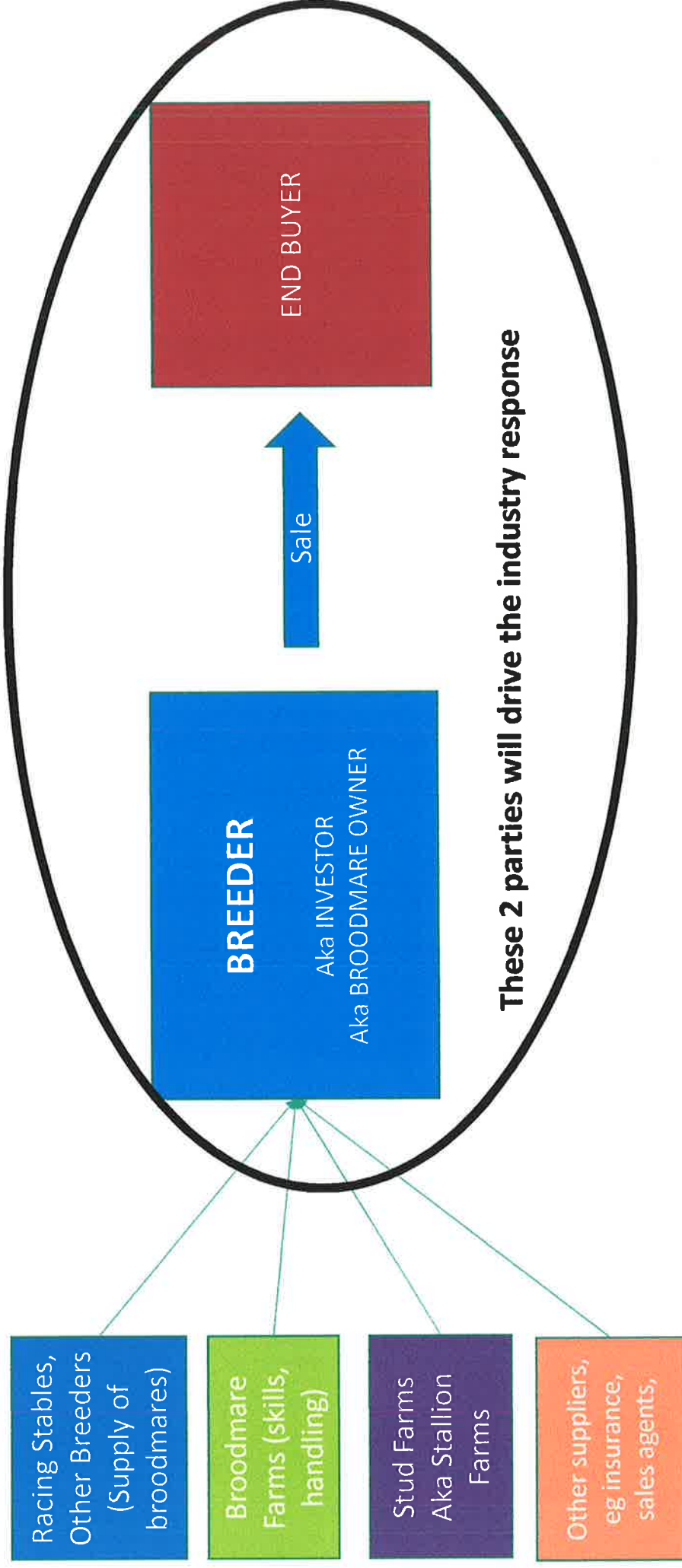


(21) Darryl Guihot

Presentation to PAC
by Long-Term Horse Breeder
and Corporate Finance Expert
Darryl Guihot

Muswellbrook 17.11.2016

The industry is a manufacturing process with a 3 year lead time, and Breeders are the manufacturers. The Breeder chooses suppliers including the stud farms, broodmare farms and others.



The Hunter Valley production process involves an annual spend of ~\$710m and end product value of ~\$800m, with a 3 year lead time

BREEDERS SPEND
\$710M EACH YEAR,
OF WHICH
\$500M MINIMUM IS IN THE
HUNTER VALLEY



THE END CROP OF ~5,400
FOALS IS WORTH ~\$800M
OR MORE

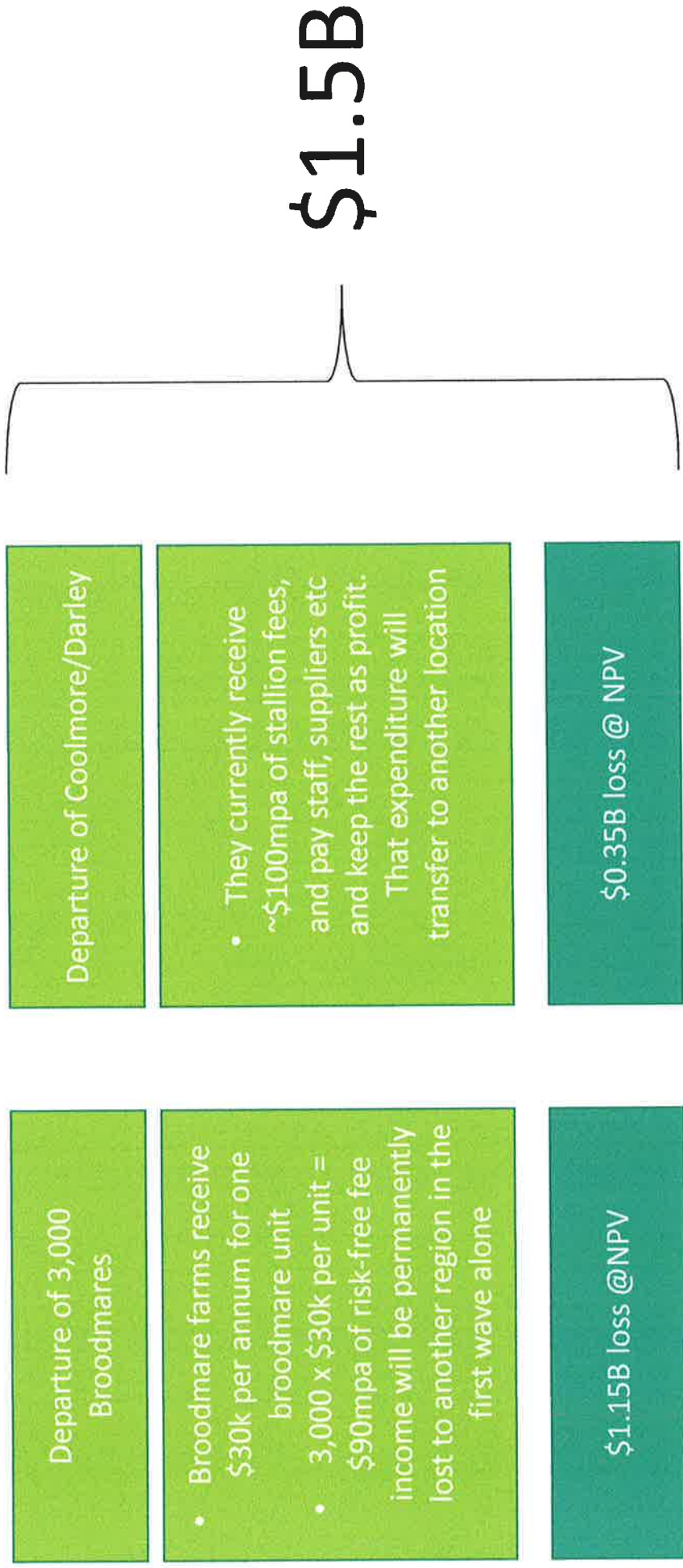
Summarising the sequence of logic to Coolmore/Darley moving

Buyers will almost certainly see offspring of Coolmore and Darley stallions as tainted

With a 3 year lead time, breeders need certainty before investing \$2B+

Accordingly, breeders will not use Coolmore and Darley stallions in situ, but a move will solve the issue for all concerned

The direct consequence of the mining approval will be a transfer of \$1.5B NPV of direct cash spending from the Hunter Valley to an interstate location or NZ.



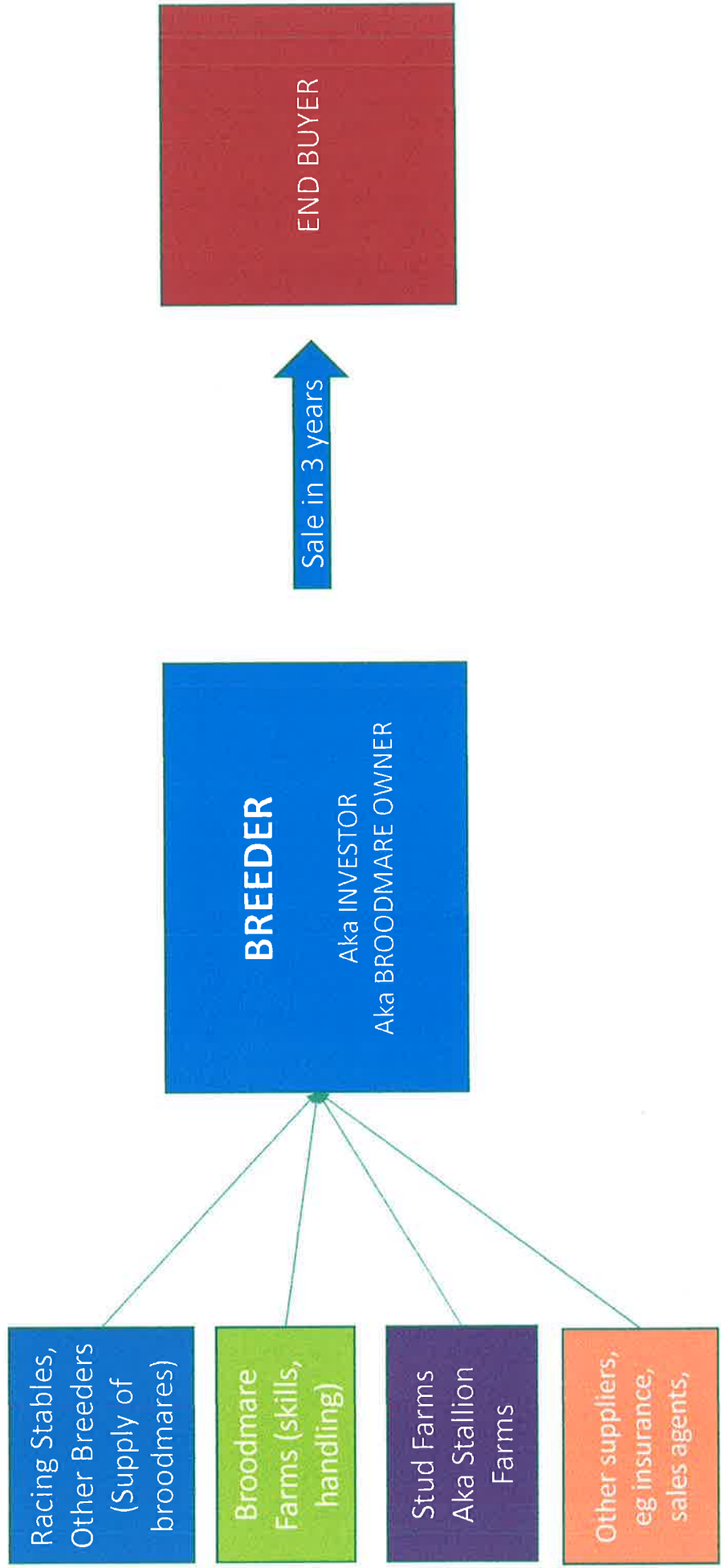
The idea that the Hunter Valley is somehow special is not borne out by history. Coolmore/ Darley have made the Hunter Valley, not vice versa

Sale Location	Average Price 1976 (pre Coolmore/Darley)	Average Price 2015 Coolmore/Darley era
Melbourne	\$7,250	\$95,886
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In 1976, NSW ranked behind Victoria, and the strength of NSW in that era was the Southern Highlands. The Hunter Valley was off the radar.

The preceding slides were a brief extract for presentation purposes. The full presentation follows

The industry is a manufacturing process with a 3 year lead time, and Breeders are the manufacturers. The Breeder chooses suppliers including the stud farms, broodmare farms and others.



Breeders, stud farms and broodmare farms have different business models and risk/return equations. The breeder takes the investment risk on the product (young horse) as a whole.

Breeder / aka Broodmare Owner/ aka Investor

- Owns breeding mares, which are freely mobile
- Owns the young offspring
- Does not have fixed assets
- Funds the production process
- Takes the equity risk, so makes the profit or loss

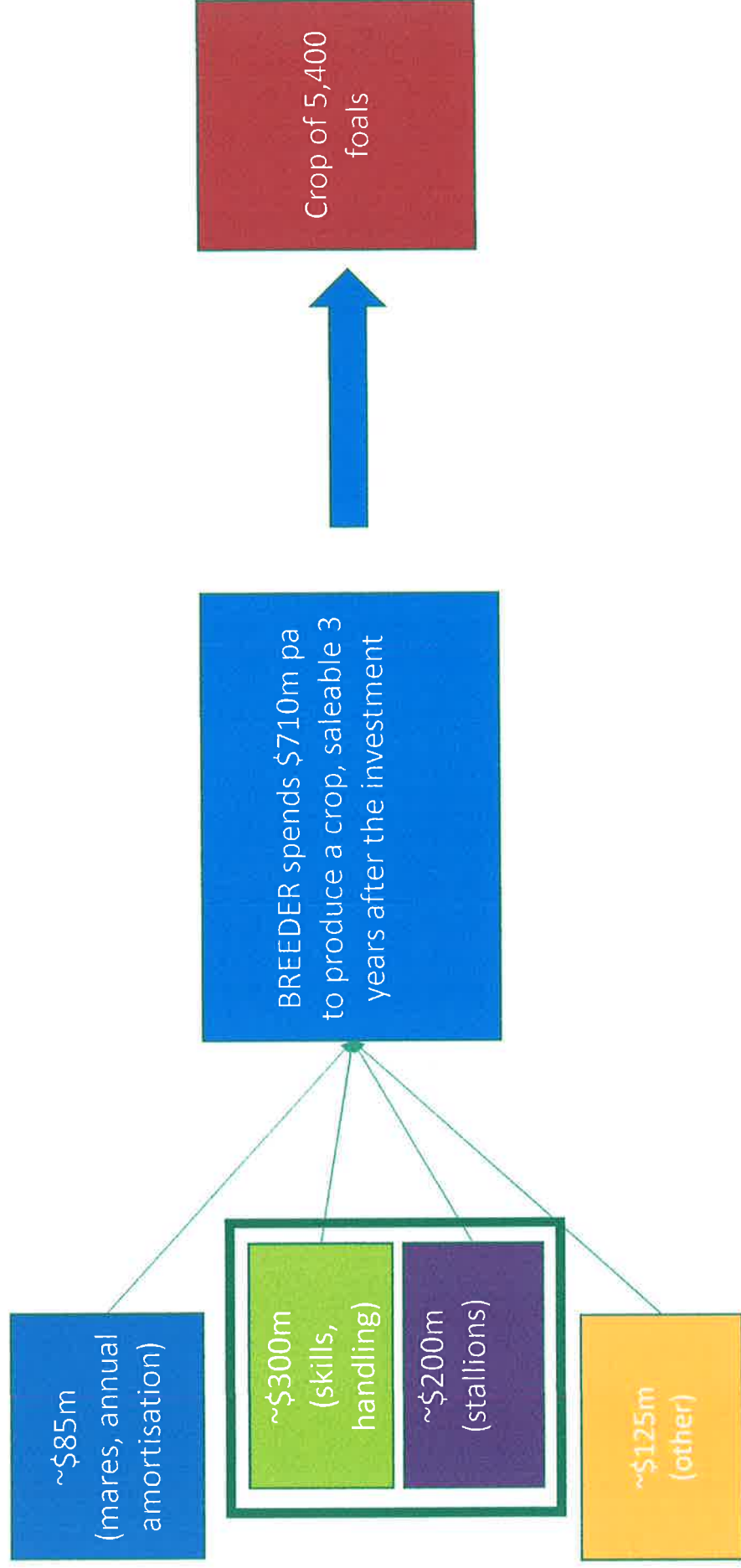
Stud Farm/ aka Stallion Farm

- Owns high value stallions, freely mobile
- Owns fixed assets (farm), small change by comparison to horse values
- Charges breeders a fee for use of stallion, based on individual attributes and potential sales price of offspring
- Fees are fixed; takes no equity risk

Broodmare Farm

- Owns fixed assets (farms)
- Does not own horses
- Specialises in caring for horses, and looks after mares and foals
- Charges daily fee for service, plus cost recovery
- Takes no equity risk, simple volume business

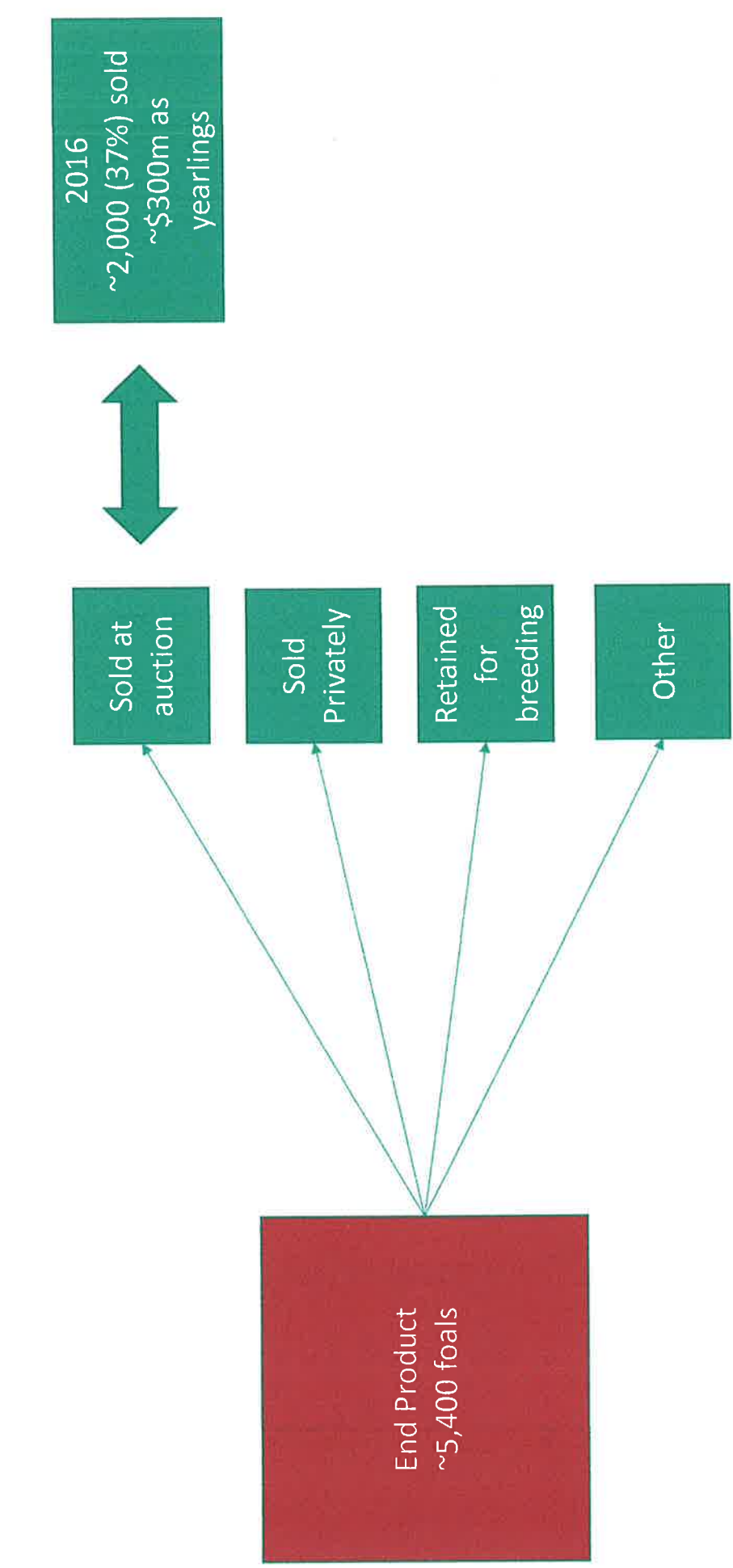
The manufacturing process costs ~\$710m each year, with ~\$500m of that being incurred in the Hunter Valley



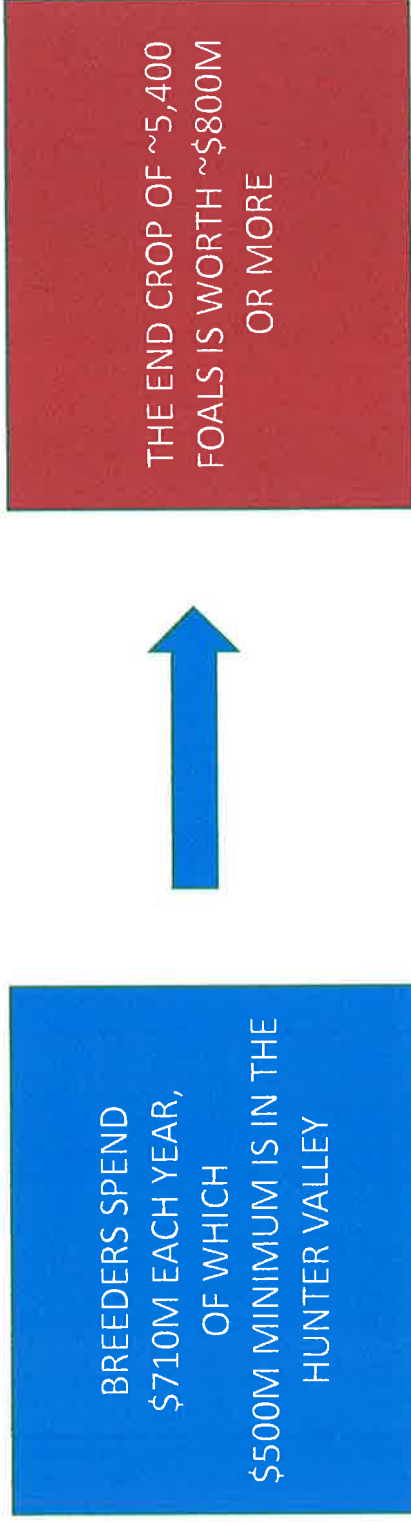
The components of expenditure are as follows:

Cost component	Calculation	Total	Hunter Valley
Fee to broodmare farms for care of mares and offspring	10,000 mares x \$30k per head of broodmare	~\$300m	\$300m
Fee to stud farms	~ 8,000 at fees up to \$200k each (Not all mares are served)	~\$200m	\$200m
Amortisation of capital purchase of broodmares	Total mare value ~\$1.0B, amortised over 12 years	~\$85m	Some, but unknown
Insurance, Selling Expenses		~\$125m	Some, but mostly capital cities
TOAL PROD COST Cost		~\$710m	> \$500m
Annual Foal Crop	Not all mares foal	~ 5,400 foals	

In 2016, about 37% of the crop was sold at auction for ~\$300m. The overall crop has an indicative end value of ~\$800m



The Hunter Valley production process involves an annual spend of ~\$710m and end product value of ~\$800m, with a 3 year lead time



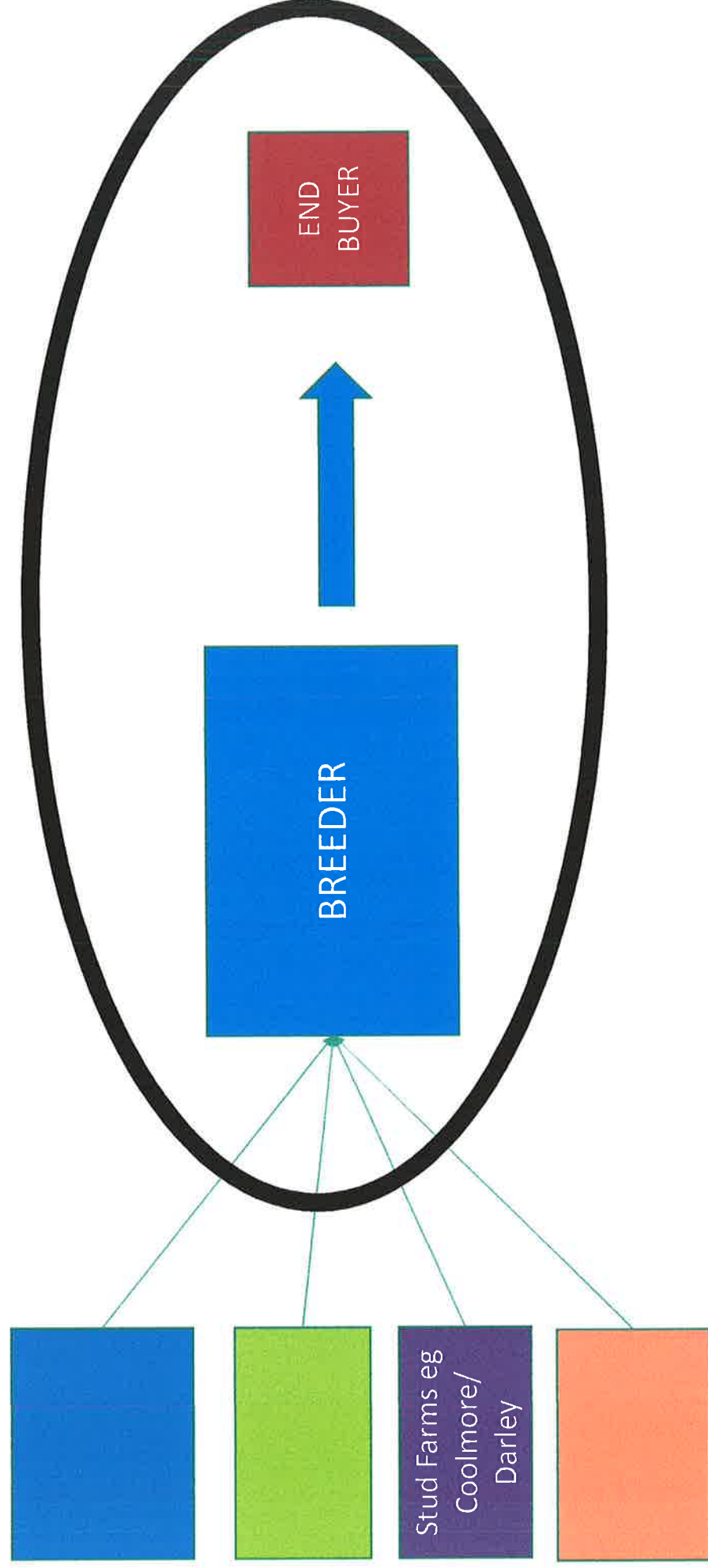
The Hunter Valley breeding industry is nearly three times bigger than the Department says it is

- In 2015, the Department said that “the Hunter Valley breeding industry generates income of \$300m annually”.
- In 2015, I advised that the cash costs in the Hunter Valley alone were \$500m, clearly putting the Department on notice that its figure was wrong.
- The Department has subsequently sought or preferred advice from people outside the industry who cannot possibly have the necessary perspective or information about the industry to know its size.
- In 2016, the Department is still advising “the Hunter Valley breeding industry generates income of \$300m annually.”

What credibility does the Department have?

- If the Department cannot come close to determining the size of an industry after six years, how is it qualified to assess of the impact of its decisions on that industry?
- If a department receives clear and direct advice that it is misstating the most basic of facts, yet continues to state those “facts” with no effort to clarify, what does it say about its commitment to understanding the subject matter?

The response to the Drayton mine will be driven by Breeders and end buyers, more so than suppliers

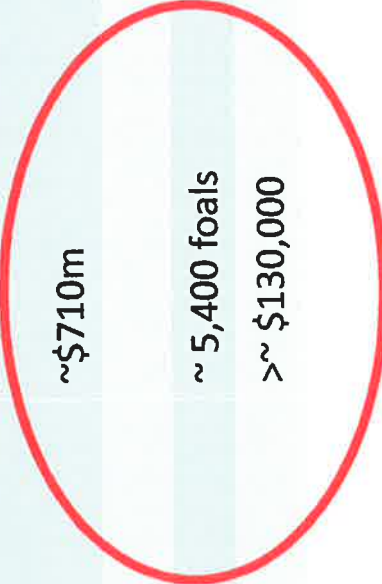


How Drayton will impact the decisions of the end buyers and breeder/manufacturers

From End Buyer's Perspective	From Breeder/ Manufacturer's Perspective
Unit production cost = \$130,000. These are not farm animals	Offspring of Coolmore/Darley stallions the most lucrative
Main influence on the value of a young horse is the father	Buyers likely to see offspring of those stallions as tainted
Coolmore and Darley have the most sought after stallions	3 year production lead time - Breeders make decisions now
At 2016 Easter sale, 53% of gross for all Aust horses	Cannot invest >\$2B (3 x \$710m) with huge pricing risk
A coal mine next to the stallions habitat is a game changer	So cannot use Coolmore/Darley stallions unless they move

The average unit cost of the Hunter Valley product is \$130,000

Cost component	Calculation	Total	Hunter Valley
Total Production Cost		~\$710m	> \$500m
Annual Foal Crop		~ 5,400 foals	
Unit Production Cost		>~ \$130,000	



The standards for extremely valuable athletes are different from farm or working horses because of their value and purpose

- Unit production cost is ~\$130,000 per each young horse produced. Sales prices need to be well above this figure to offer breeders a return on their money.
- Horses worth hundreds of thousands or even millions each are not commodities; they are unique individual products purchased for their potential athletic ability. They are as different from farm animals as formula 1 cars are from pushbikes
- My first report pointed out that the Department's 2015 report did not distinguish between thoroughbreds worth up to millions of dollars each and stock horses worth hundreds of dollars each
- Notwithstanding, the Department has still chosen a photo of a stock horse for the cover of its latest report

What is important to the buyer of a young horse?

Factor	Real Estate Buyer	Yearling Buyer
Most Important	Location	Sire
Second Most Important	Location	Sire
Third most Important	Location	Sire

Coolmore and Darley are the biggest stallion owners in the world. In Australia they are bigger than the rest of the competition put together

Factor	Coolmore/Darley out of Whole Industry
Best Performed Stallions (Racetrack performance last season)	9 out of top 15
Best Selling Stallions at Main Industry sale (2016)	12 out of top 20
Share of total gross from Aust horses sold at this sale	53% of total
Most Expensive Stallions (gauge of future expectations)	11 out of 20

How the Drayton extension would impact on the value of yearlings

- To repeat – the most important factor in the selling price of the young horses/athletes is the identity of the father
- With a coal mine adjacent to the habitat of the best stallions in the industry, buyers will be concerned about their physical attributes and temperament being impacted; or that of the mother when she is resident.
- Most horses are bought by agents - they will be even more risk averse than their clients, and will have to disclose the coal mining issue to those clients
- Yearlings by Coolmore and Darley stallions would inevitably be tainted in the eyes of agents/ buyers in a post-mine environment, with some spillover reputational impact on ALL of the end product
- By way of example, in 2007, an outbreak of equine influenza saw yearling prices from affected areas slashed; health concerns can be fatal to pricing when buyers are assessing athletes as potential million dollar purchases

The manufacturing process has a 3-year lead time

2016	2017	2018	2019
April-May, Stallion Booked			January-June, Yearling Sold
		August, Foal becomes Yearling	
Sept-Nov, Mating Occurs	August-November, Foal Born		

Manufacturers have to invest in 3 crops (\$2B+) before the outcome of today's decisions is known.

Breeders will not maintain the status quo

- Over a 3 Year Time Frame, the total spend by breeders to manufacture the Hunter Valley crop is > \$2.1B
- Breeders will not blithely maintain “business as usual” on such a huge level of investment if the appeal and pricing of the end product becomes subject to such a key uncontrollable risk as the tainting of the product to buyers

The manufacturers/breeders will drive the response of the industry, specifically the departure of Coolmore and Darley

- With a cloud over the future pricing of end product sired by Coolmore and Darley stallions, investors cannot continue to use those stallions in their current locations
- Consequently, Coolmore and Darley must move or else their business would collapse
- Breeders will move many broodmares to wherever Coolmore and Darley move to – they have the best stallions, which is the most critical component of the investment return
- There are no impediments to stallions and mares being moved; specifically, Victoria, South Australia, Queensland and New Zealand have all historically been more prominent breeding locations in Australia than the Hunter Valley, from time to time
- The idea that the Hunter Valley is too special to leave is a myth and is only claimed by people outside the industry
- The idea that the best stallions in the world can be replaced from elsewhere is a myth and is only claimed by people outside the industry

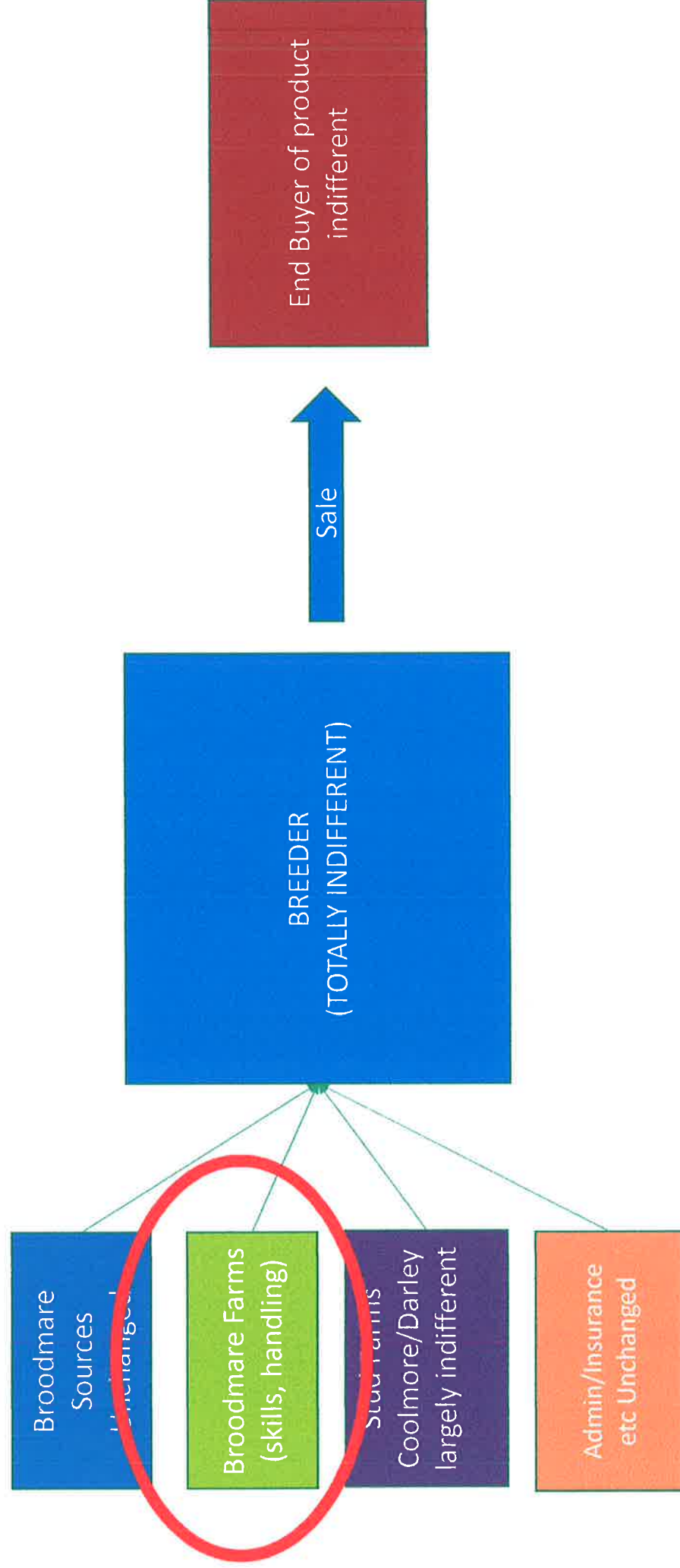
Summarising the sequence of logic to Coolmore/Darley moving

Buyers will almost certainly see offspring of Coolmore and Darley stallions as tainted

With a 3 year lead time, breeders would face unknowable outcome and unacceptable risk when investing \$2B+

Accordingly, breeders will not use Coolmore and Darley stallions in situ, but a move will solve the issue for all concerned

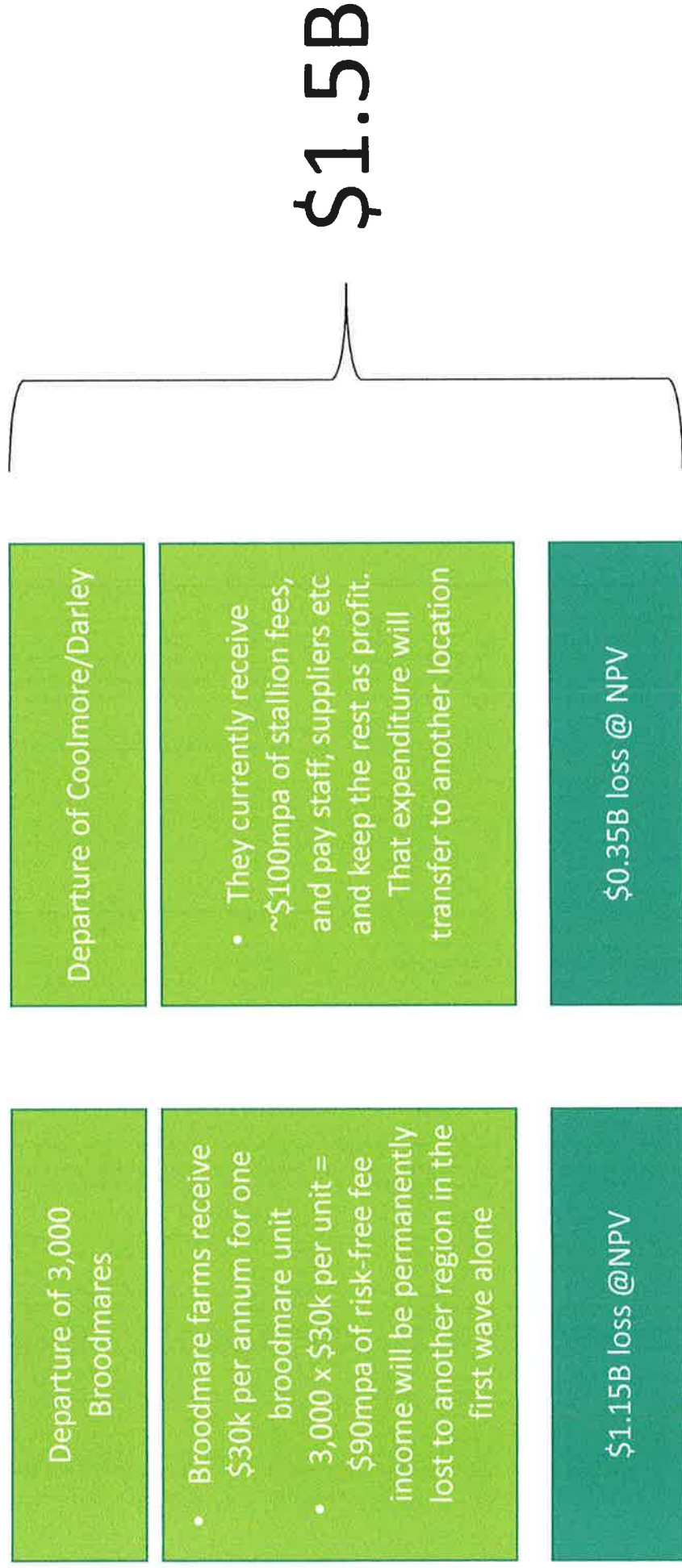
The breeders and stud farms that relocate will continue, business as normal, in another location. The losers will be the broodmare farms and suppliers that currently service the thousands of departed horses.



Coolmore, Darley and 3,000 broodmares will leave in the initial wave

- For equilibrium to be maintained, ~3,000 mares will move in the first wave. This is a calculation made by an experienced breeder, with knowledge of individual stallions. This is not an opinion.
- Over 10+ years, as mares remaining in the Hunter Valley grow old and pass on, breeders will send replacement mares to the new location of Coolmore and Darley, because stallions drive the financial returns for investors, and they will always have the best stallions
- After the life cycle of the current mare pool has died out, the Hunter Valley will return to the cottage industry status it had before Coolmore and Darley

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intro	1	1
relationships, cost	2	2 relationships, money
what buiyers will do, and investros	1	1 the three arrows
who suffers, the wash up	0.5	0.75 the \$1.5B
wrap up	0.25	0.25
total	4.75	5