

Highlights from the Art Decentralized Conference during Art Basel 2018 in Miami

Art Basel, Miami

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Executive Summary

On December 6, 2018 Bluesky Capital was invited at the Art Decentralized conference during the Art Basel week in Miami to discuss the application of blockchain technology, in particular tokenization, to the art industry. The following key takeaways emerged:

- Tokenization has the potential to attract lots of interest in the art industry as an investment in a new asset class in terms of portfolio diversification
- A regulatory framework needs to be developed to define what a token represent on a legal standpoint and provide more investment confidence for accredited and institutional investors
- Art owners will be able to liquidate portions of existing collections through tokenization
- Accredited investors will be able to invest in art funds who invest in tokenized art and achieve exposure to art as an uncorrelated asset class compared to equity and fixed income

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Key Takeaways from the Conference

Below are the key takeaways from the conference.

1. What are the mechanics of tokenizing something like a piece of art?

Tokenizing a piece of art consists in creating a dividing the ownership of a piece of art in multiple pieces through the issuance of a token linked to that piece, which is then purchased by multiple investors. This process is equivalent to an equity investment in a company, where multiple investors buy different shares in a company.

2. What are the benefits of tokenization for art?

This technology has several benefits and opens up new opportunities in the art space, among which:

- Portfolio diversification: it is now possible for accredited investors who want to invest in art as an asset class to buy a fractional ownership in a multiple pieces of art and achieve exposure to art as an asset class in an optic of portfolio diversification
- Liquidity: tokenization creates liquidity in an illiquid asset class since a piece of art can be easily traded on an exchange through a token
- Financing for artists and museums: owners of works of art, including art galleries, museums, and private owners can obtain financing for their existing art pieces and which can in turn be used to expand their collections

3. Does the blockchain technology guarantee the authenticity of a piece of art?

The technology itself does not guarantee the authenticity of a piece of art itself, which is a work that still needs human experts at the beginning. The blockchain technology in fact only allows the storage of the information regarding a piece of art, such as its provenance, author, etc., on multiple databases (ledger). If the initial information stored in the blockchain technology is misleading or counterfeited, all the subsequent records stored on multiple computers will be as well. This is a process analogous to garbage-in garbage-out (GIGO). On the other hand, once an initial expert has validated that a piece of art is actually authentic and has stored that information in a ledger, it is very difficult to tamper that information.

4. What are the legal aspects of tokenization for works of art?

Tokenization is a new technology, so regulation still needs to keep up with it. Most likely tokenizing a piece of art and selling it to multiple people as an investment configures in a similar way to an equity share in a company, so it will probably fall under security laws and be regulated by the SEC.

5. How can investors buy tokenized art now?

Since selling tokenized pieces of art is similar to an offering of securities, in the United States they are usually conducted as a private offering to accredited investors under the exemption of Rule D. Another possibility is to invest in an art fund, which pools money from multiple investors with the purpose of getting an exposure to art as an asset class of to generate a return above a specified benchmark in the sector.

6. Can retail investors buy tokenized art?

For now it is difficult for retail investors to participate in tokenized pieces of art mainly because of a lack of regulation in the sector and absence of art exchange where tokens can be freely traded. It is possible that in the future, when both regulation and technology will develop for this sector, retail investors will be able to own a fraction of an expensive piece of art like a multi-million dollar Picasso painting by freely trading them on exchanges or investing in an art mutual fund.

7. What do the artists say?

Currently artists are happy about the technology since it provides an alternative way to monetize their works of art and potentially sell their works directly to consumers, bypassing galleries, art dealers, and auction houses. It is important to underline that the greatest reward will be probably taken by famous artists who sell pieces worth millions of dollars, since the process of tokenizing and monetizing a piece of art as a form of investment makes sense only for expensive works.

8. Will institutional investors invest in art as an asset class?

We believe that the great potential offered by tokenization to create liquidity in an illiquid asset class, the low correlation of art as an asset class compared to equity and fixed income, and the low returns delivered by traditional asset classes will potentially attract substantial interest from institutional investors in art as an asset class in an optics of portfolio diversification.

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