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Equine Influenza: Is the carnival over?

By the beginning of October, the Equine Influenza ('EI') virus had infected more than 33,000 horses in NSW and Queensland, with the number increasing daily. For the Australian horse racing industry, the epidemic could not have hit at a worse time.

In the lead up to the Spring Racing Carnival – the time of year Australia becomes obsessed with horseflesh – some of the country's best thoroughbreds remain captive to their home stables; unable to set foot on the racetracks where they earn their keep.



Major racecourses in NSW are in total lockdown. Racing has been suspended indefinitely in Southern-Eastern Queensland. Racing in Brisbane is unlikely to resume before February 2008. In Victoria, the \$2 billion spending bonanza that surrounds the Spring Carnival is going ahead – but only after \$2.2 million is spent on immunising horses and the state against EI. But not even the vaccination program appears likely to stop the inevitable spread of the virus.

To put the potential racing industry losses into context, consider one of Australia's leading sires, Encosta de Lago – the first Australian horse confirmed with the disease – stranded in quarantine at Eastern Creek. Encosta de Lago would normally serve more than 100 mares a season at a fee of \$200,000 per mare. If he serves no mares this season, that is at least \$20m of lost potential income for one stallion alone.

The impact of the EI outbreak will spread through every layer of the Australian Equine Industry. Horse owners need to keep feeding their horses with no possibility of prize money or breeding income. In infected zones, vets report business is down as much as 90 per cent.

The story is the same for the feed merchants, the transport companies, the farriers, the caterers, the stable staff – no one in the industry remains untouched by this.

EI is also going to lead to some tough decisions for anyone who has provided finance for racehorses, stallions, race club facilities or racing infrastructure. In particular, small operators will be doing it tough and any operations that were marginal beforehand may be pushed over the edge by EI. Expect to see plenty of heartache.

What is EI?

EI is a highly contagious viral disease of horses and related animals such as donkeys, mules and zebras. Whilst EI is endemic in Europe, North America, South America, North Africa and Asia, Australia (and Iceland!) had remained free of the virus due to its remoteness and relatively tough quarantine laws.

The effects of EI on horses can vary enormously, although it is generally not fatal. Whilst the strain of virus in Australia is relatively mild, at the very least it will significantly interrupt a thoroughbred's campaign.

A horse is regarded as clear of the infection after 28 days, with a longer recuperation period if the fever lasts for more than four days. For a racehorse, however, where a horse is spelled for up to two months, that could equate to six months away from the racing scene. For many NSW and Queensland horses, that means missing a whole spring campaign.

Time frames

The effect on racing may be even more catastrophic: the Sydney Autumn carnival has been postponed and Magic Millions has just announced that its races and sales on the Gold Coast have been deferred by 10 weeks from January to Easter.

Where sales are postponed by several months, breeders face three key issues:

- 1 The breeder is required to retain the horse for an additional time period, incurring further feed, agistment and other costs.
- 2 There is a cashflow impact for the breeder given the delay in the receipt of funds from the sale.
- 3 Sales, particularly in the shorter term, are likely to be impacted by the fact that the wallets of owners and trainers will not have been fattened by the spring carnival. There is also the issue that prospective purchasers will be operating “blind” – not having seen the progeny of young stallions performing on the track. Confidence levels in the industry are likely to be down, eroding sale prices.

The effects on the Australian racing scene may last for years. Whilst measures are being introduced to allow some resumption of breeding in areas such as the Hunter Valley – which produces around 30% of Australia’s thoroughbred breeding – there is the prospect of many of the nation’s top stallions remaining out of bounds for this year’s breeding season.

Certain “shuttle” stallions from overseas will return to the northern hemisphere without serving a single mare in Australia this season.

This increases the risk that the major studs may be more hesitant to send stallions to the southern hemisphere in future.

Owners are likely to be reluctant to send their broodmares to infected areas where they may be required to remain for months until the area is declared free of EI. This has resulted in many mares being sent to alternative, local stallions. As a result, we can expect to see a degradation in the quality of horses coming through the sales ring in two or three years time.

Who is affected?

To put the flow-on impact of the EI virus into context, you need to consider the enormous range of industries and people that are involved, either directly or indirectly, with the horse-racing industry. Amongst the more obvious, race clubs have been hard hit through the loss of turnover, with several carnivals and cups already cancelled in NSW and Queensland.

Many horse owners and trainers are essentially stranded; unable to move their horses to compete at race meetings and hence missing out on the race winnings that are vital for many trainers simply to survive. For owners, the feed, agistment and vet bills don’t stop coming just because the income has stopped. For the vets, feed merchants and transport companies, work has dropped dramatically or stopped altogether.

Then there are the countless equestrian clubs, carnivals, shows and other events that involve horses. The Royal Melbourne Show was held without horses this year for the first time in its 150-year history.

Perhaps the best example of the wide-reaching impact of EI relates to the Sydney milliner that ordinarily would have sold several hundred hats by now for the racing carnival and associated social events. This year, however, the milliner has sold just three hats and plans to close its doors.

The financial impact

At this stage, the full financial impact is impossible to calculate. The NSW government has announced financial packages totalling \$114m, but that package is a drop in the ocean compared to the potential losses faced by the industry.

And whilst racing has resumed in many jurisdictions, betting turnover through the TAB (the source of vital funding for racing clubs) remains depressed. Tabcorp, which operates TABs in Victoria and NSW, reported betting turnover had dropped by \$150 million in the first month after the EI outbreak.

Even in Victoria – so far uninfected by the virus, and where race meetings are continuing to take place – there are significant financial implications for the race clubs. TAB wagering income for race clubs is determined by where the bet is placed rather than where the race is run. This means that while NSW and Queensland race clubs are still receiving income from bets placed in those states on Victorian races, with no interstate races for Victorian punters to bet on, Victorian clubs have seen their revenue from the TAB significantly diminished – and this while the race clubs continue funding prize money.

The Equestrian Federation of Australia has called for a \$20m assistance package from the Federal Government to protect the future of 14,000 non-racing equestrian businesses that employ 30,000 staff. The EFA claims Australia's standing as a leading equestrian nation is under threat, with three Olympic equestrian sports now at risk.

In terms of insurance, business interruption insurance policies typically have a disease exclusion relating to loss of profit provisions, so it is unlikely that everyone affected by EI will have recourse to insurance protection for their losses.

As to who will survive the EI crisis, generally the major studs are multinational businesses with the capital to endure such an event. For most owners, horse racing is an expensive hobby, but livelihoods are not dependant upon it.

The people doing it tough will generally be the smaller operators. Studs or transport companies that were marginal operations beforehand may not have the reserves to survive.

There will also be certain trainers or syndicators (people who purchase horses to on-sell via percentage interests in the horse) who have acquired horses, potentially through financing, who now face the impossible task of syndicating horses in the NSW or Queensland markets.

What should financiers do?

There will be a number of financiers who have provided funding directly into the racing industry through race clubs, owners, trainers or syndicators. Others may have financed peripheral suppliers or service providers impacted by the industry downturn.

There are a number of key issues that financiers need to assess:

- There will be a significant impact on cashflows into the industry. In Sydney for example, it is possible that the major Autumn races – including the Golden Slipper, Doncaster and Epsom – will be deferred, delaying the arrival of prize money until at least May or June 2008.

- Financiers will need to assess the underlying performance of those client businesses affected by the crisis. If the business was sound prior to the crisis, some leeway probably needs to be allowed to assist your client through this difficult period.
- Asset values (and particularly bloodstock values) are likely to be depressed in affected states and therefore realisation of security at the present time should probably be regarded as a last resort.
- Those operators that were marginal even prior to the EI crisis need to be re-examined and a detailed assessment of their financial outlook undertaken.

Has the horse bolted?

EI does not spell the end of the Australian horse racing industry, but it does threaten to wipe out some of the industry's smaller or less stable participants. It is a disaster for the 2007 racing calendar – and for those whose businesses depend upon the fashion and social circus that revolves around it – and its impact is likely to be felt in the racing industry for years to come.

Whilst the Australian equine industry will get back to its feet and racing will eventually return to normality, the reality is that EI is probably here to stay.



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