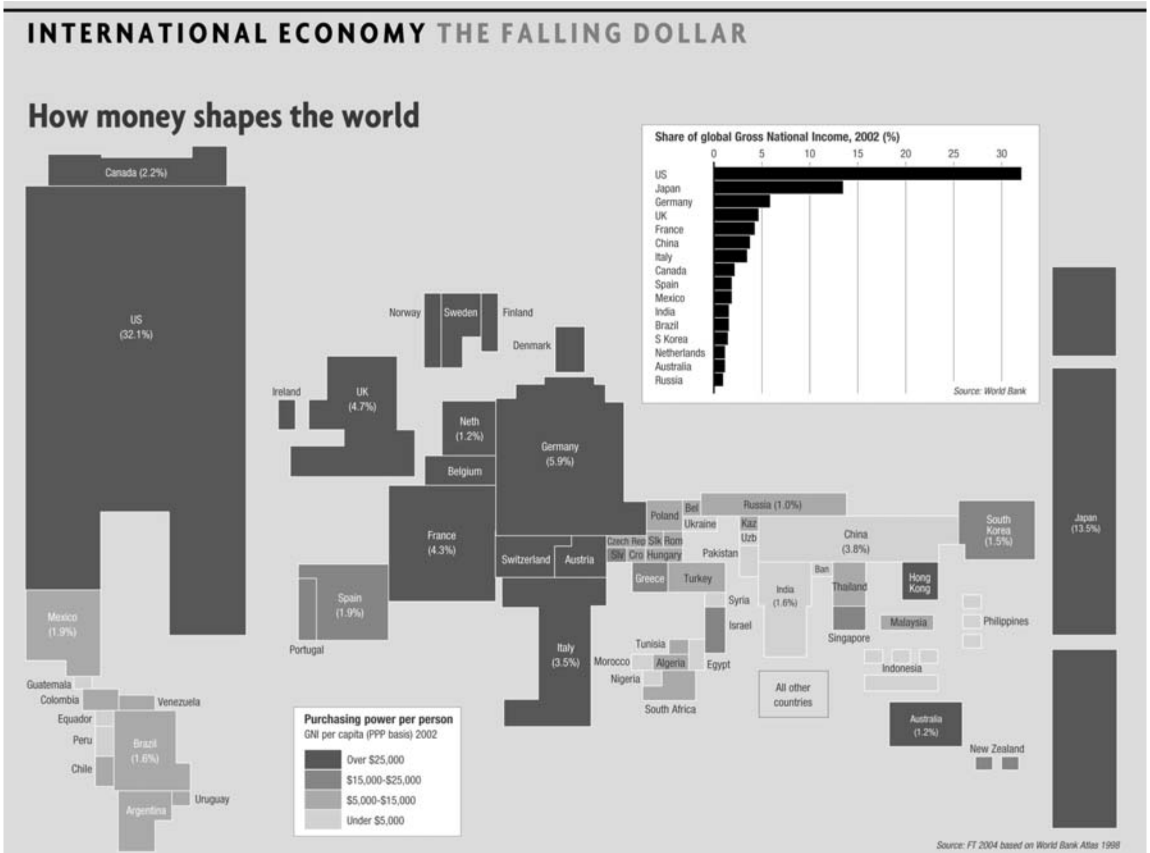

Plate 1.1 Economic world map (*Financial Times*, 2004 based on *World Bank Atlas*, 1998)

the processes by which the likes of Bernard Berenson and Max Friedlaender made their attributions. These pictorial flourishes are not always a cast iron guarantee of authorship, but as Peter Schatborn, who revised Benesch's list of Rembrandt drawings in the early 1990s, says the stylistic traits are the most important elements in determining authenticity. These people are important because the entire art market edifice rests on their pronouncements. The reduction of aesthetic judgement and valuation to a quasi-science is the reason that we have an art market, but how much of its credibility lies in the suspension of our disbelief? How much of the market is predicated on our desire for order and on our understanding that value today means money?

Art and money might still seem like uncomfortable bedmates, but in this book the relationship is sacrosanct. Art, here, is presented as a luxury commodity,[1] an 'experience good' that has to be tested or consumed before its true quality is revealed. It is also treated as an 'information good', since so much of its value is tied to an idea. The acquisition of art, a tangible 'consumption good' with 'social capital', is also seen as a positive addiction; the more that it is consumed, the more that it is desired. On the other hand, this book avoids any attempt to correlate monetary value with artistic quality or to express normative views on the quality of art. The great difficulty, however, is that so much of the value of art is tied to the 'judgements' of the commercial art establishment, that enjoy a monopoly of taste. The monopolists have access to privileged information that is not made universally available and so the market is drastically distorted in favour of the few. It is the élite nature of this market mechanism that maintains art's high unit value and encourages the perception that it is the ultimate consumer good.

This book examines art from a number of positions. The dominant one is economic and informed by Hobbes's vision of a bourgeois capitalist society in which perpetual motion, prompted by fear (the fear of death) leads to endless struggles for power. In this world, man is motivated by 'appetites' and 'aversions' and stimulated to act by the action of 'externall objects'. A crucial aspect of Hobbes's grand design is that 'appetites' continually change and are different in different men, and are incessant and of different strengths in different men. A man's power is relative to others and, 'The value, or WORTH of a man, is as of all things, his Price; that is to say, so much as would be given for the use of his Power' (*Leviathan*, Ch. 10, p. 42). Some men, Hobbes asserts, have unlimited desires, but all men seek to increase their power at the expense of others. The only society that can contain Hobbes's hungry creatures peacefully, is the Capitalist.

The international art market operates, with finesses, almost entirely on this model of bourgeois society laid out by Hobbes in *Leviathan*.

In affirmation of Hobbes, Bruno Frey declares that the economic approach to the study of art starts with the preferences or values of individuals whose views are shaped to a great extent by institutions (Frey, Peacock and Rizzo in Towse, 2003). This approach stops just short of saying what is and is not art: ‘As economists we have nothing to say on this subject; let the experts define the arts as they please, and then try to measure them economically’ (Brosio, Peacock and Rizzo in Towse, 2003, p. 17). Art is thus defined by individual actors, determined by exogenous developments and subject to changes in value, correlated to changes in taste, over time (Brosio, Peacock and Rizzo in Towse, 2003). Taste is impossible to ‘capture’ economically, which makes the task of achieving price transparency all the harder. We argue, using Hobbes’s resolutive-compositive method, that because art is determined by institutions with a monopoly of taste, art is only art when it has passed through certain mechanisms. Since money is the accepted medium of exchange for the transference of power, of which taste is one manifestation, art is only art when it has been exchanged for money. Transactions will, by definition, take place within the system. Art has by extension, therefore, latent art potential when it rests in a conduit before a sale, and is not art if it fails to appear in an art market conduit.

There is a growing body of literature dealing with the market for art. Most of it is focused on the role played by the public sector in capturing taste, arguing for or against the necessity of public arts subsidy. Frey, for example, argues sensibly for the need for the public sector to capture certain economic effects, such as public good. The Neo-Classical economist, Grampp, suggests that art should be treated like any other commodity. The Jonas Chuzzlewit school of economics – ‘Do other men, for they would do you’ (Dickens, *Martin Chuzzlewit*, Ch. 11) – is close to the reality of art market behaviour, but it has many detractors. Some writers believe that the instrumental-rational approach adopted by Neo-Classical economists in assessing the value of art to be fundamentally wrong. Those writers (Becker for example) might propose a sociological-economical network approach. Then there are the art historians, like Reitlinger, Wood and Cumming, who employ art-historical critiques alongside price histories.

The art that this book deals with is confined to the world of paintings, drawings sculptures (and their derivatives in the form of multiples), antiques and antiquities. All this art is purveyed through specialist retailers. The sales outlets are commercial galleries and the art fairs they attend, antique shops, auction houses, ‘dirt’ markets and commodities sold in so-called art warehouses by independent specialist traders, in some department stores and the artist’s studio. Two complications should be immediately evident. The first is the extreme difficulty of tracking even a small percentage of the transactions conducted daily on the international art market and the second is the implied ability of the retailers to determine what is art rather than leave it to the artist, traditional connoisseur or museum curator.

Economic determinism, which is based on the premise that economic growth promotes democratization, ensures re-election and is the key to international power, is, according to Niall Ferguson (2001), close to being conventional wisdom – particularly in the United States. Ferguson goes on to argue, persuasively, that the value of money is sustained by political power and that power in turn is determined by societal demands which are often irrational. Culture is one of those irrational demands. We do not actually need it to survive, but it is certainly a strong want. The absorption, and later export, of their culture by powerful democratic governments helps define our world. Art and antiques are a sub-set of this broadest sense culture, and being commodities are particularly affected by money. The direct association between art and antiques and money elevates our commodity to the highest reaches of the capitalist tree. In short, art and antiques are the most easily translatable of the cultural commodities into the universally understood medium of exchange – money – and are consequently, on one level, the easiest to understand.

The art market is remarkable but not unique in having a substantial degree of ongoing support from the state in the form of grants to public museums and galleries. It is positively and negatively affected by pubic sector interventionism. Other commercial industries in Europe, if not in America, are also periodically subsidized: agriculture, car manufacture, the mining and steel industries to name four, but the arts are criticized because they are unproductive and appeal to a minority of the population. The counter arguments are that the marketplace is unable to capture all of art's value, and the pleasures and rewards of art should be accessible to all. The art that is supported by the public sector is of a particular type, and many practitioners and intermediaries argue that the vast range of production over the last hundred years or so is ignored in favour of a thin commercial cutting-edge. This has happened because public sector accession policies are opaque and undemocratic and fed by favoured networks. The fact that today's political élite is not necessarily its cultural élite might appear to challenge this assumption, but the arts establishment (an agenda-driven interest group) on both sides of the Atlantic is adept at presenting arguments to satisfy the paymaster. These arguments cover a range of effects that fall within the public interest. They permit a former director of the Arts Council, Luke Rittner, to say after the sale of Picasso's 'Boy with a Pipe' that 'It would be a tragedy if this wonderful picture were to be kept from public view' (Wapshott, 2004).

One is tempted to say the public couldn't care less, but then most governments squeal on the twin pikes of access and excellence. I am inclined to agree with Robert Hughes when he says that art, like war, is a minority taste.

The public sector performs a dual function. It validates the art made today and authenticates the art of the past. It prevents, through selection and in conjunction with commercial art dealers and brokers, the market from being over-loaded, a situation that would lead to a fall in art's unit value. But it hoards and fails to release works back onto the market. There are, for example, only three Rembrandts still in private hands (Alberge, 2003). The prevention of the movement of this portable asset from one set of collectors to another is justified by a series of public good and national pride arguments. There is also an art historical argument that maintains that public gallery collections add to the understanding of an artist or movement.

There are equally strong counter arguments. Many works of art, especially religious artefacts, are best seen in the churches, temples and grottoes from which they were appropriated. Special exhibitions are just as capable of bringing great works together as are permanent museum displays. A work of art, which is made for trade, loses much of its meaning when it is wrenched from the market and institutionalized. The real reasons for the restrictions placed on the flow of art owe more to political expediency, intellectual posturing and precedent than convincing argument.

The UK political arts establishment appears to group de-accessioning beside free admittance to public collections. I would agree that once a work 'rests' in a public institution the work is public property and admittance should be free. If, on the other hand, a museum decides to sell one of its assets it should be allowed to benefit financially from the transaction. The two views can co-exist quite happily. The preciousness with which we treat our art in times of peace is matched only by our total disregard for it in times of war. Iraq is simply the latest example.

The use of art for utilitarian purposes has formed an important part of public policy in the UK since the Myerscough report in 1987. Since then there have been other reports written on the economic benefit of the arts to the general economy. UNESCO produced a report on the cultural flows of selected cultural goods from 1980 to 1998 and the Department of Culture Media and Sport produced its second examination into the monetary value of the cultural industries in 2001. These enquiries and their findings are of little help to the trade. They are aimed at persuading Treasuries to continue to fund the public sector. It is fair to say that the market does not actually need the public sector but it would rather not have to do without it.

The efficient markets hypothesis (EMH) has governed the way we view financial markets since 1970 (Fama, 1972). An efficient market is one in which security prices always fully reflect the available information. Today, the idea that financial markets (arguably the world's most perfect) can be efficient has been strenuously challenged by behavioural finance and the concepts of limited arbitrage and investor sentiment. Behavioural finance maintains that the biased, the stupid and the confused operate in competitive markets in which at least some arbitrageurs are fully rational. These factors, combined with a haphazard knowledge on how real-world investors form their beliefs and valuations, lead to very low levels of price prediction (Shleifer, 1999). If these 'realities' are true of the financial markets how much truer are they of the art market where Baumol (1986) cited in Towse (2003, p. 58) has observed:

- On financial markets, a high number of homogeneous, substitutable stocks and shares are bought and sold, whereas the degree of substitutability is almost nil in the case of artistic products, given the fact that they are unique.

- The owner of a work of art enjoys a monopoly, whereas a stock is owned by a number of investors, who, theoretically, act independently of one another.
- The transactions relative to a particular stock or share take place in time almost continuously, whereas transactions concerning a particular work of art may be several decades apart.
- The fundamental value of a financial asset is known: it is the present value of the expected flow of income; on the contrary, the work of art has no long-term equilibrium price.
- The costs of holding and transacting are much higher for works of art than for stocks and shares: insurance costs are high, there are charges borne by the seller and the buyer at auction, although on the other hand the taxes incurred by these goods may be more advantageous.
- Finally, art, unlike stocks and shares, does not provide positive monetary dividends: its ownership may imply negative dividends in the form of insurance and restoration costs; it does, however, afford psychological dividends in the form of cultural consumption and services.

Part I of this book takes a topographical view of the art market, mapping its structure. It sees it within a global context and aligns it to other markets and takes into account human behaviour. In Chapters 2 and 3 I look first at the internal forces that drive today's art market locomotive and then at how these same forces have shaped past art markets. I use financial terms to give sense to the art market and break it down into category, sector, type and commodity. The art market is not global like the food and drinks market, but it is international and operates from select centres around the world. I show that without the wealth developed by bankers and accrued from global trade, the art market would have remained undeveloped. In Chapter 4, Eric Moody questions whether these forces are manageable, and whether the market is, as Adam Smith has it, guided by an invisible hand, or indeed significantly biased in favour of a self-appointed élite. Derrick Chong examines, in Chapter 5, the three prominent relationships in the contemporary art market; dealer–artist, dealer–collector and collector–artist and looks at the art market from the Classical economic perspective of production–distribution–consumption. In Chapter 6, Renée Pfister shows how the price of a picture depends on where it is sold. The cost of importing Rothko's painting, 'No. 9', to the EU would, she explains, add $458,722 to its $8.95 million sales price excluding national sales tax. The same work would attract $686,519 import duty in Switzerland but only $11,080 if consigned to the USA. Pfister considers whether these taxes as well as those invented specifically for art, namely *droit de suite*, are good for its health.

In Part II we examine some of the major market sectors and see how well they have fared over the last decade or so. Joan Jeffri draws distinctions between the American and European management of art in Chapter 7. She directs our attention to the pre-disposition of some American museums to de-accession objects from their collections. She points also to a moral climate that permits public figures, like Mayor Giuliani of New York, to censor, on sacrilegious grounds, exhibitions such as Chris Ofili's in the Brooklyn Museum. The parallels between Jeffri's market for contemporary art in America with its tame critics and sharp dealers and the emerging art markets of East Asia are remarkable. In Chapter 8 I present the current state of development of these markets and, drawing on external 'realities' such as economic and political conditions as well as historical precedent, predict whether these markets have legs and where they are most likely to settle. I also show how great is the pricing gulf between the art of emerging and developed territories. James Spencer continues the Asia theme by introducing us to world taste in Chinese antiques in Chapter 9. It is clear from this chapter that Chinese, in particular, and Western taste for Chinese art have differed since the earliest days of the China Trade in the seventeenth century. It is also apparent that the recent economic booms in East Asia have drawn record prices from Asians for top works consigned by Western vendors. The alpha market has, significantly, also moved from London to Hong Kong and New York. If the world market for Chinese art is changing, then so is that of Old Masters. Alex Hope's observation in Chapter 10 that the price of alpha works has accelerated parallel to a huge increase in American museum endowments and a fall in the number of their acquisitions is compelling. The fact that these works, now that they have entered the institutional domain, are unlikely to re-appear onto the market has further inflated price and led to potential future supply problems. How different, Hope explains, from the days when even royal collections such as that of Charles I of England would be sure to re-appear onto the market. In Chapter 11 Patrick Boylan looks into the illegal market for antiquities and reveals a close association between the illicit traffic of works of art, drugs and guns. Plain old art theft has become a booming underground industry and governments and international agencies, perhaps because of stolen art's association with international crime, are taking preventative measures. Art is also used as a wealth-generating tool. In Chapter 12 I position art alongside other alternative investments and question the value of indices and a viable benchmark in order to establish an accurate value for this commodity. Time, place and particularly taste are the enemies of my attempts to rationalize this exotic market in which buyers often exceed their budgets and regret not this but the fact that the work of art got away. There is undoubtedly an 'X factor' to alpha art that drives buyers beyond their fiscal limits, and this makes estimates difficult to calculate. Conversely, unpopular work will regularly fail to make its reserve. Chapter 13 highlights the main themes in the book and asks fresh questions of its contents. In the final paragraph I imagine a dystopian art market, one which is efficient and autocratic.

Ultimately, the study of art markets is the study of the formation of taste informed by greed and made possible by opportunity. Those with sufficient means at the right time, persuasive powers and the least scruples build up the greatest collections. This state of reality makes it hard for us to refute Hobbes's model of a cloak and dagger world in which 'words, not money, were the relevant currency, and selves the objects of exchange' (Thomas Hobbes, *Leviathan*, 1651, quoted in Solkin, 1992, p. 22).

Note

1 The notion of art as a commodity is challenged most effectively when reference is made to public sector art galleries and museums that store and display these 'unique' and unexchangeable or irreplaceable objects. More than unique, art, it is argued, is imbued with national, regional and, at its best, international cultural significance. This book argues, however, that cultural significance can and is, demonstrably, captured economically and art, although unique, is not the only commodity to enjoy such status.

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Part I

The structure and mechanisms that fuel the art market

2 The international art market

Iain Robertson

> For by Art is created that great Leviathan called a COMMON-WEALTH, or STATE, (in latine CIVITAS) which is but an Artificiall Man; though of greater stature and strength than the Naturall, for whose protection and defence it was intended; and in which, the Soveraingnty is an Artificiall Soul, as giving life and motion to the whole body; . . . The Wealth and Riches of all the particular members, are the Strength.
>
> (Thomas Hobbes, Introduction to *Leviathan*, 1651)

We don't, in truth, need an art market anymore than we need art, but it is inevitable that when a desired commodity like art is created and made available, a distribution system forms around it. The system in this instance is replete with whispered half-truths and double talk, misinformed and misunderstood sound bites uttered by 'players' with strong vested interests, an extension of our imperfect selves, but it's all that we have and it's the best that we have. And this is how it works.

The international art market is the sole mechanism for conferring value onto art and antiques. It is also imperfect and difficult to access, consisting of thousands of élite, specialist retailers, a proportion of whom receive support from government. Government's support for parts of the art market is more subtle than the support it affords other industries, but it is no less effective. The art market, although dominated by two companies, Sotheby's and Christie's, by no means has the consumer at the mercy of a duopoly, nor is it dominated by an all-powerful, price-fixing cartel. It is perceived to be glamorous, exciting and engrossing and it carries the same allure as the fashion, film, media and sports industries. In truth, it has as much to do with entertainment as it has to the hard-headed world of global finance. Art market 'players' may appear to be aesthetes masquerading as financial traders but today the opposite is just as true – Christie's gentlemen pretending to be businessmen is a thing of the past. The sheer quantity of information that any business has to process, coupled with the international nature of art dealing, demands a greater professionalism and financial awareness from the art market's operators than at any time in its long history. This chapter