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Viability Of Art Investments

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Abstract

Artworks, encompassing a diverse array of mediums and designs, are expressions of creative imagination, emotions, and aesthetic pleasure. However, art cannot be viewed solely as creative expression. The unprecedented surge in art funding has raised questions about the viability of the art market and the risks and potential returns associated with it. This paper examines the intersection of art and economics, studying the progression of art investments over time. It also analyzes the financial potential of this investment avenue, assessing its payouts and drawbacks. Furthermore, the paper explores the future prospects of the art industry.

Introduction

Art has long been revered for its ability to evoke emotion, convey profound messages, and capture the essence of human experience. Traditionally valued for its creative and cultural significance, art has increasingly become recognized as a viable asset class, attracting investors seeking both financial returns and the intrinsic pleasure of ownership.

Art investments are not an entirely new concept. The concept of 'art as investment' originates from the late 1960s and early 1970s. In those times, ownership of art was viewed as a paragon of wealth and stature and such people served as patrons to renowned artists to gain exclusive rights to their work. Over time, the art market has evolved, expanding beyond the realm of elites to become a global investment avenue.

However, at the same time, a notion exists amongst many people that artworks cater to an illiquid market and are a high risk and opaque investment making it an irrational asset to back. Critics argue that the unpredictable nature of art valuation, coupled with market volatility, makes it a speculative market. Despite these repulsions, the recent surge in artwork funding has prompted a closer examination of its viability.

Artworks from an economic perspective

While few may consider the arts market to be a separate entity altogether, dedicated to the promotion of ingenuity, culture and aesthetics, it is dominantly governed by the discipline of economics.

The valuation of artworks is multifaceted unlike the price determination of the conventional economic products. It depends on a number of determinants ranging from the artist's reputation, the supply and demand dynamics to its historical and cultural significance. Paintings, sculptures etc. of a renowned artist like Frida Kahlo, Van Gogh are likely to be sold at higher costs than those of local artists. However, as the local artists become more established in their spaces, their art also begins to get recognition and their prices hike up. The demand of an artwork somewhat revolves around the artist's reputation as well as the desire of

the artworks, influenced by the current trends etc. among the potential buyers. The supply of the art is also an important factor in the sense that exclusive and unique artworks, which do not have ubiquitous counterfeits will produce higher margins as compared to one with multiple editions. While majority of the artists adopt this strategy of creating few pieces, few of them release several pieces a year to gain a higher profit sum. Additionally, collectors are often willing to pay higher for artworks with cultural or historical association. The artworks market encompasses both primary and secondary retails.

The primary market is where an artwork is sold for the first time, transitioning from an artist's studio to the buyer's collection. It is typically transpiring through gallery exhibitions, which act as an intermediary between the artists and the target audience. The artworks are unveiled there for the first time and the potential buyers have the opportunity to interact directly with the artists enabling them to establish a deeper connection with the piece and understand its inspiration. Other primary avenues for sales are the artist's studio itself or through their established networks. The prices in this market are stable and justifiable as they are posited by the artists or galleries, reflecting initial value of the artworks.

The secondary market is crucial as it allows for significant jumps in prices. Any sale that takes place after the first sale of the artwork falls under the domain of the secondary market. In this market, the artist is no longer involved in the transaction since ownership is transferred from one collector to another. Secondary or "second-hand" market avenues include auctions, art dealers, and online forums. The price determination revolves around negotiations among buyers, the rarity of the artwork, and the reputation of the creator. Initial buyers and investors aim to yield high returns by parting with the artworks they own.

Types of Art Investments

1. **Paintings:**

Paintings are one the most popular forms of artwork investments. They are typically bought or sold via auction houses or art dealers. The artist's reputation, condition, rarity and historical significance influence its valuation.

2. **Sculptures:**

Sculptures are completely akin to paintings in terms of investment with auction houses and dealers being the common avenues for its buy and sell and its value being influenced by the artist's stature, historical relevance, rarity and condition. Like paintings, they are also a widely embraced asset.

3. **Digital Art:**

Digital art is a non-traditional and contemporary medium for art investments. Crafted using various software tools, it is easily producible and distributable and its value is determined by the artist's standing, historical significance and uniqueness.

4. **Non-Fungible Tokens (NFTs):**

NFTs are typically digital assets which represent the ownership or a unique piece of art, recorded on a blockchain. The blockchain technology promises transparency and security and acts as a decentralized register recording creation, sale and ownership of NFTs. They have taken the art world in a storm due to their potential to create advanced economic models for digital artists and creators. The value of an NFT depends upon the artist's reputation, rarity of the work and its historical association.

Evolution of Art Investments

Artworks as an investment vehicle has witnessed drastic transformations over the course of time. Initially considered as a symbol of wealth and prestige, it was dominated by wealthy and influential individuals and

collectors who were driven by the passion for arts. People have broadened their perspective over the time by identifying its potential as an investment vehicle and not merely a cultural asset.

The first turning point in intertwining of art and economics came with the founding of the first auction house, The Stockholm Auction House in 1674 followed by the establishments of Sotheby's in 1744 and Christie's in 1766. These institutions set the stage for commercialization of artworks and recognizing their monetary significance.

1904: The first modern art investment fund was founded by Andre Level in 1904, Paris. He and his friends pooled their resources to purchase contemporary art, now known as impressionists. They hoarded these works for 10 years and ultimately sold them on the eve of the 1st World War. As a result, the money they invested quadrupled and the model set several precedents in action that helped shaped the intersection of the two domains later on in the century.

1960s: The rise of Pop Art during this decade revolutionized the history of art. Andy Warhol, the "King of Pop" started commercializing his art practices. He addressed his New York studio as "Factory" and employed assistants to help him increase the production and sales of the artworks. Gallerists like Leo Catelli provided support to artists in funding, sales etc. and by spurring the valuations of their works making them internationally acclaimed personalities. Thus the 60s was the age when an indelible link was established between art and capitalism and art was given the status of a legitimate investment asset.

1970s: Once the seed for art investments has been planted in the 1960s, investors increasingly saw art as an alternative to be capitalized upon. The 1970s saw a tremendous expansion of the secondary market. In 1973, a momentous auction, often remembered as "The Scull Auction" took place at the Sotheby's. Robert and Ethel Scull, who were passionate collectors of contemporary art sold their collections and earned high returns. This blockbuster auction was one of the defining moments in the art market history which has testified the high worth attached to contemporary art. In 1980s, the British Rail Pension allocated 40 million euros worth holdings to art investment through the Sotheby's. This large-scale operation is a definite testament to increasing trust in the art market throughout the decade.

1980s: The 80s was a decade when the art market was incredibly booming. The enticement among individuals to make big money drove the prices of artworks higher and higher. The Japanese also became increasingly interested in this segment, empowered by rapid economic growths during this interval. For the first time ever, the secondary market was a globally flourishing enterprise and the booming market no signs of relenting despite the 1987 financial crisis. Although alterations in the U.S. law in 1986 made donations to art museums and galleries less attractive, the 1897 sale of the Van Gogh Sunflowers at the Christie's was the biggest sale with its value quintupling with every bid. The bid was ultimately secured by a Japanese fire insurance company at a whopping \$39.9 million. This remarkable sale set an auction record and benchmark for incredible spectacle of auction prices.

1990s: During this age, the auction sales continued to escalate as the art prices spiraled. The hype around the market was compounded by the advent of contemporary art, specifically of the Young British Artists. Extravagant exhibitions showing likes of Damien Hirst and Tracey Emin were actively promoted.

2000s: The financial booms of 2000s stimulated the exponential growth of the art market. The market remained resilient even after the 2008 bust when the Sotheby's stock alone dropped by 83%. Factors responsible for the market resilience include the increasing global interest being captured by the contemporary artworks which enable artists to sell their pieces for enormous figures easily despite of the economic downturn. Also, the emergence of internet, which was single handedly the most important factor opened the option for online transactions and deals. Online forums such as eBay with their easy accessibility fostered art purchases.

2010s: The secondary market was given a lasting place on the internet after the rapid technological developments of 2010s. Not only were the online market platforms more accessible, they were more transparent in the sense that they provided a wealth of information available to the collectors such as historical art sale data, analytical reports, prices etc. The auction houses began conducting bids live online catering to a wider audience of buyers.

2020s: As we progress through this decade, the art market is set to transform further. The Covid-19 pandemic has spurred the population to become even more tech savvy and online-present than before, significantly impacting the art world and its market. This age has fostered platforms like MyArtBroker which provide, transparency, accessibility and abundant information. There has also been a noticeable increase in the investment of NFTs with Sotheby's and Christie's dedicating entire auctions to them.

One thing, however, is certain from the above pattern, the art market does not show any signs of regressing is just getting started.

Are artworks a wise investment?

Profits of Investing in Art

1. Tangible and Aesthetic Appeal:

Art investments provide an opportunity to possess tangible assets with inherent aesthetic value. While most investment avenues are abstract, artworks are a tactile investment. Each artwork is a unique creation depicting the artist's emotions, vision, and skillset. The individuality of art sets it apart from other investment alternatives and continues to be a continual source of pleasure for all.

2. Potential for High Returns and Appreciation:

Repeated evidence of specific artworks amassing millions of dollars testifies to the high returns yielded by artworks. Those who recognize its potential treat it as a lucrative opportunity. Additionally, artworks have the potential for appreciation over time since their market operates independently of traditional financial markets. Investments implicitly counter inflation, and the values of certain artworks or artists can increase exponentially in relation to demand. Investors also benefit during ephemeral phases of growing interest in particular art styles or historical periods. It is not uncommon for them to receive substantial returns over the years.

3. Diversification of Investment Portfolios:

By adding art investments to your portfolio, the overall risk involved in investing is reduced because artworks do not correlate with conventional stocks and bonds. As a result, they are expected to remain stable even during economic downturns, inflation, market volatility. This diversification enhances the sense of security, stability, and returns of your investment portfolio.

4. Cultural and Personal Enrichment:

The benefits of owning artworks extend beyond financial returns. Art immerses you in the world of creativity and culture, portraying a story and the artist's interpretation of it, making it a valuable investment. It also enables individuals to develop a personal connection with the pieces they own and explore various artistic movements and cultural contexts. This not only deepens your artistic and historical understanding but also contributes to the preservation and promotion of cultural heritage.

5. Tax Incentives:

Some countries offer favourable tax treatments such as exemptions, deductions, and deferred capital gains specifically for art investments. These provisions significantly enhance the financial appeal of this asset and allow the collectors to optimize their yields while ensuring minimum tax liabilities. Nevertheless, it is imperative to consult a professional tax advisor to develop a tax efficient investment portfolio.

On the whole, artworks are incrementally gaining significant as a unique and rewarding investment opportunity. Being a powerful asset, its gains extend beyond mere balance sheets.

Challenges of investing in Art

Similar to other investment domains, art investments have their share of pitfalls. Investors need to carefully consider and analyze numerous factors before committing their earnings.

1. **Illiquidity:**

The art market is known for its illiquidity, making it challenging to resell artworks quickly. Finding a buyer willing to pay the desired amount can be a lengthy and complicated process.

2. **Market Fluctuations:**

The art market is highly volatile, with values fluctuating based on consumer preferences, market trends, and global economic conditions. Artworks that appreciate rapidly can also experience steep declines, making the market unpredictable.

3. **Long Lock-Up Period:**

Art investments often require a long holding period before any significant appreciation is realized. Investors may need to wait several years, as the value of an artwork often increases as the artist gains recognition. This long-term nature poses a risk, as the capital is tied up for extended periods.

4. **High Risk:**

While art can yield high returns, it is also a high-risk investment. The value of an artwork is speculative and dependent on market demand. An artist's popularity today may not guarantee future value, and investors need to stay informed and knowledgeable about the art market to make wise decisions.

5. **Niche Market Knowledge:**

The art market is a niche field that requires deep understanding and familiarity with its rules and nuances. Navigating the market involves gaining knowledge about artists, trends, and pricing, as well as building relationships with galleries and artists. Without this expertise, investors may struggle to make informed decisions.

6. **Storage and Maintenance Challenges:**

Properly storing and maintaining fine art can be challenging and costly. Inappropriate storage conditions, such as exposure to dampness, heat, or bright light, can damage artworks. This requires additional investment in suitable storage solutions, which can be expensive and space-consuming, especially in urban environments.

Future of Art Investments

1. **Technological Integration:**

The potential integration of advanced technologies in the art market is expected to enhance transparency and significantly improve digital tools for evaluation, pricing, authentication, and provenance tracking.

2. **Environmental and Ethical Considerations:**

With growing awareness of environmental and social issues, there is a likely shift towards adopting sustainable practices in art production, transportation, and exhibition, which could influence both the creation and trade of artworks.

3. **Shift Towards Private Sales:**

As public auction houses face increasing challenges, there may be a growing trend towards private transactions, where artworks are bought and sold directly between buyers and sellers without the involvement of auction houses as intermediaries.

4. Regulatory Modifications:

As the art market becomes more financialized and attractive to investors, it could come under increased regulatory scrutiny, leading to potential changes in tax laws, anti-money laundering regulations, and other legal frameworks governing art transactions.

Conclusion

The research indicates that art can indeed be a viable investment opportunity, but it comes with significant cautions and considerations. Unlike traditional assets of bonds and stocks, art does not generate regular income and requires long-term commitment and significant expertise to leverage its investment benefits effectively. Therefore, while art is a valuable addition to an investment portfolio, it is not fitting for all investors. Passion for art should be the driving force for investors willing to back artworks. Intricate and prudent selection, knowledge and above all, patience while investing in artworks can yield substantial awards. To sum it up, art is a viable investment avenue for those who understand and appreciate its unique characteristics.

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