AFR - End of the lifestyle company as fewer explorers deliver more drilling

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Australia's mineral and petroleum exploration sector is shrinking at an alarming rate, but survivors like Talisman Mining's Dan Madden know there's more to the story if you're prepared to drill deeper.

The most populous sector on the ASX is being reshaped by two paradoxical trends: a shrinking number of explorers are spending more money and drilling more metres of the earth's crust than they have in six years.

Talisman Mining chief Dan Madden has spent more money on exploration in consecutive years. **Trevor Collens**

The trend has ramifications for the Australian Securities Exchange, which relies on exploration companies for 30 per cent of its listing volumes, and for the nation's biggest export industry which depends on explorers to be the first stage in its food chain.

It has also sparked suggestions those notorious wasters of time and money – exploration "lifestyle companies" – are increasingly being weeded out by more prudent investors.

"We drive new discoveries. Exploration companies need to stay around because we are the backbone of the industry," says Madden, who explores for copper and gold in New South Wales.

Analysis by advisory firm BDO found the number of active explorers on the ASX declined for the seventh consecutive quarter in December.

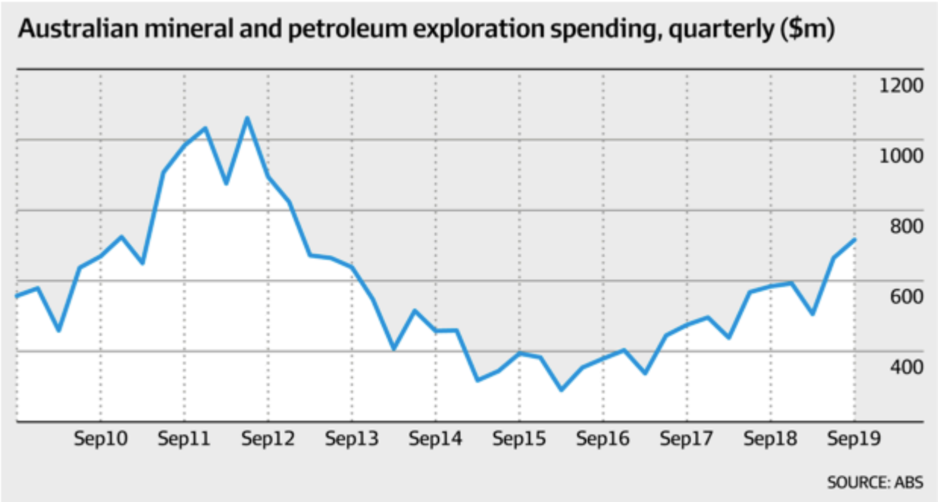
Their ranks have now shrunk by 25 per cent since 2013 according to the BDO data, which is based on the number of explorers filing compulsory "Appendix 5B" quarterly cash-flow statements.

BDO's global head of natural resources Sherif Andrawes says it's a pessimistic trend on face value, but the truth is more complicated.

Data published by the Australian Bureau of Statistics (ABS) reveals that spending on mineral and petroleum exploration has been rising for four years.

Exploration spending in the September quarter of 2019 was about 65 per cent higher than the same period of 2015.

The ABS graph depicting the total metres drilled by explorers has a similarly positive curve.



The number of metres drilled on high-risk "new deposits" has more than doubled over the past four years, and spending on such "new deposits" hit a seven-year high in September.

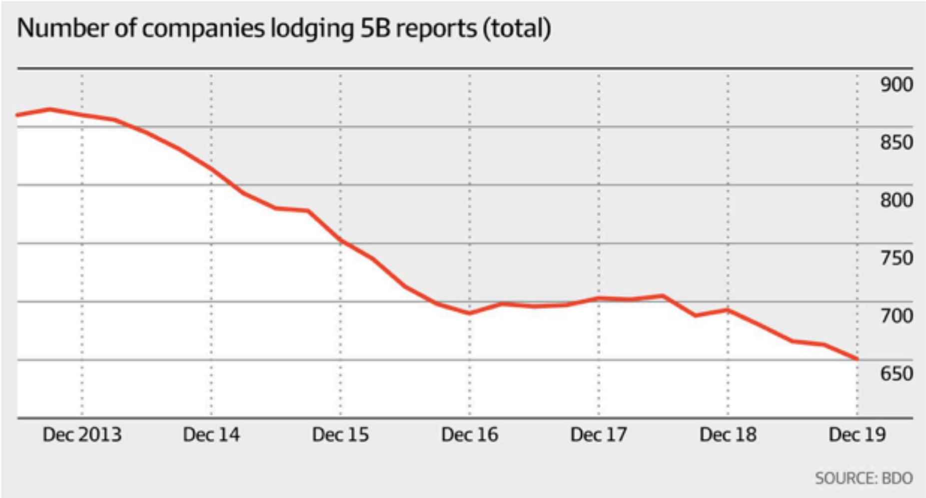
Rising spending and drilling rates have also been influenced by the fact that big miners like BHP, Rio Tinto and Newcrest – who are not counted in the number of ASX listed explorers – have returned to the exploration field with vigour in recent years.

"On face value the fact almost a third of exploration companies have gone is a bad thing, but the ones that are left behind are healthier, stronger and raising more money, which is a good thing," says Andrawes.

"That money is going into the ground; administration costs have been reducing and stabilising, so they're being more efficient.

"That might be because they are being more judicious, or because those companies that spent a big proportion of their cash on directors fees are the ones that are disappearing, what you might call lifestyle companies."

The highly technical nature of mineral exploration and the fact most drill holes will never hit the jackpot makes the sector the perfect place for lifestyle companies – those that raise money with a greater intention to pay director fees than drill holes in the outback – to flourish.



While diagnosis is subjective, it is widely accepted that such companies proliferated in junior mining ghettoes like West Perth during the peaks of the resources boom a decade ago.

A stricter watch on dormant companies by the ASX and ASIC's recent review of the conflicts of interest that abound in initial public offerings (IPOs) for explorers are also shining a light on the sector.

"You could conclude that the weeds are being weeded out," says Andrawes.

"They are trying to take action on lifestyle companies or companies with less substance, so all these moving parts are going in the same direction ... it is all resulting in the number of juniors reducing quite substantially and I can't see it changing."

Talisman is one of those boosting spending in the fashionable NSW province between Cobar and Orange, where a cluster of juniors including Alkane Resources, Sky Metals, Kincora Copper, Magmatic Resources and Emmerson Resources are gaining traction with investors.

Talisman spent about $1.5 million in fiscal 2018, then $3 million in fiscal 2019 and will spend close to $5 million this financial year.

The company had $16 million in the bank at December 31 and has managed to survive the Australian market's obsession with low-risk yield stocks by making and selling mineral discoveries, such as the Monty copper deposit which is now part of Sandfire's DeGrussa mine.

The $72.3 million Monty sale allowed Talisman to return $41 million to shareholders and give itself a $13 million cash war chest for further exploration.

"The big chequebooks are certainly gone for a general exploration project," says Talisman boss Dan Madden.

"But there is high-risk capital out there and the investors that are in the company are quite sticky. If you have shown that you can return money and you have shown you are funded and they know there is not another raising on the horizon, they are prepared to sit and wait for you to do the exploration."

Mr Madden says the "lifestyle company" slur was often unfairly thrown at explorers, and the sector was much leaner today than a decade ago.

"Over the last few years those types of companies have fallen by the wayside," he says.

"High-risk money was going in to exploration companies [during the boom], people would hear a new story and want to invest and what that allowed was executives working for more than one company, and in my view that [makes it] hard to maintain dedication to the projects.

"If you are spending meaningful money and doing systematic exploration you need to really be focused on your company and some of those companies that have fallen away are the companies that maybe didn't have that dedication."

Hedley Widdup is a geologist and fund manager with exploration specialists Lion Selection Group. While it's far from boom times, he says, the exploration sector is doing better than it was three or four years ago.

"It’s a lot harder for explorers to raise money now than it was in 2006 or 2010, when loads of IPOs got done and existing explorers could access funding for even fairly whimsical stories," he says.

"But it's also possible to raise funds for exploration, even where a target has no existing drill holes, and this was very hard or impossible only a short time ago."