

**SUBMISSION TO THE NSW DEPARTMENT OF PLANNING AND ENVIRONMENT  
IN RESPECT OF THE POSSIBLE APPROVAL FOR DEVELOPMENT OF THE  
DRAYTON SOUTH COAL MINE**

**SUBMISSION BY DARRYL GUIHOT**

**BRISBANE, JULY 4, 2016**

**Preamble**

On September 10 2015 I lodged a submission (the “original submission”) to the Planning Assessment Commission of New South Wales (“the PAC”) arguing against the development of the Drayton South Coal Mine.

That original submission explained my view that an approval would lead to significant financial loss to the Hunter Valley, and to NSW, by forcing the largest participants in the thoroughbred breeding industry to relocate, with the losses consequent on that departure far outweighing the benefits of the mine proceeding.

I followed that submission with a verbal presentation to the PAC public hearings in Denman, on September 11, 2015. (A transcript is included within this submission.)

During my presentation I offered to make myself available to officers of the NSW Department of Planning and Environment (“the Department”), or to the PAC, an offer which still stands.

In late November 2015 I learned that the PAC had recommended that the South Drayton mine should not proceed, and I observed that in its published report the PAC quoted occasionally from my submission.

In May 2016, Anglo American lodged a submission with the Department seeking to overturn the PAC’s recommendation. Anglo American tendered a report which it commissioned from Mr Greg Houston of Houston Kemp, dated March 29, 2016. I have read this report, and although a lot of figures are blacked out, the gist of the report, and particularly the opinions of Mr Houston, can be followed.

Mr Houston’s report contradicts, inter alia, the advice I provided in my original submission, but it does not do so by considering and rebutting the specific matters I advised upon. In fact his report does not seem to address the main issue that I submitted will affect the industry. Mr Houston quotes some of the comments in my submission with apparent approval, and also cites my

submission as the source for some of the factual industry background in his report. But one of my comments has been paraphrased incorrectly.

Accordingly, I wish to lodge this submission to correct the incorrect paraphrasing of my comment in Mr Houston's report, and to comment more generally on his conclusions, because I believe they reflect a lack of direct experience within the breeding industry.

#### My Expertise in the Breeding Industry

Mr Houston's report is titled as an "Expert's Report", and Anglo American refer to Mr Houston as "an expert in the equine industry".

I am not being commissioned to write this submission by any party, and it would not be appropriate for me to describe my own submission as an "Expert's Report."

However, through long-term direct investment, I believe that I have greater knowledge of the breeding industry than any outside party could have, and it would be unfortunate if someone accorded undue weight to a consultant's opinions because he had been commissioned by a third party as an "Expert", when others with greater industry understanding and knowledge, and direct practical experience, were not so described.

Mr Houston's report includes a lengthy CV, which in turn includes a long list of industries in which he has experience. This list does not mention horse breeding, although it does mention horse racing. Within the detailed content there is a reference to a report prepared some years ago on behalf of certain racing clubs on the implications of artificial insemination of racehorses. I could not find any other reference to involvement in the breeding industry, and in particular, there is no indication that Mr Houston has ever owned broodmares or otherwise invested in the industry.

The question of how broodmare owners would respond to the departure of Coolmore and Darley should be a critical component of the Department's analysis, because it is the potential departure of thousands of broodmares that would cause the greatest economic harm to the region. (As explained in my original submission and at Denman.) While Mr Houston is obviously very intelligent, articulate and broadly knowledgeable, I believe that only someone who is actually invested in the industry can appreciate how the industry would be impacted by the mine presence generally, and I especially believe only a broodmare owner – that is a customer of the stallion farms – can provide a credible insight into how broodmare owners overall would react to the departure of Coolmore and Darley.

I have 45 years of contemporaneous knowledge of the breeding industry in Australia and New Zealand, and for the last 20 years of that time I have been a significant financial investor.

Since the mid-1990s, I have continuously owned a pool of commercial broodmares, and I have also owned a share in a commercial stallion. My breeding business began as a geographically diverse operation (with mares in Victoria, NSW and New Zealand) before the market dominance of Coolmore and Darley led me to base all my mares in the Hunter Valley nearly fifteen years ago. As such, I can point to a long history of making actual decisions on matters that a consultant must bring presumption to.

Over time I have evaluated the pros and cons of literally thousands of potential matings for my numerous broodmares. I am a customer from time to time of every one of the large commercial stallion farms in the Hunter Valley. I have sold yearlings at the top end of the market, but I have also lost significant sums on horses that sold for far less than production cost. In short, like all breeders, I have experienced the highs and the lows that investment in the industry produces, and I would argue that nothing provides education about an industry as much as having large sums at risk on a regular basis.

I would be happy to share details with the Department, on a confidential basis, that would demonstrate that my investment in the industry has been significant, over a long period of time.

Further, due to my long-term interest in the industry, I have an extensive library of reference materials dating from the 1960s that would have few equals in Australia. I believe that few people would have my recall and understanding of the history and evolution of the Hunter Valley breeding industry and its competitor locations in Australia and New Zealand. (The significance of this historical understanding will be apparent in several sections of this submission that compare and contrast the Hunter Valley and the wider industry before and after the arrival of Coolmore/Darley.)

#### More General Qualifications and Experience

I have not included a detailed CV itemising every responsibility I had, or every complex matter I negotiated, during a 35 year career as a senior corporate executive, as I believe those details are not as relevant as my thoroughbred breeding experience and knowledge. If the Department wishes to consider my detailed corporate CV I would be more than happy to provide it.

For good order, I will simply repeat below the highly summarised description of my professional experience and qualifications that I included in my original submission:

#### *"Business Background and Qualifications"*

*By way of introduction, I am recently retired from a 35 year career in the corporate world, including tenure as CEO, CFO, General Counsel, Director and/or Committee Chairman in a range of large companies and industries in Australia and overseas. My last long-term role was CFO of the FKP Property Group, an ASX-200 diversified property company with Australian and international assets exceeding \$4.0B at its peak.*

*My core skills are financial. I have degrees in Economics and Law (Sydney University), and I was admitted as a Fellow of the Australian Society of CPAs in 1998 for career achievements. For part of my career I was a taxation advisor with Price Waterhouse, and I was later a corporate finance specialist in Australia's then largest merchant bank, Partnership Pacific Limited. During my career I was involved in the financial and commercial assessment of hundreds of developments, acquisitions, project financings, company valuations or industry studies.*

*I worked within or advised to the resources industry for about 25% of my career. Ironically, in the very early 1980s I was part of the Corporate Planning and Finance Team at my then employer (Esso/Exxon) which analysed the acquisition of the coal assets of CSR, including Drayton. (In 1988 CSR sold its coal assets to a variety of parties, including Esso, but Drayton was sold to Shell.)*

*As a consultant in 1989, I acted on behalf of Bond Corporation in the successful \$120m acquisition and financing of the erstwhile Hunter Valley coal interests of BHP.*

*I mention this background to illustrate that I have extensive corporate financial experience, and I have at times in my career had close links with resources, including coal. And in industries such as property, resources, media and banking I have been directly involved in many environmental or policy submissions to government or planning departments."*

### Independence

Neither my original submission, nor this follow up, has been written at the behest of any third party. I am not being paid by any party. In fact I spent money out of my own pocket to travel from interstate to Denman for the PAC hearings in September, and I have spent many hours of unpaid time on this and my earlier submission.

I decided to contribute on this matter because I am concerned that a harmful decision might be taken simply because the contribution of the breeding industry to the Hunter Valley, and the ramifications of that industry being damaged, are not properly understood. It has been widely claimed that many in the community have said they are in favour of the mine, but that is only to be expected, as few outside of the breeding industry would understand its financial contribution. If one was to ask members of the general community if they would still favour the mine if it would cause \$1.5B of economic value to leave the region, I imagine the response would be very different.

Unlike many parties that have submitted views on this matter, I have nothing to gain or lose whichever way the decision turns. I keep mares in the Hunter Valley, and for many years I have spent sizeable sums there. I have no fixed assets in the region. So if Coolmore and Darley relocate their stallions interstate, as I believe is inevitable if the mine extension is approved, then I will simply move my mares to that same location, and thereafter I will spend my money each year in that new location instead of the Hunter Valley.

With nothing personally at stake whichever way the decision goes, and given that I am not being paid or commissioned by any party, my submission is truly independent, and is sourced from a lifetime of study of the activity, and my long-term and extensive direct investment as an owner of broodmares and as a customer of Coolmore and Darley and of their competitors.

### Structure of this report

My submission of September 2015 was self-contained. This second submission is not.

This submission has been prepared as a response to opinions expressed in Mr Houston's report. Nothing in his report would motivate me to change my original submission, and in essence, the whole of that original submission stands as a rebuttal of his report.

But in order to counter what I believe to be flawed advice in Mr Houston's report, and an incorrect paraphrasing of comments in my original submission, I have written this submission to provide more detail on some of the points I already made, or to further explain matters that were mentioned but not explored in detail, or to provide back up and verification of statements that were submitted at face value.

In particular, many of Mr Houston's arguments suggest to me that he is not familiar with the history and evolution of the various breeding centres in Australia and New Zealand. I believe this historical background is vital if one is to understand how and why the Hunter Valley has come to enjoy the status it does today, and what the industry would revert to if Coolmore and Darley were forced to leave. This perspective is covered at length in this submission.

The layout of this report is that it considers a series of issues, each prompted by Mr Houston's comments or omissions. I have tried as best as possible to put them into a logical sequence, as I would see them, but I have also tried to have regard to the manner in which Mr Houston presented his ideas. This submission is sequenced as follows:

Executive Summary (page 6)

Transcript of My Verbal Presentation at Denman (p14)

Section 1 - The dominance of Coolmore and Darley in the Hunter Valley (p17)

Section 2 - What is Really at Stake Here? (p26)

Section 3 - Might Coolmore and Darley Take Different Approaches? (p33)

Section 4 - Is The Hunter Valley Too Attractive For Coolmore and Darley to Leave? (p38)

Section 5 – Are Victoria and New Zealand “Poor Cousins” of the Breeding World? (p46)

Section 6 – The Likelihood of Replacement Stallions in the Hunter Valley (p50)

Section 7 – Might Coolmore and Darley Move Elsewhere in the Hunter Valley? (p67)

Section 8 – The Irrelevance of Edinglassie (p70)

Section 9 – Will the Departure of Coolmore and Darley Cause a Collapse? (p75)

## EXECUTIVE SUMMARY

My qualification to make this and my earlier submission is that I am an experienced thoroughbred breeder/investor, and have been for some twenty years. My study and recall of the industry extends back as far as forty five years. I own a number of mares in the Hunter Valley, and at times in the past I also had mares in several other parts of Australia and New Zealand. In parallel with being a horse breeder, I also have an extensive background in complex commercial matters from a 35 year career as an investment banker and senior corporate executive in Australia and overseas. During my working career I had senior executive responsibilities in the resources, property, media, banking, retailing and health care industries.

In my original submission dated September 10, 2015, I stated my opinion as follows:

*I submit that a decision to proceed with the Drayton South mine would so potentially damage the sale value of Hunter Valley yearlings, and hence the annual earnings of the stallions owned by Coolmore and Darley, that those two studs will have no alternative but to relocate their stallions to another state or to NZ. This must and will lead to a minimum of 3,000 broodmares owned by breeders also being relocated. There are no material barriers to relocation of the stallions or mares.*

*The studs have and will presumably further advise the Commission on the financial impact on the region were they to relocate. My submission deals with the impact that will flow from the subsequent relocation of an estimated 3,000 broodmares, which I do not believe has been contemplated in the Departmental Report.*

*Based on my own expenditure over a long period, I submit that the departure of 3,000 broodmares, which will be commercially inevitable if Coolmore and Darley leave the region, will see \$89.4m per annum of direct cash payments to broodmare farms and other service providers move to another region. Given the fixed cost and low risk nature of this income stream, I calculate its after-tax NPV at \$1,023m.*

*I judge that if the mine is approved there is 85%-90% probability of Coolmore/Darley relocating, and assuming they do, there is a 100% probability of a significant relocation of broodmares.*

Having read the report prepared by Mr Houston dated March 29, 2016, I would not alter my original submission in any way. I believe that the key conclusions reached in his report overall are not those that could be reached by someone with actual experience of the industry as compared with an external perspective.

### High-Level “One-Pager” on the Issues

The thoroughbred breeding industry is hugely important to the Hunter Valley economy. And Darley and Coolmore are the two giants of the industry, not just in Australia but around the world. If they are forced to relocate away from the Hunter Valley, then the financial repercussions on the region will be swift and they will be far reaching.

Investors like myself, who largely own the many thousands of breeding mares in the Hunter Valley, currently spend some \$500m a year in cash in the region. Of that sum, about \$300m is paid to small businesses to look after our mares, and about \$200m is spent having them mated with stallions (about half of which is spent with Coolmore and Darley, and half of which is spread among their competitors). This annual cost of production is met by investors in the expectation that the crop of foals will be worth more, and that an investment profit will therefore be made. Investors put up the equity and take the risk on that outcome.

If Coolmore and Darley are forced to leave, then because they have the greatest concentrations of desirable stallions, myself and other investors can be expected to collectively cause at least 3,000 of our broodmares to relocate to wherever they move to. This is approximately one-third of the present broodmare pool in the Hunter Valley. So of the aforementioned figure of \$300m that hundreds of small farms and businesses in the Hunter Valley currently earn for looking after the broodmare pool, about \$90m of that income can be expected to seamlessly move to equivalent farms in another state, with near enough to immediate effect.

As I said in my original submission, and reinforce in this submission, this is an outcome that is foreseeable to those within the industry. My experience tells me that If Coolmore and Darley are forced out, the departure of a significant pool of broodmares will follow with 100% predictability. So, the critical issue comes down to the likelihood of this decision forcing Coolmore and Darley out.

Mr Houston argues that because the properties adjacent to South Drayton are a stallion farm (Coolmore) and a broodmare farm (Darley) the two businesses will be impacted differently, and therefore they might pursue different strategies. But as Mr Houston admits, he does not understand the Darley business model, and is unaware that Woodlands is its stallion nursery, and hence both Coolmore and Darley will approach this from the perspective that their stallions would be tainted.

Financial investors like myself know that it is the calibre of the stallions that directly underpins the prices of the yearlings sold from the Hunter Valley; and given the dominance of Coolmore and Darley’s stallions, if their stallions are compromised, then it will ripple through the pricing structure of the whole industry. Hence, Coolmore and Darley cannot possibly operate properties next door to a working coal mine without the whole industry’s financials being impacted, not just their own.

There are other locations in Australia and New Zealand that have wonderful environments for raising young horses, and some of these locations were actually more prominent breeding centres in the era before Coolmore and Darley set up in the Hunter Valley. There is no reason why Coolmore and Darley must remain in the Hunter Valley. If they leave, myself and other customers would relocate mares with them in sufficient numbers to ensure their profitability was not impacted. They would suffer only mild and short term inconvenience. So I believe that the question the Department should be pondering is not “why would they leave?” but rather “why wouldn’t they leave?”

### The Sequence of Material in This Submission

The inevitable ramifications of the mining decision on the breeding industry cannot be appreciated unless the dominance of Coolmore and Darley is understood; in the eyes of many people in the overseas breeding and racing worlds they are the Australian industry.

Mr Houston describes Coolmore and Darley as “two of the largest of the 15 or 20 stallion farms in the Hunter Valley”. However, Coolmore and Darley are not merely “two of the largest”, but are the two largest stallion farms in Australia by a sizeable margin. They are the two global brands in the stallion business, and their Australian operations are bigger than the rest of the industry put together, as will be seen in this submission.

As a breeder, I have seen the Hunter Valley lifted to worldwide prominence since Coolmore and Darley set up in the region. This matter is about them trying to stop a decision that will inevitably undermine the perception and pricing of the Hunter Valley yearling product overall. To forestall a market fall, those two businesses would have no alternative but to relocate. The major international yearling buyers see the Hunter Valley product as inextricably intertwined with the fortunes of Coolmore and Darley, so the significance of the coal mining issue would be elevated to an unprecedented degree by a Drayton approval.

Coolmore and Darley earn about \$100m per annum in Australia by selling services to their stallions to the owners of broodmares (see my original submission). If the prices of young horses produced from those matings were to be reduced because of buyer risk-avoidance, then investors like myself would not be prepared to pay the same fees to Coolmore and Darley going forward, and hence the valuations of the their stallions would drop. The risk-avoidance of yearling buyers is the major issue in this matter, but it does not appear to be prominently referenced by Mr Houston. He opines that broodmare owners will not stop using Coolmore and Darley stallions merely because a coal mine opens at the border of their stallion farm and stallion nursery respectively. But I say that it would deter us – and for reasons that go beyond those which Mr Houston addresses. These were fully explained in my original submission.

The global stature of Coolmore and Darley is the reason that the repercussions are potentially so large for the whole industry. An issue affecting the two of them is of exponentially greater significance than the same issue affecting small parties that have no international profile. This is why it is disappointing that Mr Houston’s report not only seems to understate the market dominance of Coolmore and Darley, but in my view overstates the level of competition and the amount of change within the industry, giving the impression that Coolmore and Darley are just two of many farms.

The horses in the Hunter Valley owned by Coolmore, Darley and broodmare owners are worth of the order of \$2.5B by my reckoning, and investors spend some \$500m cash per annum, in the region, to produce the annual foal crop. (See my original submission.) If the earnings potential of those assets was to be significantly reduced, then the drop in the asset values would obviously be huge. This is why I say it is inconceivable that the owners of the horses would not move them to an alternative mine-free location, which would not be difficult.



Broodmare owners like myself are “direct customers” of Coolmore, Darley, and the other stallion farms. But in a wider sense we are in a “commercial partnership” with the stallion owner, whereby we are jointly creating a young horse for future sale to our mutual customer. And it is the perception of those mutual customers which I say is the real problem. Myself and others in the industry have advised the Department of the expected adverse response of those mutual customers to what will be seen as a tainting of the Hunter Valley yearling product.

My submissions have explained that the mine will impact on the whole industry even if Coolmore and Darley are the only two parties directly affected by the mine proximity to their property. But the direct impacts on Coolmore and Darley would alone be enough to force them to relocate. The tranquil enjoyment of their properties is critical to the activity that takes place there. In my view, Coolmore and Darley could not possibly conduct their businesses next to a coal mine. I expand on that observation in this submission because Mr Houston has taken a comment from my original submission and paraphrased it in a way that implies otherwise.

Mr Houston’s focusses much of his report on an opinion that Coolmore and Darley may adopt different strategies because the Darley property immediately adjacent to South Drayton (Woodlands) is only a broodmare property; it is not where its stallions stand (Darley’s stallions live at a property called Kelvinside). However, Mr Houston is apparently unaware that Woodlands is where Darley raises many of its stallions from birth. (He concedes his uncertainty as to the Darley business model.) Some of those young horses at Woodlands will be Kelvinside stallions in as little as two years, and so Darley’s stallions will also be impacted by the mine, as will Coolmore’s.

My submission also explains why I believe both Coolmore and Darley would suffer financially if they were based in different states, a point which I demonstrate with reference to the poor performance of the Australian yearling market in past times when the market was fragmented.

Mr Houston argues that neither Coolmore nor Darley would wish to leave the Hunter Valley because it “is the best location for breeding thoroughbreds in the Southern Hemisphere”. But in this submission I present compelling historical evidence which shows that the Hunter Valley was anything but the most exalted breeding centre in the Southern Hemisphere until Coolmore and Darley arrived there.

Mr Houston also opines that Coolmore and Darley would not want to leave the Hunter Valley because that is where their main source of revenue is. I believe this to be circular logic. It is obviously where their main source of revenue is today, because investors have caused so many of Australasia’s elite breeding mares to be based in the Hunter Valley, because of the presence of the Coolmore and Darley stallions. But if Coolmore and Darley move their stallions elsewhere, then so too will it cause investors to relocate thousands of broodmares alongside them. The owners of those broodmares are widely dispersed throughout Australia and overseas, and it is of no importance to us where our mares are located, as long as they have access to the best stallions.

Mr Houston cites figures which he interprets as showing that Victoria or New Zealand do not have the affluence that would suit Coolmore or Darley, but again this conflicts with history. Immediately before the Coolmore/ Darley era, Victoria and New Zealand were actually more prominent breeding centres than the Hunter Valley. They declined in relative significance only because of Coolmore and Darley’s decision to set up in the Hunter Valley, and if they were to relocate to either Victoria or New Zealand, then either location would quickly reassume the mantle of the Southern Hemisphere’s

leading breeding centre. The historical evidence clearly shows that the Hunter Valley needs Coolmore and Darley much more than they need it.

Mr Houston argues that even if Coolmore and Darley move interstate, owners will not relocate their mares because the remaining Hunter Valley studs would put on extra stallions, or mate their existing stallions more frequently. Or else, new players would arise. As an actual broodmare owner, I believe these is the most unrealistic group of opinions in Mr Houston's paper. Stallions that have the credentials to operate in the Hunter Valley at all, let alone to be at the elite level that interest a large volume of broodmare owners, are very rare. Yearling buyers are drawn to the offspring of such stallions precisely because of that scarcity value. As I said in my original submission:

*"It is a matter of industry reality that there is no pool of alternative stallions at the elite level, because most of the elite stallions of the world are already available in the Hunter Valley each spring. They are so few in number that breeders the world over know the same handful of names.*

*And new alternative stallions of a lesser standard would be of no interest to breeders. There are already plenty of lower-priced alternative stallions in the Hunter Valley that breeders do not use to the same extent as the elite stallions. They are lightly used because they are not deemed capable of siring attractive sales prospects. The small number of elite stallions serve huge numbers of mares because that is the commercial imperative."*

In this submission I provide further explanation of the market forces at work in the selection of stallions and show that Coolmore and Darley have the majority of the best proven stallions today, and also routinely acquire the best of the new prospects. Mr Houston's advice is that if Coolmore and Darley left, the three biggest competitors would only need to put on "six extra stallions". I show in this report that these three competitor studs are currently unable to source as many as three viable new stallions each year between them on average, so sourcing their present average and somehow finding another six would represent a more than 300% lift on current activity. This could only be done by sourcing stallions of such reduced quality that broodmare owners would have no interest.

To further emphasise this point, my submission provides an example which shows that the major competitor of Coolmore and Darley has been running well under target in terms of acquiring stallions for many years, such is the level of market competition for the handful of stallion prospects.

So the idea that competitor studs could put on three times the usual number of new stallions if Coolmore and Darley were to leave, and would be of such calibre that broodmare owners would ignore the simple expedient of having their mares follow Coolmore and Darley to another attractive location, is in my view, manifestly unrealistic.

Mr Houston provided examples to demonstrate the ability for new players to emerge in the stallion market. However, my submission shows how the competitive landscape in the Hunter Valley has changed little in the 15 years since Darley followed Coolmore into the market. And while none of Mr Houston's three examples actually showed a successful new entrant, the most interesting example he gave of the type of new operators that might replace Coolmore/Darley was a Southern NSW farm that stood a small number of lowly priced stallions for a couple of years, and earned total revenues per annum about one-five-hundredth those of Coolmore and Darley, before closing.

Further to the competition issue, I also note a statement by Mr Houston that Arrowfield, Widden and Vinery have expanded significantly in the last decade. I show that he accidentally selected some very unrepresentative data. He compared one variable in the specific years of 2005 and 2014, which happens to give an impression of a group of farms experiencing rapid expansion. But my submission shows that measuring that exact same variable, over the exact same time period, just one year more recently (that is, comparing 2006 and 2015), would alternatively give the impression of three farms going backwards. These impressions are diametrically opposed, yet each can be made to appear as a trend, depending simply on whether 2005 or 2006 is used as the base year. My submission emphasises that this shows the importance of the Department taking advice on the breeding industry from people who are within it and understand it, because it is easy for outsiders to draw incorrect conclusions by accidentally chancing upon data that is not representative.

I repeat in this submission the advice I gave in my original submission, which is that having considered the stallion options at each stud farm in the Hunter Valley, taking into account their age, and their attractiveness to commercial breeders, then if Coolmore and Darley were forced to leave the Hunter Valley, I submit that about 3,000 broodmares must also be relocated, as a first wave, to wherever they move to. This is about one-third of the mares that currently reside in the Hunter Valley.

For me, as a breeder, this is not an academic exercise of the type that a consultant might undertake. It is analysis that I (and other breeders) must make in practice, because the safety of my capital would depend on my ability to accurately determine how the industry would be reshaped by the departure of Coolmore and Darley.

Broodmare owners are drawn to the best stallions, in pursuit of the profit motive. There are very few elite stallions. If that small pool of elite stallions was to suffer a forced division, by Coolmore and Darley being forced out while their competitors remained, then it is an inescapable conclusion that the pool of mares will likewise have to be divided. The elite Coolmore and Darley stallions as one group, or the elite stallions from the remaining Hunter Valley studs as another group, would each be too few on their own to handle all of the mares that would be lined up for their services. So not all of the mares could stay in the Hunter Valley and not all of them could follow Coolmore/Darley. The broodmare pool would have to be, and would be, divided. This outcome is easily foreseeable when one knows the stallions as individuals, as breeders do, and not as generic alternatives on a spreadsheet.

The loss of 3,000 broodmares to the Hunter Valley would see some \$90m of income lost to small service providers per annum. (See my original submission, my presentation at Denman and Section 9 of this submission.) That ~\$90m is direct spending only. It does not include the multiplier effect when those individuals and small businesses in the Hunter Valley spend that \$90m within the region.

Over time, as mares retire or are sold in the annual breeding stock sales, I believe that the Hunter Valley numbers would continue to decline further, if Coolmore and Darley were in business elsewhere. This is inevitable because Coolmore and Darley access the best new stallion talent each year, so buyers of mares will be confident that top class stallions will always be available wherever Coolmore and Darley are. So as mares are purchased, or as female racehorses finish racing in the capital cities and turn to the breeding phase of their lives, their owners would be more inclined to send them to the location where Coolmore and Darley had become re-established.

Mr Houston has opined that even if Coolmore and Darley left, the Hunter Valley would remain as the largest breeding centre in the country, and it would not collapse.

I submit that if Coolmore and Darley are forced to leave, then the best quality stallions in the Southern Hemisphere will no longer be based in the Hunter Valley, and immediately, a large pool of the best broodmares can be expected to start joining them. The Hunter Valley will cease to be the leading breeding centre in terms of quality within weeks or months of Coolmore and Darley leaving.

In terms of quantity, Mr Houston says that the Hunter Valley will still have more mares than anywhere else in the country, but this argument is based on what I believe to be his false premise that mares will not leave the Hunter Valley in large quantities. I submit that actual breeders like myself will cause mares to be relocated in their thousands, and as those numbers leave one location to move to another, the balance of numerical superiority will also be transferred from the Hunter Valley to whichever location Coolmore and Darley set up in. I showed in my original submission that if Coolmore and Darley relocated to the Victorian market, for example, then the 3,000 broodmares that I calculate will follow with them would give Victoria numerical superiority very quickly.

But I believe this numerical comparison is hardly relevant. If Coolmore, Darley and 3,000 broodmares leave, then the ~\$100m paid annually by the owners of those broodmares to Coolmore and Darley, and the ~\$90m paid annually by those same owners to small Hunter Valley businesses that care for those mares, will both be spent in another state or in New Zealand. When that happens, it hardly matters whether the Hunter Valley remains a narrow leader or become a narrow second. The small businesses in the Hunter Valley will not care one way or the other.

In my original submission, I advised that the ~\$90m paid annually to the small business owners had an after-tax, capitalised financial value of \$1.023B. Updating for changed interest rates – bond rates have fallen all over the world since I prepared my submission in September 2015 – the equivalent figure I calculated for this submission would be \$1.155B (see Section 9).

Additionally, the Hunter Valley region would suffer the loss of the future value of all spending in the region by Coolmore and Darley themselves; that is, the portion of the ~\$100m paid to them every year by broodmare owners that is directly spent by them in the region, as distinct from being invested in sourcing stallions in Australia and globally. I don't have enough information to formally value that component, but my reasoned judgement is that the capitalised value would run into the hundreds of millions of dollars.

When these two factors are taken together, the one-time capitalised value of the income to be lost to the Hunter Valley region would be of the order of \$1.5B, and I emphasise again, this is only the value of direct spending that would be lost. The multiplier impact on the region will be far greater.

I am not sure if a loss of ~\$1.5B in net present value is technically a "collapse", as there will still be a (much-reduced) level of activity carried on in the Hunter Valley for at least the foreseeable future. But ~\$1.5B far outweighs any conceivable benefit from the extension of the South Drayton mine, as I understand it, and the loss of ~\$1.5B will be devastating to the Hunter Valley region and to NSW.

Conversely, some other state of Australia, or New Zealand, will benefit from an injection of ~\$1.5B of future income through no effort of its own.

**I repeat my advice that if the mine extension goes ahead, the probability of Coolmore and Darley relocating outside of NSW is assessed at 85%-90%, and that if that happens, the probability of a significant migration of broodmares to that same location is judged as 100%. While there is room for some small doubt in my mind as to Coolmore and Darley leaving, because I cannot speak on their behalf, I have no doubt about the response of broodmare owners if they do move, because I am an experienced owner myself.**

**\$1.5B of lost future income might not be the biggest financial loss an Australian state has suffered from an industry disruption, but it is hard to imagine that there has been a precedent where the financial loss had been so predictable, and so easily avoidable.**

## **MY VERBAL PRESENTATION IN DENMAN, SEPTEMBER 11, 2015**

On September 11, 2015, I presented to the Planning Assessment Commission at the Denman public hearings. I did not have a slide presentation, and I spoke “off the cuff”, without notes. When I arrived home after the hearing I created a transcript of my address, which may not be accurate as to every single word, but will be very close to it.

In the interests of completeness and continuity, I am including that transcript of my presentation in this submission.

*“Madam Chairwoman, other members of the Commission, ladies and gentlemen,*

*Thank you very much for the opportunity to present my views to the hearing today.*

*I must say at the outset that I am opposed to the mine extension, and that is unfortunate, because it is not a position that comes naturally to me. I have just retired from a career in the corporate world, and during the course of that career I was involved with the coal industry on several occasions. In fact, twice in my career I was in the position of being an advocate for the Hunter Valley coal industry, so my objection to the mine certainly has nothing to do with any philosophical views. But at the same time I have also been a long time participant in the horse breeding industry in the Hunter Valley, so I’m one of the few people who can understand this issue from both perspectives, and sympathise with both parties. And I have to say that my understanding of the horse business enables me to see clearly that the decision to go ahead with this mine will end up being disastrous in economic terms for the people of the Hunter Valley.*

*I’m the last speaker, and I know you’ve had a gruelling few days listening to many presentations. And I know better than most how hard it is to understand the breeding industry because unless you are involved it is not something anyone would be expected to know. So what I want to do in my five minutes is to give a very high level overview of how the industry works, and I believe I can do that because my corporate skill set involved being able to simplify complex issues to their bare essentials and also because I am an investor in the breeding industry and hence I understand the key drivers.*

*I lodged an extensive paper yesterday so everything I will cover here I would urge you to read more fully in that paper, and for now I will use high level concepts and rounded numbers to make the points easier to understand.*

*When you drive around the Hunter Valley the horses that you see across the fence are almost always breeding mares and their offspring. There are about 10,000 of them in the Hunter Valley, and they are largely owned by financial investors like myself. People like me live in the capital cities or overseas and we invest in the breeding industry with the intention of making money. For us it is a diversification away from shares and property. By buying a few broodmares, an investor gets the right to their offspring, and the idea is to sell those offspring at a profit.*

*Now I wouldn't know the first thing about how to look after a horse. But luckily, I don't need to, because there are people all over the Hunter Valley who do have that expertise. So investors like myself pay small farms and businesses in the Hunter Valley to take care of everything to do with the upkeep of our horses. Now I know from long term financial records, and I'm happy to share this with the Commission, that it costs about \$30,000 a year to keep one broodmare and her offspring. So if you quickly do the maths you'll see that 10,000 mares at \$30,000 per head is \$300m per annum. So when I hear people ask "what does the horse industry do for the people of the Hunter Valley", well the first thing is that it leads to people like me who don't live here spending \$300m a year with small businesses in the region for looking after our mares.*

*In addition to the costs of looking after our mares, broodmare owners also pay the costs of having our mares mated with one of the stallions owned by the various stallion farms, the biggest of which are Coolmore and Darley. Each year we spend about \$200m on stallion fees, about half which goes to Coolmore and Darley and half of which goes to the other stallion farms.*

*So if you add the \$300m to the \$200m, you get a figure of \$500m, and in broad terms that can be thought of as the annual cash costs of producing the foal crop in the Hunter Valley. So if the crop of foals ends up being worth more than \$500m, we investors make money. If it's worth less than \$500m we lose money. So it is investors like myself that take the equity risk on the value of the crop each year. The important thing to grasp in this context is that the Hunter Valley breeding industry is just a very large service provider to a group of financial investors that underwrites the annual horse crop and seeks to profit when that crop is sold to racehorse buyers. The Hunter Valley industry doesn't directly take a share of that gain or loss, other than in the general sense that the industry will thrive as long as investors are happy to underwrite it.*

*Now turning to the key matter at hand, it is my view that a decision to expand the mine will leave Coolmore and Darley no alternative but to move away from the Hunter Valley. I'm not the first person to have given you that view, and I won't go into detail here because time is limited and my reasoning is set out in detail in my report. I don't have any inside knowledge of the corporate thinking of Coolmore and Darley, because my relationship with them is only that of customer. But as a former senior corporate executive I will just say that to me the decision would be a no brainer, because the risks are too uncontrollable, the money involved is too great, and the solution is too simple.*

*What I need to do though is to warn about the consequences. Some people, including the Department, seem to have their head around the possibility that Coolmore and Darley might leave, and their attitude seems to be "not to worry, life will go on". But what nobody seems to have taken into account is the flow on affect that such a decision would have on the broodmare population.*

*There is no time to go into details here, which are all set out in my report, but I show there how it can be calculated that some 3,000 mares will have to leave the Hunter Valley and follow the Coolmore and Darley stallions when they leave. Let's be blunt here. My mares are not in the Hunter Valley just because it is a nice environment. They are here because this is where the top commercial stallions are, and mating mares with the top stallions is what I have to do from a commercial point of view. If those stallions go somewhere else, then obviously my mares and thousands of others will follow. This is not supposition or conjecture; it is a predictable and inevitable outcome and I can say this with confidence because I am a broodmare owner myself and I have already had to decide what I will do if the worst case eventuates. Owners will have no hesitation in moving our mares because other parts*

*of Australia have equally nice environments for raising horses and the only thing that differentiates the Hunter Valley today is the presence of the best stallions.*

*And the 3,000 is not an alarmist figure - it is less than a third of the mares and is actually the minimum outcome. Over time it will become worse. I haven't run longer term scenarios because the minimum outcomes alone are so bad that I cannot imagine that anyone who takes the time to understand the issue will ever allow it to happen.*

*Now just to make sure this point is understood, I mentioned before that it costs \$30,000 to keep a broodmare in the Hunter Valley, so when 3,000 mares leave that will be \$90m a year of income that walks out of the Hunter Valley basically overnight. That is not income that is dependent on equity outcomes, or on commodity prices. It is clean risk-free service fee income from an industry that has been in the Hunter Valley for many years and will be here forever as long as nothing is done to derail it. And that \$90m is over and above the spending that Coolmore and Darley themselves would take interstate. I assume that you will already have a figure in mind for that, but the broodmare spending is the side of the business that only investors like me can talk to.*

*Madam Chairwoman before I finish there is something I want to emphasise, and that is that I have no vested interest in the outcome of the decision. Whatever happens, I will not be affected. I have no fixed assets in the Hunter Valley, I only have my mares and they can be moved anywhere in the country overnight. So if Coolmore and Darley move, my mares will be on the next truck behind them, and my life won't change. I will still be writing the same cheques each month for their upkeep. I will still be writing the same cheques each year for stallion fees, and I will still be selling the offspring for the same prices I do now. The only difference is that I will be writing those cheques to businesses in a different post code, so while there will be no impact on my life, it will be devastating for the hundreds of small businesses in the Hunter Valley that rely on people like me spending hundreds of millions of dollars a year here.*

*I'm sorry you have to finish the hearings on such a sobering note, but I will say again that I urge you to read my report in full, and I am happy to make myself available to the Commission or the Department if anyone so wishes.*

*Thank You."*



## **SECTION 1 – THE DOMINANCE OF COOLMORE AND DARLEY IN THE HUNTER VALLEY**

I believe it is imperative for any consideration of this issue that the market dominance of Coolmore and Darley is understood.

In my original submission of September 10, 2015, I only provided limited insights into how large Coolmore and Darley are in relation to the rest of the Australian industry. Given that the South Drayton mine had been the subject of consideration for several years before I became involved, I took it for granted that every party already involved in the matter knew that Coolmore and Darley are the two largest stallion farms in the world. I did not feel it was necessary to provide evidence as to their dominance any more than I would have assumed I needed to show that Coles and Woolworths are the two dominant supermarket chains in Australia in the third year of a supermarket enquiry.

But having read the following description in Mr Houston's report<sup>1</sup>, it appears that it is necessary to provide more clarification:

*"There are around 15 to 20 stud farms in the Upper Hunter region, with Darley Kelvinside and Coolmore being two of the largest."*

Coolmore and Darley are not "two of the largest" but in fact they are the two giants of the industry, and their Australian operations are bigger than rest of the industry put together.

This section will demonstrate the market dominance of Coolmore and Darley from multiple angles: With reference to the achievements of their "proven" stallions; how they dominate the expensive end of the stallion market most heavily utilised by breeders; and how they routinely acquire the best of the new stallion prospects as male racehorses finish their racing careers. Most importantly I will then demonstrate how mating one's broodmares with the elite Coolmore and Darley stallions maximises a broodmare owner's chances of having the offspring accepted into the premier yearling auction in Australia, thereby maximising the potential investment returns.

### **How Many Stud Farms Are There?**

As a commercial breeder, whose objective is to raise yearlings that can be hopefully sold at a profit, I say that there are 8 stud farms in the Hunter Valley standing stallions that would come under my consideration, and that would be considered by commercial breeders in general.

There are a further five farms that have between one and three thoroughbred stallions available, but none of the stallions at these five farms stand for a service fee greater than \$10,000 +GST. These farms are not typically on the radar of commercial breeders like myself, because stallions whose fee

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<sup>1</sup> All references are to Mr Houston's report of March 29, 2016. This particular quote is from page 15. Subsequent quotes will show a page number reference only.

is \$10,000 or below are not of sufficient calibre to sire offspring that will be appealing to the most prominent yearling buyers. (And hence they would not be accepted into the catalogue for the elite industry sales.) The target market for these farms and stallions is more likely to be hobby breeders that are looking to breed horses that they can race themselves in their local communities.

My own rule of thumb is that if a stud does not have a stallion that is in the top-50 most expensive in the market, it is not aiming at the investor/breeder, that is, breeders who are breeding to sell yearlings for profit. Others may have their own rule of thumb, but it will be seen in this submission that across the whole spectrum of tables and data, there will only be the same 8 stud farms that ever appear when referring to measures of success and prominence in the Hunter Valley.

So, to recap, in 2016 there will be 13 farms in the Hunter Valley that have a stallion offering of any type. Eight of those are “top-50” calibre and so they are competing, to a greater or lesser degree, with the likes of Coolmore and Darley.

But as this submission will show, the level of competition is not really a function of the number of different stallion farms, but the number of stallions. Even if several new operators thought tomorrow that they would like to get into the stallion business, finding even one new stallion between them that would be of interest to breeders would be difficult, given the demanding standards that stallions must meet, and the calibre of the options that are already available.

#### Elite Stallions Are Very Rare

When male horses demonstrate racing prowess on the racetrack, the very elite among them are sought as future stallions by the various stud farms. (Assuming they have not been gelded beforehand.) Stallions can impregnate some 200-250 mares every spring, so the number of stallions needed is only a small fraction of the number of breeding mares that is in the population at any one time.

I explained in my first submission that there are upwards of 10,000 mares in the Hunter Valley. To put the small size of the stallion pool into perspective, the following shows the number of new stallions given an opportunity in the Hunter Valley breeding industry in each of the last five years:

<b>Year</b>	<b>Number of New Hunter Valley Stallions Starting That Year</b>
2011	8
2012	13
2013	6
2014	10
2015	11
5-Year Average	9.6

That is, every year, market equilibrium requires an average of only 9-10 new stallions to enter the Hunter Valley ranks. This is partly to replace stallions who retire, but more to replace stallions that turn out to be unsuccessful when their offspring race. (See the explanation of “proven” and “unproven” stallions below.)

An intake of less than ten new stallions every year shows just how high the bar is set for a male horse to become a stallion. These limited opportunities are not just available to the 9-10 best Australian male racehorses of a given year, because the number includes stallions brought here from overseas as well, especially from Britain and the United States. Given that about 9,000 male horses are born every year in Australia alone, this underscores just how superior the racetrack performance of a new stallion needs to have been. Less than one in a thousand male horses become stallions, so any new Hunter Valley stallion will have been a household name to spectators who follow horse racing during the year.

(Although this matter will be considered in detail in Section 6, there is a point to be made while this table is fresh in readers’ minds. It can be seen from the table how few new stallions enter the Hunter Valley rosters each year to maintain equilibrium. And that number is spread across all of the studs. Arrowfield, Vinery and Widden studs, for example, between them average less than three new stallions each year, or less than one each. This will be revisited in Section 6, when I consider Mr Houston’s opinion that these three studs only need to find an extra six high-quality stallions, over and above their usual base of less than three, to counter the departure of Coolmore and Darley.)

#### “Proven versus Unproven” Stallions

A piece of industry background that it is important to understand when reading this submission is the difference between “proven” and “unproven” stallions.

As noted above, when new stallions first enter stud, they impregnate (or “service” or “cover”) as many as 200-250 mares in the first spring. The following spring, the foals from those first matings are born, and the stallion covers a second group of mares. The following spring, the original foals are one year old, the second crop of foals is being born, as the stallion covers a third group of mares. In the fourth year, as the stallion is serving his fourth group of mares, only then are the very first crop of foals old enough to commence racing, as two year olds. A few will start racing then, but the majority will not race until they have turned three years old, by which time their sire will be serving his fifth book of mares.

Reflecting on this timeline, it means that a stallion has four or five seasons at stud, serving perhaps a thousand mares in total, before the racing ability of his first offspring can be judged. So, for the whole of a stallion’s first four to five years at stud, he is referred to as “unproven”. During this period, a stallion’s fee reflects his potential; that is his own racing performance and breeding, the attributes that gave him the opportunity in the first place. There is a limit to how much the market will pay for a service by an unproven stallion, and the most expensive first season stallion in recent times is Pierro, who retired to Coolmore stud in 2013. His first year fee, based solely on his racing performance, pedigree and appearance, was \$77,000.

Once a stallion's runners begin to race, then from that point on his commercial attractiveness is based on how well his offspring can run. He is then a "proven" stallion, for better or worse, and his service fee is based on the racing ability of his collective offspring. If a stallion is proven to be successful, his service fee can rise higher, and the top stallions in the Hunter Valley can command service fees in the \$110,000 to \$220,000 range. But the majority of stallions will prove disappointing, and their fee will reduce, and in many cases they may be transferred to a second tier location.

#### The top "proven" stallions in Australia.

Throughout the year there are tables published of the aggregate performance of all racehorses sired by the various stallions whose offspring run on Australian racetracks. This is the way in which the performance of the proven stallions is measured. When the industry refers to the "Champion Stallion" of Australia, it is referring to the stallion whose hundreds of collective offspring won the greatest amount of aggregate prizemoney in the preceding year. Self-evidently, a stallion cannot be the champion stallion for his first four or five years as he has no runners during that period.

In the last complete racing season, the top 15 stallions<sup>2</sup> on the Australian stallion premiership were as follows, together with the stud at which they stand (or stood, in the case of deceased stallions.)

Position	Stallion	Stud Farm	Location
1	Fastnet Rock	Coolmore	Hunter Valley
2	Exceed and Excel	Darley	Hunter Valley
3	Sebring	Widden	Hunter Valley
4	Encosta De Lago	Coolmore	Hunter Valley
5	Redoute's Choice	Arrowfield	Hunter Valley
6	Lonhro	Darley	Hunter Valley
7	Street Cry	Darley	Hunter Valley
8	Snitzel	Arrowfield	Hunter Valley
9	Not A Single Doubt	Arrowfield	Hunter Valley
10	Northern Meteor	Widden	Hunter Valley
11	Choisir	Coolmore	Hunter Valley
12	High Chaparral	Coolmore	Hunter Valley
13	Stratum	Widden	Hunter Valley
14	Commands	Darley	Hunter Valley
15	Dubawi	Darley	Hunter Valley

It can be seen that every one of the top 15 stallions in Australia was a Hunter Valley stallion, reflecting its modern-day dominance as the main breeding centre in Australia. Moreover, the list is dominated by stallions from Coolmore or Darley, with two thirds of the stallions being from either of

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<sup>2</sup> That is, the 15 stallions whose offspring won the most prizemoney, in order, in 2014/2015. In this particular season, Fastnet Rock's offspring collectively won more than \$10m. The 15<sup>th</sup> stallion, Dubawi, was at \$5.8m. The tables run into many hundreds of stallions long and are used by yearling buyers to analyse, from many perspectives, the ability of stallions to sire good racehorses.

the two studs, and no less than 5 of the top 7. The table also shows that only two other studs, Arrowfield Stud and Widden Stud, had proven stallions within these top 15 placings.

#### The top “unproven” stallions in Australia.

As mentioned above, for their first four or five seasons at stud, stallions are judged and priced on potential, before any of their offspring have raced. During this time period they are “unproven.”

A successful stud will aim to have a mix of proven and unproven stallions on its roster. If too high a proportion are unproven then the stud may experience problems when much of its roster is found to be unsuccessful (and hence not commercially viable) when the first runners of many of its stallions prove disappointing at the same time. On the other hand, if a stud has many older, proven, stallions but few younger stallions coming through, that stud faces the prospect of its revenue streams falling away when these proven stallions retire, with nothing of equal calibre to replace them.

Of the unproven stallions at stud, that is those who have commenced stud duties in the 2013, 2014 and 2015 seasons or will enter in 2016, the list is again dominated by recent recruits to Coolmore and Darley. The following are the most expensive “unproven” stallions to enter the market recently, measured by their initial fee as they entered stud in any of the last four years:

<b>Stallion</b>	<b>Stud Farm</b>	<b>Initial Fee</b>	<b>First Year At Stud</b>	<b>Year That Majority of First Runners Will Appear</b>
Pierro	<b>Coolmore</b>	\$77,000	2013	2017
Vancouver	<b>Coolmore</b>	\$66,000	2016	2020
All To Hard	Vinery	\$60,000	2013	2017
Pride of Dubai	<b>Coolmore</b>	\$55,000	2016	2020
Brazen Beau	<b>Darley</b>	\$44,000	2015	2019
Zoustar	Widden	\$44,000	2014	2018

The table shows the year that each stallion commenced his stud career, and the year in which the majority of his first runners will appear.<sup>3</sup> It can be seen that once again, the list is dominated by Coolmore and Darley, with two thirds being owned by one of them. And once again the list only features stallions from four different studs, only one of which was not mentioned in the previous table.

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<sup>3</sup> Some of the most precocious of the runners by a stallion might appear towards the end of the previous year to that shown, but the majority will appear in the calendar year indicated, which covers the second half of their 2yo year and the first half of their 3yo year.

### Most expensive stallions, combining proven and unproven

Given that Coolmore and Darley have been shown to dominate the ranks of the proven stallions, and also to have the cream of new unproven stallions, it is mathematically inevitable that they will therefore dominate when the list of the most expensive stallions combined is considered. The table below shows the 35 most expensive stallions that will be standing in the Hunter Valley in 2016:

Position	Stallion	Fee <sup>4</sup>	Farm	Year born	Proven?
1	Fastnet Rock	\$220,000 <sup>5</sup>	Coolmore	2001	Yes
2	Exceed and Excel	\$110,000	Darley	2000	Yes
3	Medaglia D'Oro	\$110,000	Darley	1999	Yes
4	Redoute's Choice	\$110,000	Arrowfield	1996	Yes
5	Snitzel	\$110,000	Arrowfield	2002	Yes
6	Lonhro	\$88,000	Darley	1998	Yes
7	Sebring	\$77,000	Widden	2005	Yes
8	Not A Single Doubt	\$71,500	Arrowfield	2001	Yes
9	Vancouver	\$66,000	Coolmore	2012	
10	Pierro	\$66,000	Coolmore	2009	
11	More Than Ready	\$66,000	Vinery	1997	Yes
12	Pride of Dubai	\$55,000	Coolmore	2012	
13	All Too Hard	\$55,000	Vinery	2009	
14	I Am Invincible	\$55,000	Yarraman	2004	Yes
15	Written Tycoon	\$49,500	Other, Victoria	2002	Yes
16	So You Think	\$49,500	Coolmore	2006	Early
17	Brazen Beau	\$44,000	Darley	2011	
18	Teofilo	\$44,000	Darley	2004	Yes
19	Zoustar	\$44,000	Widden	2010	
20	Shooting To Win	\$38,500	Darley	2011	
21	Hinchinbrook	\$38,500	Yarraman	2007	Yes
22	Criterion	\$35,750	Newgate	2010	
23	Sepoy	\$33,000	Darley	2008	Early
24	Dissident	\$33,000	Newgate	2010	
25	Choisir	\$29,700	Coolmore	1999	Yes
26	Wandjina	\$27,500	Newgate	2011	
27	Street Boss	\$27,500	Darley	2004	Yes
28	Shamus Award	\$27,500	Widden	2010	
29	Press Statement	\$27,500	Vinery	2012	
30	Hallowed Crown	\$27,500	Darley	2011	
31	Exosphere	\$27,500	Darley	2012	
32	Dundeel	\$27,500	Arrowfield	2009	
33	Dream Ahead	\$27,500	Emirates	2008	Early
34	Animal Kingdom	\$27,500	Arrowfield	2008	
35	Starspangledbanner	\$24,750	Coolmore	2006	Yes

<sup>4</sup> The fees are inclusive of GST.

<sup>5</sup> Fastnet Rock's service fee is not publically stated, it is a matter for negotiation. The indicated fee is that which applied when it was last in the public domain.

The reason I have shown this extensive list is to highlight even more strongly the two points that are visible in all measures. Coolmore and Darley have more of the most expensive stallions, be they proven or unproven, than others put together. And secondly, only eight stud farms from the Hunter Valley are named, and only one different name from interstate appears (the Victorian stud that owns number 15, Written Tycoon).

If I was to extend this table by including the next 45 most highly priced stallions in the country, showing the top 84 in total, there would still only be the same 8 farms from the Hunter Valley represented. This is why I opined earlier that only 8 stud farms in the Hunter Valley would be generally regarded as being on the radar of those who are breeding to sell the offspring for profit.

#### Selling Prices of Offspring

Bearing in mind that the objective of investor/breeders is to produce yearlings that achieve high prices in the sales ring, it is important to confirm (as would be expected from the statistics so far) that Coolmore and Darley stallions excel in the yearling sales market as well.

In my first submission I showed that the Easter sale held every year in Sydney is the pre-eminent sale of thoroughbred yearlings in the Southern Hemisphere. Yearlings at that sale can sell into the millions, and the average horse sells for nearly \$A300,000. At the 2016 sales held recently in April, the percentages of yearlings sold that were sired by stallions from the various stud farms in Australia was as follows:

Stud Farm	Percent of Total
Coolmore	32%
Darley	21%
<b>Coolmore/Darley Combined</b>	<b>53%</b>
Arrowfield	17%
Widden	12%
Vinery	11%
Other Hunter Valley	5%
All Other Australian	2%
Total	100%

In this table, "Coolmore 32%" means that 32% of all of the Australian yearlings that were sold at the major industry sale were sired by a stallion standing at Coolmore. It does not mean the yearlings were raised or sold by Coolmore. The table largely reflects the offspring of mares owned by investors such as myself, who keep the mares at a broodmare farm, but mated them with a Coolmore or Darley stallion during the relevant spring.

The Easter Sale is the most elite sale in Australia, and the table shows that by mating one's mare with one of the top Coolmore and Darley stallions, a breeder has more chance (53%) of having the offspring accepted into the major sale than by using all other stallions at all other farms put together. Given that commercial breeders are focussed on making a profit, this shows very clearly why Coolmore and Darley stallions are popular (and why their departure from the Hunter Valley would not simply be shrugged off by breeders.)

The table also showed that the three farms that are the major competitors to Coolmore and Darley in the Hunter Valley (Arrowfield, Widden and Vinery) contributed the majority of those yearlings not sired by a Coolmore or Darley stallion.

The final table in this section shows the average selling prices of the offspring of the stallions that are most sought after by yearling buyers, using the same recent Sydney Easter sales as an example:

Position	Stallion	Stud Farm	Average Selling Price of Offspring	Service Fee 2016 <sup>6</sup>	Proven?
1	Redoute's Choice	Arrowfield	\$573,250	\$100,000	Yes
2	Snitzel	Arrowfield	\$438,000	\$100,000	Yes
3	Lonhro	<b>Darley</b>	\$350,833	\$80,000	Yes
4	Fastnet Rock	<b>Coolmore</b>	\$334,884	Negotiable	Yes
5	Street Cry	<b>Darley</b>	\$320,750	Deceased	Yes
6	Choisir	<b>Coolmore</b>	\$320,000	\$27,000	Yes
7	Medaglia D'Oro	<b>Darley</b>	\$302,778	\$100,000	Yes
8	Exceed and Excel	<b>Darley</b>	\$295,769	\$100,000	Yes
9	More Than Ready	Vinery	\$278,636	\$60,000	Yes
10	Stratum	Widden	\$245,714	\$20,000	Yes
11	All Too Hard	Vinery	\$244,048	\$50,000	
12	Sebring	Widden	\$238,125	\$70,000	Yes
13	Sepoy	<b>Darley</b>	\$222,500	\$30,000	Early
14	I Am Invincible	Yarraman	\$219,167	\$50,000	Yes
15	Pierro	<b>Coolmore</b>	\$215,000	\$60,000	
16	Savabeel	NZ	\$201,500	NZ	Yes
17	Commands	<b>Darley</b>	\$195,000	Deceased	Yes
18	So You Think	<b>Coolmore</b>	\$180,000	\$45,000	Yes
19	High Chaparral	<b>Coolmore</b>	\$180,000	Deceased	Yes
20	Encosta De Lago	<b>Coolmore</b>	\$165,000	Retired	Yes

The table not only reflects the usual Coolmore/Darley overweighting, but it also shows the extent to which a high stallion service fee is correlated with high prices received for a stallion's offering.<sup>7</sup> The obvious rule of thumb is that the more expensive the stallion fee the more valuable will be the offspring, all else being equal. This explains why, as I showed statistically in my original submission,

<sup>6</sup> Fess here exclude GST, to put them on the same basis as the selling prices, which exclude GST.

<sup>7</sup> The two stallions on this list whose fee is less than \$30,000 had only 5 and 6 sales respectively, so their seemingly good performance reflects a small sample size. Sepoy's fee has dropped this year because he is in his fifth, and highest risk, season. His fee was \$60,000 at the time these yearlings were conceived



the most expensive stallions are the ones most heavily utilised - because that provides the highest profit potential to the breeder. (This point will be revisited in Section 6.)

### Summary of Coolmore/Darley Dominance

As seen on every measure, Coolmore and Darley collectively are not just the two largest players in the Australian stallion market, they are bigger than the rest of the industry put together.

It has been shown that if mare owners want to breed to a proven stallion, 5 of the top 7 last season are at Coolmore or Darley. If mare owners want to breed to the best of the new, unproven stallions, 4 of the top 6 are at Coolmore or Darley. If mare owners want to maximise the chances of having their mare's offspring accepted at the major sale, then Coolmore and Darley stallions provided more entrants than the others put together. And if mare owners want their offspring to sell for the highest prices, then 6 of the top 8 most popular stallions at the main sale were Coolmore or Darley stallions.

Against this background, a reader might already be wondering how the departure of Coolmore and Darley would not be accompanied by a large migration of breeding mares to that same location?

The dominance of Coolmore and Darley is only likely to get more pronounced in the near future. The two oldest stallions on the 35-most-expensive list are Redoute's Choice and More Than Ready, who are the flag bearers for Arrowfield and Vinery Stud respectively. These stallions are heading into the final phase of their careers. So it is not only the case that Coolmore and Darley are already bigger than the rest of the industry put together, but the "rest of the industry" must at some point see two of its most recognised long-time stalwarts retire.

Against this factual backdrop, I believe the only logical way to describe the market position of Coolmore and Darley to an outsider is to say that they are the two dominant players of the eight farms that comprise the "top-50" end of the Hunter Valley market, and that they are bigger than the rest of the industry put together.

This contrasts with the descriptions given in Mr Houston's report:

*"There are around 15 to 20 stud farms in the Upper Hunter region, with Darley Kelvinside and Coolmore being two of the largest."*(p15)

*"Arrowfield, Vinery and Widden stud farms.....are of a similar quality to those at Coolmore and Darley, based on their average stallion fees in 2014"*(p45)

<p>And of course, if one is trying to assess the damage that might accrue to an industry from a government decision, it makes all the difference in the world if the two parties that would be directly affected are the two that dominate the industry and give it its global stature, as opposed to them being just two out of 15-20.</p>
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## **SECTION 2 – WHAT IS REALLY AT STAKE HERE?**

As the previous section has shown, Coolmore and Darley are the dominant players in the Australian stallion market.

Prior to their arrival in this country, Australian yearlings were not on the world map. They have forced their way into global buyer consciousness over the last twenty years because Coolmore and Darley introduced stallions that raised the standard of Australian-bred yearlings, and brought these yearlings to the attention of international buyers that would previously not have even thought about buying yearlings produced in Australia. I have been a breeder for about twenty years and have seen this happen first hand.

In my original submission, I described how the elite Hunter Valley thoroughbred is now ranked on a par with yearlings raised in two other parts of the world. They are Kentucky in the USA, and Newmarket in England. I then explained how the exposure of the finest stallions in Australia (some of which also stand in Kentucky or England in the Northern spring) to a coal mining environment would potentially damage confidence in the overall yearling product, and lead buyers to downgrade the value of Hunter Valley yearlings or return to the old days of ignoring them altogether.

And accordingly I outlined how this would so erode the financial fabric of the Hunter Valley industry that the two largest stud farms in the world, Coolmore and Darley, would have no alternative but to forestall that outcome by relocating their Australian operations to another part of Australasia before it happened.

So I find it disappointing that the report by Mr Houston does not appear to address this issue. He addresses (and addresses incorrectly in my view) only the direct impacts on the Coolmore and Darley properties, and the relationship between those studs and their direct customers, namely broodmare owners such as myself who send mares to Coolmore/Darley stallions.

In my original submission, I did not really touch on the specific impacts on the Coolmore and Darley properties, for two reasons. Firstly, I assumed that Coolmore and Darley would make detailed submissions on those matters that impacted them directly. And secondly, in my view, the more important issue was and remains the effect that this decision will have on perception of the whole industry, not just on Coolmore and Darley. In my original submission and in my Denman presentation I concentrated upon that “whole of industry” impact because my corporate finance background and my positioning within the breeding industry (financial investor) allowed me to give a big picture perspective that I felt had not been adequately explored in the Department’s published report of August 2015.

In this submission, I again emphasise this critical “whole of industry” impact. But later in this section I do wish to make some observations about the specific impacts on the Coolmore and Darley properties, and the perceptions of their customers. I wish to do this because Mr Houston has incorrectly paraphrased a comment from my original submission, which implies that I do not believe that the specific impacts on the Coolmore and Darley properties are important. This is absolutely not the view that I hold, and is not what my original submission said.

In that original submission, and in my verbal presentation in Denman, I warned that if the mine went ahead, it would potentially taint the perception of the athletic ability and fitness for purpose of every horse produced in the Hunter Valley when it was offered for sale. That is, I submit that the repercussions will go beyond impacts on Coolmore and Darley alone, because of their size and significance within the industry.

I will repeat the logic that builds to the damage that the whole industry will suffer, and how this will impact on the region in financial terms, which is what I believe the Department should be most focused on:

1. People who buy the yearlings raised in the Hunter Valley currently pay up to hundreds of thousands and even millions of dollars for them. They buy them at ~18 months of age for future racing, and they are priced on their potential (most notably on which stallion is their father) before their actual athletic prowess is known. Not every horse raised in the Hunter Valley sells at these high price points, but many do, and it is important to a breeder's business model that such high prices are achieved on occasion because they are needed to offset lower prices on other yearlings. (Just as a share portfolio will have a mix of shares that perform well, perform badly, or perform to an average);
2. The stallions owned by Coolmore and Darley would either live adjacent to the South Drayton coal mine (Coolmore), or may have been raised there (Darley; see Section 3 for an explanation of this point.) Prima facie, the general public have a negative view on the impacts of coal mine proximity on physical well-being, and it is members of that general public who ultimately buy young racehorses from the breeders;
3. As seen in Section 1, Coolmore and Darley stallions directly sired more than half of the elite yearlings presented in the Sydney Easter sale in April, as is typical. And given that Coolmore stallions alone provided more than 30% of that elite catalogue, it can be deduced that the majority of Hunter Valley breeding mares will visit the Coolmore property at some point within their career, to be mated with a Coolmore stallion, even if not every year;
4. So, from the early days of the mine development, nearly half of the yearlings at the leading industry sale will have a parent who has been exposed to the coal mine, and over the long-term this ratio will climb higher;
5. Buyers of yearlings are very wary of risk. Anyone who can afford to spend \$1m on an untried young racehorse did not reach that position by being careless, or by taking unnecessary risks. Given that they can buy equally well-bred yearlings from a mining-free environment in Kentucky (USA) or Newmarket (England), it is inconceivable to me that they will not devalue the Hunter Valley product to accommodate the additional health risk;
6. If and when the pricing of the Hunter Valley yearlings is reduced to reflect this additional risk, then bloodstock assets worth more than \$2.5B<sup>8</sup> will be substantially impaired, and investors such as myself will no longer be willing to collectively invest half a billion dollars a

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<sup>8</sup> I stated in the previous submission that the value of the Coolmore/Darley stallions is of the order of \$1B. As to the mares, at the recent annual breeding stock sale on the Gold coast, many hundreds of mares (a large sample size) were sold at an average of \$134,000, which implies a 10,000 strong mare population would have a total value of say \$1.3B. Together with foals on the ground, the bloodstock value at any time will be of the order of \$2.5B.

year to fund the annual foal crop (this calculation was explained in my original submission and my verbal presentation);

7. Hence, given that it would not be difficult to relocate horses to alternative pristine environments in other states or in New Zealand (which have also had the same reputation that the Hunter Valley enjoys today in times past, as seen in section 4), thereby allowing the industry pricing structure and asset values to be preserved, I believe that it is commercially inevitable that Coolmore and Darley would relocate their breeding stallions interstate, and if that happens, the owners of elite broodmares would also transfer a large pool of mares to that same location;
8. Investors like myself who own broodmares will not be negatively impacted by such a move. Coolmore and Darley will not be negatively impacted, other than having to meet the costs of relocation, which would be minor in the context of the hundreds of millions of dollars of asset values that would be lost if they did not relocate. But the consequence for the Hunter Valley and NSW would be that annual expenditure in the region of about \$190m<sup>9</sup> will be permanently moved interstate, and as time passes, more and more of such expenditure as remains will migrate also.

This logic was fully covered in my original submission and my verbal presentation. That is why the investor base of the whole industry wants the mine extension denied, because the issues run much deeper than specific impacts on the Coolmore and Darley properties, significant enough as they are. It is purely an economic issue of one industry being unable to avoid causing irreparable financial damage to another industry that is of huge financial importance to the region, and thus forcing a large component of that latter industry to move interstate, in turn causing net financial detriment to the Hunter Valley.

#### Why Will Yearling Buyers Be Concerned?

My original submission explained that the difference in ability between the winner and runner up in a horse race is as little as one thousandth of one percent, so the slightest impairment of athletic ability can mean the difference between winning and losing a race, where tens of millions of dollars can turn on the outcome.

Nobody in this matter has been prepared to say categorically that the proximity of the mine will have absolutely zero impact on horse health. Nobody can. All that can be done is to talk about “minimising risks”, or “uncertainty”. But to someone who is contemplating spending \$1m on a young, untested racehorse, there is no rational reason why they would ignore that risk, or pay the same price that they would if that risk did not exist.

Lower selling prices would undermine the whole industry. Because this point is pivotal, I repeat below an important extract from my original submission that addressed this question of buyer

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<sup>9</sup> See original submission and Section 9, but in summary, ~\$90m spent today with service providers who look after the 3,000 broodmares that would be moved interstate, and the ~\$100m spent on stallion fees with Coolmore and Darley each year.

confidence (of course, I would prefer that the Department considers the whole of my original submission, where this extract and others can be seen in context):

*“The buying of young horses is an inherently risky undertaking to begin with. Buyers are intently focused on risk minimisation to the extent possible. And this point is even more significant given that many buyers are actually agents acting on behalf of clients that are reliant upon their expertise. There is no logical reason an agent would accept incremental risk on a product that might leave him or her open to a law suit from a disgruntled owner when there are perfectly acceptable alternatives. Especially given the Department’s own recommendation quoted above.*

*The Department acknowledges that it cannot rule out there being an impact on the health and well-being of the horses. And it doesn’t matter to what extent the horses would actually be impacted. The mere fact that 16 pages of technical discussion on minutiae such as dust, noise, vibration etc. is even necessary, and results in acknowledged “uncertainty”, and an admission that there will be some “indirect and dynamic impacts” will be sufficient, in and of itself, to affect the saleability of Hunter Valley yearlings. It is common sense that with large fortunes at stake, the Australian industry would be degraded overnight given that even a 0.01% impact on performance could be decisive and that there are two alternatives available which don’t require the risk to be even contemplated.*

*This perception problem cannot be solved by giving potential buyers a report saying that there shouldn’t be much of a problem. The perception problem cannot be solved by giving 32 pages of technical data instead of 16. It cannot be solved by clever finessing of words like “uncertainty” or “likelihood” or “probability”. As long as there is a risk of burning huge dollars because of the uncertain impact of the mine on the physical or mental health of the elite breeding stock, buyers or their agents will inevitably favour buying from the two longer-established markets that are unsullied.*

*And that perception issue will not just affect Coolmore and Darley, or just horses that have spent time on their Denman properties. Overseas buyers are not going to invest the time to track the movements of every horse and those of its parents to see who spent time in which location. They will simply treat every Hunter Valley product as devalued, and not give the matter another thought.*

*If the industry did not respond, and our product was devalued, then prices of our yearlings would have to fall substantially to induce buyers to accommodate the additional risk. As a consequence, the stallion service fees that Coolmore and Darley could charge to breeders would likewise have to fall substantially. If Coolmore and Darley did nothing, the value of their stallions would collectively be eroded by hundreds of millions of dollars.*

*If one does not understand the premium price-point of the Australian product, and how the understandable risk-aversion of the buying bench will lead to a significant erosion of saleability, then it is unlikely that one can understand the competitive responses and consequences that must inevitably follow.*

*But to those like myself who understand the industry model, it is an inescapable conclusion that the potential impact on the value of their business would be so devastating that there would be no other choice open to Darley and Coolmore. They would have to relocate or their underlying business model would be compromised; and as seen further on, that will directly lead the owners of thousands of*

*breeding mares to move their mares to whatever location the studs choose as the new base for their stallions.*<sup>10</sup>

If the buyers of yearlings decide to downgrade the value of Australian yearlings because of this issue, or bypass them altogether, then Coolmore and Darley's hand will be forced, as will that of investors like myself.

I find it intriguing that in Mr Houston's report there seems to be essentially no acknowledgement of the importance of the end buyer of the product. The report gives the opinion that Coolmore and Darley will not leave the Hunter Valley, but it talks only of the interplay between Coolmore/Darley and their direct "customer", in the sense of mare owners (like myself) who pay to use their stallions. But Mr Houston does not seem to consider the bigger picture in which the stud farms, and investors/mare owners, are essentially in a collaborative partnership to produce an end product for sale to yearling buyers.

It will be seen from the extract quoted above from my original submission that much significance attaches to the fact that most of the top Hunter Valley yearlings are bought by agents rather than the eventual owners. This might be international agents who choose among the American, English or Hunter Valley products for overseas buyers at the most expensive end, or it might be Australian horse trainers like Gai Waterhouse or Lee Freedman who buy horses and then on-sell them to local clients or syndicators. If the agent/trainer did not mention the coal mining issue they would potentially expose themselves to damages one day from a client who will say that he/she was not told about the mining issue when the horse was purchased on their behalf.<sup>11</sup> This is especially so given that there are now a number of submissions on the public record talking about the uncertainty of the impact of the mine on horse health.

I also provided an example in my original submission as to how the Hunter Valley industry suffered financially in 2009 from loss of buyer confidence in its yearling product after a mild outbreak of influenza in the Hunter Valley in 2007 when that yearling crop was born (a very minor and temporary issue compared with the mining issue). Buyers downgraded yearling prices on that occasion.

Mr Houston's report has unfortunately, in my view, not focused on the issue of the reaction of yearling buyers to the coal mine, and hence he does not state why he believes buyers will continue to buy a discretionary product from the Hunter Valley with "uncertainty" due to mining risk, when they can buy a risk-free product from the two other premium breeding centres in the world. He does not address the issue of how agents will react to the possibility of litigation for non-disclosure of the mining issue, or how potential buyers would react if they were told of the risk in advance.

The influenza issue of 2007/9 that I discussed in my original submission provides an example of why the industry has every right to be concerned about how yearling buyers will react to the mining issue.

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<sup>10</sup> References to the Department in this extract from my original submission were references to the Department's report dated August 2015, SSD6875

<sup>11</sup> There are precedents for trainers/agents being sued by owners on whose behalf a racehorse was purchased.

### The Specific Implications for the Reputation of Coolmore and Darley.

I have explained above that consideration of the bigger picture impact on the industry leads me to the inevitable conclusion that Coolmore and Darley will have no alternative but to relocate interstate, or to New Zealand, if the mine extension is approved. Their size and dominance of the industry makes them a de facto proxy for the whole industry in the minds of many, especially yearling buyers from overseas, so a problem for them is essentially a problem for the whole industry.

But even if that was not the case, in my view the specific impacts on their individual properties would equally point to the inevitability of them being unable to continue operations from their current properties. I have not concentrated on this aspect because the inevitable “whole of industry” impact is sufficiently compelling on its own.

But because of the way my original submission has been paraphrased, I do wish to revisit the brief comments I made there about the relevance of the specific properties to the operations of Coolmore and Darley. In my original submission, I said the following:

*“The business model of a horse stud requires a large property in a tranquil environment but the specifics of one property over another are not particularly relevant. The character of the property carries a certain cache that is of use in branding, but is of zero direct relevance to the service activity that takes place there. Breeders choose stallions for their individual attributes, not the quality of the scenery they enjoy.”*

As the context of that quote makes clear, as long as a property is in a tranquil environment, it is not important to the activity that takes place there whether the specific setting is in the Hunter Valley, or in Victoria or in New Zealand. My original submission, and this submission in Section 4, both make it very clear that there are alternative locations in Australia and New Zealand that are equally as functional as the Hunter Valley, notwithstanding that it is a particularly beautiful area.

That is not the interpretation that Mr Houston has drawn from my submission.<sup>12</sup> Mr Houston did not quote the whole of my paragraph – which would have made my meaning clear – but has paraphrased it in a way that unfortunately implies that I support the notion that it would make no difference to Coolmore and Darley if there was a coal mine next to their properties. I emphatically reject any such implication.

For the avoidance of any doubt – not that there should be any – I submit as a breeder that it would be impossible for Coolmore and Darley to maintain their existing operations at the affected properties were the mine to go ahead. My submission emphasised the necessity of stud farms being in a tranquil environment. For the avoidance of any doubt – not that there should be any – the phrase “tranquil environment” does not envisage stud farms next to working coal mines, any more than it would envisage a stud farm next to a munitions testing site.

Mr Houston’s report says the following about image:

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<sup>12</sup> Mr Houston paraphrased my comment on page 9 of his report.

*“Stud farms are not alone in wanting to portray a good image of themselves through the physical beauty of their premises. It is common in many customer-facing industries – from vineyards to retailers, shops and restaurants – for companies to manage their image and present their business in the best possible way, to customers and potential investors. Further, in my experience it is common for businesses producing high quality products or services to expend more effort to present and promote them.”(p20)*

In my view, this comment misses the rather fundamental point that the tranquillity of a horse stud environment is not just about image for the sake of image. The need for a horse stud to have a tranquil environment is not analogous to the promotion of “image” in high end retailing. The concepts are worlds apart.

If a shop selling luxury women’s accessories somehow found itself sandwiched between an adult sex shop on one side and a needle exchange clinic on the other, there is no doubt that the shop would quickly seek new lodgings. The environment would no longer be consistent with its “image”. But in that example, the qualities of its handbags or scarves would be totally unaffected by the developments in the neighbourhood, and all that would have changed is the customers’ perception of the purchase experience. The high end million dollar fitouts that luxury retailers operate from are not critical to the functionality of the products sold there. In fact, the products could be sold from suitcases on the footpath and still be exactly the same. That is, the image is for the sake of image.

But in the case of horse studs, the need for tranquillity is not just about image; tranquillity is a necessary precondition to the well-being and activities of the horses that reside there. All horse studs have a peaceful, tranquil and relaxing setting, because, unlike the example of the handbags, this tranquil environment is critical to functionality. It doesn’t matter whether the stud farm has stallions that stand for \$2,000 per service or \$200,000 per service, they all have tranquil, picture-postcard environments. During the mating season, stallions are called upon to service mares up to three to four times a day. Mares come into season for only brief intervals, and there is an enormous logistical effort needed to schedule hundreds of mares to be mated with a single stallion in a brief three month window. Stallions need complete physical and mental relaxation between engagements, and this is totally incompatible with mine blasting being conducted next door.

If a stallion misses even one service opportunity, it can make the difference between a mare being impregnated with a potential \$250,000 foal, or missing her window of opportunity and the breeder having nothing to sell that year. For that reason, breeders like myself would not take the risk of sending a valuable mare to a stud where the mating had an elevated risk of being unsuccessful.

All stud farms need tranquillity. As the largest operators in the world, Coolmore and Darley go the extra yard to showcase their properties as particularly beautiful, befitting their status as industry leaders. But that final touch that differentiates them overlays a base case requirement for tranquillity at every stud farm, which has nothing to do with image and everything to do with functionality and fitness for purpose.



### **SECTION 3 – MIGHT COOLMORE AND DARLEY TAKE DIFFERENT APPROACHES?**

Mr Houston's report is made complicated, in my view, by his consideration of a matrix of possibilities for the responses of either Coolmore or Darley to a mine approval: He considers the possibility that one might leave the Hunter Valley while the other stays, or that one or both could move elsewhere in the Hunter Valley, or both might move interstate etc.

These different possibilities were included because Mr Houston reasons that Coolmore and Darley will be impacted in different ways by the mining approval.

This section explains why Coolmore and Darley would not be impacted differently, and shows why it is likely, in my view, they would both come to the view that relocation of their whole Hunter Valley breeding operation is a commercial necessity.

The frequent switching between multiple scenarios in Mr Houston's report had the effect, in my opinion, of making his report harder to follow. At times I found it difficult to recall which particular scenario or scenarios Mr Houston was attempting to support or negate. And that unnecessary complexity again had the unfortunate consequence, in my view, of distracting from the real issues in this matter.

#### **The Darley Properties**

Darley has two properties that are involved in its Hunter Valley breeding activities. The one adjacent to South Drayton, which also borders Coolmore's single property, is the property known as Woodlands. Prior to Darley's arrival in Australia, Woodlands was a prominent stand-alone stallion farm, and was owned by the Ingham brothers. Now known as Darley Woodlands, the property is mainly used by Darley to keep its own broodmares and their offspring, whereas Darley's other property, known as Kelvinside, is where its stallions currently reside. It is the Kelvinside property that third party mares (such as mine) visit when they are to be mated with Darley stallions.

Mr Houston's report highlights the different uses of the Woodlands and Kelvinside properties, noting that although Coolmore's stallions would be resident next to South Drayton, Darley's stallions are actually some distance away at Kelvinside. Hence, he says, Darley's issue would only be with its broodmares, which are not (he says) the subject of any interaction with the customers who use Darley's stallions at all<sup>13</sup>. Accordingly, Mr Houston offers the opinion that Darley can simply move its broodmare farm elsewhere in the Hunter Valley if it wishes, and continue its stallion operations at the Kelvinside property as it does today. And under this scenario, he argues that Darley could leave Coolmore to its fate, and in fact could take Coolmore's customers if and when Coolmore left the Hunter Valley.

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<sup>13</sup> I believe that Mr Houston overlooks the fact that potential customers of the Darley stallions do in fact visit Darley's broodmare property because inspecting the quality of the foals and yearlings by their stallions is an important part of the process by which we evaluate their stallion offerings. I was not aware that there are no directions to Woodlands on Darley's website, because as an industry participant, I know where it is. The directions for Kelvinside are there, I imagine, because members of the public often ask to see the top stallions.

### The Darley Business model

On this issue, somewhat intriguingly, Mr Houston admits an important gap in his industry knowledge. Speaking about the Darley business model, as explained in submissions by Darley itself, Mr Houston quotes Darley and says:

*“Darley’s business is to “breed to race and race to breed” which I take to mean that some of the thoroughbreds produced at Woodlands will be retained by Darley.”(p25)*

By using the words “which I take to mean” Mr Houston concedes that he is not certain what Darley’s business model is, but surmises it as best he can. And as will be seen below, his “surmise” that “some” of the thoroughbreds produced at Woodlands would be retained by Darley is off-target. As I said, this is an intriguing admission, since it is unusual in my experience that a party can openly acknowledge that they are not certain about the business model of the largest participant in an industry, interpret that participant’s business model incorrectly, yet still present as an “expert” in that industry and deign to give opinions that are at odds with the advice of that participant.

Darley owns perhaps the biggest individual pool of broodmares in Australia<sup>14</sup>, and breeds hundreds of yearlings every year by mating those mares with its owned stallions. But it does not breed these yearlings to sell. Its business model is to race all of the horses it breeds, and accordingly it is by far the biggest owner of racehorses in Australia. So the interpretation that Darley maybe retains “some” of the thoroughbreds produced at Woodlands is very much at odds with the reality that Darley’s business model does not envisage selling any of them. That is what is meant by the phrase “Darley breeds to race”.

By having many hundreds of horses from successive crops racing each year, Darley wins a lot of prizemoney on the racetrack. But its primary purpose for racing all of these horses is to have its own internal production line of future stallions and elite broodmares.

Prized stallions are worth immense sums. I gave the opinion in my original submission that the collective value of the Coolmore and Darley stallions would be of the order of \$1B, and Mr Houston quoted newspaper articles that indicated that just two of Coolmore’s stallions were individually valued in recent purchase transactions at \$60m and \$40m. By contrast, no stallion in Australia has ever won as much as \$10m prizemoney on the racetrack, which shows that the real value proposition of owning an elite male racehorse is not so much the prizemoney as the consequent stallion value. (Which is why buyers pay huge sums to buy the best bred male yearlings around the world, because the ones that prove to be the best racehorses are then worth many tens of millions.)

Statistically, Darley will find that one or more of its best male racehorses from each generation have sufficient credentials to become stallions. Likewise, those female racehorses that show racing talent are then added to the broodmare pool when they finish their racing careers.

This is why Darley described the second limb of its business model as “Darley races to breed”.

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<sup>14</sup> I am not aware of any statistics in this regard, but industry participants would agree this.

After the Darley yearlings become two year old and three year olds, and move on to their racing careers, Darley will periodically sell those horses that prove to have limited racing talent. As explained in Section 1, the criteria to become a commercially appealing stallion are very demanding, so as and when Darley determines that some horses will not meet those exacting standards, they may sell them to other buyers that are happy to aim these horses at easier races.<sup>15</sup> The handful of very elite male racehorses become Darley stallions.

This Darley business model is basic knowledge to anyone in the breeding industry.

### The Significance of the Darley Business Model in This Context

Having seen that Darley's business model is to breed its own future stallions, it should now be apparent why South Drayton would impact Darley in the same way as Coolmore. Although the Darley Kelvinside (stallion) property is physically removed from Woodlands, and hence from South Drayton, many of the stallions that stand at Kelvinside are born and raised at Woodlands.

Stallions that Darley owns at present that were raised at Woodlands include Sepoy, Exosphere, Epaulette, Denman, Sidestep, Albrecht, Helmet, Kuroshio and Skilled. The majority of those are now based at Kelvinside.

At this moment, the next generation of Darley stallions are being raised at Woodlands, and will be ready to stand as stallions at Kelvinside in as little as two years.

If the yearling-buyer market has a problem with the sires of potential \$1m yearlings living next to coal mines, as I believe it will, then Coolmore would be affected immediately and Darley would be affected within as little as two years when the next wave of stallions arrive at Kelvinside having been raised at Woodlands.

Any decisions that Darley make will be made with an eye on the long-term. No efficiently run business would make a decision today that simply postponed a problem for two years, so in my view Darley will approach this from the same point of view as Coolmore. That is to say the proximity of the mine will be an issue for each of their stallion rosters, and this will taint the whole industry because of their collective significance to that industry.

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<sup>15</sup> In fact, in one part of his report Mr Houston extols the virtues of Edinglassie (See Section 8) by citing evidence that its average price for all horses sold in a particular year was much higher than Darley's, as follows: *Edinglassie is a good comparator for the extent to which the perception of Darley Woodlands would be affected by the presence of a coal mine, since the quality of thoroughbreds sold by Edinglassie are not inferior to those sold by Darley – in 2015, the average, publicly available sale price for horses sold by Darley and Edinglassie was \$20,694 and \$74,809 respectively.*" (p23 of his report.) Even if Mr Houston had not himself expressly stated his uncertainty as to the business model of Darley, this price comparison had already said as much, because the main reason Darley's sales prices are low is that by definition, they only sell horses if and when they are proven to not have superior racing ability or future breeding potential.

Accordingly, I believe the following opinion put forward by Mr Houston is not correct:

*“The Kelvinside stud farm is unaffected by the proposed Drayton South mine and so the perception of broodmare owners considering using Darley stallions will not be changed by the mine. It follows that the proposed mine will have no effect on the operation and expected revenue from Darley’s Kelvinside stud farm.”(p18)*

#### In Any Event, Darley Might Expand

I have shown that the Darley Woodlands property is presently used to house its broodmares and their offspring, which means that many of Darley’s stallions are raised at Woodlands. But in forming the view that a mine adjacent to the Woodlands property would not impact Darley’s stallion business, I believe that Mr Houston overlooked an even simpler point. And that is that the Woodlands property, as noted above, is actually a fully functional stallion farm if Darley should wish to use it that way at any time, either in part or in full. Darley at present have a large number of stallions that they stand interstate, and this year they are even leasing two stallions to New Zealand, such is their embarrassment of riches. If Darley decided to stand more stallions in the Hunter Valley in a season than Kelvinside could accommodate, it has the flexibility of using Woodlands for that purpose, even if it is not doing so today. So again, in my view Darley would see South Drayton as something that directly impacted its stallions, as would Coolmore.

#### The Importance of Co-Location for Coolmore and Darley

For reasons shown above, it is likely that Darley and Coolmore can each be expected to consider the consequences of a mine approval from the same perspective – that is, that it will directly impact on their stallions.

Even if the integration between Woodlands and Kelvinside did not work in the way that it does, I believe it is still a matter of commercial logic that Coolmore and Darley would not want to base themselves in different locations. Both Darley and Coolmore, understanding the industry, will be aware that the Hunter Valley has attained its exalted status only because the two of them are located together, and that if they were to be in different parts of Australia, then the Australian industry as a whole would be the loser, including themselves individually.

Members of the public, even if they don’t have any formal expertise in retailing, instinctively understand that retailers do better when they are gathered together in a large shopping mall. Having Myer, David Jones, Harvey Norman et al under the one roof works better for all the retailers than having them in stand-alone locations on opposite sides of the city.

And so it is with breeding. If Coolmore and Darley are both in the same location, as they are today, it ensures that the best broodmares in the country will be gathered in that same location; and hence buyers cannot afford to miss the sales of that region’s yearlings because they are of a uniformly high quality. By contrast, if Coolmore and Darley were in different states, then the best mares would not be concentrated in one location, and buyers would be less inclined to attend both sales.

As a very real demonstration of this point, it will be shown in Section 4 that before Coolmore and Darley both set up in the Hunter Valley, the Australian industry had no had no single standout centre. Victoria, South Australia, the Hunter Valley, Southern NSW, Queensland and even Western Sydney all had individual breeding centres, and they each experienced times when they had the best stallions in the country. Hence, before Coolmore and Darley arrived, the sales in different states waxed and waned in pricing depending on which states had the best stallions from time to time.

The problem that this caused for the Australian breeding industry in those days was that this meant that not all of the best product was gathered together. The Victorian sales sold the best and the worst Victorian yearlings, the Sydney sales sold the best and the worst Sydney yearlings, etc.

The impact of this was highlighted by John Messara, in 1987, in his capacity as CEO of Australian Racing and Breeding Stables, which later became Arrowfield Stud. He said<sup>16</sup>:

*“For buyers, attendance at Trentham (New Zealand) is virtually compulsory. This cannot be said of any Australian Yearling Sale. Very few buyers are willing to travel to five or six Australian yearling sales in order to choose from the top Australian yearlings; even if they did so the very fragmentation of the Australian marketplace makes for cautious buying patterns. The result – lower prices for Australia yearlings – acts as a depressant on investment in the industry. The solution is equally simple and obvious: a National Select Yearling sale in Australia. In a nutshell, it would be the showcase and shopfront of our industry.”*

Accordingly, if Coolmore and Darley were to now be in separate locations, the Australian industry would revert to the 1987 situation, where it would not be possible to find all of the best horses in one location. And that would again lead to “lower prices for Australian yearlings”, and “depressed investment in the industry”. And of course lower prices for yearlings and lower investment by people like myself would mean lower fees received by Coolmore and Darley.

So contrary to the opinion of Mr Houston that Darley, acting rationally, might remain in the Hunter Valley and try to profit from Coolmore’s departure, history suggests that strategy would be a negative for Darley and the whole industry. Darley and Coolmore are both likely to be aware that if they are in the same location, be that the Hunter Valley or interstate, then and only then would they both prosper to the maximum. It is as I said in my original submission:

*“The Hunter Valley, Kentucky and Newmarket provide wonderful environments for raising young horses, but the same could be said of several other locations in Australia and the rest of the world. What sets the horses produced in these locations apart from horses produced elsewhere is that they are the three locations in the world where the elite stallions and breeding mares are located in deep concentrations, and result in a critical mass of premium product that compels the attention of international buyers and their agents.”*

Mr Houston has raised the further possibility of both Coolmore and Darley relocating to new farms in the Hunter Valley. That opinion is considered in Section 7, after other propositions have been established in the intervening sections.

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<sup>16</sup> Article in “Turf Monthly”, May 1987 edition, p24

#### **SECTION 4 – IS THE HUNTER VALLEY TOO ATTRACTIVE FOR COOLMORE AND DARLEY TO LEAVE?**

At the end of the preceding section I recalled an extract from my original submission which stated that the Hunter Valley today ranks alongside Kentucky (USA) and Newmarket (England) as a centre of world-renown for the production of young thoroughbreds. That paragraph stated that the Hunter Valley and the two overseas locations are by no means unique in their physical attributes, and that what sets them apart is the concentration in a small area of many stallions and broodmares of world standard. In my original submission I continued after that paragraph as follows:

*As to the existence of infrastructure in the Hunter Valley, the same infrastructure is available in other parts of Australia and in New Zealand. Victoria, for example, has infrastructure that currently supports around 6,000 mares, nearly two-thirds the amount of the Hunter Valley. What sets the two locations apart is the value of the stallions and mares in each, not the quality of the land.*

*It is a matter of record that a racehorse named Black Caviar, raised in Victoria, became the world's highest rated racehorse during her career that ended in 2013, so there is no question mark over the ability of the Victorian environment to produce great racehorses. In fact, before the arrival of Coolmore and Darley took the Hunter Valley to a new level, there were many years in which Victoria hosted the leading stallion in Australia.*

*A similar case could be made for Queensland, and an even better case could be made for New Zealand. The latter country has a world-wide reputation for raising excellent horses, and it is only the decision by Coolmore and Darley to set up in the Hunter Valley that took money out of the NZ industry and saw many of its best breeding mares move to the Hunter Valley.*

The very clear advice I gave in my original submission was that there is nothing inherently compelling about the Hunter Valley that means that it must be the leading thoroughbred breeding centre in Australia, let alone Australasia. There are several other locations that have attractive natural environments, and equally storied histories. If Coolmore and Darley had set up in one of those alternative locations then that alternative would enjoy the status the Hunter Valley now does.

I repeat that advice here; it remains the case that if Coolmore and Darley were to relocate tomorrow to another part of Australia or New Zealand, then the Hunter Valley would lose its status to that new location, and huge numbers of top class broodmares (3,000 to begin with) would follow. That new centre would become, very quickly, the leading breeding centre in Australasia in terms of both quality and quantity.

By contrast, Mr Houston has offered the opinion that the Hunter Valley has inherent physical and commercial qualities that make it the best place in Australia for Coolmore and Darley to be located, and that accordingly (he says) any threat to leave is hollow.

In his report, Mr Houston states that:

*“The Upper Hunter region has a number of economic characteristics that make it a particularly attractive location for breeding thoroughbred horses, including:*

- *it is close to major ports and markets (in particular Sydney);*
- *It has the best reputation of any thoroughbred breeding area in the southern hemisphere;*
- *it has a large number of high quality service providers that are required by the thoroughbred breeding industry;*
- *it has an ideal environment for breeding thoroughbreds, including a temperate climate, protected aspect and varied terrain combined with a lack of tropical diseases. The resultant moderate climate, low risk of pests and diseases, topography, and reliable irrigation options are ideal for producing premium quality horses.”(p27)*

As to the first, third and fourth of these points, the same can be said of other places. For example, every capital city in Australia, and New Zealand, has a high-class sales facility. The buyers of Australia’s best yearlings come from around the world, not just Sydney. Sydney is the major market today because the best yearlings are bred in the Hunter Valley, but if the best yearlings were bred in Victoria, then the same buyers would go to Melbourne.

If Coolmore and Darley were to move to Victoria or New Zealand, then they would also have access to an ideal environment for raising horses (as demonstrated below) and access to all of the quality service providers that they currently have in the Hunter Valley. Victoria breeds many thousands of horses every year, and it hosts one of the most prominent horse racing carnivals in the world (the Melbourne Cup carnival). The idea that hundreds of the most valuable racehorses in the world spend months in Victoria but that it does not have every modern facility for the care of valuable horses would seem unlikely.

In any event, I can give direct evidence as to the calibre of the support industries in both Victoria and New Zealand, having had mares reside in both locations for some years in times past.

As to the second of Mr Houston’s dot points, which states that the Hunter Valley has the best reputation in the Southern Hemisphere, I believe this is circular logic, because the Hunter Valley only has that reputation because Coolmore and Darley are based there and not elsewhere.

Despite having merely listed a handful of virtues that are shared with several other locations, Mr Houston reaches the following conclusion:

*“the Upper Hunter is the best location for breeding thoroughbreds in the southern hemisphere and moving away from the region is likely to reduce Darley’s profits”(p17)*

He offers no further explanation or evidence as to why the Hunter Valley is inherently superior to other locations that have equally attractive attributes. And the historical information presented below will show quite clearly that several other parts of Australasia were regarded as having equal or superior breeding environments before Coolmore and Darley entered the industry, and would today have the same reputation as the Hunter Valley had Coolmore and Darley settled there.

#### How the Hunter Valley Was Viewed Before the Coolmore and Darley Era Began

The town of Scone today is the epicentre of the Hunter Valley breeding industry, which is the most important nursery for young horses in the Southern Hemisphere. So dominant is the Hunter Valley today that it is natural to assume that it has always been seen in this light by breeders. Given everything we know today, Mr Houston's claim that the Hunter Valley is the best location for breeding thoroughbreds in the Southern Hemisphere would seem a reasonably safe assumption.

However, having followed the developments in the industry for a long time, and having an extensive library of historical information, I can say that in the era before Coolmore and Darley set up in the Hunter Valley, it was not regarded in the same way it is today. Its exalted reputation has come about solely because of the modern-day presence of the world's two largest stud farms, and not because it has intrinsic qualities that make it better than other locations.

I mentioned in Section 1 a stud farm called Yarraman, which is nowadays one of the eight most prominent commercial studs in the Hunter Valley. In the 1960s the property changed hands, and a thoroughbred industry journal at the time described Scone as *"one of the oldest and richest grazing areas of New South Wales."*<sup>17</sup> The purchaser of the property at that time announced the intention of breeding some horses (which the property had not done for many decades), and said<sup>18</sup>:

*"I am giving Yarraman Park a five-year trial as a property for the production of thoroughbred stock. If I feel that it is not successful or worth the efforts of my family and staff I'll cut back to a few mares and go in for cattle and crops."*

It seems remarkable today that in an era that was less than 30 years before Coolmore arrived, an industry journal would refer to Scone and not even mention any association with horse breeding; and it seems equally remarkable that Yarraman Park's purchaser was only prepared to "trial" it with respect to horses given its current-day success.

Clearly something significant changed between the 1960s and today, and it is not that the Hunter Valley changed its climate, topography, or its proximity to Sydney. What changed the area's fortunes was the decision by the world's two largest stallion farms to set up Australian operations there.

The relevant date that changed the area's fortunes was 1989. Coolmore at that time was the largest stallion farm in the UK, and did not have a permanent presence in Australia.

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<sup>17</sup> Article in "Turf Monthly" September 1963 edition, p2

<sup>18</sup> Article in "Turf Monthly" September 1963 edition, p10



In 1989, Coolmore's then principal, Robert Sangster, agreed to "shuttle" a top class UK stallion to Australia for the first time, named Last Tycoon. Coolmore had previously shuttled stallions to Australia as far back as in the 1970s, to Victoria and South Australia, which in that era were prominent breeding centres, as will be seen below. But those early transactions were not with the best of Coolmore's stallions. Last Tycoon was in another league, and it happened that the farm that sought him for shuttling (Segenhoe) was based in the Hunter Valley.

Last Tycoon went on to be champion stallion in Australia on the back of his first crop of Australian-bred runners alone (none of Coolmore's earlier shuttle stallions had achieved this). The following year, in 1990, Coolmore sold a 50% interest in one of their top UK stallion prospects (called Danehill) to John Messara of Arrowfield Stud, also in the Hunter Valley, and pursuant to that partnership, Danehill commenced to "shuttle" between the UK and the Hunter Valley in their respective springs. Danehill also went on to become champion stallion in Australia.

The instant success of Last Tycoon and then Danehill showed Australian breeders that the Coolmore stallions were a class above the local stallions of that era. It also showed Coolmore that the attributes of its British stallions translated readily into Australian conditions, and that there was an Australian market for its English stallions that could effectively double their earnings capacity by standing in two hemispheres in the same year. Around the same time, beneficial changes were made to the tax depreciation regimes for stallions and broodmares by the Hawke Government, which had the effect of allowing the Australian industry to compete more effectively against New Zealand.

Off the back of these developments, Coolmore decided to set up in Australia. The Hunter Valley was not the standout breeding location in that era, and Coolmore's decision to settle in the Hunter Valley was said at the time to be influenced by the fact that Danehill and Last Tycoon were already settled there and had attracted a customer base. Coolmore repurchased Arrowfield's 50% interest in Danehill, and also bought the property that he was standing at (then known as Arrowfield and now known as Coolmore). The reason Danehill was brought to the Hunter Valley in the first place was because it was John Messara who was the individual who assessed him as ideal for Australian conditions and bought 50% of him. Had a Victorian stud master spotted Danehill's potential first, then Danehill would have stood in Victoria, and Coolmore would probably have set up operations there instead, and the Hunter Valley economy would be very different today.

Of course when Darley also chose to set up in Australia in the early 2000s, the decision to set up in the Hunter Valley was an obvious one. Coolmore was already there, and the presence of the world class Coolmore stallions had already led to most of the nation's elite broodmares being moved to the Hunter Valley. (My personal actions were indicative of that trend, as I concentrated my own mares in the Hunter Valley, having previously kept mares in Victoria, and both the North and South Islands of New Zealand as well.)

To verify my statement that the "pecking order" in breeding was very different before Coolmore and Darley decided to set up in the Hunter Valley, I have prepared the following table which shows the location of the champion Australian stallion in the quarter century before Coolmore arrived first, and the quarter century since.

ERA BEFORE COOLMORE AND DARLEY			ERA POST COOLMORE AND DARLEY		
Season	Champion Australian Stallion	Breeding Location	Season	Champion Australian Stallion	Breeding Location
1963/64	Wilkes	Southern NSW	1989/90	Sir Tristram	New Zealand
1964/65	Star Kingdom	Hunter Valley	1990/91	Marscay	Hunter Valley
1965/66	Better Boy	Victoria	1991/92	Nassipour	New Zealand
1966/67	Alcimedes	New Zealand	1992/93	Marscay	Hunter Valley
1967/68	Agricola	New Zealand	1993/94	Last Tycoon	Hunter Valley
1968/69	Wilkes	Southern NSW	1994/95	Danehill	Hunter Valley
1969/70	Alcimedes	New Zealand	1995/96	Danehill	Hunter Valley
1970/71	Better Boy	Victoria	1996/97	Danehill	Hunter Valley
1971/72	Better Boy	Victoria	1997/98	Zabeel	New Zealand
1972/73	Oncidium	New Zealand	1998/99	Zabeel	New Zealand
1973/74	Matrice	South Australia	1999/00	Danehill	Hunter Valley
1974/75	Oncidium	New Zealand	2000/01	Danehill	Hunter Valley
1975/76	Showdown	Victoria	2001/02	Danehill	Hunter Valley
1976/77	Better Boy	Victoria	2002/03	Danehill	Hunter Valley
1977/78	Showdown	Victoria	2003/04	Danehill	Hunter Valley
1978/79	Century	Victoria	2004/05	Danehill	Hunter Valley
1979/80	Bletchingly	Hunter Valley	2005/06	Redoute's Choice	Hunter Valley
1980/81	Bletchingly	Hunter Valley	2006/07	Flying Spur	Hunter Valley
1981/82	Bletchingly	Hunter Valley	2007/08	Encosta De Lago	Hunter Valley
1982/83	Sir Tristram	New Zealand	2008/09	Encosta De Lago	Hunter Valley
1983/84	Vain	Hunter Valley	2009/10	Redoute's Choice	Hunter Valley
1984/85	Sir Tristram	New Zealand	2010/11	Lonhro	Hunter Valley
1985/86	Sir Tristram	New Zealand	2011/12	Fastnet Rock	Hunter Valley
1986/87	Sir Tristram	New Zealand	2012/13	Exceed and Excel	Hunter Valley
1987/88	Zamazaan	New Zealand	2013/14	Redoute's Choice	Hunter Valley
1988/89	Sir Tristram	New Zealand	2014/15	Fastnet Rock	Hunter Valley

This table shows very different scenarios before and since the Coolmore/Darley era. On the right hand side, it can be seen that nowadays, including every year since the Hunter Valley hosted both Coolmore and Darley (2001 onwards), it is a given that the champion stallion in Australia will be found in the Hunter Valley. However, as can be seen from the left hand side of the table, before the Coolmore/Darley era, it was only occasionally the case that the Hunter Valley had the top stallion in Australia – 5 times in 26 years. It was less likely to attain this honour than Victoria, and in turn Victoria was in the shadow of the New Zealand industry, which became more dominant as the 1980s progressed. In the era before Coolmore and Darley, even breeding centres in South Australia and Southern NSW at different times hosted the top stallion, an unthinkable situation today.

Because the best stallions were likely to be found anywhere from one year to the next before Coolmore/Darley arrived, the best breeding mares were scattered around the different locations.

There was no reason to send a South Australian mare to Victoria for example, because there was as much chance of the best stallions being found in South Australia the year after. Only when Coolmore and Darley brought the best stallions in the world to one place did it compel the owners of top class breeding mares to gather them in the Hunter Valley. The two giants were the catalyst for bringing a dominance to one centre whereas prior to that development the Australian industry was a collection of individual state industries that jostled with each other for leading status from time to time.

Over the course of the 20<sup>th</sup> century, all parts of the Australian breeding industry took turns for their day in the sun, purely as a function of the success they had in standing the right stallions from time to time. The Hunter Valley was strong in the 1930s, the 1950s and the early 1960s, and parts of the 1980s. Queensland was very strong in the 1940s, and Southern NSW was very strong in the 1960s. Victoria and South Australia were very strong in the 1970s and 1980s, and New Zealand was strong throughout, and especially in the 1970s and 1980s.

If one looks at not only the single top stallion, but at the underlying depth, the contrast between pre and post Coolmore/Darley is even more pronounced.

In Section 1, I showed that every one of the top 15 stallions in Australia can be found in the Hunter Valley today, such is its dominance over the rest of the Australian and New Zealand industry. But before Coolmore and Darley, it was a very different story. The following table shows the location of the top 15 stallions in Australia in 1990/91, immediately as the Coolmore/Darley era was about to take off.

Position	Stallion	Location
1	Marscay	Hunter Valley
2	Star Way	New Zealand
3	Loosen Up	Victoria
4	Luskin Star	Southern NSW
5	Sir Tristram	New Zealand
6	Don't Say Halo	South Australia
7	Salieri	Hunter Valley
8	Victory Prince	Southern NSW
9	Imposing	New Zealand
10	Godswalk	South Australia
11	Noble Bijou	New Zealand
12	Century	Victoria
13	St Briavels	Tasmania
14	Balmerino	New Zealand
15	Durham Ranger	Victoria

That is, in 1990/91, there were only two Hunter Valley stallion on the top 15 list, and Victoria and South Australia were just as prominent. But New Zealand dominated the list, with five of the top 15

stallions based there. This 1990/91 year was not an aberration; I could illustrate the same point during other years of the 1980s.

Looking back to the previous decade, I clearly recall that the breeding industry in the Hunter Valley ranked behind Victoria and even South Australia. For example, the table below shows the location of the top 10 stallions in Australia in 1972:

Position 1972	Stallion	Location
1	Better Boy	Victoria
2	Wilkes	Southern NSW
3	Smokey Eyes	Queensland
4	Bluescope	Western Sydney
5	Showdown	Victoria
6	Matrice	South Australia
7	Sunset Hue	Northern NSW
8	Pakistan II	New Zealand
9	Latin Lover	Victoria
10	Alcimedes	New Zealand

A second look may be needed at this table because it seems so counter-intuitive today. That is, In 1972, as recently as the second decade before Coolmore and then Darley entered the local market, not one of Australia's top ten stallions was to be found in the Hunter Valley. By contrast, Victoria, South Australia, Queensland and New Zealand all had stallions, in some cases multiple stallions, which were better performed than any in the Hunter Valley.

To repeat: The Hunter Valley had no particular aura that made it more prominent than other parts of Australia in the times before the Coolmore and Darley era began.

This reinforces my point that a number of Australian and New Zealand locations have suitable environments for the raising of young horses. The only time that a particular location has ever been dominant in the Australian breeding industry is the domination that has evolved in the Hunter Valley this century. The domination is unprecedented, and it is purely due to the good fortune (for NSW) that the world's two largest stallion farms, Coolmore and Darley, chose to establish their Australian headquarters in the Hunter Valley.

But had Coolmore and Darley decided to establish themselves elsewhere that alternative location would today enjoy the economic dominance that the Hunter Valley and NSW enjoy. And most importantly, given the mobility of the horse assets, that alternative scenario could easily become reality overnight because there has never been a compelling reason that Coolmore, Darley and investors like myself have to be based in the Hunter Valley, and there may shortly be a very compelling reason to leave.

This historical perspective shows clearly that before Coolmore and Darley set up in the Hunter Valley, the area's proximity to ports, the presence of support industries, and its climate and topography did not serve to make the Hunter Valley any more attractive than other locations and arguably less so. It could not have been said in the 1970s or 1980s that the Hunter Valley "is the best location for breeding thoroughbreds in the Southern Hemisphere".

The reason I have set out this historical information in some detail is to counter the view put forward by Mr Houston that Coolmore and Darley will not move away from the Hunter Valley because it has inherent attributes that compel the leading studs to be based here. As a breeder I appreciate that the Hunter Valley is a superb, natural environment, but there are several other locations in Australia and New Zealand that are more than acceptable alternatives. When these other selected locations have hosted quality stallions in times past, they have clearly shown that their underlying breeding environments lack nothing in comparison with the Hunter Valley. (And as will be seen in Section 5, their yearlings sold accordingly.)

#### The Ownership of Assets is Very Important

On pages 41 and 42 of his report, Mr Houston includes a sub-section called "The ownership of assets is not important". He lists a number of ownership changes that occurred in the Hunter Valley over a period of time and then states as follows:

*"The equine industry in the Upper Hunter has been successful throughout the period of the studs listed above changing hands. This indicates that it is not the name of the owner of each stud farm that is important. Rather, it is the underlying characteristics of the industry, its reputation, the skilled workforce, the Hunter environment, the quality and quantity of bloodstock in the region, and the hundreds of businesses that are part of the equine CIC that are more important."*(p42)

However, as I have shown above, the Hunter Valley did not have its current reputation and levels of success before Coolmore and Darley arrived. It is relevant to note that every example that Mr Houston provided of "changes" in the industry occurred during the period that Coolmore and Darley have been in the Hunter Valley, so of course the industry remained successful while those events took place. It is the presence of Coolmore and Darley, and only the presence of those two farms, that has given the Hunter Valley its present stature.

Contrary to Mr Houston's opinion, I believe all industry participants would say that the names of the studs in the Hunter Valley are very important, especially if those names are "Coolmore" and "Darley". By hosting stallion farms with those names, breeders know that the best stallions in Australia will be found in the Hunter Valley, and so they have sent the best mares in Australia to reside there also.

But if those two stud farms were to move elsewhere, then I have no doubt that thousands of mares would follow the stallions, the Hunter Valley would lose its leading reputation, and the Hunter Valley environment would again be seen as nice, but no nicer than other places: As it was before Coolmore and Darley caused the best stallions available in Australia – highly-mobile stallions it should be added - to be based there.

## **SECTION 5 – ARE VICTORIA AND NEW ZEALAND “POOR COUSINS” OF THE BREEDING WORLD?**

Mr Houston offers two observations about the competitor markets of Victoria and New Zealand, which I believe are at odds with their actual history. The statements seem intended to support his contention that Coolmore and Darley will not leave the Hunter Valley.

### Victoria

Mr Houston gives the opinion that Coolmore and Darley will remain in the Hunter Valley, because that is where its main customers are, and he says of Victoria, firstly, the following:

*“In addition, the total stallion fees paid in 2014 by broodmare owners in the Upper Hunter was \$192,298,040, whilst it was \$36,139,959 in Victoria. Although some of this difference is due to the better quality stallions in the Upper Hunter, it seems likely that the willingness of broodmare owners to pay for stallion fees is likely to be lower in Victoria.”(p28)*

I believe that Mr Houston misses a fairly basic point, which is that the owners of broodmares do not generally live where the broodmares do. Just as most shareholders of Anglo American do not live next to South Drayton (although some may well do), the owners of mares that are kept in the Hunter Valley do not generally live there (although some may well do). Mr Houston’s reference to “broodmare owners in the Upper Hunter” should be a reference to “owners of Upper Hunter broodmares.”

As I verbally advised the PAC, broodmare owners are largely investors looking for portfolio diversification, and might live in any Australian city or overseas. In fact the ownership base of the broodmares in the Hunter Valley would be every bit as diverse as the shareholder register of a public company. The fact that a mare is located in the Hunter Valley says nothing about where the owner lives, and if a large pool of mares was to move to Victoria, or to New Zealand, the owners of those mares would still be living in the same cities they do now, with the same financial capacity.

But, as it happens, even if the only clients of a re-located Coolmore and Darley were Victorians, history shows that Victorians have historically paid the highest stallion service fees when the best stallions were located there.

In the previous section, I provided some historical perspective on the industry in the period leading up to the arrival of Coolmore and Darley in the Hunter Valley. In that era, the industry was very fragmented along state lines, and it was the case that the owners of mares in Victoria were more likely to be Victorian, and so on.

During that era, Victoria had more successful stallions than in the Hunter Valley, and they were priced accordingly. In 1971 and 1972, the most expensive stallion in Australia was named Showdown, and he stood in Victoria at a fee of \$5,000 and \$4,000 respectively in those two years. And, as unlikely as it would seem today, in 1976 the most expensive stallion in Australia (in fact the

most expensive in Australian history to that point) was a South Australian-based stallion called Without Fear, who stood for a \$10,000 service fee. So when the Victorians and South Australians hosted the best stallions in their region, they demonstrably had no problem paying the appropriate fees.

As further evidence of Victoria's historical strength, in the 1970s a Victorian stallion farm purchased a stallion called Beau Brummel, in Europe, in what was the most expensive auction purchase of a stallion anywhere in the world that year. This is hardly the sort of history that would lead one to assume that Victorians are inherently "unlikely" to be willing to pay high service fees.

The changed fortunes of industry sales over time is also very revealing. Those who are involved in this matter would be aware that today the most lucrative yearling sale in Australasia is the Easter Yearling Sale in Sydney. In the current era, the Easter sale in Sydney dwarfs all other sales in Australia; the average yearling at Easter sells for about 3 times the average yearling sold at the premier yearling sale in Melbourne, and nearly 10 times the average yearling in Adelaide.

So against this background, it is interesting to look at how different the sales landscape was in the days before Coolmore and Darley set up in the Hunter Valley. The following table shows the average prices paid at the Sydney Easter yearling sale in 1976, as compared with the sales averages in Melbourne and Adelaide; and for contrast, it shows the 2015 outcomes, which were included in my original submission.

Sale Location	Average Price 1976 (pre Coolmore/Darley)	Average Price 2015 Coolmore/Darley era
Melbourne	\$7,250	\$95,886
Sydney Easter Sale	\$6,667	\$291,743
Adelaide	\$6,599	\$32,588

That is, only 15 years before Coolmore and (later) Darley changed the breeding landscape in Australia, the Sydney Easter sale sold horses at a lower average price point than in Victoria, and merely on par with those of South Australia. (To anyone who is not fully acquainted with the breeding industry, this table **alone** should be stark evidence as to how Coolmore and Darley have drawn industry investment to New South Wales, and conversely, what would be handed to another state if they are forced out.)

In the days immediately before Coolmore and Darley arrived in the Hunter Valley, Victoria had the best stallions, which stood for the highest prices and accordingly sold yearlings for higher amounts than anywhere else in Australia. Today, thanks to Coolmore and Darley, the Hunter Valley has an unprecedented dominance of the best stallions, which stand for the highest prices, and accordingly the Hunter Valley produces the horses that sell for the highest amounts.

So the supposition floated as “likely” by Mr Houston, that Victoria is some poor cousin in breeding industry financial terms is not vindicated by its past history. The only thing true of Victorians is that like anyone else, they do not pay A grade prices for lesser-grade products, which their stallions are in a collective sense today compared with those in the Hunter Valley. But if Coolmore and Darley move the best stallions to Victoria, then the best mares will be moved there, and Victoria will resume its previously-held position as a more affluent breeding centre, at the expense of the state of NSW.

It is understandable that others may not have my historical understanding of the industry before Coolmore and Darley, because such information is not easily obtainable from the internet. But a more relevant example that could have been considered today is the highly-credentialed stallion “Zoustar”. He stands alternative years in the Hunter Valley and in Victoria, and his fee of \$44,000 is exactly the same in both markets. One might consider that the same stallion standing in both markets today for the same price hardly suggests that it is “likely” that one of those markets is less willing to pay justified high stallion service fees than the other.

### New Zealand

Mr Houston says of the breeding industry in New Zealand the following:

*“Finally, the total demand for thoroughbreds in New Zealand is much lower than in Australia. For example, the total value of yearlings sold in New Zealand and Australia in 2014 was \$69,625,000 and \$342, 420,700, respectively. It follows that the demand for stallion services required to produce these yearlings will also be much lower in New Zealand.”(p29)*

*“...and the demand for yearlings is much greater in Australia than in New Zealand.”(p42)*

Mr Houston seems to be unaware that the New Zealand yearling market has historically outsold the Australian sales very significantly from time to time, although not since the Coolmore and Darley era began. The concept is not one of demand for yearlings in New Zealand or by New Zealanders, as much as it a question of demand by yearling buyers for yearlings from Australasia, wherever the best ones are to be found.

And at those times in history where the best products in Australasia have been found in New Zealand, yearling buyers have accordingly spent more money in New Zealand.

I showed in Section 4 that in the 1970s, the best Australasian stallions were to be found in Victoria, and as seen in this section, the yearlings raised there sold accordingly. I also showed in Section 4 that in the 1980s, the best stallion talent was to be found in New Zealand, so it should be no surprise to learn that in the 1980s, New Zealand’s yearlings not only outsold Australia’s, but by a significant margin.

So strong was the New Zealand industry in the 1980s that many of Australia’s best stallions and racing mares ended up there for their breeding careers, and hence the yearlings offered at the New Zealand sales had pedigrees far better in average than what Australia could offer. (To some extent



this was due to more generous tax regimes in New Zealand at that time, but irrespective of the reason, the point is that the stallion pool was better, as shown earlier.)

To put the strong performance of the New Zealand industry in the 1980s into perspective, in 1987 John Messara described the competitive situation as follows<sup>19</sup>:

*“The example of Trentham (New Zealand) is right there before our eyes. The sale average at Trentham in January this year was \$A93,807. NO Australian yearling sale has ever averaged half of this amount. (Capitals are his emphasis.)”*

As Mr Messara said, shortly before Coolmore and Darley would arrive in Australia, the New Zealand industry was outselling Australia by two dollars to one. It is logical that the same situation would re-occur today if Coolmore and Darley were to relocate to New Zealand, and within a few years, the New Zealand sales would once again be higher than any Australian counterpart.

In my view, Mr Houston seems to be observing how things stand today, and assuming that because they are that way today, it must always have been the case. But in fact horses are extremely mobile, and history shows that wherever the best stallions are located, the best broodmares will be sent there, and their geographically-diversified owners will pay the appropriate service fee wherever that happens to be. And buyers will go to that state capital (or Auckland) to buy the yearlings that are produced from those matings.

Coolmore and Darley have those best stallions today, and hence the Hunter Valley and Sydney have been the beneficiaries. But as the history suggests, they would be welcomed by any competitor breeding centre in Australasia.

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<sup>19</sup> Article in “Turf Monthly”, May 1987 edition, p24

## **SECTION 6 – THE LIKELIHOOD OF REPLACEMENT STALLIONS IN THE HUNTER VALLEY**

Of all the claims made in Mr Houston's report, the most unrealistic to me is the suggestion that if Coolmore and Darley leave the Hunter Valley, broodmares will not leave the Hunter Valley to any significant extent. His advice is that the other stud farms will simply bring in additional stallions to cover the departure of the stallions who leave, or new entrants will come into the market bringing new stallions with them. Or, in addition, breeders will utilise existing stallions that are not used to capacity today. We breeders will, to paraphrase Mr Houston, largely leave our mares in the Hunter Valley and breed to those replacement or under-utilised stallions.

I believe that Mr Houston's opinion that the owners of broodmares would not decide to relocate large numbers of them, if the best stallions in the country were moved interstate, is inconsistent with commercial logic and common sense. I have previously stated why I believe it is certain that thousands of broodmares are going to be moved so that they can continue to be mated with the stallions whose offspring sell for the highest prices, and hence offer the largest potential profits to breeders.

I submit that the likely response of broodmare owners to the departure of Coolmore and Darley is critical to the Department's decision, because it is the departure of broodmares that will have the biggest financial impact on the Hunter Valley economy. So I urge the Department in its assessment of this matter to carefully consider my comments because, as a breeder, I am an experienced proxy for individuals that collectively spend ~\$500m cash in the Hunter Valley each year at present, and the response of individuals like myself to the departure of Coolmore and Darley will be the reason for much of that expenditure migrating interstate.

### **The Quality of the Coolmore and Darley Stallions**

I have explained again in this paper, as I did in my original submission, that broodmare owners mate their mares with the best stallions, in the largest numbers, because that is the strategy that maximises potential profits when the offspring are sold. Yearling buyers pay the largest sums to buy the offspring of the best (most expensive) stallions.

Coolmore and Darley do not have every good stallion in the Hunter Valley, but they have the best overall rosters by some margin. In Section 1, I showed Coolmore and Darley's dominance on every measure, and summarised it as follows:

*"It has been shown that if mare owners want to breed to a proven stallion, 5 of the top 7 are at Coolmore or Darley. If mare owners want to breed to the best of the new, unproven stallions, 4 of the top 6 are at Coolmore or Darley. If mare owners want to maximise the chances of having their mare's offspring accepted at the major sale, then Coolmore and Darley stallions provided more entrants than the others put together. And if mare owners want their offspring to sell for the highest prices, then 6 of the top 8 most popular stallions at the main sale were Coolmore or Darley stallions.*

*Against this background, a reader might already be wondering how the departure of Coolmore and Darley would not be accompanied by a large migration of breeding mares to that same location."*

If Coolmore and Darley are forced to relocate, then in my view, the financial repercussions on the Hunter Valley will be swift and far-reaching. The majority of breeders have no fixed assets in the Hunter Valley, so if the best stallions were moved interstate, it would take little effort for many mares to be moved to that same location. I showed in Section 4 that in the era before Coolmore and Darley arrived, each of Victoria, New Zealand and even South Australia were ranked equal to or better in terms of reputation than the Hunter Valley. So if the best stallions were to be relocated, there is a commercial imperative that ensures that many broodmares would re-join them, and there is no physical or environmental reason that owners would not do this.

The idea that the remaining Hunter Valley studs would simply put on extra stallions to cover for the departed ones of Coolmore and Darley, and that commercial breeders like myself would happily use those replacement stallions, is not consistent with how breeders like myself approach the business. Looking again at the first italicised paragraph on the previous page, the reader is reminded of just how compelling the attributes of the Coolmore and Darley stallions are.

#### Stallions Are Very Hard To Find

I showed in Section 1 that the credentials for a male racehorse to become a stallion are so demanding that not even 1 in a 1,000 are of a calibre to appeal to the owners of mares in the Hunter Valley. There are many thousands of male racehorses born every year, but only a handful can emerge as the best of a crop, and it is these elite few who rise above their contemporaries that are given an opportunity.

Accordingly, I showed in Section 1 that only 9-10 stallions, drawn from all over the world, commence at stud in the Hunter Valley in a given year. I repeat that table, but this time add columns to show where those new stallions have been based, as this section is about competitive balance:

Number Of New Stallions					
Year	Coolmore/ Darley	Arrowfield/ Widden/ Vinery	Emirates/ Yarraman/ Newgate	All Other	Total
2011	1	4	0	3	8
2012	4	3	2	4	13
2013	2	2	2	0	6
2014	4	3	3	0	10
2015	6	1	3	1	11
Total	17	13	10	8	48
Average	3.4	2.6	2.0	1.6	9.6

With no disrespect to the farms summarised in the “All Other” column, they generally host low-value stallions that make little impact and are moved on very quickly. Of the 7 stallions in the “All Other” column that went to stud in 2011 and 2012, 4 of them are no longer in the Hunter Valley, and none of the other three stand for more than \$10,000. These types of stallions are not serious competition to any of the larger studs, let alone Coolmore or Darley.

Of the larger farms, it can be seen that on average, over the last five years, Coolmore and Darley have added just over 3 new stallions each year between them, Arrowfield, Widden and Vinery have averaged somewhat less than 3 between them, and the next tier, Emirates, Yarraman and Newgate, have commenced an average of 2 new stallions each year between them. These are not very large numbers, which shows how hard it is for individual studs to source any more than one stallion a year that would be of any interest to breeders. Even Coolmore and Darley, with their worldwide reach and their financial resources, do not average as many as two new stallions every year each.

Speaking specifically about the prospects of other studs compensating for the loss of Coolmore and Darley, Mr Houston says:

*"It is reasonable to assume that at least the Arrowfield, Vinery and Widden stud farms could expand by taking on a number of additional high quality stallions because....they had 32 stallions in 2015 and so the addition of, say, six stallions would be an increase in the number of stallions by 19 per cent."*(p45)

This sentiment is repeated on a number of occasions throughout Mr Houston's report, whereby various studs can arguably put on "extra" stallions.

The impracticality of the suggestion that "Arrowfield, Vinery and Widden" would just put on "six extra stallions" is very clear from the table. Those three studs are presently unable to source an average of three new stallions a year between them. So to not only source their usual quota, but to also find another six, they would have to collectively more than treble their normal success rate in securing acceptable and affordable stallions.

And this would have to happen under circumstances where Coolmore and Darley, having moved interstate, could be expected to compete even more strongly than usual to obtain the very best stallions to make their new location ever more compelling to broodmare owners.

Despite Mr Houston's argument that this would only be a 19% increase (sic)<sup>20</sup> in the number of stallions that they have, this is not a statistic that someone in the industry would regard as relevant. It is no harder or easier to source a stallion whether one has 5, 10 or 20 stallions already. The reason that Coolmore/Darley put on slightly more stallions a year on average is not so much their size as their business model, in that they breed many of their own stallions, especially Darley (as explained in Section 3). Their greater financial strength is generally manifested in them being able to obtain the very best of the new prospects rather than more of them.

If there is a male horse in Australia or elsewhere in the world that has the attributes to be a commercial stallion in the Hunter Valley it is known to everybody in the industry, and it is already there, or there is a good reason why not. The reason that elite stallions command service fees into the hundreds of thousands of dollars is that they have attributes that are shared by less than a dozen horses in the world.

Stallions are not found in boxes on Bunnings shelves. Studs do not simply "decide" to put on extra stallions, let alone high-quality ones.

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<sup>20</sup> Mr Houston's arithmetic is based on his assertion that Arrowfield, Vinery and Widden Studs had a total of 32 stallions in 2015. I believe they actually stood 10, 11 and 7 respectively, for a total of 28.

### Capital Needed For These Six Extra Stallions

And in my view, Mr Houston has not considered a very practical barrier to this scenario. Stallions are very expensive. Mr Houston himself quotes the examples of two Coolmore stallions, So You Think and Vancouver, who are understood to have cost \$60m and \$40m respectively. This season they are the 9<sup>th</sup> and 16<sup>th</sup> most expensive stallions in Australia, which implies there are even more valuable stallions than those two.

Clearly, commercially viable stallions cost many tens of millions of dollars, so it is to be wondered how Arrowfield, Vinery and Widden would approach an investment that would run to many hundreds of millions of dollars to put on nine high quality stallions in a single season. Even if such a number of alternative, high quality stallions existed, which I believe is not the case, and even if these three studs collectively had the capital, which is not certain, it would be a very bold step for them to invest hundreds of millions of dollars in an environment where Coolmore and Darley were leaving, which by anyone's reckoning would be a period characterised by confusion and uncertainty.

In my experience in the corporate world, businesses are less inclined to invest significant amounts of capital in times of significant uncertainty, not more so.

### The Only Options would Non-Commercial Ones

I have shown thus far in this section that the three largest competitors of Coolmore and Darley struggle to find even one new stallion a year each on average. Even if the net is widened to include not just Arrowfield, Vinery and Widden, but to also bring in Emirates, Yarraman and Newgate, the table shows that these six collective studs are still unable to source an average of 5 stallions a year between them. And even to achieve this number means that at the lower end, the quality begins to fall away.

To broodmare owners/investors, the choice of stallion each year is the most critical factor in determining the eventual result of their investment. For a given broodmare, the difference between choosing the right stallion and the wrong stallion can be literally hundreds of thousands of dollars in the sales ring in a given year. Broodmare owners mate their mares with a specific stallion, because of its individual attributes, to achieve specific commercial objectives in terms of returns and risks.

It will be recalled that in Section 1 there was a table that listed the stallions whose offspring enjoyed the highest average sales prices at the leading industry sale, the Sydney Easter sale. Offspring of the top stallion sold for \$573,000 on average, whereas the equivalent figure for the 10<sup>th</sup> stallion was \$246,000, the 20<sup>th</sup> stallion was \$165,000 and so on.

This is why higher priced stallions attract more mares than cheaper ones. Coolmore and Darley dominate the most expensive stallion rosters, which is why they receive essentially as much revenue from stallion services as every other Hunter Valley stud put together. (See my original submission where this was explained in detail.) Broodmare owners do not just want any male horse, they want

the specific top stallions whose offspring are most prized by yearling buyers because that is how the highest potential returns on investment can be made in the sales ring.<sup>21</sup>

I showed in Section 1 that of the best new stallions coming through (that is, the ones that are still “unproven”), the majority are on the rosters at Coolmore and Darley. So, it follows, that the new stallions being put on each year by their competitors are of lesser potential on average. This does not mean that every expensive stallion proves to be successful, or that every slightly cheaper stallion is unsuccessful, far from it. But on average, over a period of time, the most expensive untried stallions will have a better chance of succeeding than inexpensive ones. The two largest studs, Coolmore and Darley, habitually buy the best of the racehorses when their careers finish, and are therefore more likely in the long run to have a higher proportion of the best proven and unproven stallions.

Even non-racegoers may have heard of horse races such as the Golden Slipper. It is one of about 8-10 races each year that are referred to in the industry as “stallion-making races”, in that a male winner of one of these races will be chased hard by the studs as an attractive stallion prospects. Sometimes one of the races might be won by a filly or gelding, and sometimes a colt might win more than one, so generally about 4-5 future stallion prospects emerge from these races alone, and these are the colts that commence their stud careers at the highest prices. Outside of this qualification path, there are only a few remaining spots for other male horses of lesser (though still high) distinction, and these generally have to be priced comparatively cheaply when they are first offered.

It follows that if the competitors of Coolmore and Darley were to significantly raise the number of new stallions they sourced - in accordance with Mr Houston’s advice that they could put on 6 extra stallions - then these extra stallions would self-evidently have to be even further down the quality curve. If the winners of the Golden Slipper and other key races are already at stud, then alternative stallions cannot, by definition, have won those races. They can at best have won races of lesser stature, which means they will not be as appealing to broodmare owners. Even today, some of the small number of new stallions every year are at the \$10,000-\$15,000 range, and these are borderline in terms of their appeal to broodmare owners. In a hypothetical scenario where Coolmore and Darley had left, and the competitor studs were looking for six extra stallions, then the only possible alternatives would be the winners of even lesser races.

And therein lies the point. Putting on extra stallions – Mr Houston’s suggested strategy if Coolmore and Darley left – could only be done by attaining stallions of lower standards that would attract few broodmares. If the best ten prospects are already taken, then the next best available can only be the 11<sup>th</sup> best. And the 11<sup>th</sup> best prospect is not commercially viable today and is not going to be any

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<sup>21</sup> On this point, I believe that Mr Houston does not accurately describe the motivation of most breeders. He says “*Mare owners will seek to maximise their returns to breeding by selecting a stallion that will generate progeny with the best expected racing ability, at the lowest possible cost (including stallion service fees).*” That is not how breeders actually reach a mating decision, I submit as a breeder myself. The objective of a commercial breeder is to breed a yearling that will sell for the greatest profit in the sales ring. Sometimes that may also be the horse that is judged to have the best racing potential, but it is often not the case. Consider the example of unproven sires. I explained in Section 1 that stallions can stand at stud for 4-5 years before anyone knows whether they can actually produce good runners or not. If broodmare owners were only concerned with producing the best racehorses they would never mate their mare with an unproven sire. But in fact, first season sires are extremely popular with yearling buyers, who are always hoping to get in early on the next big thing, and broodmare owners heavily patronise them accordingly.

more commercially viable in an environment wherein Coolmore and Darley have moved their stallions interstate.

Broodmare owners do not fully utilise the cheaper stallions today, and even more so they would not be interested in stallions who are not judged good enough to be at stud today. It is commercial reality and common sense that if the majority of the best stallions - that is the stallions that enable mare owners to achieve the highest profit potential - leave the market, then many broodmares will be relocated with them.

#### Can The Competitor Studs Have Their Stallions Do Extra covers?

Mr Houston further opines that if Coolmore and Darley left the Hunter Valley, other stallions already owned by their competitors could serve more mares because they are presently not being used to capacity. In my original submission I explained that the reason that these horses are not being used to capacity is that broodmare owners don't rate them highly enough to use them to a greater degree. And there is no reason that broodmare owners will use these non-preferred options in future when the alternative of following the preferred Coolmore and Darley options to another location is so simple.

Generically counting up how many stallions at so many services would be needed to bridge the gap does not, in my opinion as a breeder, reflect how breeders approach the exercise of choosing a stallion. Mr Houston made comments like the following on multiple occasions:

*"Other stallion owners in the Upper Hunter would also benefit from Coolmore leaving and can be expected to increase the number of covers they undertake....." (p40)*

*"Figure ....shows that the existing stallions in the Upper Hunter could undertake additional covers and replace almost all those provided by stallions from Darley that have fees under \$50,000"(p43)*

*".....shows that the existing stallions in the Upper Hunter could undertake additional covers and replace the vast majority of those provided by stallions from Darley and Coolmore that have fees under \$50,000. The net effect of Darley and Coolmore leaving and expansion by other studs is that there would be a loss of around 1,314 covers (16 per cent of the total), which is equivalent to around eight good quality stallions."(pp45-46)*

For the avoidance of doubt, broodmare owners choose which stallion they use. They consider the suite of alternatives available across all the studs. I have shown in my original submission, and repeated here, that the most attractive stallions attract the highest numbers of mares because that is the commercial imperative. Stud farms cannot simply "decide" to increase the number of covers made by their stallions, any more than David Jones can "decide" that its customers will buy 500 shirts tomorrow.

If certain stallions have extra capacity today, it is because they are not as attractive as other options in the eyes of broodmare owners. They will not become any more attractive simply because the first choice stallions move interstate. Not when it will be no trouble for broodmare owners to move their mares interstate.

Mr Houston's line of argument seems to rest upon broodmare owners being so motivated to stay in the Hunter Valley that they will react to the departure of Coolmore and Darley by settling for non-preferred options and compromising their profitability. But as shown in Section 4, the idea that the Hunter Valley is an "irresistible" location for either stallion or mare owners in the absence of Coolmore and Darley is inconsistent with the history of the breeding industry in Australia.

#### How Many Broodmares Will follow Coolmore and Darley if They Are Forced Out?

For my original submission I calculated that for equilibrium to be maintained, some 3,000 mares would need to be relocated to wherever Coolmore and Darley went. I considered alternatives at the competitor studs, and their age and relative appeal, to calculate how the broodmare pool would have to be divided to allow the appropriate number of elite mares to be in the same locations as the available number of elite stallions if Coolmore and Darley moved interstate. I also took into account the fact that not all mares are mated in every year. I explained why, and showed how this influenced the mathematics in my original submission.

I cannot emphasise too strongly that to me this is more than a mere academic exercise of the type that a consultant might undertake. For me, this is a very practical assessment I must make so as to ensure my own capital is best protected if Coolmore and Darley leave the Hunter Valley. Every breeder will have to undertake this same analysis because failing to think it through would potentially prove very costly.

The figure of 3,000 that I calculated is less than one-third of all mares presently in the Hunter Valley. But even that one-third leaving would be enough to financially devastate the Hunter Valley, because service providers currently receive about \$30,000 each year for looking after each of those mares and their offspring, and 3,000 mares at \$30,000 each is \$90m per annum. (See my original submission, and Section 9 of this submission for more on the calculations.)

In my view, this \$90m figure would be certain to increase over time as female racehorses who finish their racing careers in the capital cities would be more likely to be sent to wherever Coolmore and Darley were, than they would be to go to a Hunter Valley in decline. So as the remaining mares in the Hunter Valley grow old and pass away, they would not be replaced on a one for one basis.

I remind the Department that I have judged that the probability of a large pool of broodmares following Coolmore and Darley to be 100%. And because of its importance, I offer the following as a practical demonstration of how hard it would be for competitors to source suitable stallions to stop this happening.



### Practical Evidence of How Hard it is to Find Stallions or Increase Covers

It is telling to note some practical issues that Arrowfield Stud has publically spoken of over the years. Arrowfield is the largest of the competitors to Coolmore and Darley, and its Chairman, John Messara, is greatly respected.

In May 2000, Mr Messara announced the construction of a second stallion barn at the Arrowfield property, to increase its stallion capacity from 10 stallions to 16. Mr Messara said at the time<sup>22</sup>:

*“We have an outstanding roster of 10 horses for the 2000 season, and our long term plan is to stand 16 world class stallions at Arrowfield. We are taking Arrowfield to the next level, especially with 70% of our stallions now in the proven category. Our core business is stallions, and this is where we have been successful.”*

Despite building capacity for 16 stallions back in 2000, Arrowfield has never stood more than 12 stallions and in 2007 stood as few as 7. The reason the target has never been achieved is clearly that Arrowfield is unable to secure enough stallions that would appeal to broodmare owners at a price that it believes to be viable.

As I explained above, it is not simply a matter of finding a male horse, because a stallion is of no interest to breeders unless he has a full complement of attributes in terms of elite racing performance, physique and pedigree. There are very few horses that meet those criteria, and hence when they do come along, every stud wants the same horses, and they are very expensive.

When Mr Messara made his statement about expanding his business to 16 stallions, Coolmore had entered the Australian market, but Darley would not buy their first property until two years later. Even before the entry of Darley, Mr Messara talked in 2002 about the difficulties he faced in competing with Coolmore in financial terms. It was public knowledge that he and Coolmore had each desired full ownership of the stallion Danehill, who was auctioned to dissolve a partnership between the two (as mentioned in Section 4). Mr Messara recalled in May 2002<sup>23</sup>:

*“My intention was to end up with Danehill and I was shattered when we weren’t able to secure him, but on reflection Coolmore was always going to win because they had more money than we had. We could have virtually kept on going forever with Coolmore continually offering that bit more.”*

Like all investor/breeders, I rate John Messara very highly. I believe he is as good a judge of horses as you will find in the world, and he has built Arrowfield Stud from small beginnings into a business with a great reputation, and the largest Australian-owned stud farm<sup>24</sup>. In his time, he has sourced successful stallions from all over the world. I could write chapters about Mr Messara’s talents, but the salient point is that by his own admission, he has to compete with two global giants for the small number of attractive stallion prospects that everybody wants.

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<sup>22</sup> Australian Bloodhorse Review Magazine, May 2000 edition, p99

<sup>23</sup> Australian Bloodhorse Review, May 2002, p9

<sup>24</sup> He achieved the substance of this before Coolmore and Darley set up in Australia.

If John Messara is unable to source enough stallions that broodmare owners would support, at a commercially sensible price, then it is obviously very difficult to do. Fifteen years after announcing his business plan of standing 16 stallions, he has not achieved that number. It is not that he can't identify the small handful of appealing prospects, but that Coolmore and especially Darley breed their own stallions in large numbers, and can also outbid him for the most attractive prospects owned by other parties. And of course Widden, Vinery, Emirates, Yarraman Park and Newgate will want them as well.

Mr Messara, like everyone else with actual industry expertise, knows that there is no commercial advantage in standing stallions that broodmare owners will not support. For example, some years ago Mr Messara purchased 25% of, and arranged to "shuttle", a highly credentialled American stallion named Unbridled's Song to Arrowfield. After coming out to Australia for several years, Mr Messara announced that the stallion would not return from America in 2001, saying:<sup>25</sup>

*"There is little point in bringing the horse down when we need to struggle to fill a book here at \$A25,000 while the stallion's nominations in Kentucky are selling as high as \$US75,000, or the equivalent of \$A150,000."*

This speaks volumes about the competitive nature of the Australian stallion market. A stallion, whose attributes were so compelling that American breeders paid the equivalent of \$150,000 for a single service, had comparatively mild interest from Australian mare owners at one-sixth the fee. That shows how exacting broodmare owners are about the attributes they want, which makes it all the more unrealistic in my view for Mr Houston to offer the opinion that the remaining studs would simply decide to put on extra stallions if Coolmore and Darley left, or that they would decide to increase the numbers of covers their stallions undertook.

John Messara's comments, as Chairman of Arrowfield Stud, that he has been unable to source enough stallions of calibre to have met his business plan for the last 15 years are in contrast with the advice of Mr Houston that if Coolmore and Darley leave, John Messara and his two peers at Widden and Vinery can put on, "say, 6 extra stallions. "

#### It is Even More Difficult for New Entrants

In addition to the existing competitor studs putting on extra stallions to cope if Coolmore and Darley leave, Mr Houston also offers the advice that other new operators can enter the market to assist in making up the difference.

As shown, the criteria for a male horse to be a commercially successful stallion are so demanding that existing, large and experienced operators like John Messara at Arrowfield cannot find enough suitable stallions at a realistic price. The idea that completely new operators would somehow find what people like John Messara cannot, is even more difficult to envisage.

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<sup>25</sup> Australian Bloodhorse Review, July 2001, p19

It is the case that from the time Coolmore and Darley set up in the Hunter Valley there has not been a single new operator start in the Hunter Valley stallion business that has proven successful, and the relative market positions of the main stallion farms remain essentially as they were 15 years ago.

In Section 1 I showed a list of the 35 most expensive stallions standing in Australia in 2016. The following table compares the ownership of the 35 most expensive stallions in both 2002 and 2016. (The relevance of the year 2002 is that it was the first full season where Darley competed in the market with stallions under its own name in Australia.)

Stud Farm	Number of Top 35 Stallions in <u>2002</u>	Number of Top 35 Stallions in <u>2016</u>
Darley	11	10
Coolmore	7	7
Arrowfield	5	5
Vinery	3	3
Widden	3	3
Yarraman	0	2
Emirates	1	1
Newgate	0	3
Other	5	1
Total	35	35

As can be seen, the tables are practically mirror images of each other, and show the opposite of a constantly evolving market. In 2016, just as in 2002, Coolmore and Darley have about half of the 35 most expensive stallions, including the biggest concentration of the most expensive. The three biggest competitors in 2002 were exactly as they are today, namely Arrowfield, Widden and Vinery, with the same portion of the market between them. Between them, the top 5 studs had the top 28 most-expensive stallions in 2002, exactly as they do today.

The only movement at all is at the very bottom of the table. At first glance, it might look like the table is showing two new entrants since 2002, namely Yarraman Park and Newgate. But Yarraman is not a new entrant; it is actually one of the oldest studs in the area<sup>26</sup>, and has been mentioned several times in this submission. In 2002 it stood 3 stallions which were each positioned just outside the top 35, and as such they narrowly missed the table whereas today they have 2 stallions that are inside the boundary. Yarraman's position in the market today is essentially the same as it was 15 years ago.

The other new name is Newgate, which did not exist 15 years ago. As it is the nearest thing to a meaningful new entrant seen for two decades I discuss its market position at length below, and show that it is not actually adding at all to the market competitiveness within the Hunter Valley industry. Because competitiveness comes from the number of stallions, not the number of

<sup>26</sup> In Section 4 I referred to Yarraman's 5 year trial as a thoroughbred operation that commenced in 1961.

operators. If there are only twenty stallions in a market that are of interest to breeders, then makes no difference whether two farms have ten of those each, or four farms have five each.

### The examples of new entrants

I have indicated that the number of stud farms in a market is rather less important than the number of stallions that are available. So to a large extent, the likelihood or not of there being new entrants is irrelevant. But because Mr Houston emphasises often the likelihood of new entrants moving into the industry, it is relevant to consider the three examples he gives.

#### Patinack

This was the brand name given to the stud farm established by Nathan Tinkler.

Tinkler's story is fairly well known, even to the general public. He came into a lot of money through mining, and used some of that money to indulge his interests in "toys", including buying an NRL team, an A-League soccer team, and a huge string of racehorses. He set about establishing his own thoroughbred stud farm in the Hunter Valley, to which end he bought two properties and amalgamated them. His buying spree of yearlings and older breeding stock was unprecedented (certainly in my 45 years of following the industry). The main industry publication reported in April 2009 that he had acquired more than 200 broodmares in less than 12 months, and that in the 2008 year alone he had purchased as many as 173 yearlings at Australian/NZ sales, plus more in the US, France and Japan. And these were only the transaction in public arenas; there may have been private purchases as well.

It did not help that a large volume of Mr Tinkler's purchases were undertaken just ahead of the GFC, which saw a severe correction in the value of thoroughbreds. For the money that Mr Tinkler outlaid he had comparatively little success as an owner. He became overwhelmed financially, and his breeding operations collapsed and many of his assets were forcibly sold by creditors.

In the current context it can simply be observed that Nathan Tinkler's short and spectacular failure in the industry is anything but an example of a successful new entrant.

#### Wattle Grove

I believe that the citing of Wattle Grove is an unwitting error on Mr Houston's part.

Mr Houston's comments on this "new entrant" are worth noting in full:

*"Further, the exit of Coolmore would provide an excellent opportunity for entry by another stud farm. For example, Wattle Grove became a stud farm in about 2011 after the owners*

*noticed that a number of stallions had left the area with the closure of Darley's stud at Cootamundra and the nearby Riverdene Stud scaled back its activities. One example of how it was able to acquire stallions was that it secured a proven and well-recognised stallion from a stud farm in Victoria. This is consistent with the conclusion of the Australian Competition and Consumer Commission (ACCC) in 2008 that "barriers to entry into the national market for breeding thoroughbred horses appear to be relatively low."(p35)*

It will be remembered that successful stallions cover books of mares sized anywhere from 200-250 strong. The champion Coolmore stallion Fastnet Rock, for example, in 2012 served 208 mares at a fee of \$200,000 each plus GST. That amounts to potential earnings of more than \$40m from one stallion alone in a single season. Last year, in 2015, Fastnet Rock again covered more than 200 mares, and his career peak in terms of numbers was in 2009 when he covered no less than 273 mares.

So, against this background it is relevant that the "proven and well-recognised stallion" that Wattle Grove was "able to acquire" from a stud farm in Victoria in 2011 was a stallion named Helenus, who, in his final year in Victoria, had sired a grand total of two foals, at a fee of \$6,000 each. That is not 200 foals, but 2, for total revenue of \$12,000.

It would be evident to anyone with industry knowledge that such a stallion would have essentially no sale value, and Helenus was almost certainly given away to Wattle Grove, yet Mr Houston's report refers to Wattle Grove being "able" to acquire him. It hardly seems a useful precedent for how new entrants might acquire stallions to replace those of Coolmore, who even Mr Houston has acknowledged can cost as much as \$60m individually.

In the 2012 season at Wattle Grove, Helenus' service fee was dropped from \$6,000 to "negotiable". Wattle Grove actually stood a couple of other not-very-commercial stallions from 2011-2015 before retiring from the stallion business. During its brief existence as a stud farm, the total revenues from the entire stallion roster at Wattle Grove averaged just over \$200,000 per annum. To put that into perspective, the entire annual revenue of the stud's business from as many as three stallions was about the same as one service by one of Coolmore's stallions.

My highlighting of the limited achievements of Wattle Grove's stallion business is not meant in any way as a criticism of its management. More than anything it speaks to the industry dynamics that I have repeatedly emphasised in my submissions, which is that the entry of Coolmore and Darley into the market in the Hunter Valley resulted in such a cluster of elite stallion offerings that successful commercial breeding centres in other parts of Australia lost their best broodmares to the Hunter Valley as a commercial imperative.

In the days before Coolmore and Darley, Southern NSW was actually very significant in the breeding industry. Newhaven Park Stud at Boorowa was probably the most successful stud in Australia at times in the 1960s, and as recently as 1991 (just as the Coolmore/Darley era was beginning) it still hosted two of the top six Australian-based stallions. Other studs such as Woodlands Cootamundra, Riverdene and Koorngal at Wagga Wagga, Boscobel near Young, Loch Hill at Crookwell, Meringo Stud and Mungererie Studs at Moruya, Inverness at Bowral, Lockyersleigh and Loudoun Studs at Goulburn, Yllier Lodge at Nowra, and Huntworth Stud at Moss Vale, also stood stallions in the 1990s,

and the owners of commercial broodmares could keep their mares in Southern NSW and have plenty of stallion options at all price points within a comfortable drive.

The Hunter Valley centralisation that followed the arrival of Coolmore and Darley changed the market dynamic, and whereas those named Southern NSW studs stood 20 stallions between them as recently as 2001, that had reduced to 4 by 2010.

Wattle Grove took a calculated risk that the reduction in stallion numbers and quality was too extreme, but clearly found that it wasn't, and that there are not enough even modestly-commercial broodmares left in Southern NSW to support more than the small number and modest standard of such stallions as remain between Sydney and the Victorian border.

So while no criticism attaches to the Wattle Grove's testing of the market, it would take a rare degree of industry expertise to believe that a stallion that served two mares at \$6,000 is a useful example of the types of stallions that might be brought to the Hunter Valley if Coolmore and Darley were to leave, and thereby induce commercial breeders not to have their mares follow Coolmore's Fastnet Rock, for example, interstate; he being a stallion whose potency and popularity with yearling buyers currently sees breeders support him to the tune of up to \$40m a year in stallion service fees.

In my view, the use of Wattle Grove in this context was not worthy of being included in a serious submission to the Department. I believe that Mr Houston would not have included it had he known the full details, and I strongly suspect that one of his assistants simply "googled" and chanced upon a press release or advertorial from 2011 in which Wattle Grove (naturally) talked up their "new stallion business".

### Newgate Farm

The only other example that Mr Houston has put forward is Newgate Farm, which has emerged in the last three years, and which in 2016 will offer nine stallions, which is a large roster. But there are a number of points that need to be made which in my view counter the description that Mr Houston applies to Newgate.

Firstly, Mr Houston says that Newgate was a "broodmare farm" which established a stallion division. Newgate actually commenced business by leasing a stallion farm known formerly as Wakefield Stud, and it began looking for suitable stallions straight away. It began to acquire mares of its own to support its eventual stallion purchase, and it acquired its first stallion within a short period. It then purchased a former stallion farm known as Brooklyn Lodge, which had been very prominent in the 1970s.

As someone in the industry, I would not describe Newgate as a broodmare farm that later started a stallion business. It was conceived as a stallion business, commenced on historic properties that were fitted out for the standing of stallions, and it merely happened that it bought mares while it was searching for its first stallion. Broodmare farms and stallion farms are very different operations, with very different physical infrastructure, very different financial models, very different levels of

capital needed, and very different skill sets, so I do not agree with the following comment made by Mr Houston:

*“There are a large number of broodmare farms that could enter the stud business”. (p36)*

Secondly, although Newgate has nine stallions in its roster, it is not (at this time) pitching to the top end of the market. The most expensive stallion at Newgate stands for \$32,500 plus GST, and it was shown in the table in Section 1 that this does not fall within the top 20 most expensive stallions in the market. The average price point of the stallions at Newgate in 2016 is \$20,000 plus GST. Newgate is not really competing at the top end of the market, certainly at this time, and breeders would not see it as on the same level as Coolmore and Darley.

Thirdly, while I wish Newgate all the best, and their management is well-regarded, they have only recently commenced their business. It will be some years before it can be seen whether Newgate will be sustainable, and it is important to note that it has adopted an extremely high-risk strategy. Of the nine stallions available at Newgate this year, only one of them has actually had any offspring to race, and even that stallion only has his first, 2yo, runners, and the results so far are inconclusive. So virtually all of Newgate’s stallions are unproven at this time.

It will be recalled from Section 1 that for the first 4-5 years of a stallion’s career they attract mares based on potential, and only when their first runners appear towards the end of that timeframe can it be seen whether they are actually capable stallions. Most stallions do not prove to be successful. If one looks at the table of the 35 most highly priced stallions in the market, also shown in Section 1, it showed the birth year of each of those stallions, and it can be seen there that of the stallions old enough to be proven, there are at most one or two remaining representatives of any given year. So, of the 10 or so stallions that commence duties in the Hunter Valley in a given year, history suggests that no more than one or two will still be plying their trade at the elite commercial level a decade on.

Because most stallions do not succeed in the way hoped, successful studs typically ensure that their roster has a mix of proven and unproven stallions. For example, in the 2016 season, 60% of Vinery Stud’s stallions are proven, and for Darley, Arrowfield and Widden the figure is about 50%. In all cases it is their proven stallions that command the highest fees.

So by having virtually the whole of its stallion roster as unproven, at around the same age, it follows that Newgate is facing a high statistical probability that the majority of its current stallions will be found to be uncommercial in a few years’ time. At that time, Newgate will almost certainly face restocking issues, so it is far too early to tell how it will fare in the long run.

So in my view the following statement by Mr Houston is not supported by facts:

*“Newgate stud is now an established top tier stud.”(p36)*

Newgate is not yet “established”, and its stallions are not at the most expensive end, so I would submit that it is neither of these two things today. It has embarked on a strategy that may position it as an established stud in future, but to have “top tier” status it would need to find stallions of a much higher calibre than it does today. At that time, it will no doubt find that Arrowfield, Vinery, Widden, Emirates and Yarraman, not to mention Coolmore and Darley, will have an interest in those same stallion prospects.

#### In Any Event, Newgate Is Not Growing The Stallion Market

But the most important point of all, is that Newgate is not actually adding any new stallion capacity to the market. It is simply a case of another party taking a slice of an unchanged pie.

I showed before that Arrowfield Stud has capacity for 16 stallions but this year it will stand only 12. The following table shows the number of stallions standing at the five largest competitors to Coolmore/Darley in 2016 (before considering Newgate), as compared with their maximum capacity, evidenced by either known capacity, or by the highest number of stallions they have stood in recent years:

<b>Stud Farm</b>	<b>2016 Roster # of Stallions</b>	<b>Maximum Capacity # of Stallions</b>
Arrowfield	12	16
Vinery	10	11
Widden	8	11
Emirates	4	6
Yarraman	2	3
<b>Total</b>	<b>36</b>	<b>47</b>

This table shows that the five established major competitors to Coolmore/Darley will this year host a combined 36 stallions, which is 11 stallions below their known capacity. So the fact that Newgate Stud is standing nine stallions is not an indication of an expanding market. Six studs standing 45 stallions (the number this year when counting Newgate as a sixth force in the group below Coolmore/Darley) is not an expansion of a market whereby the five older studs have capacity for 47 stallions. A table earlier in this section showed that Arrowfield/Vinery and Widden are between them only adding only one new stallion in 2016. This is below their longer-term average, and in my view is explained by Newgate buying stallions that would otherwise have gone to one of these more established competitors.

Far from showing the scope for successful new entrants, I believe the fact that these were the only examples that Mr Houston offered shows, in fact, just how difficult it has been to bring new participants to the market. This is why, as the table earlier in this section showed, the list of participants, and their relative standing, is basically unchanged today from what it was 15 years ago. Even very capable and established operators, with rich history, strong skill sets and sound financials cannot source suitable stallions to run at capacity despite aspiring to.



### Are Arrowfield, Vinery and Widden Growing?

Mr Houston also makes the comment that Arrowfield, Vinery and Widden are expanding. He says:

*“those stud operations have been expanding their number of covers and stallions over the last decade – for example, Arrowfield, Vinery and Widden have collectively increased the number of covers they undertake per year by about 33 per cent from 2005 to 2014.”(p35)*

This comment says less about the trends at Arrowfield, Vinery and Widen over the last decade than it does about the dangers of using selective statistics to “prove” a trend.

As it happens, comparing these three studs between the specific years of 2005 and 2014 provides a very misleading picture. 2005 was a cyclical low point in the number of stallions at Vinery Stud.<sup>27</sup> By contrast, the 2014 year was a record year for the three studs in terms of high stallion numbers, and those numbers have since reduced again.

The following table shows the number of stallions that the three studs had in four relevant years:

Year, and Movement	Arrowfield	Widden	Vinery	Total
2005	10	7	5	22
2006	9	11	9	29
2014	10	10	13	33
2015	10	7	11	28
<b>10 Year Movement 2005-2014</b>				<b>+50%</b>
<b>10 Year Movement 2006-2015</b>				<b>-3%</b>

The table shows the number of stallions that stood at Arrowfield, Widden and Vinery in 2005 and 2014, but also in the years immediately following those two, namely 2006 and 2015. Mr Houston has stated that between 2005 and 2014, the three studs expanded significantly, as I quoted above. It can be seen from the second last row of the table that by comparing the two specific years of 2005 and 2014, it would appear that the three studs were expanding because their collective number of stallions in 2014 was 50% higher than in 2005, which is 33 stallions compared with 22.

But if one performed the same 10-year measurement, just one year later - that is from 2006 to 2015 – as I have done in the last row of the table, it could be made to appear that the three studs were in decline, because the number of stallions offered between them actually fell by 3% between those two years, that is from 29 stallions to 28.

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<sup>27</sup> Vinery had earlier overinvested in “unproven” stallions, and in foreign stallions. In 2002, it stood 10 stallions, all of which were foreign, and few of which were proven. By 2005, it was discovered that only 2 of those stallions were successful once their first runners appeared, so Vinery was caught very short for numbers.

I do not believe that Mr Houston deliberately chose two specific years to create a false impression of expansion. But it does provide a very salutary lesson for the Department. That is, if the Department wants to understand what is happening in the breeding industry, and what may happen under hypothetical circumstances in future, it should seek advice from people within the industry who truly understand it.

Stallion numbers fluctuate from one year to the next depending on the availability of suitable prospects, and their attainability. Studs do not simply decide to put on extra stallions. Farms are in a competitive market and they have to find stallions that are of interest to breeders, and then be able to acquire those stallions in the face of competition from their peers. And then of course they have to hope their new stallions prove successful when their four or five year “unproven” window finishes, and on top of all of that, they have to hope that those stallions that do prove successful live long and healthy lives.

In real life these matters rarely go to plan, so the numbers of stallions at the different studs can fluctuate widely from year to year. Vinery stood 10 stallions in 2002, 5 stallions in 2005 and will stand 11 this year. Picking any two single years to prove a trend can give very misleading results.

#### Conclusion: Many Broodmares Will Follow Coolmore and Darley

If the South Drayton mine is approved, I have shown why I believe it will be the catalyst for the world-renowned Hunter Valley breeding industry being effectively split into two. It will force broodmare owners, who currently pump \$500m a year into the Hunter Valley, to make a decision as to whether to leave their mares in the Hunter Valley or follow Coolmore and Darley interstate.

In considering the response of broodmare owners, such as myself, to a departure of Coolmore and Darley, it is critical to note that those two studs have the best overall stallion rosters by every measure that is important to breeders. So if breeders are forced to make a choice, I firmly believe it is a battle that the stud farms left in the Hunter Valley cannot win. About a third of the breeding mares will leave immediately, and that percentage will grow over time. (As was set out in my original submission.)

In the short-term the movements would be about equilibrium. That is, in the immediate spring after the departure of Coolmore and Darley, it would be about broodmare owners doing whatever is necessary to have access to one of the elite stallions owned by Coolmore and Darley, or by their competitors. But over the long term, I believe any breeder would judge that the financial strength and world-wide reach of Coolmore and Darley will ensure that they will always have the best stallion rosters. No one knows the individual identity of the stallions that will be available to breeders fifteen years from now, but no breeder would doubt that Coolmore and Darley will have the best line-ups, whoever those future stallions may be.

This is not a comment on the credentials of Arrowfield, Widden or Vinery, or of Emirates, Yarraman and Newgate. They each have excellent management, but the reality is that the world wide reach of Coolmore and Darley, their ability to develop their own stallions internally, and their financial firepower, collectively mean that broodmare owners would perceive that they will stay at the top of the industry going forward.

## **SECTION 7 – MIGHT COOLMORE AND DARLEY MOVE ELSEWHERE IN THE HUNTER VALLEY?**

Mr Houston has raised the possibility that one or both of Darley or Coolmore could simply relocate within the Hunter Valley geographical area, which would, from his perspective, solve their problems in a far easier fashion than relocating interstate.

This is a notion that makes superficial sense in Mr Houston's report, because as I stated in Section 2, in my view his report does not address the major issue confronting Coolmore/Darley/the industry. By presenting it as a problem of impacts only on the specific properties adjacent to the mine, and how that would affect the perception of those studs in the minds of their broodmare customers only, Mr Houston limits the problem to one that arguably could be solved by one or both of the studs simply moving "up the road".

However, as I emphasised in my original submission and again in Section 2 of this submission, I believe this issue will have far greater ramifications because of the significance of Coolmore and Darley in the minds of all yearling buyers. I believe the real concern facing the industry is the impact on the end-buyers' preparedness to continue to pay hundreds of millions of dollars collectively for young horses that they may perceive to be tainted in terms of their athletic ability.

In my view the business issue confronting Coolmore and Darley is whether moving elsewhere in the Hunter Valley would deal with this problem once and for all. And I believe they would reason that it does not, because:

- i) If Darley and Coolmore moved elsewhere, then who is to say that their new location might not be caught up with another mining application in future? Breeding supports the sport of horse racing, and has been a vibrant industry since Australia was colonised. Stud farms and breeders rightly take a long term view of their business, so Coolmore and Darley would be mindful of threats that might occur in 10, 20 or even 50 years' time;
- ii) By moving to another location in the Hunter Valley, Coolmore and Darley would be setting a precedent for the whole industry for the future; any time that a mine or any other future use inconsistent with the breeding environment threatened the industry, the argument would be that Coolmore and Darley moved the last time, so they or others would be expected to do the same again; and
- iii) Most importantly, the problem is one of perception, and perception by its very nature does not lend itself to closure. If Coolmore and Darley moved to other properties in the Hunter Valley, the fact of their moving would be a major news event in worldwide industry trade publications. (Because of their size, everything they do is news.) So moving to another location in the same geographic region would actually focus world-wide industry attention on just why they are moving, and it would be likely to bring the mining proximity to the attention of people who were not otherwise aware of it. If a racehorse-owning German hears a snippet about Australian horses being impacted by coal mines, he is not going to get out a map, or the Mr Houston report, or read technical reports by vets. He will simply tell his agent to make sure he spends his money in the alternative markets of Kentucky or Newmarket from then on.

For these reasons, I would expect Coolmore and Darley to each assess a move within the Hunter Valley as not necessarily solving the problem. They would be likely to form a view that such a course of action would only be a last resort, if there were no better options available.

But as I have consistently argued, there is a better solution that would bring closure to the issue. To repeat what I said at the public hearings in Denman:

*I should emphasise that I don't have any inside knowledge of the corporate thinking of Coolmore and Darley, because my relationship with them is only that of a customer. But as a former senior corporate executive I will just say that to me the decision would be a no brainer, because the risks are too uncontrollable, the money involved is too great, and the solution is too simple.*

In that Denman address, my reference to “the decision” was a reference to a decision to move interstate or to New Zealand.

In my view, much of Mr Houston's report is based on the fallacious premise that it would be undesirable for Coolmore and Darley to leave the Hunter Valley, because (he says) it would undermine their business profitability. This interpretation means that he portrays it as a step they would be very reluctant to take, to the point of accepting sub-optimal solutions. Mr Houston essentially positions the question as “why would they leave”?

But I believe the “burden of proof” (if I can call it that) should be the exact opposite. Other parts of Australia and New Zealand offer equally attractive environments for raising young horses, and Coolmore and Darley's direct customers – broodmare owners such as myself – must and would follow them in such numbers as to maintain equilibrium. Therefore, the business profitability of Coolmore and Darley, and that of the broodmare owners, would not be hurt by a move.

Accordingly, I believe that the question that should be posed, and which should be in the minds of the Department, is actually the following:

“Why would Coolmore and Darley, the two dominant players in the industry, not move their operations interstate and end once and for all the threat of their financial model being compromised, when there are several attractive alternative locations and a move would not be difficult or hurt their business?”

There is no commercial impediment to Coolmore and Darley leaving, and in terms of inconvenience it is not much different moving interstate as compared with moving 20 kms up the road. They would still have to make a property fit for purpose, wherever that property is. Every necessary supplier and service is available in Victoria and New Zealand. It would involve inconvenience to staff, but the breeding industry is an industry where many staff already move between the different centres around the world anyway. (It is a bit like the mining industry in that respect.)

It should not be forgotten that Victoria and New Zealand, as the most likely places that Darley and Coolmore would relocate to, already have large breeding industries, and have histories that were

even more celebrated than the Hunter Valley in the immediate pre-Coolmore and Darley era. The stallions, mares and yearlings in those locations may not be as valuable as the Hunter Valley bloodstock assets at the present time, but the skills of looking after horses are the same whether a thoroughbred is worth \$5,000 or \$100,000.

Even if existing staff did not move, there are thousands of people in the Victorian and New Zealand industries that would leap at the chance to be involved with some of the best known horses in the world. Such difficulties as will unfold will fall on workers and businesses in the Hunter Valley who cannot relocate, or Victorian/NZ businesses that might lose key staff to a newly arrived Coolmore and Darley. Awkward as those circumstances might be for other parties, they will not be problems for Coolmore and Darley per se, so in my view they are not reasons that they would not/could not leave the Hunter valley.

And in fact Darley already owns a stallion stud in Victoria that has stood up to 9 stallions in recent years. In a map of Darley's Australian operations shown on page 19 of Mr Houston's report, Darley's Northwood is described as a "breeding facility" instead of a stud farm, which was the description given to the equivalent Kelvinside property in the Hunter Valley. Being a fully functional stud farm, it is the case that Darley could move its stallions to Victoria very quickly and seamlessly.

The main assets of the horse industry are the horses themselves. It is hard to imagine another industry selling a physical good where such a high proportion of the invested capital is more mobile. While a move by Coolmore and Darley would involve some inconvenience, and would cause confusion in the market for maybe the whole of the first mating season, the participants would find a new point of equilibrium very quickly. The cost and inconvenience of moving would not be that significant in the scheme of things, not when the alternative would see hundreds of millions of dollars wiped off the commercial value of the horses owned by the parties involved.

I believe that the Department should be under no illusions that it would be too difficult or too undesirable for Coolmore and Darley to move. For reasons outlined in my original submission, and expanded upon here, I believe that moving would be the most logical step for Coolmore and Darley to take if the mine approval is given. And I have already given my insider's perspective on how the financial consequences for the Hunter Valley would be devastating if that came to pass.

## **SECTION 8 – THE IRRELEVANCE OF EDINGGLASSIE**

Mr Houston’s report mentions the existence of a broodmare farm, known as “Edinglassie”, next to a working coal mine.

This farm has been championed by mine supporters throughout as proof that the proximity of a mine to a horse property does not impact racing performance, and that it has not affected the preparedness of broodmare owners to keep mares at that property.

I will show later in this section why I do not believe that the recent history of Edinglassie gives any support to those claims. But more importantly, in my view Edinglassie doesn’t have any relevance to the whole-of-industry concern that I have raised in my original submission and revisited in Section 2 of this report.

### **Edinglassie is Irrelevant to the Real Issue**

Mr Houston has characterised the issue as one of possible change of “customer perception” of the Coolmore and Darley properties if the mine was to expand. He says that Edinglassie still has its broodmare-owning clients, and if they are not concerned by the presence of the coal mine, then why would Coolmore and Darley’s customers be concerned?

As I have said a number of times, my real concern in this matter is about the attitude of end-buyer customers of Hunter Valley yearlings, not the attitude of Coolmore and Darley’s direct broodmare-owning customers. The whole point of the thoroughbred breeding process is to produce young racehorses to sell to end-buyers who buy them to race. If those yearling buyers downgrade the value of Hunter Valley yearlings overall as a result of the mining issue impacting the two largest players in the global breeding industry, then the industry’s underlying economic fundamentals would be irreparably damaged.

Only by focussing on what the real problem is does the irrelevance of Edinglassie become apparent. In terms of significance within the industry, it is simply not on the same scale as Coolmore and Darley. At the industry’s main sale (the Sydney Easter Sale, which I have referenced many times in this submission), it will be recalled from Section 1 that 53% of the Australian yearlings were sired by Coolmore or Darley stallions in 2016. That 53% contrasts with Edinglassie’s portion of the catalogue which over the last seven years has averaged about 1%. Edinglassie, of course, is a broodmare farm, and no single broodmare farm has anywhere near the reach and influence of the stallion farms.

And the average sales price of all yearlings sold by Edinglassie over those 7 years at the Easter sales has been 85% of the weighted average sales price of all yearlings sold at those sales. That is, on average, the yearlings sold by Edinglassie over the last seven years have fetched below-average

prices. In fact, but for the sale of two expensive yearlings that were half-siblings from the same mother, one in 2012 and one on 2015, the Edinglassie average sales price over the last 7 years would have been only 68%, or nearly one third below, the weighted average sales price of the catalogue as a whole.

The purpose of providing these statistics is not to diminish the credentials of Edinglassie's management and staff in any way. They have an exceptionally high reputation in the industry. I raise them only to highlight that Edinglassie is not a very big part of the industry. (There are hundreds of such farms in the Hunter Valley that individually are not very big but which collectively house the many thousands of mares that live in the Hunter Valley.)

Given that the major issue in my view is the concern that buyers of yearlings will have as to the Hunter Valley product in general, it is relevant to summarise the comparative significance of an issue affecting both Coolmore and Darley to that same issue affecting Edinglassie:

<b>Major Industry Sale April 2016</b>		
<b>Factor</b>	<b>Coolmore/Darley Combined</b>	<b>Edinglassie</b>
Portion of Catalogue	~53%	~1%
Average Sales Price <sup>28</sup>	\$270,254	\$149,000
International Profile	Huge	Modest if Any

Given this stark contrast in the size, horse quality and significance of the two global giants as compared with a single broodmare farm, it seems inconceivable to me that anyone could argue that a given issue affecting Coolmore and Darley would have no wider repercussions to the industry than that same issue affecting Edinglassie, or any other single broodmare farm.

There is another more technical reason that the impact on Coolmore and Darley would go even beyond that which could be expected from their sheer size. This has to do with the nature of their global business, which is to say that many of the stallions standing at either Coolmore or Darley spend part of the year in the Hunter Valley but part of the year also in Kentucky or Newmarket. As has been stated in a number of submissions, those Northern Hemisphere environments are pristine, and mining free. It is not clear how the commercial breeders in those locations would react to the thought of a shuttle stallion coming from the Hunter Valley "mining environment", as those stallions would then sire hundreds of offspring that would influence the local gene pool. At the very minimum, one could expect that operators other than Coolmore and Darley in those markets would attempt to exploit or publicise the issue, which would only serve to increase worldwide focus on the Hunter Valley environment to the detriment of our market.

Obviously, this issue is not relevant in the case of Edinglassie as it only houses broodmares, who do not travel to other environments on an annual basis.

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<sup>28</sup> This was the average price of yearlings sold at Easter 2016 and sired by a Coolmore or Darley stallion.

Coolmore and Darley are the giants of the breeding business, and an issue affecting both of them will be news within the international breeding world. Buyers and agents will be confronted for the first time with the decision as to whether to ignore the mining risk, or play the safer option of buying a risk-free product from Kentucky or England. Those same end buyers are unlikely to be familiar with Edinglassie, so the latter is of no use as a precedent.

This is why I emphasised in Section 1 the size and industry dominance of Coolmore and Darley. It is because of their size and dominance that anything affecting them has ramifications that go well beyond their discreet individual interactions with broodmare owners who utilise their stallions. It is why I said earlier:

*“If one is trying to assess the damage that might accrue to an industry from a government decision, it makes all the difference in the world if the two parties directly affected are the two that dominate the industry and give it its global stature, as opposed to them being just two out of 15-20.”*

#### The Specific Claims Made About Edinglassie

I have shown above that Edinglassie is very small in the context of the industry, so in my view its experience says nothing about how the international buying market will react to the two global giants of the world industry having coal mining conducted next door to their Australian properties.

However, I do wish to make several observations with respect to the claims made by Mr Houston and others before him about exactly what Edinglassie proves or does not prove.

Mr Houston states that:

*“Edinglassie continues to produce winning racehorses, despite its proximity to coal mines.”(p23)*

A moment’s thought would show that the fact that a horse raised on Edinglassie won a race is not proof that its natural ability had not been compromised by inhaling coal dust. It may simply mean that the horse’s native ability was so abundant that it was able to win despite some retardation of its natural ability. A horse might have the native talent to win a race by 5 lengths, but if his ability is diminished by mining side-effects he might still win but only by one length. To argue that the fact of a win proves anything is only supposition. It would be equally nothing more than supposition to suggest that every time the horse was beaten was proof of a negative impact.

The only matter of relevance is the attitude that the general buying public would take when evaluating yearlings if the mine impacted the majority of Hunter Valley yearlings at the major sales. Buyers know, as I outlined earlier, that the difference between winning and losing a race can be as little as one thousandth of one percent, so if they are merely concerned that the presence of a coal



mine might reduce a horse's capacity to even 99.999% of natural ability, they can look elsewhere. Their perception would be the reality, given that they are the ones writing the cheques.

Mr Houston also states that Edinglassie sold a horse for \$700,000 in 2015, and says as follows:

*"In my opinion, the continued success of Edinglassie, including the sale of a horse in 2015 for \$700,000, strongly indicates that owners are not concerned by the presence of a coal mine nearby, even for very high quality horses."*(p26)

*"Numerous broodmare farms in the Hunter valley are not located as close to a coal mine as Edinglassie and, as such, broodmare owners could be expected to choose other farms if Edinglassie's proximity to the coal mine had a material effect on their perception of that farm. If such perceptions were in fact held by broodmare owners, Edinglassie would not be able to survive in its current location. In my opinion, the fact that Edinglassie is flourishing demonstrates that its customers do not generally perceive its proximity to mining operations to be a significant problem."*(p24)

Again, these paragraphs appear in my view to comprise one supposition after another.

Mr Houston refers to Edinglassie's "continued success" and states that Edinglassie is "flourishing" but there is nothing to indicate how this is known or measured. In fact on several other occasions Mr Houston again refers to Edinglassie's success, or successful operations, which seem to be assumed as a given.

I mentioned earlier in this section that in the last seven years Edinglassie has sold two horses for large amounts. These were in fact two yearlings from the same mother, "Amelia's Dream" in two different years. The two sales were the \$700,000 yearling in 2015 referenced by Mr Houston, and an older half-sister who sold in 2012 for \$910,000. Absent those two sales, which are outliers in the context of the farm's recent sales history, the average price of Edinglassie yearlings over the last seven years has been 68% of the sale average as a whole. There are obviously many factors that influence that statistic, but at face value it hardly justifies the supposition that the farm must be home to "very high quality horses" owned by "owners" written in plural.

Further, the fact that a yearling is sold by a particular farm at a yearling sale does not necessarily mean that the yearling's mother resides at that property, or that the yearling itself was raised there. It is quite common in the industry for horses raised at property A to be sold under the name of property B at a sale.<sup>29</sup> That is, Mr Houston is again merely supposing that the mare, Amelia's Dream, the mother of the \$700,000 yearling and the \$910,000 yearling, actually resides at Edinglassie.

In fact, there is reason to doubt that supposition.

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<sup>29</sup> There are many reasons for it to happen. Preparing a yearling for sale takes a special skill that not all farms have, or some that have the skills may have more numbers than they can manage, etc. And some broodmare owners may have a small property that is adequate for young horses to grow up at, before they are sent to a full service farm to be prepared for sale.

In December 2011, an article about the upcoming sales season said:

*“Meanwhile, Michael Talty’s Edinglassie Stud Farm has been given the honour of preparing the outstanding Encosta De Lago – Amelia’s Dream filly for owner (named).”<sup>30</sup>*

This article was referring to the filly that went on to sell for \$910,000, and this article strongly suggests that the filly and her mother did not actually reside at Edinglassie. If they did it would be inconsistent with a press article that a particular farm had been chosen to prepare her for the sale. I don’t know specifically whether the mare Amelia’s Dream actually resides at Edinglassie (or has ever done so), but it is only supposition for Mr Houston to assume that she resides there, let alone to assume that her owner does not consider the proximity to the mine to be a problem.

To this latter point, the most prominent client of Edinglassie has been its original founder, Bob Oatley, who I believe maintained many mares there after he sold the property some years ago. Mr Oatley’s decision would presumably have had to do more with sentiment than being a statement on the attributes of coal mining. It is usual in this industry for the various broodmare farms to have long-standing and loyal clients. (I have been a client of my particular broodmare farm for 16 years.) Mr Oatley died earlier this year, and at the recent bloodstock sales on the Gold Coast in June, Edinglassie offered some 11 mares for sale.

Mr Houston does not explain whether Edinglassie’s clients are long-term or have become clients recently. He does not explain if those clients were friends of, and loyal to, Bob Oatley or the current manager. He does not explain whether those clients follow matters closely, or simply leave the farm to manage their investments without interfering. Mr Houston states only that Edinglassie sold a yearling in 2015 for \$700,000 (the equal 24<sup>th</sup> highest priced lot of that sale), and from that information his report extrapolates that the farm is flourishing and successful, that the breeder of that yearling keeps the mother at Edinglassie, that in fact owners “plural” keep quality horses there, and that these owners have no problem with the coal mine.

In my view, that is supposition on top of supposition on top of supposition, and once again it has the unfortunate result, I believe, of drawing attention away from the real issue.

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<sup>30</sup> Sportsman Weekend Edition December 9, 2011, article by Shane O’Cass. I have left out the owner’s name as irrelevant.

## **SECTION 9 - WILL THE DEPARTURE OF COOLMORE AND DARLEY CAUSE A COLLAPSE?**

This submission argues that Mr Houston's report is compromised by a lack of actual industry experience, a lack of historical perspective, and a lack of understanding of major participants' business models. So it is to be expected that I disagree with his conclusions.

He states that the Hunter Valley equine CIC will not collapse if Coolmore and Darley leave. He says:

*"It is even less likely that both Coolmore and Darley would leave the Upper Hunter (as distinct from either one of them leaving), because each stud farm would stand to benefit materially from the other leaving by expanding to fill the gap left by any stallions that may also leave. However, the equine CIC would not collapse if they both left the Upper Hunter because it would still be approximately double the current size of the next largest thoroughbred breeding areas in Australia and New Zealand, even before the likely expansion by other, competing stud farms is taken into account."(p6)*

However, this submission has challenged each limb of that conclusion.

I believe that Darley and Coolmore are not likely to consider this as an "opportunity" to take business from each other, because each understands the industry's fundamentals and would know (for reasons I have explained at length) that to stay in the Hunter Valley would lead to hundreds of millions of dollars being wiped off the value of their bloodstock.

The argument that the Hunter Valley will still be bigger in size than the next largest breeding area in Australia, even if Coolmore and Darley leave, is based on the premise that breeders will not move their mares out of the Hunter Valley. I have consistently advised from my original submission onwards that some 3,000 mares will leave the Hunter Valley in a first wave alone if Coolmore and Darley go elsewhere. In my original submission I had already advised that this would make Victoria the largest breeding centre in numerical terms alone, and obviously by hosting the Coolmore and Darley stallions it would quickly become the leading centre in terms of quality.

But in my view, it needs to be asked even if the Hunter Valley still had slightly more numbers than Victoria, in what way is that somehow a win for the region and for NSW? If the region and the state lose more than \$1.5B of economic value (as I advise below that they will) it would hardly seem to be any comfort that the downsized remaining industry was still technically larger than that of the beneficiary of the move.

Finally, the idea that new entrants or new stallions would enter the Hunter Valley, and have such compelling attributes that profit-orientated breeders would ignore the obvious option of putting their mares on a truck and continuing to mate them with the best stallions in the country, is at odds with commercial reality, for reasons I discussed at length in Section 6.

The Hunter Valley was not the pre-eminent breeding centre in Australasia before Coolmore and Darley established themselves there. New Zealand dominated the Australasian industry, and Victoria was more prominent than NSW in a solely Australian context. If Darley and Coolmore relocate to either of those locations, then the fact that the Hunter Valley and NSW will lose its reputation and much of its economic activity from breeding to that other location is, in my opinion, not even a fit matter for debate.

The fact that NSW currently enjoys the economic benefits of the largest and highest quality breeding industry in the Southern Hemisphere is largely a matter of serendipity, and with the mobility of breeding horses, much of that economic benefit can, and would, disappear overnight.

### Calculating the Economic Loss

If Coolmore and Darley leave, as I believe will follow inexorably if the mine extension is approved, then there will be severe financial loss to the Hunter Valley, and to NSW.

This hardship will not be suffered by Coolmore and Darley, and it will not be suffered by myself and other investors in the industry who own broodmares. Horse assets are mobile, and within a short period the breeding stallions and mares will be resuming a “business as normal” routine somewhere interstate or in New Zealand.

The economic loss will mainly be suffered by those Hunter Valley farms and businesses whose income is currently earned by looking after breeding mares and their young offspring. Those businesses have land and improvements and other fixed assets that cannot be moved interstate, and they will be left competing with each other to look after a pool of mares that will have shrunk by about one-third as an initial response to the Coolmore and Darley move, and which will keep on shrinking.

In my original submission, I gave evidence that for each broodmare in the Hunter Valley, investors such as myself pay local service providers about \$30,000 per annum. (Mr Houston quotes this figure in his report, citing my submission as the authority.) So if 3,000 mares leave the Hunter Valley, that will be some \$90m of income lost to the Hunter Valley businesses. That is direct spending only, and does not take multiplier effects into account as that money circulates around other small businesses within the community.

In my original submission, I utilised my investment banking background to calculate the net present value of that lost future income. I took the after-tax sum of \$62.6m and capitalised it at a rate of 6.12% to calculate a net present value of \$1,023m that would be lost to the Hunter Valley by way of future income forgone. The methodology of my calculation was described fully in the original submission, and took into account the risk profile of that income and the historical growth rate of the industry.

In the nine months since my original submission was presented, risk-free interest rates have moved sharply lower. When I lodged my original submission, the Australian 10 year bond rate was 2.71%. It is currently about 2.01%.<sup>31</sup> Adjusting for the movement in the underlying risk-free rate, the same methodology would today produce an after-tax net present value of \$1,155m.

I submit that I am able to make an accurate calculation of that component because I have direct and extensive personal knowledge of the costs of keeping broodmares in the Hunter Valley, and of the nature and risks of that part of the business.

This component is only one element of the potential losses to the Hunter Valley and to NSW. But in addition to the future economic value lost from the departure of broodmares, there would also be the loss to the Hunter Valley of the spending undertaken in the region by Coolmore and Darley

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<sup>31</sup> Calculation made Monday, June 27, 2016

themselves. Those stallion farms have large rosters of personnel, and will have many suppliers involved in the care and maintenance of their horses and properties.

Coolmore and Darley currently receive some ~\$100m of stallion fees per annum. (This is calculable from disclosed information, as I showed in my original submission.) I do not have direct knowledge of how much of that is spent in the region by Coolmore and Darley on operating expenses, but I believe that I know enough about their business to make a useful estimate.

My judgement is that the net present value of income lost to the Hunter Valley by the operations of Coolmore and Darley themselves moving interstate would be in the hundreds of millions of dollars rather than the billions, but when added to the figure for the broodmares it almost certainly takes the total figure to somewhere of the order of \$1.5B of future income that will be transferred from NSW to another state or to New Zealand.

In the longer run, there would be many other implications to the state of NSW if the status of the elite breeding centre transferred from NSW to Victoria, for example. The amount wagered on horse racing events is correlated with the quality of the horses that race in particular locations. The best quality racehorses race in Sydney and Melbourne, and accordingly more money is wagered on racing in those locations as compared with say, Brisbane and Adelaide. (Even people who live in Brisbane and Adelaide bet more on Sydney and Melbourne races than they do on their home states' racing because the quality of the horses interstate is so much higher.)

If Darley and Coolmore move interstate, and large numbers of elite breeding mares follow them, this must raise the quality of horses bred in Victoria and lower it in NSW. Even though many young horses are sold as yearlings and can end up racing anywhere, a large proportion are also not sold, and tend to race close to where they were raised. Merely losing Darley on its own, as the largest owner of horses in the country, would lessen the relative size and quality of racing fields in Sydney in favour of Melbourne.

If the quality of horses racing in NSW drops, and is lifted in Victoria (the most likely outcome in my personal opinion) then over time this will lead to a migration of wagering revenue from Sydney races to those run in Melbourne. This is something that the Department should be factoring into its consideration of this matter, as state governments are known to be sensitive to income streams from wagering turnover.

**To conclude, I am not sure if losing \$1.5B of future income from a region like the Hunter Valley would technically constitute a "collapse" as Mr Houston would define it, but in plain English it would be a disaster for the region and for the state of NSW.**

**\$1.5B of lost future income might not be the biggest financial loss an Australian state has suffered from an industry disruption, but it is hard to imagine that there has been a precedent where the financial loss had been so predictable, and so easily avoidable.**

**I repeat my advice that if the mine extension goes ahead, the probability of Coolmore and Darley relocating outside of NSW is assessed at 85%-90%, and that if that happens, the probability of a significant migration of broodmares to that same location is judged as 100%. While there is room for some small doubt in my mind as to Coolmore and Darley leaving, because I cannot speak on their behalf, I have no doubt about the response of broodmare owners if they do move, because I am an experienced owner myself.**