ART MARKET VS. PREDATOR

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Soon after finishing art school in 2011 Lucien Smith, an American artist, started to get rave reviews. By February 2014 there was such a buzz that when “Feet in the Water” came up for sale Phillips, an auction house, thought it would sell for £40,000-60,000 ($63,000-95,000). Instead it went for £194,500. Two days later another painting with a £60,000 upper estimate sold at Sotheby’s for £224,500. By March Christie’s had re-evaluated Smith’s prices: “Love Story, a Woman Under the Influence”, now had a top-end estimate of $150,000. The painting sold for $233,000. Smith was on fire.

Two years on things are different. On June 28th, “TBT”, a work from a series of “rain paintings” – abstracts gesturing towards precipitation – that were selling for close to $90,000 (then around £56,000) in New York in 2014, went for a little over £30,000 in London, a drop of almost 45%. But this was a good result. Smith’s paintings now tend to be estimated at £10,000-15,000 ($12,350-18,500), and go at the lower end.

Smith is not the only young artist whose work has been subject to this sort of volatility. In 2012 the prices of work by a group of painters, mostly men under the age of 35, started to rocket. By 2014, they were superstars: paintings by David Ostrowski, Parker Ito, Dan Rees, Jacob Kassay and Hugh Scott-Douglas reached prices of between $100,000 and $245,000. In 2016 none hit six figures, with most pieces selling for under $30,000.

Many in the art world are worried about bubbles. The market, they say, is becoming too fast, and too short term. They have reason to fret. The price swings for these artists – rises and falls of 500% or more in less than two years – make this market more volatile than even the most turbulent financial ones. Mini-crashes are becoming more common. They risk doing both financial and creative damage to the art world – financial, because it could put off serious, long-term investors; creative, because artists burn out before they really get started.

The blame for this is directed at a new breed of art dealer, known as “flippers”. In contrast to a traditional dealer, who may stay with an artist for a lifetime and keeps tight control over who buys his work, flippers buy low and sell high to anybody who will buy. They treat art as though it were a financial instrument.

The man accused of leading the charge is Stefan Simchowitz. He was the first buyer of a Lucien Smith rain painting, snapped up early works by Parker Ito for less than $750 and was an early champion of Oscar Murillo, a current superstar.

If Simchowitz’s nose for success is impressive, so is the hatred he inspires. He has been likened to Michael Milken, an inventor of junk bonds and convicted fraudster; he has been called a Sith Lord and Satan. The complaint is that he is a short-termist, prioritising quick profits over sustainable sales. He is accused of buying too greedily: cornering the market early by snapping up much of a young artist’s catalogue (he bought lots of work by Murillo early and cheap) before flipping the work to collectors who are themselves seeking profit rather than good art.

Simchowitz has been a Hollywood producer (his films include “Requiem for a Dream”) and has started and sold a tech company (MediaVast, a photography site, was bought by Getty Images for around $200m in 2007). He studied economics at Stanford, lives in Los Angeles and his partner is an ex-model. His clients include the young and famous, such as Orlando Bloom and Sean Parker. A South African by origin – he was born in Johannesburg and moved to America as a boy – Simchowitz is as Californian as they come.

He does not try to fit in. The standard art-world look is three parts Mayfair financier, one part literary agent: close-cut blue suit, crisp white shirt, brogues or moccasins, horn-rimmed spectacles for a hint of bookishness. When Simchowitz wears a suit it has a French-smock-style jacket; his camera is always around his neck, a lopsided beanie hat on his head. At a Christie’s evening auction where I saw him in action, he wore a long grey cardigan, half-mast harem pants, and far-from-fresh running shoes that started life orange. He wants to stand out, and he does.

The criticisms of him, he maintains, are “bullshit – not an exaggeration of what I do but a complete misunderstanding of what I do". As he talks – quickly on the phone, and even faster in person – his world view pours out. It is clear, clever and controversial. To understand both the failings of the art market and how he wants to change it, he says it is helpful to look at the writings of his two favourite economists.

The first problem, he says, is elucidated in "Four Quadrants of Stupidity", an essay by Carlo Cipolla. "Stupidity", for Cipolla, has nothing to do with education: it is about the effect you have on yourself and others. People who make both themselves and others better off Cipolla calls "intelligent". Those who enrich themselves by impoverishing others are "bandits"; people who endure losses to help others profit are "helpless". There is logic to all of these forms of behaviour, Cipolla argues. But the final group is the biggest, and makes no sense: most people make both themselves and others worse off. They are plain "stupid".

Portrait of the artist as the coming man

Lucien Smith at his home in Claverack, New York, in 2012

The essay is obscure and wacky. But the basic idea, and a problem Simchowitz often returns to, is one that does have strong currency. Economies can end up in lose-lose situations when people take decisions that are bad for themselves and for the group as a whole. Herd behaviour – mimicking others' actions – is a good example. In the "paradox of saving", collective thrift means that shops are starved of spending and a recession ensues, which hurts everyone. Simchowitz thinks the art world is like this: filled with bandit insiders who gain at others' expense, or stupid copycats who believe that price and value are the same thing.

Simchowitz says he wants to make the art world more “intelligent”. His plan is based on his second big influence, the notion of “creative destruction” set out in Joseph Schumpeter’s book “Capitalism, Socialism and Democracy”. The idea is that true capitalist competition is much more radical than charging lower prices or providing a better service. It is about completely changing the way things are done – setting up new types of firm that revolutionise the way industries operate. Simchowitz dislikes the art-world hierarchy, which he thinks excludes people from buying art; he would like to dislodge it and make art easier to see and buy. In doing this he positions himself as the art market’s version of Travis Kalanick, the founder of Uber – the disruptor of a staid, closed and uncompetitive industry.

Over the past 30 years art has become an important asset class, outpacing other so-called “alternative” investments like fine wine or classic cars. Total sales were worth $64bn in 2015 according to a recent report by Clare McAndrew, an art economist. This makes the art economy bigger than Luxembourg’s. While China has emerged as an important player, two-thirds of all sales take place in Britain and America.

In the past, the art market has tended to shift slowly. In the 1980s impressionist and post-impressionist painting dominated, with sales of work by Cézanne, Monet and Van Gogh leading the way. Modern art, roughly defined as work by those born between 1875 and 1910 (Pablo Picasso and Alberto Giacometti, for example) started to become more popular, but it wasn’t until after the turn of the century that it took the top slot.

Things changed after the 2008 crash. At first, all types of art bounced back strongly. But in 2011 the markets for old masters, impressionist and modern art all stagnated, while contemporary work – by artists born after 1910 – shot past its pre-crisis peak. In 2015 sales of work by the three artists – Francis Bacon, Andy Warhol and Cy Twombly – who top the contemporary list were worth around $1bn at auction alone. By 2015 the contemporary-art market was 340% its 2009 size, accounting for close to 50% of industry revenues.

The rise of contemporary art has created new opportunities. A collector will rarely get a Warhol or Bacon for a bargain: the long-term value of these pieces is known, and is already priced in. But according to McAndrew, 90% of contemporary-art auction sales are for artwork under $50,000, with 45% under $5,000. It is here that tomorrow’s stars are to be found – and “flippers” can make a killing.

The flippers’ technique is what economists call “arbitrage” – spotting and exploiting large price discrepancies between markets. These arise because art is bought and sold in three distinct ways.

New work is sold by the main gallery that represents an artist. This is the “primary” market. Some sales happen at the gallery; around a third happen at art fairs like Frieze or Art Basel. Prices are rarely displayed, but you can ask for a list. These agents do more than display and sell work: they store and conserve paintings and manage loans to public galleries and museums. They research the market, publish books and handle journalists. They also try to control who buys – a museum (very good), a long-term collector (good) or a flipper (bad). For these services a gallerist takes a big slice of an artist's primary-market sales, 50% being the norm. Gallerists deal too, but their main function is as long-term supporters of their artist's career.

After its first sale an artwork can be traded on the "secondary" or private market. This is a murky and opaque place. Buyers and sellers rarely trade directly, but via a web of intermediaries. For a significant piece of work there can be three or four links in the chain, says Heather Flow, a New York-based art adviser. This is because information is scarce. There is no public register of who owns each piece of art, and where sales are driven by death, debt or divorce, discretion is valued, so finding a painting for a client can be hard. Gallerists deal in this market too, buying, selling and acting as middle-men. Here the commissions are lower, at around 5-10%, with each person in the chain taking a slice.

The final option – buying and selling at auction – is the polar opposite of the private market. Auctions are public and transparent. Everything that is up for sale is put on display, and heavily advertised ahead of time. Detailed lists of results are published soon after each auction, and put on the internet where anyone can access them. All this free information means auctions are the art economy's focal point. Dealers call them the industry's thermometer, benchmark and beacon.

Auctions used to be dull affairs, mostly attended by dealers. Now they can be high drama. The room is packed with oligarchs, their bejewelled wives, hangers-on, photographers and journalists. Conversation bubbles, prices rise fast, bidders – often going for just one piece – have little time to think. A sudden surge in a price will elicit cheers from the crowd.

The big names of the art world mostly operate in two or all of these markets. The business's most respected figure is probably Iwan Wirth. He and his wife Manuela Hauser were jointly ranked 1st in *ArtReview*'s list of art-world power and influence in 2015. He is primarily a gallerist, who is also an active dealer in the secondary market, buying and selling works of artists he represents, and those he does not. The profits he makes as an intermediary allow him to fund challenging and risky work. The two roles he plays are symbiotic: the dealer is cross-subsidising the gallerist.

Wirth, who has galleries in Zurich, London and New York but is based in Somerset in the west of England, has a reputation for supporting ambitious and (initially) uncommercial artists, such as Martin Creed, who won the Turner prize in 2001. He is credited with raising interest in Louise Bourgeois, whose eight-legged spider-like structure filled the Tate Modern's turbine hall when it opened in 2000.

Simchowitz occupies the opposite end of the respectability scale. He does not own a gallery and represents just one artist in the primary market. The vast majority of his activity takes place, and profits are made, in the secondary and auction markets. He is not just the most talked-about player in the art market these days, but also one of the most active. At a recent London auction he was upfront alongside the powerful Nahmad family, outbidding them in a £2.6m purchase of Jean Dubuffet's "The Rural Life" – just one of a large number of pictures he bought.

He also scours small galleries and degree shows for new talent. He was an early investor in Oscar Murillo, buying more than 60 paintings – half for himself, half for clients – often for less than $5,000, since 2011. Today, Murillo is an art-world darling. Represented by David Zwirner, one of the most powerful gallerists, his paintings sell for $200,000 or more. Simchowitz's early investments in art by Sterling Ruby and Tauba Auerbach (both now sell for $500,000 or more) will have done even better.

Simchowitz holds on to some of what he buys. His personal collection runs to over 1,000 artworks and he tends to display as much as possible. A dealer describes being astonished by the quantity of art on the walls in a New York townhouse he had been renting. But his mission is to sell, and his method is novel.

Gallerists tend to talk about "placing" rather than selling pieces. Customers are selected according to their behaviour and their status. The collectors with a reputation for holding on to art are favoured. Those that sit on boards of museums are the most cherished. The idea is to put the work in the hands of someone whose ownership increases the value of the art. These are not Simchowitz's target customers. "They don't care about art. They care more about what table they get at the museum, whether they get Table 1 or Table 2, since this defines their importance in the social structure in which they envelop themselves."

Art-world influence

Iwan Wirth in the frame

Once Simchowitz owns an artist's work, he promotes it hard on Facebook and Instagram. For interested buyers, he is easy to get hold of (his website lists his personal email and phone number). A recent operation at ICM Partners, a Los Angeles talent agency, illustrates his determination to open up the market. He was initially commissioned to buy a few works of art for Ted Chervin, one of the senior partners. Instead, he persuaded Chervin to let him take over the walls of the whole company, installing 400 paintings by 90 artists. This makeshift gallery, which he called Museum 2.0, led to sales not just to senior partners, but to junior ones too. Some of the youngest assistants got great art on their walls, and have asked Simchowitz about collecting. All this should "expand the gene pool" and broaden access to culture, he says.

Simchowitz's boast is that he is bringing new people and money into the market. He has no truck with the way galleries discriminate between customers. "Someone that buys and holds art is seen as a good collector, and influential. Look at the lists of influential collectors: they are just billionaires who will never need to sell. Meanwhile the collector who stretches to buy art and later needs to sell to fund his kids' education is seen as a bad collector. It is extremely alienating to anyone that is outside the system."

His critics complain that he is attracting not long-term investors but flippers like himself – short-termists who are prepared to dump art at bargain prices, often using the losses thus incurred to reduce their tax bill on other profit-making investments. The rise of online auction sites such as Paddle8, where the world can watch unwanted art being offloaded, sharpens critics' concerns about what the likes of Simchowitz are doing to the market – and to art.

Rising star

Oscar Murillo shows off his work

David Ostrowski, like Lucien Smith, was a star in 2014.Vice called him the "golden boy" of abstract painting. He was hanging out with Heidi Klum. Everybody wanted him at their parties. His auction prices were, on average, more than twice his primary-market prices, according to ArtTactic, a consultancy. The same happened to other young painters' work.

The upside of this price gap is that it provides evidence that a gallerist knows what he is doing. Trusted clients are pleased to see that the work they bought in the primary market has appreciated in value. The downside is that a gallery's grip starts to slip: whereas galleries control the primary market and can influence the secondary one, auctions are a free-for-all.

When the opportunity arises to buy a work, sell it immediately at auction and make a profit, trust evaporates. So gallerists, who know the risks of fast-rising prices, conduct background checks worthy of the security services, digging into a client's history, network and record for buying and selling. Anyone suspected of flipping is put on a blacklist. In response, dealers like Simchowitz use intermediaries to buy art. It is so hard to tell what is going on that some London galleries are wary of selling to anyone based in Los Angeles.

A sudden price surge may affect not just the market but also the goods. It is hard to look through Lucien Smith's catalogue and conclude that early financial success has not influenced his work. He has produced 600 pieces since 2010 – more than two a week. There are hundreds of the once-popular rain paintings.

Higher prices tend to raise an artist's output; at the same time, gallerists sitting on a pile of paintings may be tempted to cash in too. As all parties – collectors, flippers, artists and gallerists – move in the same direction, more art comes to market.

Rocketing prices bring greater scrutiny. Art-world coverage of Smith, Ostrowski, Rees and Kassay started to sour. At first, it was gentle jibes: calling their technique "MFA Abstraction" (a reference to the Master in Fine Art degree, and a dig at their age) or "Crapstraction". But the high prices of early 2014 turned up the heat. In April, Walter Robinson, an artist and art critic, described the work as "Zombie Formalism". The name stuck.

Once the movement had a name, critical bile poured out. Some accused the Zombie Formalists of mimicry: one critic took photographs of rows of paintings to show how similar they were. Others claimed they used processes in place of ideas: Smith sprays pigment with a fire extinguisher; Kassay silver-plates canvases; Rees uses Artex (decorators' material) in place of paint. Worst of all was the accusation that the work was made to be smartphone-friendly – that the Zombie Formalists were pumping out large (but not too large) portrait-shaped paintings that looked good on Instagram to please interior designers and their hedge-fund clients.

And so the crash came. According to Artnet, an art-market website, of five paintings by Kassay recently consigned to auction, one sold for $25,000 and four failed to sell. In November 2013, one of his pieces went for $317,000. Ostrowski's high-water mark was in July 2014, when a work sold for $293,000. In October 2016, a work estimated at $20,000-30,000 sold at auction for $18,750. His primary market prices are about twice that. The reversal of the gap between gallery and auction prices means that many collectors will be sitting on a loss – something which can damage an artist's reputation irreparably.

Busts always hurt, but they are particularly bad for young artists. The case to fear is that of Anselm Reyle, now in his mid-40s. Ten years ago he seemed unstoppable. He was selling for over $500,000 and getting rave reviews. He was backed by Larry Gagosian, the biggest dealer. But his collectors were burned in the 2008 crash, and he has not bounced back.

A quick turnover

Stefan Simchowitz holding test prints of works by Petra Cortright

The art market, says Wirth, is like salmon fishing. A good fisherman knows the technique for catching a salmon – the right line and fly for the conditions on the river on that day. Yet since salmon do not actually feed in rivers, but in the sea, no one really knows why they bite at the fly. Similarly, says Wirth, people don't need art in the way they need food. But sometimes – inexplicably, unpredictably – they want it.

For gallerists like Wirth, patience is key to success. Even exceptional fishermen can have days without a bite. The market often gets things wrong: it sets young artists on fire and watches them burn out while ignoring other, better work. That's increasingly true as volatility rises. All the more important, then, that gallerists hold their nerve, stick with artists they believe in and cultivate long-term relationships with collectors.

For Simchowitz, this way of operating is elite, unhealthy – and in retreat. In part thanks to his efforts, he believes, the market is opening up. More players and more trading mean prices are increasingly fluid. Volatility is helping create a "healthy ecosystem" and undermining the pernicious notion that "things are relevant only when they are expensive".

In this sense, the vagaries of today's art market contain a lesson that everybody, including economists, should learn – that price and value are different things. Bad art can make a pile; good art can fail to sell. Volatile prices can reward people richly in the short term, and destroy them in the long run. For Iwan Wirth volatility is something to manage. For Stefan Simchowitz it is something to embrace.