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Less Barking, More Tail Wagging from Art Market Facts

By Michael Cervino

On May 1 we will launch our evergreen fine art-secured lending fund. A report completed by Art Basel and UBS on the health of the global art market in 2018 provides insights that corroborate our investment thesis:

- A large growth market for high-end art
- Dealers (and some collectors) need reliable financing solutions
- In the absence of traditional lenders, demand for financing is left unmet
- Strong demand in an underserved market can provide stable prices and loan terms favorable to the lender

\$67.4 billion of fine and decorative art and antiques changed hands globally in 2018, the second-highest peak in the past 10 years. Strong sales came on the back of 39.8 million transactions, the largest volume since 2008. Auctioneers brought the hammer down on art worth \$29.1 billion. Top-tier works (\$1 million+) stole the show, accounting for just 1% of the lots but 61% of the total value (a 13% increase over the previous year). Strong top-end sales growth is encouraging given our focus on museum-quality, high-end art for our Art Lending Fund (“ALF”).

But how did fine art dealers fair? If one were a dealer holding top-tier art inventory heading into 2018, it was a great year. Total dealer sales swelled 7% to \$35.9 billion. Mirroring trends in the auction market, works going for north of \$1 million accounted for 40% of the total dealer sales but only 3% of transactions. This top-heavy concentration underscores buyers’ expensive tastes. For dealers vying to get hold of top-tier art for their inventories, ready money is key. However, sitting on cash is wasteful given the unpredictable availability of best-quality works.

Robust sales are inspiring, but fine art dealers continue to find it challenging to access credit. Commercial banks shun dealers and galleries due to the general absence of audited financial statements and their reluctance to take on hard asset loans versus more traditional cash flow lending. But high-end dealers are not just peddlers with exceptional wares – they have several advantages over borrowers in other industries:

- High-end art dealers do not rely on local clients: U.S. dealers with an annual turnover of \$10 million+ draw more than half of their customers from overseas.
- Clients enjoy their experience: Dealers with annual sales over \$1 million derive 75% or more of their sales from repeat customers. Success breeds success.
- Dealers and galleries are resilient: 73% of those surveyed have been in business for a decade or longer (compared to 58% for U.S. retail and 48% for the U.S. private sector businesses). Dealers with annual turnover greater than \$1 million have been in operation for a median of 26 years.

With reliable access to credit, dealers would be more nimble and better prepared to face the challenges ahead. In a survey conducted by Art Basel and UBS, dealers and galleries were asked to rank their anticipated challenges by order of importance:

| Challenges | 2018 rank | 2017 rank |
|---|-----------|-----------|
| Finding new clients | 1 | 1 |
| The economy and the demand for art and antiques | 2 | 2 |
| Financing your business and debt | 3 | 8 |
| Participation at fairs | 4 | 3 |
| Competition with auction houses | 5 | 4 |
| Internet and online sales | 6 | 9 |
| Overheads for your business premises | 7 | 5 |
| Accessing supply of objects, works of art, artists | 8 | 7 |
| Political instabilities | 9 | 6 |
| The increased regulation of the art market and cross-border trade | 10 | 11 |
| Competition with other galleries | 11 | 10 |
| Currency issues and exchange-rate fluctuations | 12 | 12 |

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Dealers consistently rank “finding new clients” as the top challenge they will face over the next five years. Many rely on exhibitions, shows, and fairs to foster new client engagement and boost visibility. Art fairs, ripe with potential clients, are prohibitively expensive for many dealers and galleries. Financing allows dealers to pay the upfront costs required to take on growth projects whose benefits are realized over an extended period of time.

Bringing in potential clients is the first step. Turning potential clients into buyers and cultivating ongoing relationships with those buyers is the ultimate goal. Dealers must be able to offer highly sought-after works of art to satisfy buyers’ tastes. High demand for top-tier art, evidenced by the top-heaviness of the market, creates intense competition between dealers to source the best examples of artists’ works. Dealers hunting for high-end inventory need to act fast when a desired piece becomes available. With access to financing through lenders who can remit cash quickly, dealers can jump on these opportunities.

Demand for financing is increasing: “Financing your business and debt” leapt from #8 to #3 in the rankings above. Within an art market deserted by traditional finance, art-secured lending is an oasis. Dealers can more efficiently manage cash when given the ability to leverage art in their

inventories. Specialty finance companies providing art-secured loans, such as ALF, have the speed and flexibility dealers require to compete for in-demand inventory and fund expansion efforts.

Accelerating demand in a “capital short” market creates a need for privately funded groups to step in. Art-secured lending is a compelling yield investment. Fine art has historically appreciated. It can be shipped around the world to take advantage of fluctuating currency strength. Lenders can take possession and control of the collateral. Modest loan-to-value ratios protect principal from valuation changes and short terms mitigate interest rate risk. ALF launches on May 1 to take advantage of this special opportunity. We encourage you to join us.

For a brief overview on ALF, please visit www.shinnecock.com. For a deeper look, our online data room (access available upon request) contains numerous articles and studies on art-secured lending and the fine art market.

Upcoming Events

See attached schedule of industry related events at which Shinnecock will be sharing more in-depth information and let us know if you’ll be attending so we can look for you!



Upcoming Events

Shinnecock will be in attendance and/or speaking at the following events. We'd be happy to have you join us!

May 14 – San Diego

IvyFON Family Office Event

*Details to come

For information and registration, contact Marty Secada: martysecada2008@gmail.com

June 2-4 – Rancho Palos Verdes

Context West 2019

Terranea Resort

100 Terranea Way, Rancho Palos Verdes, CA 90275

For information and registration: <https://contextsummits.com/west/>

June 4 – Los Angeles

IvyFON Family Office Event

*Details to come

For information and registration, contact Marty Secada: martysecada2008@gmail.com

June 13 – New York City

Beryl Elites Forum – Innovations in Asset Management 2019

The Cutting Room

44 East 32nd Street, New York, NY 10016

For information and registration: <https://berylelites.com/innovations-in-asset-management>

Nov 4-5 – New York City

Agecroft Partners: Gaining the Edge

The Roosevelt Hotel

45 East 45th Street, New York, NY 10017

For information and registration: <https://www.apgainingtheedge.com/>

Nov 11-12 – New York City

3rd Annual Beryl Elites Alternative Investment Conference

The Cutting Room

44 East 32nd Street, New York, NY 10016

For information and registration: <https://berylelites.com/3rd-annual-beryl-elites-alternative-investment-conference>