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The Secretary
House of Representatives
Standing Committee on Industry and Resources
Parliament House
CANBERRA ACT 2600

2nd July 2002

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| House of Representatives Standing Committee on Industry and Resources | |
| Submission No: | 52 |
| Date Received: | 26 JULY 2002 |
| Secretary: | <i>P. W. Lee</i> |

Dear Committee,

INQUIRY INTO RESOURCES EXPLORATION IMPEDIMENTS

Please find attached the Drillex submission to the Inquiry into Resources Exploration Impediments.

Drillex greatly appreciates the opportunity to contribute to this Inquiry and in submitting a document of its recommendations it hopes to contribute towards the Federal Government's mandate to:

- Increase the levels of investment in mineral exploration in Australia, by understanding the impediments experienced in:
 - Resource endowment;
 - Small companies;
 - Access to capital;
 - Land access;
 - Approval processes;
 - Indigenous relationships; and
 - Regional development.
- Take action to achieve a level of exploration that will sustain the resources sector's crucial role in the Australian economy.

Thank you for this opportunity and Drillex looks very much forward to following your progress during this Inquiry.

Please feel free to contact the undersigned with regard to this submission.

Yours sincerely,

Dr Amanda Burt

On behalf of:
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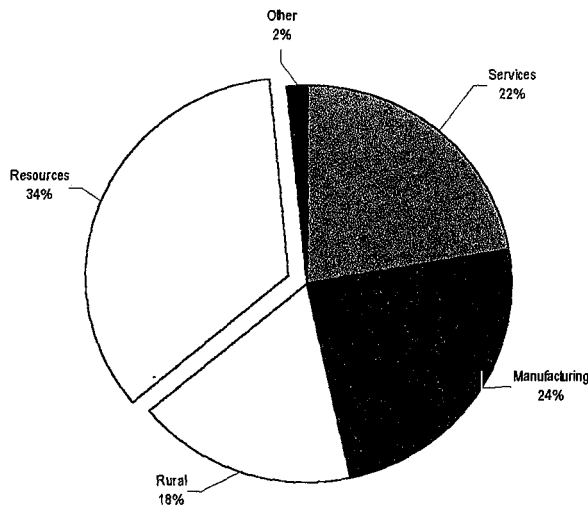
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THE DRILLEX SUBMISSION TO THE INQUIRY INTO RESOURCES EXPLORATION IMPEDIMENTS

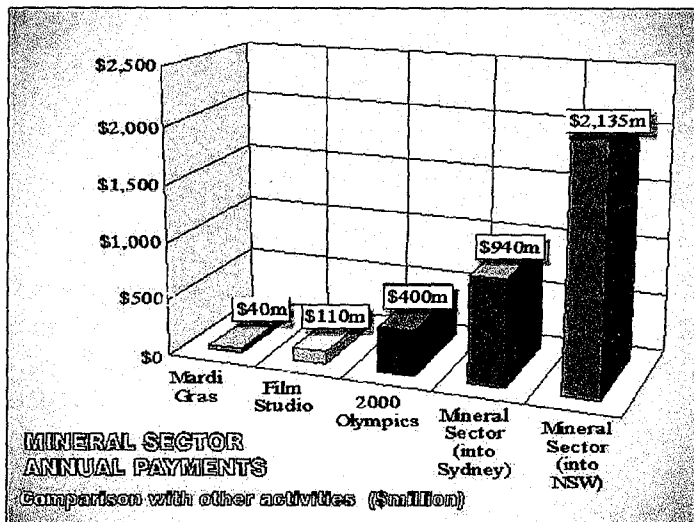
Background

Drillex recommends that the Inquiry aim to promote a profitable, sustainable and financially self reliant mineral exploration drilling sector now and into the future. It is in the national interest for the Federal (and State) Government to assist in ensuring such a long term viable mineral exploration drilling sector and help the industry out of the exceptional circumstances experienced over the past five years. Mineral exploration drilling companies, many being small family businesses such as Drillex have been financially seriously affected by this downturn.

The resources sector is by far the most important sector for Australia¹ in terms of export earnings as the following figure shows (ABS, 2001):



The following graph (Dr Bruce Hobbs, CSIRO, 2001) illustrates the generally 'unknown' and 'overwhelming' importance of the mineral sector to NSW. And henceforth to Western Australia and Australia (A\$31.6b²)!



A new major ore body such as a new Broken Hill would take Australia from 6th to 5th wealthiest nation (Dr Bruce Hobbs, CSIRO, 2001).

¹ Total Australian Exports for 2001 was A\$132.9b (ABS, 2001).

² The real value of exports of metals and other minerals in 2001 (Australian Commodities, vol. 9, no. 1, March quarter 2002).

The ability of Australia's minerals and energy sector to sustain its strong growth and expand its contribution to national economic performance in the medium and longer terms depends critically on levels of investment in minerals exploration (Australian Commodities, vol. 9, no. 1, March quarter 2002).

Drilling metres have fallen to less than 1/5th the level five years ago! As quoted in the press recently:

"Drillers say the number of metres drilled this year is down to 800,000, compared to 4.2m metres five years ago" (The Australian Financial Review, 13th June 2002).

From a Western Australian perspective, the Western Australian resources sector generates nearly A\$27b annually and directly and indirectly employs about 165,000 people. In addition, the A\$1.2b in royalties paid to the WA State government by resource companies funds much of WA's infrastructure. WA Development Minister Clive Brown stated that:

"Mining and petroleum development is the economic lifeblood of this State, accounting for more than 70 per cent of our exports, about half of private capital expenditure and around 30 per cent of Gross State Product";

"We have a challenge because this State relies on resources, yet total investment in mineral exploration has decreased by more than 40 per cent since 1997, while expenditure on new exploration areas (Greenfield's) has decreased by a much larger percentage";

"WA exploration expenditure in 2001 was only A\$409.6m compared with a peak of A\$998.3m in 1997"; and

"This fall in expenditure means we are in serious danger of not finding enough mines for the future. It is no exaggeration to suggest this threatens the long term future of the industry, which in turn underwrites our high standard of living" (Minebox 26th April 2002).

Drillex believes that the Australian exploration drilling businesses that have managed to survive longer than other's have done so because of, but not exclusively, their ability to secure contracts overseas to subsidise the poor domestic situation; hence benefiting the populations of other nations with the development of their new mines. These businesses will continue to follow the work of the leading international mining houses as they choose to explore overseas.

Despite what seems to be a short term upturn in the mineral resources sector with respect to the recent modest increase in the gold price, and hence the increase in the number of mining IPO's, entrenched long term problems remain in the Australian mineral exploration drilling industry. These include the following observations by Drillex:

- There has been a demise (or takeover due to financial circumstances) of several drilling exploration and technology businesses over the past five years;
- With the reduction in mining investment there has been a shortage of mineral exploration drilling work for the past five years. In 2000-01, capital expenditure on mining was less than half the record in 1997-98 (A\$12.4 billion in real terms) and among the lowest in the past twenty years (Australian Commodities, vol. 9, no. 1, March quarter 2002);
- Exploration drilling (along with mining) is an extremely capital intensive industry;
- Capital equipment upgrades in exploration drilling have been neglected over the past five years as any excess funds have mostly been redirected to repay creditors and financiers;
- Capital equipment in exploration drilling is desperately requiring an upgrade after five years of limited funds;
- In order to compete with increasingly powerful multinational drilling companies, capital is required for technological advancements. There is an increasing need to develop more effective, lower environmental impact, and cheaper mineral exploration systems;
- Exploration drilling is a labour intensive industry with an increased focus on health and safety regulations;

- During the past five years there has been an increase in the cost of adhering to health and safety regulations forcing margins even lower;
- Current margins for mineral exploration drilling are unsustainable longer term;
- Exploration drilling prices are currently at the level of those of about 20 years ago while overheads have continually increased;
- There is a long term downward trend in commodity prices;
- The recent IPO's may not work wholly on new (exploration) projects but partly completing older projects due to native title land access; and
- Larger mining houses may cut back on exploration programmes while waiting to purchase IPO exploration discoveries.

Drillex believes that the desperate position of the Australian exploration drilling industry calls for both short term (immediate) and long term (sustainable) assistance measures. Drillex has some short term and long term recommendations for the Federal Government Inquiry and are presented below.

Short Term Recommendations

Short term recommendations are to assist in the immediate correction of a five year lack of free capital in the exploration drilling industry due to the priority of creditor and financier repayments. For Australian family owned mineral exploration drilling businesses:

- Financial assistance by way of expense assistance and/or tax relief is required:
 - For the upgrade of rigs (structural and technological),
 - To assist in the implementation of health and safety regulations (training, time, and infrastructure), and
 - To free up capital required to repay creditors and financiers.
- The implementation of grants and/or assistance for Exceptional Circumstances (EC) relating to the five year 'drought' of the Australian mineral exploration drilling industry.

Drillex believes the mineral exploration drilling industry qualifies for EC assistance or similar. Precedents for types of assistance have been set by other industries traditionally considered important contributors to the Australian economy such as the rural (EC provisions) and building (first home builder/owner scheme) industries. For example, since the Coalition won office federally, in excess of A\$350m has been expended through Exceptional Circumstances to farmers. Drillex believes that the Government needs to recognise that there are rare and severe events which impact on the mineral exploration drilling sector and are outside the scope of drillers' normal risk management strategies. EC assistance could be designed to provide short term targeted support to assist the long term viable Australian family owned mineral exploration drilling businesses to cope with these adverse impacts. Criteria for the assessment of EC applications were agreed by State and Commonwealth Ministers in March 1999 (for farmers) and must demonstrate that:

- The event for which application was made was rare and severe;
- The event must cause a severe downturn in income (a downturn which is likely to occur in a region only four or five times in a century);
- This downturn must last for more than twelve months;
- The impact must be on a significant scale within a region or industry; and
- The event must not be predictable or part of a process of structural adjustment.

Short term assistance needs implementation to ensure the short term survival of many Australian family owned mineral exploration drilling businesses.

Long Term Recommendations

Long term recommendations are to assist in ensuring an ongoing exploration drilling industry by ensuring sustainable financial returns in the mining sector, and hence in the exploration drilling sector by addressing the current taxation regimes and the current lack of incentives for high risk capital investment. Drillex believes the mining and exploration drilling sectors would benefit from:

- Strategies to increase investment in the mineral resources sector and hence the services of the exploration drilling sector by providing:
 - Capital expenditure incentives. Perhaps the implementation of a "flow-through" share scheme has potential to help arrest the fall in exploration expenditure, as apparently it has done with great success in Canada where tax benefits of exploration costs are transferred from the company directly to the shareholders (The Australian Financial Review, 8th June 2002);
 - Research and development incentives;
 - Health and safety incentives; and
 - Land access facilitation.
- Implementation of hedging and insurance facilities for exploration drilling businesses to insure contract prices, contract lengths and weather conditions using:
 - Derivative products such as forward contracts and options; and
 - Tailored insurance.

Long term strategies need implementing to ensure the long term survival of the Australian mineral resources sector, and therefore the Australian economy.

In Summary

In summary Drillex believes that the desperate position of the Australian mineral resources industry and hence the mineral exploration drilling industry as outlined in *Background Information* calls for both short term (immediate) and long term (sustainable) measures as outlined in *Short Term Recommendations* and *Long Term Recommendations*. It is in the National (and State) interest for the Federal (and Western Australian) Government and to assist in ensuring a long term viable mineral resources sector and hence mineral exploration drilling sector, and to help the drilling industry out of the exceptional circumstances it has experienced over the past five years.