

PRACTITIONER'S POINT



Philip Hoffman, Chief Executive,
The Fine Art Fund.
Since it was launched in 2004, the
fund has had an annual return of
58%.

Can "art for art sake" = "art for pay sake"?

We invest in art as investors - with a financial hat on! "Beautiful" or not; our aim is to identify "good quality art work" that comes from good or great artists and can be acquired at a price that lends itself to an appreciation of 40% in a year or is worth double the money in three years. We would rather invest in a great work by a second rate artist than a poor work by one of the greatest artists.

Who, over what time horizon and how much should be invested to make art a viable investment?

A private investor should consider allocating at least USD 5 -10ml in art for a period of 3 to 10 years. Smaller sums such as USD100,000 could finance the acquisition of one good painting but commensurately rolls up the risk as there is no diversification. Alternately an investor could invest with a fund, such as ours, with an initial allocation of USD250,000. We aim to return between 10-15% annually compounded over a span of 3 -7 years. With investments in contemporary art - returns can be between 20% and 100% in a year.

Do you think the margins charged by auction houses considerably dilute the true profit potential of an art object?

We estimate a painting's worth or how much it could be sold for. By doing so, we arrive at an "all-inclusive" amount we would acquire it for. This amount is not dictated by whether it was bought at an auction or otherwise. If we believed a great quality painting could earn us 15-20% we would want it. Most of our buying and selling is done privately. A private investor would have to account for a spread of 30% per transaction, whereas through a fund this can be reduced to 5% or less.

Why have art hedge funds tended to be unsuccessful?

Once they have got an art fund started, most have failed in their ability to pool together a team of good and independent experts. Barriers to entry are high as depth of expertise is critical. There are 50 sought after experts, of which we have 8. It is rather difficult to get more than a few of them to work together. Also, an art fund like ours requires to be staffed by some 20-30 people.

Your opinion on investing in art indices?

I think art indices serve as a good guide and provide an overview of the market - but they are not highly accurate and neither are they good at providing specifics. In contrast, we provide pure "alpha" - expertise, ability to arbitrage and source art through distressed sales.

Do you think the art market can provide capacity for institutions looking to make large allocations?

There is an estimated USD30bn invested in art. Big institutional investors making allocations of USD1.5bn - would have the unwanted ability to move markets.

Would you recommend integrating art in a balanced portfolio for diversification purposes? Is it really a diversifier - given that art prices tend to be "inflated" and more is sold during booming financial markets and vice-versa... i.e. it tends to mimic /follow financial market cycles?

Yes. Investing in art exhibits a low correlation to stocks and is negatively correlated to bonds. It provides diversification benefits, lowers risk and reduces the overall volatility of a portfolio. Investing in contemporary art does tend to mimic boom and bust cycles. Currently a lot of this market is being patronised by hedge fund managers. It fits in with their lifestyle; the publicity that surrounds owning art, the fairs - it has become the new attraction and has taken on the significance of owning a second home! But what gets forgotten is that there are 70 different art categories. For instance, investing in "The Old Masters" bears a very low correlation to stocks as it is driven by collectors and museums that are willing to pick up the price tag even if the economy has slumped.

Your views on the work of artists such as: Gerhard Richter, Sigmar Polke, Georg Baselitz, Eberhard Havekost, Jonathan Messer - as investments?

The first three names are on my radar screen. In this regard we behave like seasoned stock pickers - we have a pool of 100,000 names we follow, 1000 that are of "significance" - which then is filtered down to about a 100 artists, at any given time, who are on the "buy" (under priced), "hold" or "sell" (take profits) list.

How do you identify artists as "investment vehicles"? How much can be attributed to talent and how much to hype?

I believe 95% is talent and 5% is hype. The former category renders profitable over a span of 3 -7 years, whereas with hype related names we have the potential to make huge amounts of money in a very short time.

A lot of really "expensive" art is "ugly"? What then, justifies the price tag?

"Ugly" is a subjective issue and has no relevance or bearing on the profit a painting can earn. A painting that I considered "ugly" - sold for four times what it was estimated and set a new world record.

What role, if any, do art critiques play in influencing prices?

Art critiques can affect prices in a small way. The more influential museum curators and art dealers are to be focused on.

Do you think investing in art is going through a bubble?

No. Some of the top 200 artists have peaked, but there are thousands of artists out there. As with stocks, one needs to be disciplined. One needs to know what to buy, when to buy and when to cut one's losses.

Do the returns justify and make it worthwhile to invest in art?

Yes, if you know how to diversify and have the time. Investing in art, as the American would say: "Is a 'no-brainer!'"