The real alternative investment – tangible passion assets

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Profitable passions, from arts to wine

Scarcity drives the markets for luxury assets

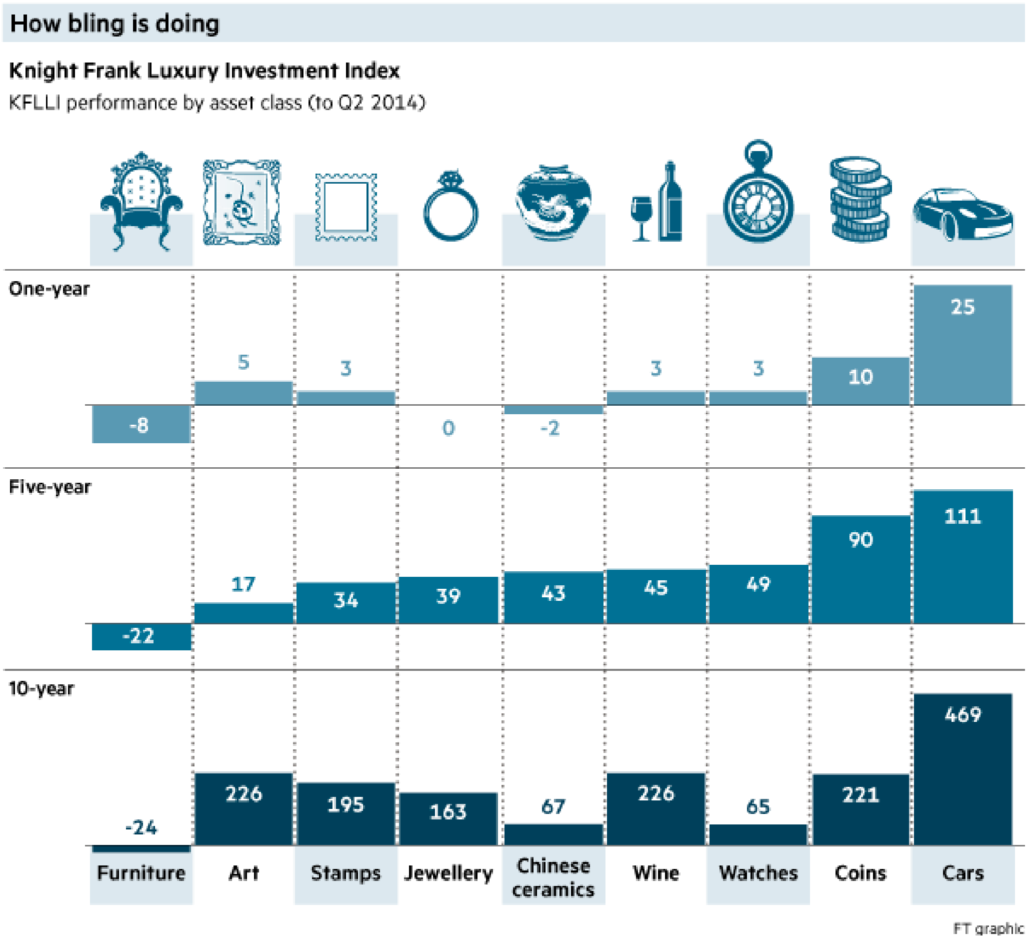
On the final day of the 20th century, the FTSE 100 index of leading UK shares set a record, closing at 6,950.6. Almost 15 years later, it has still not retaken that level. Last week's bout of market volatility unwound a year of gains. It's against this background that interest in so-called "passion investments" – tangible assets such as art, cars, stamps, wine and coins – has increased strongly.
Global sales of art and antiques reached €47.4bn in 2013, close to the record high of €48.1bn in 2007, according to the annual art market report by the European Fine Art Foundation.

The financial crisis took its toll in 2009, causing sales to plunge to €28.3bn. But the market staged a rapid recovery driven by Asian buyers, bouncing back by 52 per cent in 2010 to €43bn.

Prices have also been buoyant. Knight Frank's Luxury Investment Index tracks the prices of nine such passion investments. It has risen 182 per cent in the 10 years to June 30 2014, easily outpacing the 51 per cent gain in the FTSE 100 over the same period. A similar index compiled last year by Coutts, the private bank, tells the same story.
Some components of the indices have risen by even greater amounts. Topping the Knight Frank index over one, five and 10 years are classic cars – as measured by the Historic Automobile Group indices. Other strong performers include art, wine and coins (see graphic).

Drivers of performance

Why have such asset classes performed so well? An obvious factor in almost all cases is scarcity. The supply of Ferrari 250 GTOs, Van Goghs and penny blacks is finite, and very limited. The supply of Château Lafite wine is at best constrained.



The relative wealth of "baby boomers" in the west is also a factor, especially away from the very top end. Paul Jason, who runs The Motorcycle Broker website, says he is getting plenty of enquiries from people in their fifties who may have ridden motorbikes when they were younger. "They've paid off their mortgages, the kids have left home. Their money's not working in the banks and they can see the prices of classic bikes have gone up a lot," he says.

Demand is growing fast in the emerging world, too – from Russian oligarchs to Chinese entrepreneurs.

"Geographically, it's difficult to differentiate. There may be collectors from emerging markets but they act through established channels in Europe and North America because there is often no classic car infrastructure in emerging markets," says Dietrich Hatlapa, the founder of HAG. Its indices track the prices of 50 different classic cars, and rose a staggering 47 per cent in 2013.

"China was a real game-changer for fine wine," says Nick Martin of the Wine Owners Club. "It was a very new market, very immature and very brand-driven. Buyers were fixated on a small number of top, iconic brands."

Ultra-loose monetary policy is helping too, thinks Mr Hatlapa. "Global liquidity flows and central bank policies have been big drivers. That is definitely something to watch in future," he says, referring to the increasing talk of policy tightening and the end of quantitative easing in the US. The increases in HAG indices this year have been much more modest.

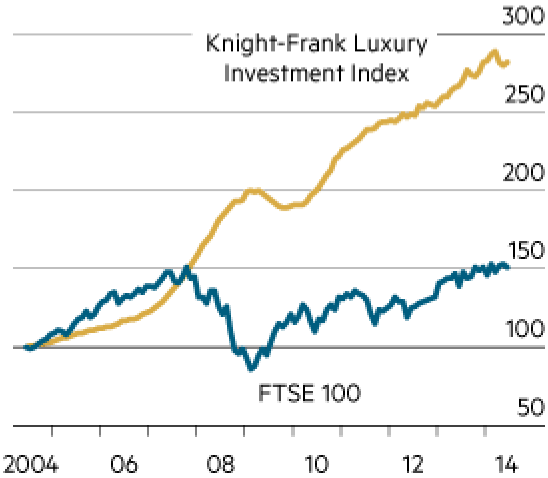
But passion investments are also a lifestyle choice, and it is maybe no coincidence that the investments which have done best are those which are easiest to show off to others. "You can have a lot more fun with a classic car than you can with a stamp collection," points out Andrew Shirley, the researcher who compiles the luxury index.

How the model works

- The Knight Frank Luxury Investment Index tracks the performance of a theoretical basket of selected collectable asset classes using third-party indices
- The indices for art, Chinese ceramics, antique furniture, jewellery and watches are calculated by Art Market Research & Developments
- The indices for stamps and coins are calculated by Stanley Gibbons
- The indices for classic cars are calculated by Historic Automobile Group. They are published monthly
- The indices for fine wine are calculated by Wine Owners; prior to 2014, Knight Frank used the Livex 100, which was more biased towards Bordeaux

Luxury as an investment

Indices (rebased)



Sources: Knight Frank Research; HAG; Stanley Gibbons; Wine Owners; Art Market Research & Developments

"It's partly a lifestyle thing," acknowledges Mr Hatlapa. "Participation in classic car events and even competition is an entry ticket to that lifestyle."

Inexact comparisons

Comparing the prices of such tangible assets to the likes of shares and bonds is far from an exact science. A share in Vodafone confers exactly the same rights upon its holder as each of the other 26bn shares in the telecoms company, but alternative assets are inherently unique.
There's no such thing as the art market – there's just a lot of individual paintings
- Melanie Gerlis, art market editor for the Art Newspaper

Melanie Gerlis, art market editor for the Art Newspaper, says: "If one work by [Piero] Manzoni sells for $20m but another doesn't sell at all, it doesn't make the average price for a Manzoni $10m. There's no such thing as the art market – there's just a lot of individual paintings."

Transaction levels are low and the various indices that track the prices of alternative assets capture only a small cross-section of the overall trade.
Auction houses provide figures on art sold at auction, but that accounts for only 47 per cent of the market against 53 per cent for unpublicised private sales. Galleries and dealers – and the burgeoning private sales wings of auction houses – have little incentive to shed light on their dealings with wealthy private collectors.

Most indices are recalculated on a quarterly or annual basis; by contrast, the FTSE 100 is computed every 15 seconds and covers all trades reported to the stock exchange.

A straight comparison of the indices also makes no allowances for the considerable costs of buying and owning alternative assets. A wine merchant will take commissions of 10-15 per cent from the seller, for instance, while an auctioneers' "buyer's premium" is typically 20-25 per cent.

Storing small items such as stamps or coins is fairly straightforward, although they should ideally be insured separately. But fine wine will require controlled temperature and humidity, certain types of art will have specific storage needs, while the cost of storing and maintaining classic cars can be very high.

Daniel Aitkenhead, a communications manager living in London, owned a 1976 Ferrari 308 GT4 for six years. "I sold it at a good profit but I reckon that I came out just about even overall," he says – the cost of garaging in the capital, plus spare parts and specialist servicing, accounted for a big chunk of expenditure. "But I absolutely loved the car."

Speculate and appreciate

Alternative assets also generate no dividend income, so all the return has to come from price appreciation net of costs.
Comparing the returns on alternatives to the returns from equities including dividends paints a completely different picture of relative performance. With reinvested dividends – something easily captured using accumulating units in a low-cost index-tracking fund – the FTSE 100 is up 50 per cent per cent since its supposed “all-time high” in 1999, and by 117 per cent in the 10 years to June 30, the period covered by the Knight Frank indices.

Changing tastes can lead to some genres outperforming others. The biggest gains in the art index have been led by modern art, then impressionist and contemporary art: the former rose by 286 per cent, well ahead of gains of 153 per cent for Old Masters over the same period. In classic cars, Ferraris were the star performers in 2013 – their sub-index gained 60 per cent – but so far this year Porsches are in the driving seat, up 24 per cent in the nine months to September.

Alternative assets are also prone to price bubbles. There was a big boom in stamp prices during the 1970s, and another one in classic cars in the 1980s. Fine French wine has become the latest passion investment to see a big speculative run-up in prices followed by a slump.

“Brokers were starting to get into speculating about which wine would be next to catch on in China, based on things like how easy it was to pronounce the name in Mandarin, or whether the son of the château owner had been on a marketing trip to Hong Kong,” says Mr Martin.

Prices shot up. A case of 2008 Lafite went from £1,800 in April or May 2009 to a peak of about £14,000 in less than three years. But it all came juddering to a halt in 2011. A clampdown on corruption and gift-giving in China, growing fears about forgeries and a couple of poor vintages – relative to the blockbusters of 2009 and 2010 – saw prices correct sharply.

Less famous French and Italian wines benefited. Something similar has happened in art; Clare McAndrew, founder of research company Art Economics, thinks the second tier market still harbours value for less well-heeled buyers, particularly in areas such as Old Masters.

“There is value in the lower tiers because people are slightly insanely focusing on a few names,” including Pablo Picasso, Francis Bacon and Roy Lichtenstein.

Lack of collective exposure

It can be difficult for investors to achieve diversification across alternative assets, in the way they would with shares or even property, because of a lack of collective investment vehicles in the sector.

In August 2013, the financial regulator banned the promotion of what it termed “non-mainstream pooled investments” to ordinary investors, having previously said that such individuals were “at particular risk in relation to inappropriate promotion”. UK-based firms may now only target clients who are “sophisticated” (defined as having extensive investment experience and knowledge) or “high-net worth” (defined as having annual income in excess of £100,000 or investable assets of more than £250,000).

For this reason, most schemes that offer exposure to passion investments tend to be based offshore and have very high minimum investment requirements.

Stanley Gibbons, the dominant company in philately, runs various stamp investment plans from its Guernsey office. They are a effectively a portfolio management service; the company’s experts acquire and store stamps on the investor’s behalf, and share in any profit when they are sold. The schemes are unregulated and not covered by the Financial Services Compensation Scheme. Plans to launch a stamp fund were abandoned.

Many wine investment products (including the FT’s fine wine club, operated by Berry Bros & Rudd), work on a similar basis. Peer-to-peer sites like The Wine Owners Club allow collectors to sell to each other at lower cost than dealers or auction houses. The Count of Custoza Family Office runs a Classic Car Fund allowing investors to own a share in a collection of vehicles. The minimum investment in the Liechtenstein-managed entity is €10,000, there is a 5 per cent subscription fee, 2 per cent annual management charge and a performance fee too. It hasn’t been triggered because despite the performance of the HAG indices last year, the fund is only up 3.7 per cent since inception in September 2012.

The Fine Art Fund currently has no funds open for subscription, but previous offerings have had similar charging structures to the Classic Car Fund. The group, run by ex-Christies finance director Philip Hoffman, also runs an art advisory service.
Sometimes, individual shares can be a proxy for the returns on alternative assets. Stanley Gibbons shares trade on the London Stock Exchange, and the company is expanding beyond its philatelic heritage to become a diversified dealer in collectables. Avarae, an Isle of Man registered investment company whose shares trade on Aim, invests in coins.
Additional reporting: James Pickford

Tax breaks

Owners of cars which are more than 40 years old do not have to pay vehicle excise duty. Classic car investors are also exempt from capital gains tax (CGT) – a levy on any profit made on the sale of an asset or investment. The exclusion of vintage vehicles from CGT is shared with other possessions classed as "wasting" assets by HM Revenue & Customs. Anything mechanical is judged to have a useful life of 50 years or less, and to have little or no value after that.
Fine wine is a grey area. HMRC says that it applies the 50-year rule to judge whether wines are "wasting" assets that will be little more than vinegar after a long period. But some fine and fortified wines with long storage lives do not qualify. Where a bottle is not a "wasting" asset, any gain made on its disposal would be exempt from CGT if its value is less than £6,000 – the allowance for personal items.
This threshold also applies to the sale of paintings, antiques or jewellery. Personal chattels are not exempt from inheritance tax – unless they are gifted – but can pass to the surviving spouse or civil partner on death.
Buildings, land and artworks of heritage value may be exempt from IHT, if the owner preserves them and allows public access.
Adam Pali

Price evolution (1984-2015 in £)

Make-Model	Price 1984 in £	Price 2015 in £
Porsche 911 2.4 T	4'950	80'000
Aston Martin DB4	6'975	650'000 to 1 million
Ferrari 375 GTS	28'500	2-3 millions
Jaguar E 3.8 S1 Roadster	9'000	150'000
Lamborghini Espada	7'850	160'000
Bristol 411	6'950	60'000
Dino 246 GT	14'950	250'000
911 2.7 RS Touring	19'500	1'000'000

But reversals can be severe and last long (1989-2004)!!!

NB: The drawdown period from 1980-2008 was 15 years (1989-2004) for cars!

The Knight Frank Luxury Investment Index (Q4 2004 to Q4 2014)* Luxury asset

Luxury asset	Price Growth		
	12-month	5-year	10-year
Cars	16%	140%	487%
Art	15%	61%	252%
Wine	7%	38%	234%
Coins	13%	92%	232%
Stamps	3%	34%	195%
Jewellery	2%	35%	168%
Coloured diamonds	2%	73%	167%
Chinese ceramics	9%	46%	69%
Watches	4%	49%	68%
Furniture	-9%	-25%	-28%
KFLII**	**10%**	**62%**	**205%**

Sources: Art Market Research (Art, Watches, Furniture, Jewellery, Chinese Ceramics); Stanley Gibbons (Stamps, coins); HAGI (Classic Cars); Wine Owners (Wine); Fancy Color Research Foundation (Coloured diamonds).

* Except coloured diamonds (Jan 2005 to October 2014)

**KFLII is weighted based on the contribution of each component