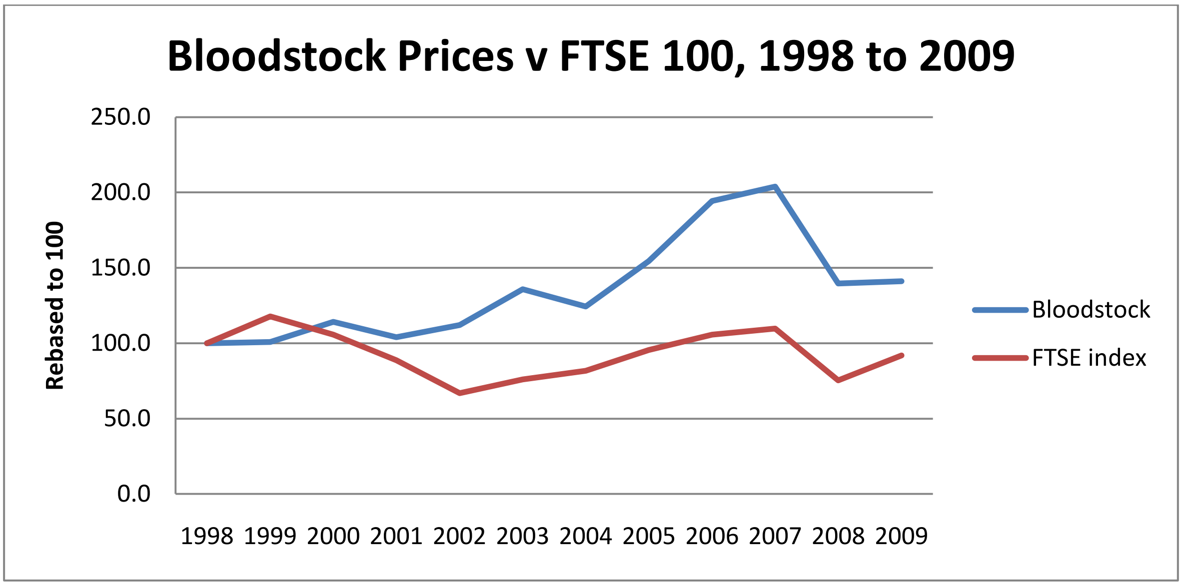
INVESTING IN BLOODSTOCK – A LEGITIMATE PART OF ONE'S PORTFOLIO OR A RISKY WAGER?

Investing in bloodstock can be an attractive option for high net worth individuals who wish to broaden their investment portfolio, and are happy to accept a higher degree of risk and reduced liquidity. In return, there are attractive tax advantages under the Enterprise Investment Scheme and excellent investor relations programmes offered by some providers.

The bloodstock market has a degree of correlation to the racing industry, and the wider global economy, but does not tend to be very well correlated with equity markets, hence an exposure to bloodstock can help to diversify one's portfolio. Set out below is a graph, comparing the aggregate selling prices at Tattersalls in the UK against the FTSE 100 index, which helps to demonstrate this. We believe that bloodstock correlates better with property prices.



Bloodstock trading has been going on for centuries, and significant fortunes have been won and lost. Currently, the biggest players in the market are Coolmore and the Arab operations of Darley and Godolphin, both of whom have racing, stallion and breeding operations across the globe, and have billions of dollars tied up in the business. You don't have to play at that level, although trading bloodstock makes more sense at the higher end of the market, because of operational gearing – it costs much the same to feed a valuable horse, as it does the proverbial donkey. And, a portfolio of bloodstock is important. Concentration on one or two assets, or one particular subcategory, can significantly increases the risk.

In bloodstock trading, the underlying asset is generally the horse itself – no one has yet developed the mechanics for trading futures or derivatives! People trade on their own account, in partnership or in small syndicates. There are some specialist corporate entities that trade as well.

Bloodstock trading has a number of subcategories. Buying foals to sell as yearlings, or buying yearlings to sell as "breeze up" two year olds are two common areas of activity, and are known as "pinhooking".

Alternatively, buying fillies in one market to sell as broodmares, possibly in another market, has proved popular. For example, one might buy a filly privately in Europe in the autumn, campaign it in the United States in the following spring, having put the mare in foal, and then sell it that fall as a broodmare at public auction. Breeding Capital did this very successfully in 2007 – three mares acquired for £500,000 in 2006 were sold for £2.1 million twelve months later.

Buying fillies, and putting them in foal and selling the resulting foals as either foals or yearlings is another subcategory, but it takes rather longer. With a filly acquired off the track and the resulting foal sold as a yearling, an investor will not see any return for three years. In the meantime, there are nomination fees to pay, and keep fees. Success for the relations of a broodmare – called "updates" - can enhance the mare's value, and that of the progeny, significantly.

One further category is stallions, or shares therein. Top calls race horses can command fortunes as stallions, and a successful stallion is the ultimate cash cow. Galileo, possibly the most successful stallion in the world, earns its owners in excess of €20 million per annum. Stallions always used to be syndicated, but now they are often bought outright by stallion masters. However, some stallions are syndicated, and a share can give both income, through the sale of nominations – ie the right to breed – and capital gain to the shareholder.

Trading bloodstock can benefit from the tax reliefs under the Enterprise Investment Scheme. These attractive tax reliefs allow high net worth individuals to reclaim 20% of their investment, and any losses can be offset against income tax. So, with 50% tax rates, a highest rate tax payer is only risking 40% of their investment. After two years, the shares are outside the scope of inheritance tax, which appeals to those who are keen to prevent HMRC snaffling their assets. However, these reliefs are only available through investing in a qualifying company.

Investor relations can add interest over and above returns, and investing in bloodstock can be more amusing than investing in less exotic industries. Racing and bloodstock lends itself extremely well to the digital age and investors can stay in touch with what is going on in the portfolio.

So, how do you get involved in trading bloodstock? If you are very rich, you can buy yourself a stud farm, and visit Keeneland in the States or Tattersalls and Goffs closer to home, and buy a few fillies, mares, and foals. You will also need to employ people to look after the bloodstock!

Alternatively, you can buy the stock and rent space at somebody else's stud farm - this is called "boarding". Unless you are very well informed, or very foolhardy, you will need to employ a bloodstock agent, who will help you purchase and hopefully sell the bloodstock assets. Establish your proposed timeframe – are you looking to make a quick turn, or are you in for the longer term?

Or, you could invest in bloodstock trading company, that aims to deliver returns to investors over the medium term by buying and selling bloodstock. Breeding Capital (www.breedingcapital.com) is an example of such a company. Breeding Capital trades a portfolio of high end bloodstock, in Europe, Australasia and the US, and has a strong investor relations programme. The minimum investment is £10,000.

You will certainly have fun, and you may make some money, but it carries a greater risk than bank shares! Or does it…..?