INDEPENDENT SUBMISSION

TO THE

STANDING COMMITTEE

ON INDUSTRY & RESOURCES

COMMONWEALTH GOVERNMENT OF AUSTRALIA

"INQUIRY INTO RESOURCES EXPLORATION IMPEDIMENTS"

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Prepared by:

Andrew Crooks

Unit 98, 8 Ashton Street,

Rockdale NSW 2216

Tel: 61-2-9553 4948

Email: asheldon@rivernet.com.au

Prepared for:

Standing Committee on Industry & Resources

Commonwealth Government of Australia

Attn: The Secretary

Tel: 61-2-6277 4594, fax: 61-2-6277 4516

Email: ir.reps@aph.com.au

Impediments to Resources Exploration

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TERMS OF REFERENCE - CALL FOR SUBMISSIONS

The House of Representatives Standing Committee on Industry & Resources, chaired by the Hon Geoff Prosser MP, invites you to make a submission on:

Any impediments to increasing investment in mineral & petroleum exploration in Australia, including:

- An assessment of Australia's resource endowment and the rates at which it is being drawn down;
- The structure of the industry and the role of small companies in resource exploration in Australia;
- Impediments to accessing capital, particularly by small companies;
- Access to land including Native Title and Cultural Heritage issues;
- Environmental and other approval processes, including across jurisdictions;
- Public provision of geoscientific data
- Relationships with indigenous communities; and
- Contributions to regional development

BACKGROUND OF THE AUTHOR

The author, Andrew Crooks, is a 33 year-old mining analyst with 12 years experience in the mining industry. I have a Bachelor of Science with majors in geology & geophysics, and minor credits in finance, economics and accounting. Post-graduate studies included a Graduate Diploma in Mining Engineering & Mineral Processing. This included practical electives covering mining project finance & assessment, geostatistics & mine planning and mine economics.

Early practical mining experience was gained with exploration and mining companies in New South Wales and Queensland, including Lachlan Resources, New England Antimony Mines, CRA Exploration (now Rio Tinto) and Cyprus Minerals. This experience exposed me to a number of metals mines and the mining workforce at a grassroots level.

Mid-career experience was gained with Barlow Jonker, a reputable international coal mine engineering & market consultant with a large international client base. As an coal analyst, I principally prepared reports related to coal projects and coal supply and demand, offering exposure to related downstream industries (such as power, steel and cement) and transport. Numerous site and research trips were required in Australia and overseas.

Recent career experience included 1 year with W.H.I. Securities Pty Ltd, a boutique finance company focusing on the provision of finance to small mining & exploration companies in Australia or overseas. This experience gave me considerable contact with mining company executives (operators), retail stockbrokers (sponsors) and fund managers.

Small resource companies have been a personal passion since I commenced trading at the age of 11 year. Childhood interest was sparked by exposure to the Australian Financial Review (1980-2002) in the family home. The AFR along with family stockbroking contacts offered exposure to the tales of mining, finance and entrepreneurs like Alan Bond. Since the 1990s the profile of mining stocks in the community has been overshadowed by IT stocks, as well as generally depressed commodity prices.

At university I came to appreciate the importance of philosophy and psychology in understanding human behaviour and contemporary management structures and politics. Twelve years of personal study in the humanities will be evident throughout this submission, both in terms of clarity of thought and integrity. During my career, I took the opportunity to live and work in Japan for a year, the primary reason to gain a 'cultural experience' as well as providing an external prospective of the Australian socio-political edifice. I have a passion for information collecting and analysing which recognises few limits.

THE FUTURE OF THE AUTHOR

Dismayed by the lack of integrity and wisdom displayed in political and management outcomes, I would like to invite readers of this submission who see merit in the values expressed to contact me. I am interested in establishing a think tank in future, so I will be seeking support from the broader community. The integrity and wisdom expressed in this report is just the tip of a very large iceberg. Political aspirations and humility aside, I would hope this submission is more than 'accepted', but read, understood and critically assessed as well. In the spirit of accountability and understanding, I would hope that this is a process which involves ongoing dialogue, as I am sure I have a lot to offer the public debate on this and other issues. Personally I prefer debating than submissions as a means of expressing

ideas.

Impediments to Resources Exploration

1. Abstract

Readers of this submission might make disparaging remarks about the breadth of its determinations. This is not to suggest I have swayed from the ‘terms of reference’, but rather that the constraints upon the resource industry raise issues across a multitude of sectors, which requires an integrated strategy. I have addressed those issues pertinent only to my experience in the industry. There is always a broader context, and if it is not addressed in people’s minds (values), no resolution will be adopted in practice. Change requires integrity and conviction. People who see this as merely a ‘management’ or ‘commercial’ or ‘regulatory’ issue are prejudiced by the narrow scope of their inquiry, perhaps the fragmented nature of their values and their lack of strategic, long-term objectives or goals. More critically, perhaps they are not able to see the long-term trends in the mining industry.

Summarise what I have said elsewhere

2. Introduction

This submission will primarily concern itself with the impediments to mineral and energy investment arising from its relationship to the finance industry, regulation and resource-related legislation.

Outlined below are reasons why I think the terms of reference were ill-conceived, such that the parliament may choose to re-define them should it call for further submissions.

There is a tendency for governments to look at the absolute allocation of resources rather than the efficient application of these resources. The reasons are philosophical. Business is concerned with the maximising the return on capital, whilst government is concerned with achieving community standards, which is measured in terms of equity rather than profitability. This is a moral flaw. The influence of 2000 years of Christianity is that people are predisposed to place intentions above outcomes. An altruistic government which gives $100 million to a ‘noble’ program is morally superior to a less generous outcomes-orientated program which focuses on the effectiveness of that expenditure (ie. purpose as the standard of value). Some might argue that welfare can be effective, but this avoids the question of self-reliance and how the psycho-epistemology which sustains it. For this reason, the government should look at how it might facilitate improvements in the effectiveness of capital spending in the resource industry, rather than merely increasing expenditure at a time when there is a surplus of many commodities.

The simple answer to how the government can “increase [the effectiveness of] investment in mineral & petroleum exploration in Australia” is **simply stated** - by developing and implementing an integrated policy which rises above vested interests in the community. To that end we would be better served by statesmen rather than politicians. The difference being that a politician’s values are defined by the people and institutions which support his aspirations (ie. status). A statesmen is primarily concerned with truth, integrity and justice, and rises above perceptions to define values and management systems to regulate society. By focusing on the goal unrecognised benefits will accrue to the whole country which will sweep aside the prior concerns of narrowly-defined vested interests.

The worth of public submissions might also be questioned, given that the committee is under no obligation to address criticisms from the community, and in that sense is just as unaccountable as the

parliament. Politicians have no capital invested in their decisions, and the public have long since lost interest, because they have no ownership over the process. In recent years, even parliamentary committees are being stifled by executive government. There is a perception that parliamentary committees are being compromised by lack of resources as politicians inquire into less political sensitive issues to avoid more pressing community concerns.

Secondly, I will briefly outline of the principal variables impeding [a better allocation of investment for] resource exploration in Australia.

3. Mining Industry & Capital Market Structure

Capital markets play a crucial role in the development of the Australian resources industry. Market operating procedures have an important bearing on investment returns and international perceptions of our capital markets, whether we are concerned with primary capital markets (financiers) or secondary markets (stock exchanges).

MINERAL INDUSTRY PARTICIPANTS

The mining industry basically comprises three types of mining and exploration companies.

a. **Global consolidators:** These companies are interested in acquiring or developing world-class resources which have the potential for long-life, low-cost production. The ability to draw strategic marketing advantages from capturing significant market share, as well as the logistical benefits of lower delivered cost, product blending are derived from having a global portfolio of assets. For investors, these companies command a higher price-earnings ratio (ie. market capitalisation) because of their perceived longer risk profile (ie. diversified sovereign & technical risks) resulting in a lower cost of capital. The reoccurring earnings of these companies mean they are essentially self-funding, and valued at a premium by fund managers who require considerable liquidity to take an equity position and to liquidate it. These companies are typically capitalised between $A0.5-50 billion, higher for the oil companies which have vertically integrated into downstream industries.

b. **2nd tier producers** are often acquired by the global mining 'consolidators', or will themselves amalgamate with similar-sized companies to improve their market rating or profile. In some cases, these companies might be mature metal producers, but because their operations are high-cost (sometimes complex mining or metallurgy) operations, they may be essentially cyclical market players. In some cases, they are involved in niche business areas like rare earths where they can have a significant market share. These companies are typically capitalised between $50-500 million.

c. **Project sponsors:** These represent those mining entrepreneurs who assemble a portfolio of exploration or resource assets and list them on the market. These companies tend to rely on stockbrokers to fund development because of difficulty sustaining earnings - if they ever arise. They are an attractive client base for brokers because they offer 'unique' high profit opportunities for them and their clients, plus corporate finance fees. They are volatile stocks because they tend to lack support in the market by institutions. These companies are typically capitalised between $2-50 million.

FINANCIERS

Capital markets are managed by commercial banks, investment banks, stockbrokers and fund managers

(life insurance, mutual & superannuation funds). These corporations use a variety of risk management strategies and financial instruments to invest in the resources sector. A number of them involve a hedging strategy which runs contrary to the best interests of small investors. Marginal or sub-economic projects can be financed and developed if you ensure protect revenues by locking in commodity prices and exchange rates, however the interests of shareholders are not considered. Investors take positions in companies to take advantage of commodity prices, yet executives might be more interested in preserving his job and investment banks is selling their financial instruments. We have seen a number of Australian companies hit by these 'risk management strategies' using derivative products. Eg. Pasminco, Western Metals, MIM and Sons of Gwalia to varying degrees. Investors are being exposed to these risks which are perhaps better managed by institutions with comprehensive research & treasury departments, rather than being 'sold' to inexperienced small company managers. The government might consider ways to better manage the utilisation of these tools because considerable wealth has been lost because of these products. On a bigger scale, look at the damage done to NSW finances when the public-owned power utilities entered into long-term power contracts at excessively high fixed prices. These enterprises had little real-world commercial experience in a newly deregulated market, yet they were sold on the benefits of derivatives.

a. Fund Management

The great majority of equity capital comes from fund managers (including offshore managers) and retail investors (whether high net-worth, novice or foreign investors). The unfortunate aspect of recent super reforms is that the 'regulation-stimulated' growth in assets under management has not prompted fund managers to seek more profitable investments (namely in the small company sector). They have instead pursued a very conservative index-linked strategy where they seek only to out-perform ASX indices. For this reason, they tend to avoid ASX stocks which are not represented in an index, despite the under-rating of companies in this market segment. The management of small resource companies (between $30-200 million) are only too pleased to place stock with institutions, and the low price-earnings ratios (commonly 2-4 compared to 15-30 for the blue-chip companies) make them worth pursuing.

The reluctance of fund managers to invest in the small company (not just resources) market segment is due to:

- **Lack of liquidity:** The lack of trading and stock on issue makes it difficult can make it difficult for institutions to enter and exit these stocks.
- **Market representation:** These companies are too small to cover and don't over adequate sector representation.
- **Lack of earnings:** Small resource companies tend to require funding to get projects off the ground.

All of these issues are valid concerns, yet they are easily resolved by a number of fund managers jointly establishing one or more independently-managed small resource funds. Small companies most basic need is for project finance. Project finance should only be forthcoming when commodity market analysis suggests the project should proceed. By taking advantage of counter-cyclical financing, fund managers would be able to realise 300-500% returns over a period of 3-4 years. Exceptional profits are possible, eg. 3200% return on Aquarius Platinum options over 3 years (25c to $8.25) or 2000% on Minotaur Resources in a matter of months. The risks are not excessive for trained analysts.

Having addressed the points above, the resources sector has some very attractive features:

- ❑ **Exploration upside** - Some mining projects demonstrate considerable potential to increase reserves and therefore mine life. Strategic opportunities often exist to develop other resources nearby.
- ❑ **Global market** - Most commodities have a global market, where their is always a market to clear product
- ❑ **Natural hedge** offered by weak $A (with commodities sold in $US)

An independent resource fund could have the resources to monitor commodity market trends as well as the fortunes of the individual ASX stocks. They would be a preferential source of capital for the industry because of their willingness to take equity, and they would be in a position to participate in Initial Public Offerings (IPOs). Currently fund managers do not have the resources to look at these sectors and the quality of most stockbroker analysis is inadequate because their margins are too thin. Often analysts working for brokers will rely totally on sponsor for information rather than purchasing 'third party' commodity market research. A few pure resource funds already exist but they are supported by retail shareholders rather than fund managers.

A resource fund as such could be an ASX-listed vehicle, of sufficient size and liquidity that fund managers could invest in the stock. They include Challenger Gold International and Lion Selection Group. Lion Selection tends to focus on foreign-based resource projects. A fund of significant size would be in a position to undertake strategic analysis, which might well add value to a number of projects. Eg. Perhaps a centralised gold processing plant serving a number of gold mines, or a gas pipeline serving a number of projects. In these cases, the fund would be encroaching on areas served by investment banks like Macquarie Bank, which is a leader in corporate advisory work. Its efforts could very well underpin the creation of a coal seam gas industry on the east coast of Australia, with enormous implications for rural development and cheap energy supplies.

The Australian government has adopted a number of legislative reforms leading to considerable change in the resource industry. These include:

1. Compulsory superannuation contributions (increasing 1% to 9% in July 2002) - which has boosted the size of the local capital market.
2. Tax reform
3. Third party access arrangements for infrastructure (Competition policy - rail, gas & electricity)

The government should do more to improve the attractiveness of Australia as a investment destination. Increased capital inflows would strength the Australia dollar and prompt fund managers to invest in Australia rather than overseas. Clearly this requires a government committed to further tax reform and building secondary industries in Australia. Despite considerable rhetoric about opportunities in resources processing, there is no pool of capital servicing the resources sector because of disinterest by fund managers in small companies and lack of market appreciation (by retail markets). Projects which come to mind include:

a. Hitec Manganese Dioxide plant in Port Hedland, WA

b. A ferro-alloy (chrome & nickel ferro-alloys) in Port Hedland, WA

c. SAMAG magnesium metal & alloy plant in Port Pirie, Sth Australia

d. AuIron's integrated coal-power-iron ore-pig iron production facility in Sth Australia

e. Batchelor magnesium plant in the Northern Territory

There are other project opportunities as well:

f. Downstream processing opportunities for niobium & zirconia ores at Dubbo, NSW

g. Ferro-vanadium plant in WA

Traditionally, the sponsors of these projects have been beholden to consumers to develop these projects because of the lack of manufacturing of complex manufactured products in Australia. Given the high operating costs in developed countries, and the sovereign risks in mineral producing countries (eg. South Africa, Russia, etc), Australia should be attracting more downstream investment opportunities in a number of areas. The question is could we be attracting more investment in material sciences, most of which is currently undertaken in consumer markets.

Australia is already the 7th largest pension fund market in the world, however previous privatisations by the government have soaked up a large portion of this capital. Such a rapid increase in the amount of funds under management has surely placed pressures upon fund managers investing in a whole range of industries. Funds managers need the support of industry sector analysts. With the workforce lacking the combined technical (including mining) and financial skills to assess specialised industries, the pressure is on the fund managers to invest in the large diversified companies, which forces them offshore. Unfortunately, fund managers have been slow to capitalise on the potential of Australian small (resource) companies by failing to employ specialised analysts to look at the smaller companies offering higher returns. There are many small profitable resource companies which were trading at PE ratios of 3-5 in 2001 (eg. Consolidated Minerals, Selwyn Mines, Mincor). These companies have risen 200-300% with fund managers being relatively late entrants on the share register because they are considered too small. Instead they have become complacent, relying on the growth of the market (funds under management growth) to increase fee revenue.

It is lunacy that fund managers will not invest in these companies until they register among the Top 300 resource stocks. By that stage they have missed most of the capital growth potential. Investing in companies at an early stage in fact reduces much of the commodity risk which arises once these projects start producing. As an investor in these types of companies, I know that if the market goes soar, I can always take a long term prospective and benefit handsomely in the next bull market. Of course, an analyst by assessing the commodity cycles can do better than that. Lion Selection Trust, an ASX-listed resource fund, invests in small exploration companies demonstrating large resource potential. Companies like Lion Selection are run by commercially-astute geologists and mining engineers, and I suggest there is a greater need for such companies, and perhaps its appropriate that fund managers be prompted to invest modest a modest share of their funds (2 rising to 5%) in such companies across a range of industries. There is a tendency also for fund managers not to exert any influence over the companies they invest in. Often they do not even vote their stock.

There is no regulatory requirement for fund managers to invest locally, yet Australian markets have out-performed foreign markets in recent years. Fund managers have placed a considerable share of their funds in under-performing offshore markets. They have lost on the recent correction in the S&P as well

as the strength of the $A. Australian funds were under-weighted in resource companies during the recent spike in gold prices. Fund managers were slow to invest in gold producers. Bendigo Goldfields, which controls a 12 million ounce resource in the Bendigo area of Victoria, took a $50 million placement from South African miner (Harmony Gold) to get long term (4 years) capital - a considerable discount to the real worth of the project. No technology transfer was required. There is actually an opportunity for a hands-on fund manager to bundle and fund small mining companies with world class projects and hold them until those assets are producing, then float them onto the market. The alternative is to finance the project for a significant passive equity (like Lion Selection Trust).

In recent years we have seen an increase in takeover activity in the Australian resource sector (particularly gold) which has corresponded to weakness in commodity prices and the Australian dollar, as well as a global need to rationalise excess production capacity. There is the perception that Australian assets are too cheap because of the low $A. If that were the case, acquisitions would drive up the $A. In fact, in the last 13 years Australian investment overseas has grown by 13%pa to $A176 billion, compared to 9.2% for foreign companies investing in Australia. Foreign-owned assets remain a fraction of total Australian assets, and any change in that equation would lead to a rapid strengthening in the $A. Foreign transfers of assets should be viewed as a healthy trend towards an increasingly global economy. In the process, Australian investors are selling out of multi-nationals companies trading at **price-earnings** (PE) ratios of 20-30 to buy smaller companies trading at 3-15. Vested interests in the community tend to consider 'globalisation' a cost, but in fact it creates an opportunity for retrenched executives to create new enterprises from the proceeds of the asset sale, as well as for investors to buy back assets with growth potential in at lower PE ratios, whilst we continue to benefit from taxation receipts and wages paid by the foreign companies operating mines in Australia. Where foreign corporate interests are judged to be contrary to Australia's interests, as was the case with the thwarted takeover of Woodside by Shell, the government need only ensure reciprocal bilateral access and guidelines when Australian companies acquire foreign companies. This places Australia at a disadvantage in bigger markets and advantage in smaller markets…so these considerations should define foreign policy.

b. Stockbroking industry

The adoption of online share trading and the licensing of Australian Stock Exchange (ASX) data to non-ASX members, the stockbroking industry has changed considerably. The ability of online trading systems to scale-up to meet demand at minimal cost has seen market leaders like Comsec undercut traditional brokers with low margin fees to grab a significant market share. As a consequence, there are too many stockbrokers in the Australian marketplace, and few are making money. Those that have not rationalised or merged with other brokers have been forced to enter into other services such as boutique corporate finance & advisory services or wealth management, which offer higher margins. Small brokers will continue to depend on pushing transactions by 'novice or technology-impaired' investors, be they inexperienced or senior citizens. There is significant scope for these customers to be mistreated by client advisers with very short time horizons. There is nothing new about brokers 'churning' clients investments like their is no tomorrow. Having worked in the broking community, its amazing the contempt client advisers can show for their clients. The biggest issues are:

a) Client advisors have no analytical skills (knowledge of the stock's fundamentals), and being unable to cover the whole market they are poorly positioned to attend to their clients needs

b) Clients are pushed into making a decision by client advisers who are trying to free up the telephone

line. The process does not allow much time for discussion. Tight margins mean these brokers have little ability to offer meaningful research

c) Client advisers have a conflict of interest - they profit from clients buying & selling, rather from the provision of good advice. Volatile (risky) stocks present more opportunities to make commissions. Most will not trade 'low risk' retirement savings on speculative stocks, however there is a solid basis for dabbling clients money on 'spec stocks'. They might place the client in some good growth stocks, but they will be seeking to 'churn' their risk capital.

d) Initial public offerings (IPOs) and placements to clients are another means by which client advisers raise earn commissions. Brokers is these circumstances often recommend take up of an issue because the company raising the funds is offering a generous fee to brokers. Such issues are an easy sell if they are trading up to the 20% below their average trading price for the last 5 days, or if there is a free attached option. Client advisers supporting a new capital raising will sometimes profess to having 'inside information'. Eg. "The company is going to make an announcement soon". The worse the market conditions, the more company directors are prepared to give analysts private briefings.

It is through these practices that some very mediocre companies are able to obtain listing, and obtain support for further capital raisings. Exploration companies have even more dubious claims. When you look at the quality of certain tenements packaged together, it soon becomes apparent that they have no intention of exploring them, but rather will use shareholders funds in the listed vehicle to pursue other opportunities. A big 'gold strike' creates a dubious foundation for some companies with tenements in the vicinity to list on the ASX, when in fact there is very little likelihood of a repetition. Consultant geologists will look favourably upon any project which offers them work because there is always the recognition (or rationalisation) that its a risky investment….but really they just want repeat business. In fact the only person you can trust is a person who puts his own money in a company. Escrow conditions placed upon shares & options do prevent directors from liquidating their shareholding in the medium term, however directors will value being paid to find new opportunities. The challenge is to ensure the veracity of the projects in which people have been lead to trust. That is no easy task.

Mining entrepreneurs are often just looking for a vehicle to 'milk the market'. Favorable commodity markets provide such opportunities. An early listing is preferred so that your stock holdings are released from escrow before the commodity cycle busts. The 1990s highlighted the 'opportunism' with some 80 exploration companies moving into hi-tech areas. Most of these investments had little commercial merit, and in the wake of the tech-wreck, some of these executives have returned their companies to mining - just before the gold market strengthened. The rationale was to pursue value where the market saw it. But where was the accountability.

The linking of advisory and financing activities creates an enormous conflict of interest that needs to be addressed by governments. There is a tendency for companies whom receive a negative stock recommendation to limit disclosure to those companies. Companies will often travel inter-state promoting their activities. Those that listen often get a better informed view of the stock than the market. This includes an insight into the company. Ie. Insider trading. When you consider that these directors are dismayed by the lack of interest in their company, you might appreciate their desperation. Sponsors pursuing projects with the market does not take the time to understand are particularly frustrated.

The intention of insider trading rules is to prevent a financially advantageous dissemination of information to privileged people in the community. The reality is that the practice is rife and very difficult to police. Anyone watching a Reuters screen enjoys a privileged position compared to those that have to work for a living, and are focused elsewhere. More to say here.

4. Market Mechanisms

The demand and pricing of commodities is cyclical in nature, and ultimately is determined by global economic activity and commodity stock levels. Commodity prices generally move together, and tend to reflect the changing perceptions of procurement managers who 'sheepishly' (due to lack of market disclosure) decide to purchase raw materials fearing they might have to pay more next month as global demand recovers. In these circumstances, commodity prices tend to overshoot, and when demand subsides, they tend to get dumped. There is no question that the price signals (movements) influence the behaviour of decision makers, whether they are investors, buyers or sellers. The problem is markets are only as effective as the participants - and their personal efficacy depends on access to accurate market intelligence and transparent transactions.

Consider the scope for the executives of a large South African mining company to sell some very attractive, advanced exploration projects to a small Australian listed company. Australia has no existing platinum mines, is prone to under-value such projects. The executives of the South African company face constraints getting capital out of the country, but by transferring quality corporate assets they are able to invest what little money they can withdraw in the Australian listed company to which they sold the project. The smaller Australian company offers them much greater leverage when the Australian market recognises the value of the project. Because the transfer of assets is cross-jurisdictional, regulators are none the wiser. The asset sale in South Africa does not require shareholder approval because the projects were a small share of the company's market capitalisation. In fact they were required by the South African government to release the assets to increase access to the prized 'Bushveld Complex'. Such a favourable transaction raises the possibility of a dubious transaction.

I question whether how well the market is informed, and the rationale for market outcomes. Consider the following:

1. **The efficacy of price signals:** Rallies in commodity prices generally result in capital raisings to support greater exploration and development. The lead time for exploration is 3-10 years, or 1-3 years for a dormant project (proven resource) and will ultimately lead to an over-supply. Whilst these price signals ultimately corrected the market shortage, the additional supply is not timely, and nor were investors rewarded for their finance. Why? Poor equity market information and conflicts of interest. The lack of integrity and subjectivity of market analysis only increases risk (volatility) and creates cynicism among investors who would otherwise support good business concepts.

2. **Disclosure:** Contractual terms for commodities are generally not disclosed or they are masked by 3rd parties. Often it is not possible to gauge whether product has been delivered to consumers, or whether traders are attempting to speculate. Such speculation can harm the confidence of end-users, eg. cobalt.

3. **Poor information collection:** Developing countries are particularly inept at gathering and maintaining statistics which assist market analysts understand the flow of goods. Corporations in these countries are similar prone to under-state raw material purchases, just as they under-state

revenues, to minimise their taxable income. Raw materials provide an indication of your consumption, so you have to understate those as well.

In the long-term commodity prices are declining in real terms on average by 2% per annum, and for this reason, Australia is required to boost its export volumes in order to maintain its trade balance. Fortuitously, a lower exchange rate encourages more development of Australian resources because commodities are sold in $US. In as much as our competitors are also primarily commodity producers, and are similarly reducing their costs, to a large degree, we compete with these countries on exchange rate as well as the $US price. For most commodities, miners participate in a perfect market with a multitude of buyers and sellers. Transport costs, grades (or product quality) and access to infrastructure are the principal gauges of low cost operations.

The major companies are in a much better position to forecast metal prices because of their large resource base and direct impact on the market as a result of recent consolidation by the likes of BHP Billiton, Rio Tinto, Newmont and Anglogold. For the minor companies, we are seeking stockbrokers using unsustainable prices to support a project which will not achieve production for 1-3 years. In as much as high prices stimulates more exploration, this time lag is likely to see new capacity commissioned during periods of low prices. The banks which financed the project will be OK because they have ensured the company has hedged sufficient revenues and sold under long term contracts sufficient capacity to ensure their loans are repaid. However, there is no one protecting the interests of small investors, who are essentially misinformed by brokers with a vested interest in pleasing companies to obtain commissions or obtain information.

The structure of the mining industry described above means that the 'global consolidators' fund an ongoing exploration program (if they don't rely solely on acquisition) from their reliable cashflows, whilst the small explorers and emerging producers (or 'project sponsors') are funded by equity markets. Equity markets are cyclical, so companies not producing an income are oversold during periods of depressed commodity prices. Raising equity during these periods would excessively dilute existing shareholders, and there is every likelihood that such a capital raising would fail. For this reason, some of these companies will trade at less than cash backing, and small producers can trade at exceptionally low PE ratios of 2-4, despite offering excellent growth prospects.

The problem is that 'project sponsors' are able to get a project funded on the basis of high commodity prices, despite the fact that most of those projects will be commissioned after prices have fallen. Derivatives can ensure that these projects are sustained, but often not to the advantage of shareholders. There is a pool of market knowledge and analysis which fails to permeate the corporate finance ambitions of the brokers, who will support a prospectus with little or no market analysis which places the project in a global context. These companies need to be able to demonstrate a global commodity supply (production) cost curve demonstrating that they are within the lowest quartile of suppliers. Such a position is likely to ensure they are profitable in any market. Less scarce commodities like coal and magnesium have a flatter supply curve, so prospective suppliers need to ensure they have contracted for a high proportion of their production capacity to remain profitable. A prospectus will highlight all the elements of risk subsumed by the investment, but little attempt is made to quantify the risks by independent parties.

Sadly stockbrokers are ill equipped to produce research which can adequately forecast trends in commodity prices. The canny investor will buy speculative resource stocks when commodity prices are at their lowest, and these points are roughly predictable by looking at what price roughly ½ the volume

of global production is unprofitable. At these prices, high cost producers will be rationalised and prices can be expected to recover if the market is supported by higher demand. There is science to predicting the 'optimum' buy point. Similarly, you would expect to see less support for new mining projects when prices are peaking. The reality is the opposite.

The best means of improving investor returns and hence market recognition is to adopt new legislation to separate advisory and retail broking roles, and place shareholders before banks in the claims upon the capital of a defaulting enterprise. The later suggestion is difficult because it requires global reform. Consider that banks are better positioned to judge risk than shareholders, as there role requires an understanding of commodity prices to forecast economic cycles, yet they are placed before shareholders. It could be argued that shareholders are putting forward 'risk capital', but why when the market offers them no capacity to judge its merit. There needs to be a change in attitudes towards the small investor, as investment is an important skill for the 'novice' to learnt, yet most will turn away because of the perceived risk. This volatility leads to a transfer of wealth from the less informed to the more informed, and it doesn't result in better market outcomes because new projects are commissioned at times of low prices. Would it not make more sense if banks worked with market consultants to determine which projects and when they should be commissioned. Australia has a number of commodity research houses like ABARE, AME Mineral Economics, Macquarie Bank and Barlow Jonker. They are competing with larger research houses (publications) in the UK and USA. None of these businesses attempts to make forecasts. They would argue that there is insufficient disclosure to do so, and that consumer sentiment (demand) and project start-ups are difficult to gauge. The Australian government could play a role in encouraging developing countries to improve their information reporting.

In the 1990s, I recall seeing a long term financial analysis for the major mining companies, like Rio Tinto, BHP and MIM. Shareholders made considerable money in the short-term by trading commodity booms, but over a 10 year interval, BHP and RIO minor minor returns whilst MIM performed badly with substantial losses in real terms. Such positions arise because at that time few places understood the market realities because no one had a significant market position like BHP-Billiton and RIO do today after considerable consolidation.

The question is could the global mining patriarchy conceive of an orderly market economy where project sponsors jockey for the status of 'emerging producer' based on lowest assessed costs of production. That assessment would have to be based on a contractual agreement with project engineers to complete the project. We have such order in the electricity market…why not minerals. Why are free markets equated with hedonistic or chaotic markets….rather than reasoned and thoughtful. This is not to advocate collectivist planning for a 'higher good' but rather a meritocracy based on quality and substance.

Investment in resources is very much driven by the multi-national mining companies which stimulate the market by engaging in take overs, increasing exploration or stimulating commodity price increases by cutting back on production. Consumers demands are better understood by the market because they are reflect historic trends in consumer sentiment. The convergence of supply and demand establishes the markets. Commodity cycles tend to maintain a degree of alignment with global economic cycles. In the last decade, commodity cycles have departed from this trend due to changes in comparative metal demand (due to changes in metal ratios in alloys), as well as comparative metal supply (as metal ratios change as new mines are developed). Other metal cycles are driven by new applications. Eg. Consider the substitution of magnesium for aluminium in car designs, the growth of tantalum demand in

capacitors, the unusual strength of lead demand as its % in copper-lead-zinc orebodies declines.

Commodity cycles are poorly understood because of lack of disclosure of mine production, inventories, exports, imports, mine costs, as well as output. The issues are similar on the demand side, and the impact is particularly strong in commodities heavily impacted by markets such as China and Russia, which have very poor records on information collection and disclosure. Often in these developing countries, statistics are manipulated to reduce taxes. Information is paramount to the health of the commodities sector. There is a multitude of metal projects around the world at various stages of development. Sadly metal price surges tend to ensure that all these projects are funded. So long as the market is properly informed and these projects are in the lower quartile of production costs, they should be profitable over the life of mine. The question is: Are governments doing enough to ensure old and unprofitable mines are closed at the appropriate time? The problem only arises where mines are subsidised by governments, by other mining activities (in the case of diversified mining companies) or where single project mines are running down cash reserves. The non-responsiveness of the market to these factors can only be explained by lack of information disclosure or inadequate analysis. Market consulting is a fragmented business, and clearly government intervention and corporate non-disclosure are clearly the greatest impediments. There is however scope for a coordinated improvement in disclosure by both producers and consumers.

Exploration should be funded when market analysis suggests that a commodity shortage will arise in 7 years, as this is the average period it takes to develop new projects. It is worrisome that brokers are supporting platinum floats at the peak of the boom. If these projects ever find anything, they will have spend $2m demonstrating the occurrence of platinum, but unless the grades are exceptional, it will be at least another 5 years before the project is financed. It is the opportunist at the other end of the commodity cycle who makes the money. I would suggest then, that prospectuses should require detailed commodity studies. Clearly this requires greater disclosure by companies who have dubious reasons for preventing take-overs.

It has be appreciated that speculators benefit from lack of disclosure, as do the mineral explorers, however these price surges have to be sustained, and they rarely are. Commodity price surges result in buoyant prices for about 12-18 months, sparking a global search for the commodity, and culminating in depressed prices for 10 years as those projects slowly find their way onto the market. In the 1990s, this occurred in platinum and tantalum. Majors want stability and certainty, so they are the consolidators, however the mis-information is at the other end of the market, and its largely supported by brokers. Investors are enamoured to high returns - yet the prospects of an exploration project becoming a profitable mine are really not relevant to the investor. The seed capital investor in an exploration company is the least likely to make a profit. Project sponsors have only one interest - to develop the project, as the salary earnt is their bread and butter. Brokers are in the habit of rolling their clients into such dubious investments because they get an attractive commission from the company. I'm aware of cases where analysts have written negative reports on a stock, but senior management have supported the stock because of the high commission paid. In other instances, management might place pressure upon the analyst to change a recommendation. This practice is particularly common today because online brokers are squeezing traditional brokers profit margins. Many are not making profits. Some have exited the industry. Most have established boutique corporate finance arms, which I'd suggest creates a conflict of interest with their broking arms.

5. Business Ethics

The value of any market is only constrained by the ideas and ethic of those that participate in it. There is no shortage of ideas and capital in Australia to sustain a vibrant economy. The constraints arise from:

a. A tragic or passive sense of life which makes certain people a burden upon others

b. A collectivist ethic which undermines people's self-reliance and mental efficacy.

Business people are unlikely to suffer from a passive or tragic sense of life, but are prone to have a collectivist ethic based upon their family and cultural education. The implications of a collectivist education is that one's sense of value is social. A collectivist wants to impress others, and wants the validation that others can provide him. Money, job, status and notoriety are all products of efficacy, but they are also craved by those lacking efficacy who will otherwise accept a pretense of it.

A number of business people are 'supreme egoists' in the sense that they see themselves as providers to the 'corporate family' in a patriarchal sense, rather than just an efficacious cog in a very efficient wheel. This heightened sense of value derives from the traditional 'hierarchical' structure of the company, the lack of accountability the MD has experienced, or their unwillingness to yield to it. The difference between confidence and arrogance is an egoist with a objective sense of reality and one with a social or 'arrogant' sense of reality. His sense of reality (or focus) is determined by his education and subsequent conscious convictions.

The solution to this problem is education, but the nature of the required changes is beyond the scope of this report.

6. Market regulation

Perhaps the greatest constraint upon commodity markets is the lack of regulation. Most regulation of the resource sector has related to environmental, planning, employment, health & safety and other issues. Historically, Australia also has export price controls, and certainly there are some industry standards governing disclosure and other practices.

Other standards which might otherwise assist the industry are:

a. **Capacity ramping:** A practice supported by traders and metal consumers, whereby they provide adequate finance for a project to ensure it gets developed. Shareholders make minimal returns because the sponsors and consumers have created an over-supply. Sponsors should be obliged to contract for at least 80% of production capacity before the project is funded. Banks have an interest only in projecting themselves, as the recent financial closure of Australian Magnesium Corporation will demonstrate. Governments also support the practice to meet dubious policy objectives. Japanese traders have for decades pursued this policy in the coal industry. Only in recent years, has consolidation in the coking coal, bauxite (alumina), iron ore and manganese sectors prevented the practice, allowing prices to appreciate.

b. **Claim to assets:** Another means of getting better outcomes in industry is to place shareholders (excluding directors & related parties) before banks (and other lenders) in the liquidation of companies. This would increase the cost of capital, however banks are better able to analyse the outlook for these companies, and it would encourage better industry analysis. Brokers have no

ownership or loyalty to clients because they make little money from them anymore. Really they only need them to get good distribution of a stock, and in a boom everyone will take it. Clearly clients are poorly positioned to appreciate when the bull will buck, and when it will 'bear'.

c. **Disclosure:** Confidentiality is a common commercial practice to ensure competition does not gain any insight into future strategies. The implication is that the industry will make poorer decisions for the market, as well as prevent related businesses from making informed decisions. A lack of disclosure is a major obstacle to the optimum allocation of resources, and hence a considerable cost to all industries. More often than not disclosure prevents accountability, fair valuation, whilst permitting tax avoidance and exploitation. Certainly, there needs to be rules governing what information needs to be disclosed. I would suggest the information pertinent to the mining industry is: procurement, finance (cost of capital), mining costs, future planning, product quality, etc.

d. **Civil rights:** Does the government have a role to play in vetoing resource development in foreign countries. Australian companies are leading the push into foreign markets. The exception is when the corporate interest is contrary to Australian interests, as was the case with the thwarted takeover of Woodside by Shell. These exceptions tend to be a rarity, and should be approved for the sake of 'global integrity'. Shell is likely to commission those projects which satisfy its commercial interests, and I think they are the same as Australia's from a broader perspective. Ie. If it develops gas resources in Oman before Australia, its because those resources are more competitive.

Information Disclosure

The effective functioning of markets depends on the availability of timely and accurate information. In a global context, various organisations have a vested interest in not disclosing information that has a bearing on supply, demand and pricing of commodities. When you consider that prices are determined by marginal supply & demand (excess or shortage), and not by the bulk of long-term, captive contracted supplies, then the possible impact on prices is significant. Often such impacts are not sustainable.

Research Support

The long-term supply and demand for commodities rests with new applications for metals, as well as new, more effective or cheaper techniques for identifying minerals. Certainly developments in geophysics in recent decades has enhanced discovery rates even before a drill hole is placed into the ground to validate the occurrences of commercial mineral concentrations.

7. Strategic Development

There are several strategic industry and econonic issues that need to be addressed by the government, namely:

6.1. **Terms of Trade**

Australian exports are overly reliant upon commodities, the average price of which are declining by 2% a year. To some extent we can compensate by shipping higher volumes, but imports are increasing in real prices at a faster rate.

Historically the government has intervened in the market when it sees the prospect of creating new

downstream industries. The problem is such intervention has been ad-hoc and expedient. Such intervention has served narrow political interests rather than national strategic objectives. I raise 4 specific examples:

a. **Stuart Oil Shale Project** was supported by the government to reduce Australia's dependence on imported oil at a time when OPEC controlled a large slice of the market. The federal government has maintained its support of the project despite its high cost, environmental impacts, technology risks and a global surplus of oil, and a trend towards reduced oil consumption. It would be better advised to upgrade Australia's rail infrastructure.

b. **Australian Magnesium Corporation** recently raised $A1.3 billion to fund its magnesium alloy project in Queensland after 2 failed attempts. The failures were attributed by the company to the poor commodities market, but many analysts had doubts about the marketing strategy and robustness of the project. The cost competitiveness of the Chinese, the similarities to coal marketing meant that contracting to sell just 50% of capacity was a huge commercial risk for shareholders and the government to carry. Lastly, brokers felt compelled to support the listing just to get the attractive 5% broking commission.

c. The **WA Gas Pipeline** and **Alice Springs to Darwin Railway** are more positive examples of government investment, as long as they are supported by conservative commercial parameters and are based upon a national strategic plan.

The government does have a role in developing strategic plans and projects which support the broader interest of national development, as such investments have significant multiplier effects. Politically expedient objectives like encouraging employment in rural areas to support better services is a dubious objective. Its runs counter to commercial realities.

The consolidation of several mining industries like coal, iron ore, chrome, manganese and vanadium has meant that companies like BHP-Billiton and Rio Tinto can achieve premium prices, so these trends should be viewed positively, because these companies are best positioned to understand the market. Ill-conceived however is coal exploration in Queensland (particularly where infrastructure is required), when Chinese and Russian markets offer more promising projects. No doubt a future QLD government will subsidise the development of rail links, brokers will talk up the industry, coal consumers will contract for 50% of capacity (not at fixed prices mind you, but annual benchmark prices). The result will be subdued prices for some years, yet mining executives will retain their jobs. In the interim, there are commodities which have enormous potential like niobium, rare earths, but Australia is ill-equipped to develop these markets. Market analysts are only starting to take the time to understand them.

If the government feels compelled to get involved it should be in the least intrusive possible ways. It always amazes me that politicians think they can have a greater understanding of commercial issues when they remain so aloof from reality. Few politicians have even worked in the commercial world, but rather have arisen through the safety of union, legal practices or political party. I would suggest that corporates have insufficient time for such activities. Companies tend to be more concerned with the 'now' to focus on long term and strategic issues. Companies in Australia tend to be under-manned, so the need for strategic planning is sacrificed. Industry associations doing this on an industry-wide basis are well placed to motivate non-performers. It might be argued that companies are not accountable to their peak body. No, but they require their input???

Producers and consumers be encouraged to carry a levy on output?

Mining companies have a vested interest in reducing the delivered cost of their product. From their perspective, new technologies and methodologies represent the best means of achieving a broad reduction in mining costs, whilst research into processing techniques (perhaps funded by mineral processors levy) represents another means of reducing costs. There are 2 ways by which the industry can enhance returns:

a. **Increasing volumes:** Reducing the costs of delivered product will open up new markets and applications for a particularly commodity, however these sales will not necessarily translate to higher revenues because historically metal prices have declined by 2% per annum in real terms every year.

b. **Increasing product quality** by improving the purity or grain morphology of individual metals, or perhaps downstream processing these metals into higher value alloys and materials such as metal powders, represents an alternative means by which producers can add value to their product. Regrettably Australia does very little work in material sciences because we historically have not developed downstream applications. Our small population has discovered such developments.

Australian industry has principally pursued Strategy A (higher volumes). Often the major Australian producers, competing in a global market, will make price concessions to buyers in return for greater market share (ie. Higher volumes). National GDP growth therefore rests upon much faster growth in volumes to offset a decline in real prices, not to mention higher imports. It must be noted as well, that miniaturisation is also reducing the intensity of metal consumption, however this to some extent is being offset by new products. But then consider the impact of manufacturers bundling more of these devices together in a single unit in the 'digital age'. It is unrealistic to expect Australia to compete in the long-term with emerging mines in Africa, South America and Asia. These regions have lower compliance (regulatory) costs, have lower exploration costs (as they have cheap labour and are lightly explored), and many of these countries already have establishing mining industries. Fortunately, Australian companies are playing an important part in developing these regions.

1. Costs of compliance

Increasingly mining companies are being compelled by the community, industry and other vested interest groups to achieve higher standards of compliance, in order to achieve environmental, health & safety, or social values. For the most part these hurdles are sensible, and I think the challenge should be placed upon:

a. **Government** to ensure developing countries are matching the same standards. A levy upon metal output to fund best practice is the best means of ensuring environmental, safety & health and community goals. The costs carried by Australian companies might also include social programs for aborigines. More importantly, such a program would ensure (cost) parity (or competitiveness), but also see a greater share of the metal value retained in the producer nation's (eg. Australia), rather than passed onto end-users (eg. Europe, Japan and the USA). Collecting levies in developing countries is harder because of the lack of enforcement, yet clearly such governments would have incentives to enforce given they are missing taxation and potential levies. The bulk of this product is sold in developed countries, which makes double-entry accounting the best means of ensuring compliance, recognising the need for certification of product shipments to ensure compliance among developing countries.

b. Companies

8. Infrastructure

There is no question that the government could justify a string of new mining projects by supporting new infrastructure projects, eg. A rail links from Gladstone to the Surat Basin, a high capacity gas pipeline from Darwin to Moomba, or from the NW Shelf to Moomba. Such investments should have a commercial basis and should be privately operated.

The government does not have a role to play in resource planning. This is best achieved by industry associations who will use the infrastructure. They should establish regional councils to address such issues along with other related industries such as farming, chemicals, energy, etc.

9. Risk management

Risk management is an interesting concept because it often leads to mis-management. Consider the impact of hedging on the performance of Australian mining companies, namely Pasminco, MIM, Western Metals and Orica (explosives). One wonders whether hedging should be stripped from the operational investment, so that investors can ensure they have a clear understanding of the business. Interestingly Enron was considered an oil & gas industry leader in risk management. Perhaps hedging should be a 'risk' carried by the personal investor as these products are becoming increasingly difficult to understand, eg. contingent put & call options with all sorts of conditions. At a time when broker margins are tight, quality research is hard to come by, and to the dismay of Sons of Gwalia, whom some brokers struggled to understand their hedging.

10. Human Resources

Transient commodity cycles are not helpful to technical professions employed in the industry. Many geologists in Perth drive taxis due to the volatility of the market. Clearly better forecasting will highlight opportunities in the troughs. One might see a role for these people in the downstream service sector, however changes in financial markets have otherwise ended careers in these areas.

During my university studies 15 years ago at both NSW and Macquarie University, it was evident to me that there was a lack of mentoring for students. Students very much had to struggle with themselves as far as career direction. Little attempt was taken at school or university to highlight the skills needed in a certain career. The little advice given seemed to highlight only the myopia of the advisor. I would have thought the Industry Associations (eg. NSW Minerals Council) have a role to play in highlighting the career options and requirements of their industry.

11. Intellectual paralysis

Research: CSIRO is a useful organisation, however it should be in the hands of the private sector, or industry associations which represent it, rather than the government. The private sector should own the process if they are to value its work. I recommend privatising it or better still giving it various segments to various industry bodies. In as much as facilities are shared between industries, perhaps infrastructure should be retained by a central agency which can charge those associations for its resources - at a nominal rate to ration useage (capacity) as well as to fund infrastructure maintenance and

improvements. I suggest by being responsive to industry, industry associations managing these resources will be more commercial and better marketers than the government, which is somewhat detached from commercial realities.

Academic: Academics are detached from the industries in which they participate. I would suggest that academics should be employed by industry bodies for research, or direct by companies if otherwise unsupported, and they also work in universities which manage the infrastructure. I suggest the associations should take over the teacher & student recruitment, and they can reach agreements with other groups as required. This should bring university and academics closer together. Evidence of this split is the lack of support for CSIRO initiatives and the corresponding low profitability of basic research. The government may choose to fund more basic research, but it should merely be matching private research rather than 'owning the activity'. Industry ownership gives industry a means of sponsoring & distributing info on the activities through its publications. Adequate student enrollments becomes an issue for the industry, as should funding them. One would expect that as soon as this becomes an industry concern, employers would be willing to carry scholarships and training programs.

Issues for effective investment

I would suggest there are a range of issues which determine the effective allocation of funds to the resources industry. The first question is 'effective' to whom. Fund managers, corporate sponsors, brokers, investors and end users (consumers) interests are very different. A lot of people profit from volatility, namely entrepreneurs & traders, whilst other vested interests benefit from less volatility. Volatile prices tends to undermine product demand by consumers of raw materials (eg. The development of new applications for cobalt was undermined by recent shortages). Employees would certainly prefer less volatility to ensure job security.

Intellectual paralysis

There is a requirement in the Australian finance sector and mining industry for a number of reforms, and I would also like to suggest the government consider another series of issues for further consideration.

Intellectual Paralysis: Institutions are established and managed by individuals, yet individuals develop their attitudes (values) in a social context. It is therefore important to look at the decision-making process at each step of their development. This is a personal responsibility, but I'd like to highlight people's predisposition to certain outcomes.

The principal factors effecting investment in mineral & energy resources are the following:

Effective Investment should be the standard

The government should not just seek to increase investment in the minerals & energy sector, but rather improve the effectiveness of that expenditure. Effective investment is more likely when project sponsors are more accountable, when brokers have no conflict of interests, and their research is scrutinised. We want to concern ourselves with maximising returns on investment, otherwise we are under-utilising our financial resources. One argument is that we should be spending less on mineral exploration because their is an overall over-supply of most commodities. The counter-argument is that the most developed and cost-competitive projects will proceed.

Returns are maximised when project life corresponds to peak metal prices, by minimising exploration and mining costs, and by maximising revenues through hedging and other practices. To some extent, the $A provides a natural hedge because it falls when commodity prices fall.

12. Recommendations

I would recommend that the government undertake a number of reforms across several areas. Namely:

a. **Foreign policy:** Assist foreign developing countries to adopt accounting practices and effective enforcement of their corporations, as well as to improve customs clearance and taxation functions. Countries such as Malaysia and India are particularly laxed in these areas. These governments should be encouraged to match Australia on environmental & health & safety compliance, as we will be matching them on these standards, and we should be willing to offer technological transfer. If all mineral exporting countries are encouraged to accept these standards, the costs can be passed onto consumers and the cost addition means more value stays in Australia.

b. **Research & development levy:** The Australian government should support the establishment of levies on mineral production, processing and consumption. The proceeds from miners used to fund cheaper exploration and mining methods, the proceeds from processors used to fund research into lower cost processing techniques or reagents, and consumer-paid funds used to undertake research into new applications for metals. Producers and consumers should be obliged to obtain accreditation to ensure they report all production, sales and shipments and pay the R&D levies and national taxes. These issues are best dealt with through the CAIRNS group of countries. The US, Europe and Japan should be encouraged to lobby primarily consumer countries.

c. **Environmental levies:** The government can similarly pursue such strategies on carbon credits and environmental compliance.

d. **Government monopolies:** Governments should be subject to the Trade Practices Act just as business is. Some governments have been using their monopoly over services to extract higher returns from private operators. In these cases private enterprise is subsidising inefficient work practices. In these cases, if the corporation can demonstrate that their competitors (often governments overseas) are more competitive, then the Australian miners should be able to win access to develop their own rail service. Clearly this would prevent governments from using the sale of privatised entities as a hidden form of taxation. Ie. Using legislation to lock in higher revenues.

e. **Mandatory fund allocations:** Fund managers should be given mandatory guidelines for investing a small (minimum) amount of funds under management into small companies. They could do this directly or through smaller, specialised small company funds. The intention should not be to subsidise small companies, but rather to encourage more sophisticated ands specialised assessment of corporate worth by establishing specialised professionals offering better understanding between industry and finance. These need only be 5-7 year limits to establish the market structure and long-term returns.

f. **Stockbrokers conflict of interest:** Anyone who makes a commission from trading any asset class, including shares, options and real estate should be prevented from offering advice on the subject. There is an enormous conflict of interest. Talking to brokers its very evident to me that too many of them consciously few their clients with contempt (as 'suckers') because they make a commission no

matter what. Particularly because of the business cycle and the transient nature of the trader. These people get a reputation and then leave. I can't imagine real estate is much better because real estate investments are one-off and tend not to be location specific.

g. **Stockbroker remuneration:** Brokers should earn transaction fees (without advise) or act in a consulting capacity by selling research or by acting as an agent where they have a material position (equity) in the stocks they are buying. Ie. They only earn a commission on profits. The same conflict of interest exists for fund managers, but they don't make their income by encouraging 'churn'.

Stockbrokers: Changes to the way broker fees, legislate to separate finance, broking & advisory roles. Restructuring the industry. Advisory capacity to be strengthened, particularly with consideration of the broader issues. Strategic parameters. It might even serve the investment community if companies were required to hold forums on their website. The company can regulate the commentary, and provide its own insight. This is actually a good way to stop brokers from getting favoured treatment. The companies can integrate the commentary into research reports. A single ASX website could exist for each company. There is not the depth of knowledge in capital markets to provide credible analysis.

1. **Economy:** Tax & regulatory reforms to encourage foreign investment. We should have a strong $A policy to keep inflation low and spur investment in manufacturing & mineral processing. Should we have 2 Forex rates, a commodities one (Cairns) in the west, and a Aussie one along the east coast. It would be complicated, if used in day-to-day trade, or is it just used for foreign transactions.

2. **Regulation:** Companies not just to disclose the risks, but required to get an independent assessment of the risks for these issues. Corporate directors required to disclose certain info more often. Insider trading rules are a nonsense? In-house presentations offer clients favourable treatment.

3. **Currency:** The international supply of commodities is in $US. The result is that Australia and other commodity exporters compete not just on price, but forex rates. For Australia, and other commodity producers, this makes it difficult to develop a manufacturing base. Single currency? Benefit?

4. **Training:** University courses should encourage commerce electives. Graduates should have some commercial knowledge when they exit. I'd like to see some mentoring. Get people from the industry to go and speak to school children, to explain the skills they need, the nature of the jobs.

Fund Managers: They are only interested in major companies. They are placing too much of their money offshore. I think the government needs to maintain support of the Australia dollar through better policy, ie. Boosting competition, such that fund managers will bring back & invest savings locally. Fund managers should be encouraged to invest in small companies through 'specialised funds' including resources and small cap.

The government should legislate for fund managers to place a certain proportion (say 10%) of their funds under management into small company sectors, and perhaps <1% into non-profitable, growth companies like hi-tech enterprises. This would in fact improve private investment in Australian R&D considerably, and it would also result in greater understanding by financiers of specialised hi-tech industries. We have no historic strength in these industries, yet they are required if we are to develop new industries and attract foreign investors.

Most corporates are too pragmatic when it comes to exploration. Consider the exploration success by Minotaur Resources. It was a conceptually based program - a very successful one at that. The discovery of Olympic Dam style mineralisation in South Australia totally re-shaped attitudes to the mining industry. Exploration in my experience has long been driven by 'scientific empiricists' with little conceptual backbone. I think a better balance needs to be reached and its because the conceptualists in universities (or rationalists perhaps) are far removed from the commercial world. They need to be brought together. Industry funding of the academics is the only way to do it. Commit them to mineral royalties to fund the work….just let them decide how to spend the money.

PS: Apologies for the unfinished work…ran out of time. Not the best integrated piece of writing….feel free to work it out. Last recommendation is: PAY ME and I'd do a better job of it. Hope there is nothing in there I'm sorry I said. Maybe it needs a disclaimer.

Disclaimer: SORRY…well someone bad to say it…better me than the PM.