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The Art Market - It's a Rigged Bet

By Burke Files, CDDP, President, Financial Examinations & Evaluations, Inc (01/01/2014)

Oh did I get in trouble. I received all sorts of calls and emails after a short quote in the Wall Street Journal. "Art funds always lose money...investors always lose in an engineered and contrived market." was the quote printed by a dear friend, columnist and author of some cool financial thriller books, Norb Vonnegut.

The quote was part of a far ranging discussion on Madoff and frauds in general. Madoff from the beginning was a fraud by design. There never was any pretense of trading or investing - it was a scam from concept, through design to implementation.

The art market is not a fraud, but it is an engineered market, an artificial market. There are no arm's length transactions. The art market's 'police men' are the dealers, auction houses, experts, and critics - also known as the cabal of foxes. These are the same foxes who are charged with guarding the art market chickens as well as writing their own performance reviews. There cannot be a problem - as they are all experts - never mind the MASSIVE conflicts of interest.

The quote was harsh, brutal and accurate to the word.

Please do understand I do enjoy the arts, music, dance, theatre, painting, sculpture, and writing. I enjoy them both in the process of discovery of the language of the artists as well as how the message, the artist's communication with the viewer (consumer), ensues and unfolds.

That being said, art, other than that the highly commercialised forms of art such as movies and music, are not suitable to any conventional business model. They are thus wholly unsuited for any investment model known to date. Not even random work can be applied to the art market. The individual pieces of art are truly unique - thus one cannot draw parallels well with other pieces in a "family of art", nor can one draw any meaningful conclusions from price data, as they are all unique pieces. Also the art market transactions are rarely arm's length, it is not even open or free or transparent - the art market is wholly engineered. Mind you it is also engineered to favour those who are in the "family of art" - this is only natural.

> An estate had six paintings of a respected landscape artist. The estate had the paintings professionally appraised at US$1 million for all six paintings. A clever art dealer, being made aware of the circumstances, approached the estate and proposed a transaction. The art dealer was already aware of a museum that currently possessed a collection of 10 works by this artist. The art dealer, being shrewd by nature and design, arranged for the museum to purchase one of the six paintings for US$1 million. The painting was added to the museum's already impressive collection and featured in an art event at the museum. Several months after the exhibit the estate managers were so impressed with the exhibit - they donated the remaining paintings, now valued at US$1 million each, to the museum.

So what fiscally just happened? The museum went from 10 paintings valued at about two million gross to 16 paintings valued at about 16 million. How? The market, once the million dollar purchase was engineered, was now the benchmark market price for the

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artist's works. As it was a public price paid the art work was considered bought in at the US$1 million per unit price and thus the artist had a 'bull' moment in the price of their paintings. It was also a net increase for the museums holdings of 14 million dollars in one afternoon. Not a bad bit of market engineering.

The estate got the full US$1 million in cash based upon the initial appraisal as well as a US$5 million deduction against future taxes for the donation. A very significant achievement for the estate managers.

What did the art dealer get - one can only surmise. I am sure the art dealer got a bit of the cow as it was sold, some when it was bought, and no doubt some option on any of the offspring and milk produced by the cow and the cow's progeny - probably for at least two generations. It is how these things are engineered.

Or conversely,

> A series of Chinese ceramics from the Han period were "allowed" to be exported from China, several years ago, as they were "obviously" not of high quality according to group of ceramic experts and were sold privately for about US$75,000 apiece. A severe drop in prices for this period of Chinese Ceramics, almost an 85 per cent drop, occurred as a result of these reported transactions. However, once in front of the real experts in Chinese ceramics in London and New York (gag and sputter) - the ceramic pieces were not only declared to be of value but from the more valuable Qin dynasty. The experts and dealers declared that these items were no doubt unique and significant pieces of cultural heritage. When these pieces were sold at auction the buyers of the pieces were Chinese nationals and they specifically declared that these "looted treasures by western imperial powers must be repatriated". Truly great art and great theatre at the same time. (The buyers must have not read the provenance very closely as the ceramics were in China up to about four years prior to the auction). China allowed an exemption to the currency export control laws so the buyers could repatriate these works of significant cultural heritage.

Here the need to launder money forced the prices of certain objects significantly lower than, conversely, significantly higher to achieve the aims not of any collector but the needs of the buyers to get money out of China. I also expect that these are of a more - dare I say it - recent vintage of dubious origins! I expect more historical pieces to come to the market in the near future - so this well rehearsed "repatriation scheme" can run a few more times. One may find that the beneficial owner of the art, after a few layers - the buyer and the seller might become indistinguishable.
These engineered perturbations of price have been getting stronger in the art market and remind me of the American Quarter Horse market when it was literally invaded by Mexican drug cartels as a way to launder drug money. The drug cartels were buying and selling these horses on either side of the US / Mexico border driving the prices of American Quarter Horses through the roof as the recession that dragged on the prices of the horses ran counter cyclical. It was very easy to move horses worth millions as opposed to moving millions with mules. I see many of these similar market perturbations in the art markets - where demand is stiffening and prices are very strong though overall the world economy is still weak. Yet the visibility of the art bought and sold has not changed. Meaning we do not see more of it in museums or private collections on display. It seems little of the art is passing from party to party but the art never leaves the Zurich or Singapore free trade zones where there are large - and I do mean very large - vaulted art storage facilities. One does not need to move the art, only change the name of the warehouse receipt.

The art market is an engineered market and engineered on behalf of its creators, the dealers, auction houses, experts, and critics. Just ask any of the art forgers who being gifted artists in their own right started forging works of art to show the cupidity of the cabal of foxes. They were frustrated that their own works of art were not appreciated so they went to show the world with their forgeries that the entire process was rigged from the beginning. Problem is - most forgers as soon as they passed a few forged works of art kept forging along because the money was so good, better than what they could have made with their originals.

Somehow, one can only bring to mind the image of Humphrey Bogart and Claude Rains in the opening scenes of Casablanca... to understand the vitality of engineered markets in the face of all threats to the contrary.

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