OVERVIEW ON THE
CURRENT STATE OF THE ART MARKET

Prepared by IMUA’s
Arts & Records Committee

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Rosita Cantres - XL Group
Robert Crozier - Crozier Fine Arts
Paul Fritsch - ACE Group
Randi Glazer - Hiscox
Andrew Cristina - Travelers
Simon Hornby - Crozier Fine Arts
Michelle Impey - Chubb
Melissa Lalka - Chubb
Christopher Marinello - Art Loss Register
Sheila O’Keeffe - General Re
Jennifer Schipf - XL Group [Co-Chair]
Gregory Smith - Berkley Asset Protection [Co-Chair]
Dorit Straus - Chubb
Elizabeth vonHabsburg - Gurr Johns
Victor Wiener - Independent Appraiser
Katja Zigerlig - Chartis

INTRODUCTION

The following paper was written by the IMUA Arts and Records Committee as a guide for underwriters, brokers and other insurance industry professionals who are concerned by perceptions of the state of the art market today, and who may be interested in reviewing the art insurance coverage of their clients.

This paper is written from several perspectives – the personal lines underwriter, the commercial lines underwriter and the appraiser. As respects the latter profession, fine art appraisers have been obliged to factor into appraisal assignments considerations of current market conditions; the following insights are offered in the hope that they will prove useful to the insurance professional.
The following article reviews the current state of the art market and should help to emphasize the importance of having updated valuations, particularly in times of economic downturns and uncertainty.

**GENERAL STATE OF MARKET TODAY**

Following the collapse of Lehman Brothers in September 2008, the art market experienced a retrenchment in total sales for works of art offered at auction, both on a per item and aggregate basis. Although hard to quantify because of a lack of credible statistics, private art galleries and dealers have also experienced dramatic downturn in their sales volume.

However, the art market has often proved to be resilient, and, to a certain extent, is independent and not necessarily in step with trends in the financial markets. For example, when the stock market crashed in 1987, the art market continued to escalate until the beginning of 1990 when it, too, for the first time, experienced a downturn.

As measured in auction sales, the art market experienced a dramatic downturn in the fall of 2008; however, beginning in the fall of 2009, a significant, but selective, recovery could be seen. Whether this recovery will be sustained will be seen in the coming months and at future industry sales.

To get a sense of the 2009 results, Kelly Crow, a staff reporter, ran some numbers on the art market in *The Wall Street Journal* in a January 2010 edition. Comparisons to 2008, of course, are shocking. Overall, both major houses were down around 50% in the major art categories with Sotheby’s having a slightly steeper fall.

- Sotheby’s said it auctioned off about $2.3 billion of fine and decorative art last year, down 53% from 2008. The 2009 total included $441 million in contemporary art, down 68% from 2008; $471 million in Impressionist and modern art, down 57%; and $190 million in jewelry, down 13%.
- Rival Christie’s International PLC said it auctioned at least $2.5 billion of art, down 45.6% from $4.6 billion in 2008. Closely held Christie’s said it would make available complete sales figures, but to date statistics are not available.

Fewer than 550 artworks crossed the million-dollar mark at auction in 2009, half as many as in 2008 as reported by Artprice, a Paris-based database that tracks global auction results. According to Thierry Ehrmann, founder and CEO of Artprice:
"2009 will go down in history as a year when the art market shed its excesses and narrowly avoided a complete meltdown. A drastic purge of the contemporary art segment; slashed revenue figures; and renewed interest in Old Masters and modern art... but also a strong signal that the art market has reached a stage of maturity that allows it to fluctuate at the same speed as economic indicators and financial assets... the key point to remember about 2009 is this historical and sociological change in the art market”.

MARKET OVERVIEW FROM A PERSONAL LINES INSURANCE PERSPECTIVE

There were many challenges facing the personal insurance fine art market in 2009. In all lines of coverage, insurance carriers were under pressure to reduce rates as a result of the economic downturn. This often resulted in reduced premiums for the same insuring terms and conditions. Competition amongst carriers remained fierce as companies fought to retain customers and market share.

Valuable articles, including fine art, seemed to be the area of coverage customers were most willing to self-insure in an attempt to manage their overall personal insurance costs. As articles were removed from previous schedules, reduced schedule limits on previous fine art schedules became a frequent request with some customers choosing to insure only their most valuable pieces. In addition, there was a significant drop in endorsement activity as collector acquisition of new pieces declined in 2009.

One of the leading trends in 2009 was customer’s reluctance to have their existing schedules re-appraised. From an insurance carrier’s perspective, appraising works of art on a regular basis is an important underwriting consideration for a number of reasons –

- to know what the client’s collection/investment is worth;
- determining if any items were added or sold, but were not reported;
- to assist in estate planning and tax purposes; or
- to make certain the insurance on the item is set at the correct value.

The more complicated question beyond the reasons why to reappraise is when to reappraise. This question can be more challenging to answer in an economic downturn, but from an insurance carrier’s perspective, this remains an important time to ensurevaluations are current.

A private collector may respond to such requests with -

- I just had my work reappraised three years ago so I don’t need the values updated.
- The economy is down, so the value of my art must be down as well.
• *I will end up paying more for my insurance if I get reappraisals.*

To dispel some of these common beliefs it is important for the client to understand what is going on in the art market that may lead their agent or broker [producer] and/or insurance carriers to suggest reappraisals.

Depending on the genre of the work, the value may have fluctuated substantially - up or down - in the past few years. In an economic downturn, no customer wants to pay more for insurance than they feel is necessary, but these customers also do not want to be told there was insufficient coverage [limits] after they suffer a loss. It is imperative that insurance carriers and producers understand when customers last had their works appraised, what the collection is made up of, and any changes that may have occurred so they can guide their customers accordingly on the need to obtain reappraisals.

It also becomes very important for the private collector to understand what they should obtain when requesting reappraisals as art appraisals can be written for different purposes and require different types of valuation methods. One trend seen throughout 2009 was updated appraisals reflecting the fair market value assessment, and not the replacement value of objects. Insurance carriers and producers should request the appraiser’s report mirror the intent of the valuation clause in the personal insurance policy which is most often based on the price one would likely have to pay on the open market to replace the item with similar and like kind and quality within a limited period of time. The replacement value determined by the appraiser is almost exclusively applied to insurance policies. In the event of a claim this is how an insurance carrier would replace an item. Fair market value is predominately for IRS purposes and based on the price that a willing buyer and a willing seller would sell the object for in the open market, with neither being required to act immediately around the transaction. Upon rare instances fair market value may be used for personal insurance purposes, in such instances the reason for using it should be addressed in the appraisal. Replacement value tends to be higher than fair market value due to the limited amount of time to replace the object.

**MARKET OVERVIEW FROM A COMMERCIAL LINES INSURANCE PERSPECTIVE**

The economic climate of 2009 resulted in a variety of trends among commercial buyers of fine art insurance. Ultimately, a reduction of premium was the most common goal among buyers as everyone sought to reduce expenses wherever possible and take advantage of a marketplace flush with abundant capacity. Decreased art values resulted in lower limits of liability and therefore less insurance being purchased.
Trends experienced among specific risk types included -

- Many **not-for-profit institutions** (museums and foundations in particular) reduced the size of their staffs to decrease payroll expense.
- Far fewer traveling, short term exhibitions were organized due to cutbacks in institutional budgets and corporate sponsorships.
- Lower loss limits and increased deductibles were considered as in prior years, but were more frequently selected than in prior years.
- In several unusual instances, museums considered de-accessioning permanent collection objects to sustain operating budgets.
- **Galleries and dealers** also reduced staff and purchased less new inventory as a result of decreased sales volume. As a result of decreased consumer activity, many dealers reduced their participation in fine art fairs as well.
- **Corporations** with large art collections were not exceptions to these trends. They, too, sought to reduce premiums and like all other commercial buyers of insurance, entertained reductions in loss limits and increased deductibles to achieve savings. As in many prior years, risk managers for corporations sought premium credit for the implementation of various risk management techniques such as improved security, updated valuations with more current appraisals and other improved management procedures.

Each of these trends led to less insurance coverage being purchased; mid-term requests to decrease policy limits became more frequent; fewer transit exposures were realized and therefore, less additional premium revenue was seen throughout the year. Lastly, business closures also increased in 2009 and some insurance buyers chose to self-insure for the first time. One benefit of this downturn in insurance buying was the decrease in claims frequency as a result of transit, traditionally the most common cause of loss.

**CATEGORIES MOST SENSITIVE TO TODAY’S RECESSION**

The categories of artworks which appear to be most sensitive to the current recession are the categories which have been prone to speculation and to huge escalation in ‘sold’ prices prior to the 2008 financial crisis. The most sensitive categories have been Contemporary Art and Impressionist and Modern Art.

During the years preceding the downturn, prices for sold art in both the auction and private gallery marketplaces had escalated considerably, and in many instances these escalations outpaced price increases for investments in the financial markets.
Whether this escalation was a true bubble or not is uncertain; what is certain is that it was ready to burst, as had been foretold by many analysts, and this happened in the fall of 2008.

**CATEGORIES WHICH APPEAR TO BE WEATHERING THE STORM**

Not all general categories of collecting have been subject to an aggregate deflation of sold prices. Some categories have maintained their price structure during this turbulent financial period and other categories have continued to grow.

The market for Old Master Paintings which has grown steadily during the past decade continues to grow today. Increases in prices for most works may not be dramatic but they have been slow or steady.

The market for Asian Art has also grown. Perhaps this reflects the fact that there are many new buyers from countries such as China who have not suffered financially over the past year and who still have a desire to acquire works of art of high quality.

During times of economic unrest, jewelry sales tend to do well. This may be due to the fact that such assets are truly portable and there is always a significant demand for them. Current auction sales have been particularly strong.

**ARE ALL WORKS OF ART WITHIN A “SENSITIVE” CATEGORY SUBJECT TO DEVALUATION?**

The fact that a specific category has been subject to general devaluation in sold prices due to questionable general financial conditions does not necessarily mean that all works of art within that category have been or are subject to the same devaluation.

Works of art are not commodities and are not subject to blanket factors of devaluation. Each work of art deserves to be looked at for its own specific strengths or weaknesses.

As a general rule, during hard economic times when the art market becomes more critical and less expansive, works of art that fall in the so-called “middle market” are the first ones to suffer. These are works which may be attractive and desirable but are not unique or exceptionally special. In other words, if a collector feels that another similar and like piece could easily be found again, the chances are that a prospective purchase in hard economic times may be deferred to a future date when the economy is stronger.

On the other hand, if potential buyers were to feel that it would be highly unlikely that a
similar work will be found in the future, then the market for a unique or extremely special work will continue to be strong.

Examples of this phenomenon can be seen during the worst periods of the current economic downturn. During the fall of 2008, a Kandinsky painting brought the exceptionally strong price of close to $17 million at auction. This was the second highest price for a work by Kandinsky to be sold at public auction.

And, in the spring of 2009 during another season of weak auction sales, a small Mondrian painting with noticeable condition problems sold for over $9 million at auction, far surpassing its high estimate of $4 million.

Moreover, if a whole category of works of art is viewed by the collecting public as extraordinary or “never to be seen again” then caution may be thrown to the wind and the market may respond as though an economic crisis did not exist.

In September, 2008, on the eve of the collapse of Lehman Brothers, Sotheby’s, London held a monographic sale of works by the contemporary artist Damien Hirst and achieved an auction record for a single owner sale of close to $300 million.

In February 2009, during a worsening economic downturn, Christie’s surpassed the Sotheby’s record when it sold the collection of Yves Saint Laurent for close to $500 million. It would appear that collectors believed that they would never see sales like the Hirst and Saint Laurent auctions again and wanted to be participants despite bad economic times.
POLICY

The above overview, hopefully, will indicate that it is extremely questionable to apply generalizations to the art market, even during times when aggregate sales would seem to expand or contract across the board.

The art market does not function in the same way as financial markets because the works of art which are bought and sold are individual items and not general commodities.

However, an insurance carrier or broker can look for general characteristics when reviewing a client’s portfolio. Clearly in hard economic times neither the client nor the insurance company will benefit necessarily from having a scheduled item on a policy which has been overvalued. The client will pay an inflated premium and the carrier will have to compensate the client an unjustified amount should there be a total loss.

Consequently it is in the interest of both the client and the carrier to review the fine arts schedule carefully when a general contraction of the art market has been noted.

Specific considerations of such a review should include the following points:

- Does a specific work of art belong to a category of collecting that is subject to a current market correction -- such as Contemporary Art or Impressionist and Modern Art?
- Are the works of art on a schedule unique or extremely special or do they fall in the middle areas of collecting?
- Does one have reason to believe that the condition of the scheduled objects has changed? During hard economic times, the art market may be more critical of works of art in compromised physical condition.

Such factors should be examined and analyzed in light of new general market conditions.

In order to perform such a comprehensive schedule review, the carrier or the client may require the services of a professional appraiser. Consideration should be given to this especially when general market conditions have changed.

PROSPECTS FOR THE FUTURE: HOW OFTEN SHOULD A POLICY SCHEDULE BE REVIEWED IN TODAY’S MARKET ENVIRONMENT?

While it is hard to generalize, a safe rule to follow is that policy reviews should be mandated by the category of scheduled items on a policy and general market conditions. In a period of market retrenchment, such as the situation at present, it is especially
important to review an insurance schedule carefully.

During normal times, most art professionals agree that schedule reviews should take place every 3-5 years depending upon the type of works on a schedule.

Volatile categories such as Contemporary Art may merit more intense or frequent scrutiny depending upon which artists appear on the schedule.

Upon occasion special categories of art or collectibles may require very frequent re-examination. For example, during the 1980s silver was subject to great market speculation with the melt-down value rising as much as five times in less than a six month period. At that time, many insurance companies were requiring frequent re-examinations of policies with silver collections.

As a general rule, insurance professionals and clients should keep abreast of developments within the art market and be aware of what would appear to be volatile or anomalous situations.

If this is perceived to be the present, it may be time to consider a schedule review.

**CURRENT/EMERGING HOT TOPICS**

Outside of sale values and appraisal issues, one of the biggest changes on the horizon is the Transportation Security Administration [TSA] mandate that beginning on August 1, 2010, all items shipped as cargo on commercial passenger airlines [estimates are that as much as 20% of art shipped around the world moves this way] will have to go through TSA airline security screening, or be packed by a TSA approved entity. For more information on this issue, see the February 2010 IMUA Newsroom Article entitled “NEW RULE ON CARGO IS SHAKING THE ART WORLD” or visit the Transportation Security Administration website [www.tsa.gov](http://www.tsa.gov) and search for their list of licensed packers said to be made available later in 2010.