Collector Car Funds: Is this the Next Market Development?

We should all bear in mind what every financial prospectus reminds us: past results are no indication of future performance

1953 Bentley R Type Continental

Those who follow financial markets are familiar with the specialized investment funds that concentrate exclusively in collectible assets, such as art and fine wine.

A new development for 2011 is specialized funds that will invest solely or primarily in those assets closest to our hearts—collector cars. This past winter, plans for two such funds were launched In Europe.

The Classic Car Fund

The first to announce was The Classic Car Fund, launched by a team led by Swiss-based enthusiast and financial expert, Filippo Pignatti Morano di Custoza. It is headquartered in Liechtenstein, a tiny, financially-oriented principality that adjoins Switzerland, where di Custoza's family office will manage the fund.

The unit of investment of this open-ended fund is 20 Euros ($29), with a minimum investment of 100 Euros ($145). The plan is that these units can be traded and encashed on the Hamburg Stock Exchange. As of early June, di Custoza told me that the fund has not yet reached its initial capital-raising target of 5 million Euros ($7.3m). When it does, the fund will start buying "certain high-quality, rare and historically relevant vehicles."

The managers plan to invest roughly 70% of the fund's available cash in classic automobiles, although exactly what era, type and value of cars are not specified. Five generic classes of collector car are listed on the website (www.theclassiccarfund.com).

A little stardust

Indications show that the fund will invest only in the highest-quality cars. Photographs on the website show a Jaguar E-type, post-war Bentleys, and the 1962 Le Mans-winning Ferrari 330 TRi/LM. The Ferrari is included as an example of a car whose value has increased strongly in the past—rather than as an indication of what the fund hopes to acquire.

The balance of the fund will be invested in a mixture of cash deposits, money market funds and the securities of companies in the automotive field; all of which is intended to provide the managers with the liquidity for further car purchases and investor encashment.

The fund documentation states that its cars may be loaned to film companies, museums or private exhibits, and the net cash generated from these activities will enhance the financial return to the investor—and also raise the profile and value of the cars. The fund's cars may make occasional appearances at various events, to which investors in the fund will be invited (perhaps to enjoy the stardust of their cars being shown to the public).

While the cars will probably be in professional storage, di Custoza plans a "sound, smell and touch aspect," which will let investors enjoy the fund's cars. This may involve investors using a car, as long as this does not diminish its value.

The team of advisers to The Classic Car Fund includes historic racer Peter Blond and various current and past luminaries of Christie's and Sotheby's, and is mainly Swiss-based. The management fee is set at 2% per year of the value of the fund, with a further performance fee of 20%. There will be a bi-annual valuation of the fund's cars, which will contribute to the performance rating, along with buying and selling activity. Investors can also monitor progress from the daily stock market quote, which will reflect the net asset value of the fund.

The IGA Automotive Fund

The other fund, announced in January 2011, is a Guernsey limited partnership named The IGA Automotive Fund. A trio of Monaco-based British entrepreneurs and car guys, led by Ray Bellm, launched the fund. Bellm was a World Sports Car champion driver who until recently raced a Ford GT40. As is ever the case, much of the press coverage concentrated on celebrities Nick Mason and Gordon Murray, who are outside advisers to this fund. The fund will use U.S. dollars, and the plan is to raise up to $150m. A minimum of $500,000 is required to buy into this fund, although presumably a group of individuals could club together and commit their cash through a suitable investment vehicle.

One purpose of setting up the IGA Fund as a limited partnership is to try to preserve the immunity from Capital Gains Tax, which British tax resident collectors (and those in many other non-U.S. tax jurisdictions) enjoy when making financial gains on selling a historic car.

This fund is not open to U.S. investors, given the very real regulatory complications of selling financial securities to Americans. However, the principals intend this to be the first of several similar investment vehicles, and—if this first fund is a success—a similar fund will be created specifically for U.S. investors.

This will be a closed-end fund, somewhat like the traditional private equity fund. On achieving the final closing, when all accepted investors have committed their cash, the fund will be closed to further investors—except possibly where the seller of a car accepts units in the fund as part of his sale price. When the managers make a cash call on the investors (as suitable purchases are identified and secured), the investors will stump up their funds, the cars will be bought and will then be held until the managers feel the time is right to sell each car.

No flipping here

The IGA Automotive Fund will be a long-term investment, and investors will be unable to sell or encash their investment until the fund has sold its cars, and has “cashed out.” For this reason alone, this fund is for very wealthy individuals and institutions who would not go hungry if (in the worst case) the collector car market suffered a major downturn, as it did between 1990 and 1995—or who do not need immediate liquidity during the likely holding period of seven to nine years.

The annual management fee is 1.5% of the net asset value of the fund, plus a performance fee on encashment. This is like a profit share arrangement, once a minimum return of 8% compounded interest has been returned to the investors, mirroring how the private equity industry works.

The glossy IGA glossy brochure states that “investment will be limited to ‘best of class’ examples of the world’s most desirable limited production collectors’ cars, and will be diversified between make of car, unit value and usage ensuring there is diversification of risk.” To be more specific, Bellm has emphasized that Ferrari constitutes some 40% of the collector car market by value. This, and the fact that six of the 14 cars pictured in the brochure are V12 Ferraris, gives a strong indication that Enzo’s most desirable 250 GT models will feature strongly on IGA’s shopping list.

When funds permit, I would expect there to be added the odd 8C Alfa Romeo and/or pre-war Mercedes, a McLaren F1, an Aston Martin DB4GT (maybe Zagato), and a smattering of Jaguar and Porsche sports racing cars.

An interesting quote from the paperwork is that “the Fund Manager will appoint a small number of experienced individuals to identify, source and acquire vehicles within their own specialist area of expertise in the market.” Bellm has declined to say who they will be, which makes good sense—if the acquiring dealers were identified as IGA representatives, it would not make their task any easier.

The stated financial objective of the fund is that the “targeted internal rate of return is intended to be 15% per annum, net of fees and expenses.” While this may sound aggressive, a fund brochure argues that historically, high-quality cars appreciate in value at a fairly rapid pace.

If glossy investment-fund brochures accurately predicted the future, the world would be awash with billionaires. A few of my own opinions may be found in the sidebar.

McLaren F1

Car Fund Q and A

Will these two funds get off the ground, and will they soon be out there buying cars?

I believe yes for CCF, but probably at a relatively modest level in 2011.

I expect that the IGA Fund will achieve its first closing by the end of the summer. The sum committed by investors will probably be more than $82m, which would enable the managers to buy a few major cars before the year end.

Will owners be prepared to sell their cars to these purely financial funds?

Yes, I believe so. There are plenty of collectible cars out there that their owners will happily sell to a fund, including the occasional large collection whose owner would like to diversify into cash or other assets. Ray Bellm told me that since they launched the IGA Fund the managers have been offered cars totaling $150m.

Will the investors get to enjoy the cars owned by their funds in any manner?

Probably not, in the sense of an investor borrowing the fund's 300SL Gullwing for the weekend, as the insurance and administrative downsides of such a system would surely outweigh the rental and/or goodwill benefit to the fund. The most that an investor should expect is senior bragging rights while stroking the radiator cap of the fund's prize exhibit at a Villa d'Este champagne reception.

Will the anticipated gains in value be swallowed up in start-up, storage and maintenance costs and management fees?

This is a risk, but if values rise significantly over the fund period it should not be a major risk. The IGA fund paperwork allows for a maximum 3% commission of the initial money raised to be paid to introducing agents, which would leave the fund with 97% to invest. While this level may be a norm in the investment industry, it is steep in my view. Ideally the management fees (as opposed to out-of-pocket outgoings) should be back-end loaded by reference to performance—and not taken along the way in large chunks bleeding the fund of cash. The costs of storage, insurance, upkeep, restoration and maintenance of the fund's cars are necessary and unavoidable, and if the value increases prove to be anyway near the historical statistics, I doubt that these costs (or indeed the management fees) will present a problem.

Are these funds a welcome development in the collector car scene?

SCMers will no doubt have their own views on this one. My approach is pragmatic. If a new factor appears in the market (love it or hate it) be prepared to get used to it. Who remembers the collector car world before "matching numbers" became an important factor? Ferrari's Classiche program attracted some criticism in its early days, but most traders will now tell you that a big V12 Ferrari that is not certified will likely suffer a discount.

Are there more car funds getting ready to launch?

I believe there are several groups or individuals who are planning—or maybe thinking about—launching a private or public car fund. Very likely they are waiting to see how these first two funds pan out. As they say in the comics, watch this space. ♦

MARTIN EMMISON is an English solicitor practicing in London, who specializes in transactions and disputes in the historic car field. He can be contacted at memmison@gdlaw.co.uk.