

INVESTING IN ART

By Rose M. Anderson, CFP®

Art is hot. The record price for a single painting was broken three times in 2006. The big auction houses Christie's and Sotheby's sold a combined \$1 billion worth of contemporary art last fall and attendance is surging at art fairs such as Miami's Art Basel and the Armory show in New York. With people making huge sums from managing hedge funds, it's only natural they want to show off their new found wealth. And, while the wealthy have always invested in art, I believe that more of us are finally realizing that as an asset class, art belongs in an investment portfolio.

Successful investing is about knowledge and risk.

Risk:

Every investor understands the importance of diversification; by distributing capital among different investments the potential risk of the portfolio diminishes. There are two types of risk, systematic and unsystematic. Unsystematic risk can be controlled by diversification within an asset class while systematic risk can only be mitigated by diversification between asset classes. With different asset classes moving in different directions at different rates, the portfolio will perform more consistently.

It makes no sense to talk about an asset class unless you have a means to measure the returns of that asset class. Two professors from NYU's Stern School of Business have created the Mei-Moses Family of Fine Art Indices® and have tracked the return of art since 1956. I have created Table 1 to show the comparative returns of American Art prior to 1950 and the All Art Index versus other more common investments. As you can see from the table, art can be not only a very good investment, but also a diversifier for an otherwise well balanced portfolio. Michael Moses says that because of the low correlation, he suggests an allocation of 10% for those investors who have at least \$500,000 in assets. Nearly all of the research into this asset class indicates that art is riskier than stocks however; Mei and Moses created a series of graphs that show the risk/ return tradeoff of adding art to a diversified portfolio. Their data from the past fifty years demonstrates that adding American art to an investment portfolio diminishes its level of risk; an expected return of 8% on a portfolio without American art carries an almost 11% risk, whereas the same return on a portfolio with American art carries only a 6.5% risk. Furthermore, when the expected return rises to 10%, the portfolio without art holds a risk of 16.5%, while the portfolio with American art only experiences a risk of 9.5%.

So, now that you've made the decision to diversify your portfolio with art, where do you start?

Knowledge:

There are many ways to acquire the knowledge that will give you the self-confidence you need to purchase fine art for investment. Note that investing in art is different from selecting art to adorn your walls because you fall in love with a painting.

For the client interested in the investment value of art, my first piece of advice is to learn everything you possibly can regarding the period or artist in which you are interested. This isn't as difficult as it may seem. Visit museums and galleries. Ask questions and ask again until you

understand what they are telling you. There are a number of books in most libraries covering art history and many articles in current publications on more contemporary artists. The only way to gain a sense of self confidence to make that first purchase is through knowledge. It may take you a year to feel you know your stuff but take your time. Buying that first piece of investment art shouldn't break the bank, after all, you're just starting out in this new endeavor and you want to purchase wisely. Still unsure of yourself? Don't worry; there are other ways to feel secure in making these decisions. An art consultant can help. This person will work with you, and within your budget, to acquire the works that fit your time period or your artist. This person should take the time to understand what you know about the art you are trying to collect and teach you some of the nuances that make one piece of art more valuable than another. You're investing in art and these nuances will become more significant over time.

For example, many of the masters are still available but may be out of your price range. The most notable work from Andy Warhol has escalated rapidly in value but there are lesser-known pieces available for more affordable prices. Salvador Dali is perennially popular and much more affordable for the beginning collector. If you like Picasso, there are selections that will not only add value to a collection but will give you years of pleasure hanging on your wall. Another prolific artist is Joan Miro whose work is readily available for the novice and intermediate collector.

Another method of collecting for investment is to select work from the emerging artists. These are artists of unproven quality and generally with no history for price comparisons. But it's fun to search them out and make your own discoveries. It's certainly riskier but you should be acquiring this artwork at lower prices to the established artists and certainly lower than the most marketable artists. You need to have a trained eye for this type of purchase which is where a consultant could certainly help. You might want to visit the local Art Association and do so several times. Ask questions and take notice of those artists who are winning awards. Follow their careers for a year or so and see who else is buying their work. An artist with work going into a significant private collection or a museum collection is definitely someone to watch closely. Only when you feel confident should you make your first purchase from an emerging artist.

While the process is not stress free, it should give you a good feeling that you are acquiring something of rising value that you can enjoy on a daily basis. My motto, surrender to the beauty of fine art.

- 1) More information on the Mei-Moses® Art Index can be found at www.ArtAsAnAsset.com

Table 1: Compound Annual Return Art Indices vs. Financial Indices

Mei Moses®	American Art	S&P 500	US Treasury	US Treasury
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	All Art Index	Before 1950	Total Return	10 Year Notes	90 Day Bills	Gold
Last 50 Years	10.1%	13.1%	10.6%	6.7%	5.5%	5.5%
Last 10 Years	8.5%	10.5%	8.5%	6.9%	3.6%	3.0%
Last 5 Years	11.6%	10.5%	6.1%	5.5%	2.1%	13.8%
Last Year	18.3%	34.6%	15.8%	2.7%	3.1%	18.4%

Written by Rose M. Anderson, CFP®, owner of Anderson Financial, Inc. and Pure Gallery, Inc. www.PureGallery.net. Ms. Anderson can be reached at rose@puregallery.net.