Q4 – EXPLORER QUARTERLY CASH UPDATE

BDO

RESEARCH INTO THE FINANCIAL HEALTH OF AUSTRALIAN-LISTED EXPLORERS: Q4 (QUARTER ENDED 30 JUNE 2016)

EXPLORATION EXPENDITURE BUCKS DECLINING TREND FOR FIRST TIME IN TWO YEARS – HAVE WE SEEN THE WORST OF THE EXPLORATION HIATUS?

- EXPLORERS WELL PLACED TO DEVELOP ASSETS
- NET CASH FLOWS FROM FINANCING MORE THAN TRIPLED
- GOLD CONTINUES TO OUTPERFORM OTHER COMMODITIES

BDO's report on the cash position of Australian-listed explorers for the June 2016 quarter (based on quarterly Appendix 5B reports lodged with the ASX), shows that there has been a marginal increase in total exploration expenditure coupled with significantly higher net financing and investing cash flows, despite the number of companies reporting continuing to decline.

For the quarter ended 30 June 2016, 713 companies lodged an Appendix 5B report, which was 24 less than the 737 to lodge in the March 2016 quarter and 67 less than the 780 companies that lodged during the same period last year. The declining number of companies reporting exploration activity is primarily attributable to technology companies using exploration companies as a means to list on the ASX via reverse takeovers, and companies being delisted or suspended from the ASX. We note that the ASX proposed changes to the listing rules during the quarter, which are expected to reduce the attractivness of reverse takeovers. Consequently, it is likely that we will see a dramatic decline in the number of reverse takeovers and increase in the number of IPOs going forward.

Despite a decline in the number of reporting companies, average exploration expenditure has increased for the first time in nine quarters. Furthermore, pockets of rallying commodity prices have been the catalyst for an increase of $946 million in total net financing cash flows compared to the March 2016 quarter, which clearly indicates that there has been a resurgence in investor appetite for businesses demonstrating strong fundamentals and reasonable valuation levels. In particular, gold stocks and oil & gas stocks received significant financing cash flows, with 10 gold companies and 6 oil & gas companies raising in excess of $10 million during the June 2016 quarter.

The interest in gold is reflective of heightened economic uncertainty that arose during the quarter due to Britain's dramatic exit from the European Union ('Brexit') and uncertainty around the outcome of the US presidential election. The apprehension surrounding Brexit and its effect on the global economy will continue until an exit agreement is negotiated. It is too early to know the full extent of Brexit on the natural resources sector, however, BDO's paper 'Brexit & Energy and Natural Resources' provides some insight to the risks and opportunities stemming from Brexit.

Increased financing cash flows have strengthened company cash positions, with the average cash balance increasing by more than $1 million over the quarter. Total net investing cash flows have also increased, from $47 million during the March 2016 quarter to $149 million in the June 2016 quarter.

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In summary, the key findings of the quarterly update reveal the following:

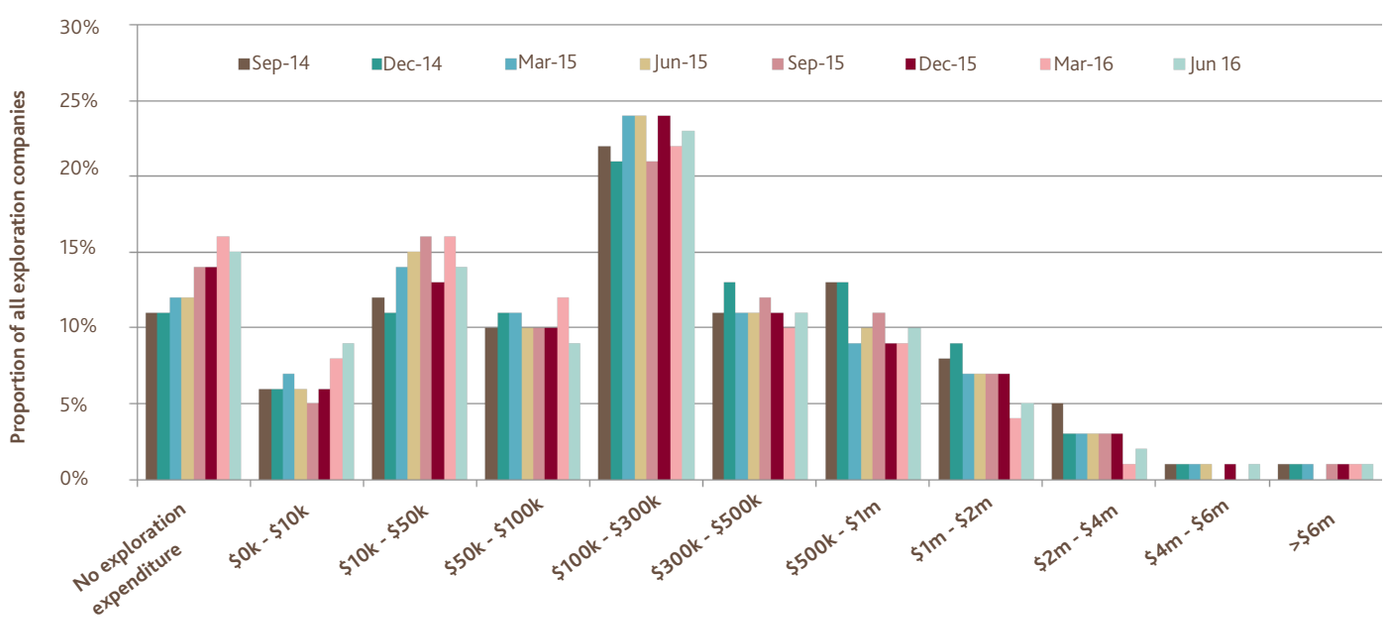
- The average exploration expenditure increased for the first time in nine quarters, from $360,000 in the March 2016 quarter to $418,000 in the June 2016 quarter.
- In the June 2016 quarter, 713 companies lodged Appendix 5B reports, a decline of 3.37% from the 737 companies that lodged reports in the March 2016 quarter.
- Reasons for the reduction include 14 companies being the subject of backdoor listings, 12 of which were technology related companies, and 13 companies being delisted or suspended.
- There was a significant increase in the number of companies with positive financing cash flows, with 50.9% of companies being able to raise funds via either capital raisings or through borrowings during the June 2016 quarter. This is an increase of almost 9% compared with the 42.3% of companies with positive net financing cash flows for the March 2016 quarter.
- Total net financing cash flows increased by $946 million, with the average per company increasing from $0.56 million in the March 2016 quarter to $1.91 million in the June 2016 quarter.
- The number of companies that raised in excess of $10 million in the June 2016 quarter was 33, up 26 from the seven in the March 2016 quarter. In coming quarters we may see an increase in explorer development expenditure and potentially more companies transitioning into production.
- Average cash reserves increased from $4.82 million for the March 2016 quarter to $5.85 million for the June 2016 quarter. This signals a potential turnaround in the market, with explorers being able to attract both debt and equity funding.
- The amount of explorers with a net investment in capital expenditure has remained consistent at approximately 33% between March 2016 and June 2016. However, total investment expenditure has more than tripled from $47 million during the March 2016 quarter to $149 million in the June 2016 quarter.
- 14 companies were used as listing vehicles for backdoor listings, 12 of which were technology or biotechnology assets.
- Six companies were delisted during the quarter, two exploration companies conducted an IPO and seven were suspended from the ASX.
- Shareholders showed keen interest in gold stocks in response to increased economic uncertainty resulting from Brexit and the outcome of the US presidential election.

JUNE 16 QUARTER CASH POSITION

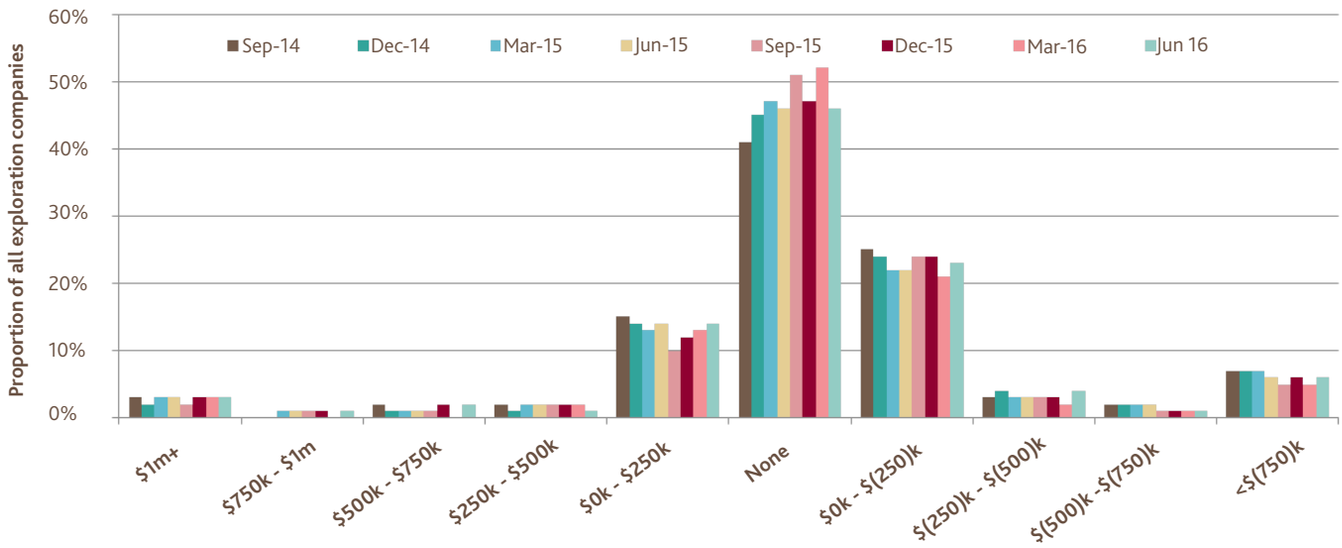
	MARCH 16 QUARTER		JUNE 16 QUARTER	
	No.	%	No.	%
TTotal number of companies lodging Appendix 5B's	737	100%	713	100%
Net Operating Expenditure				
- Companies with one quarter cash reserves	183	25%	145	20%
- Companies with two quarters' cash reserves	125	17%	114	16%
Administrative Expenditure				
- Companies with one quarter cash reserves	121	16%	90	13%
- Companies with two quarters' cash reserves	72	10%	59	8%

The following graphs provide a snapshot of the operating, administration and exploration expenditure across the sector:

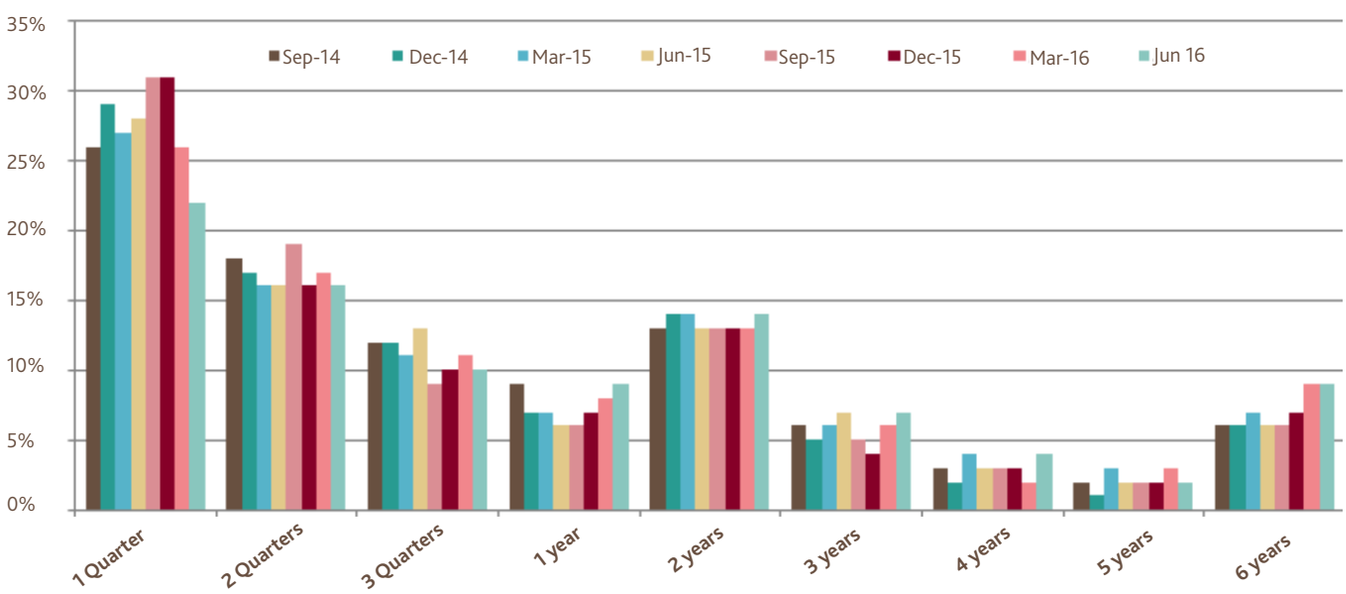
TOTAL EXPLORATION EXPENDITURE



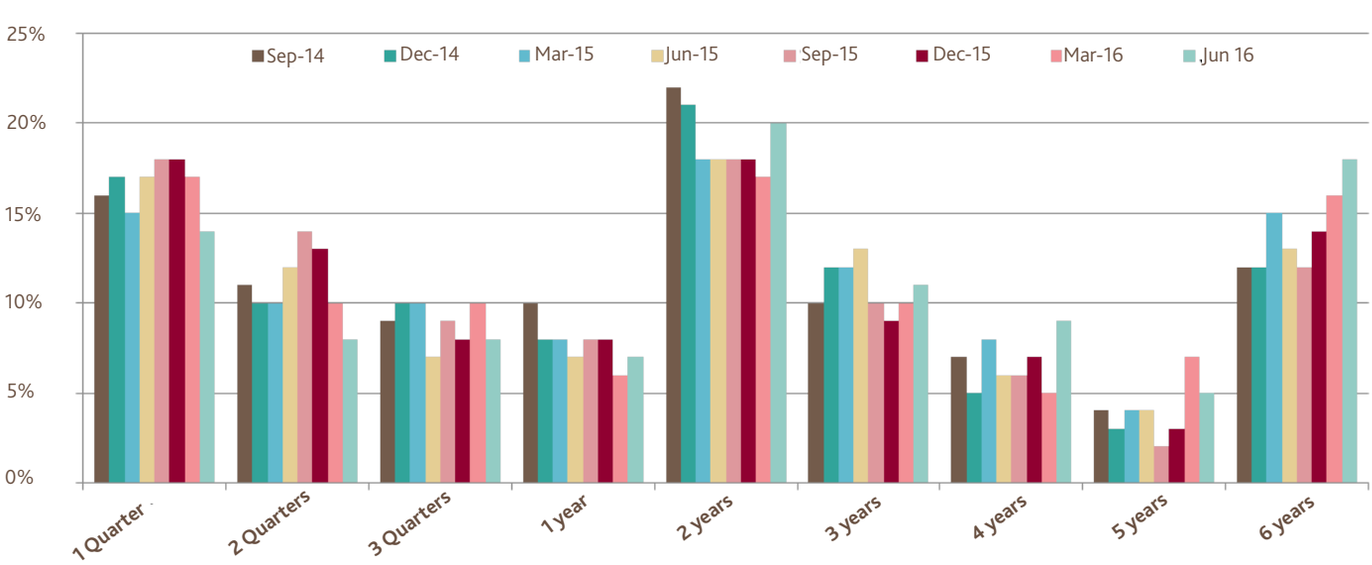
NET INVESTING CASH FLOWS



OPERATING EXPENSES - CASH BURN RATE

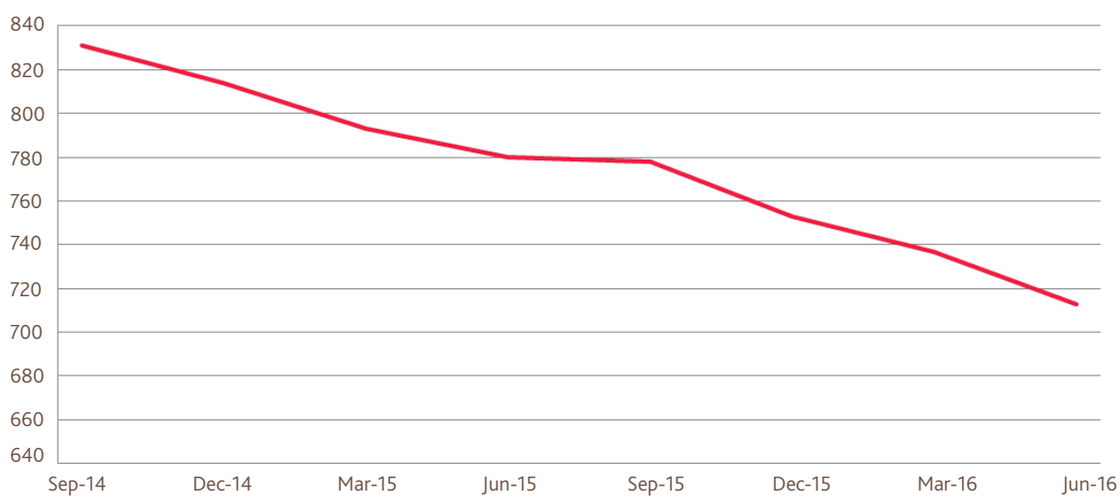


ADMINISTRATION EXPENSES - CASH BURN RATE



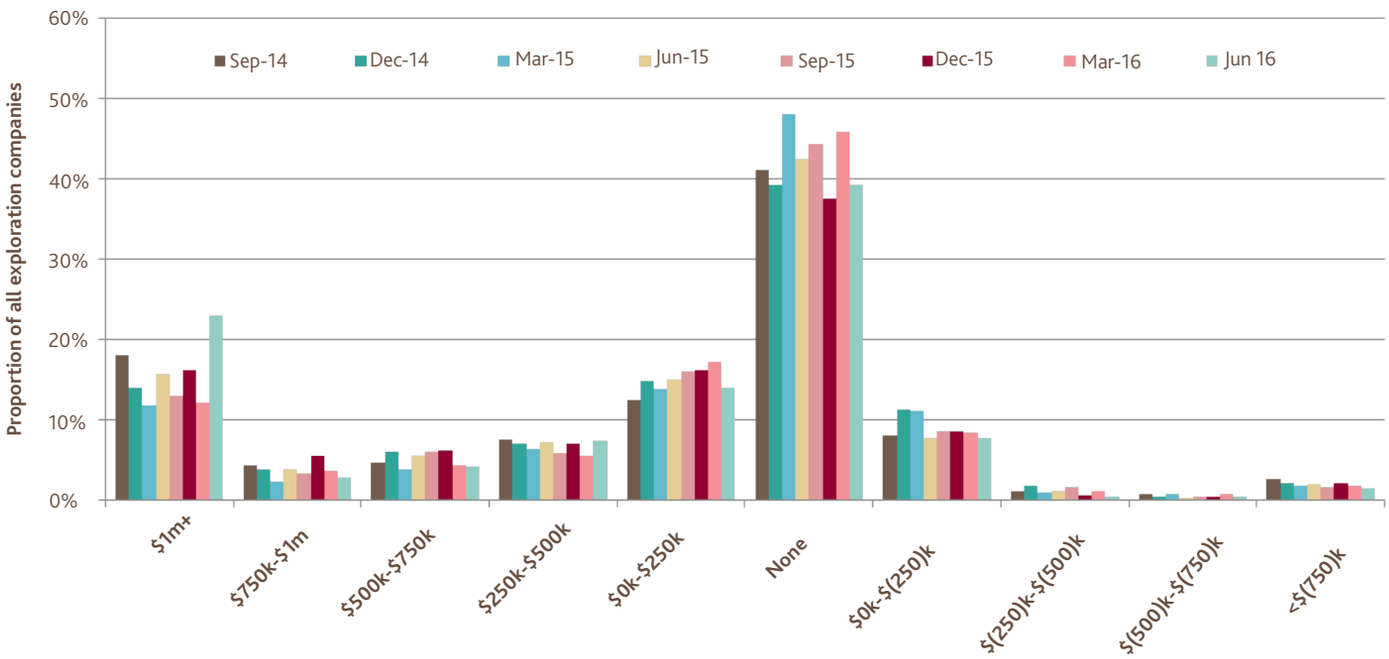
- The average exploration expenditure has bucked a declining trend to increase for the first time in nine quarters, from $362,000 for the March 2016 quarter to $418,000 in the June 2016 quarter. The median expenditure also increased from $91,000 to $115,000, which indicates that there has been a widespread increase in exploration expenditure, rather than just at the larger end of the market.
- In line with previous quarters, the majority of companies had exploration expenditure of between $100,000 and $300,000 over the June 2016 quarter. This accounted for 23.3% of the reporting companies, an increase of 1.5% from the 21.8% for the March 2016 quarter. There was also an increase in the percentage of companies that had exploration expenditure in excess of $300,000, from 25.8% in the March 2016 quarter to 29.2% in the June 2016 quarter.
- In addition to increased exploration expenditure, there are also a number of companies generating value by developing existing assets towards production. One of these success stories is Gold Road Resources Limited who have had mining leases granted and raised approximately $74 million for long lead time capital items for the Gruyere Gold Project.
- In recent periods, there has been an increasing trend in the percentage of exploration companies with nil investment expenditure. However, for the June 2016 quarter, there was a decrease of 5.7% from 52.1% for the March 2016 quarter to 46.4% for the June 2016 quarter. This indicates that the reluctance by explorers to invest may be diminishing as commodity prices and general market conditions improved over the quarter.
- Based on the June 2016 quarter's operating cash flows, there has been a continued decline in the percentage of companies that will burn through their cash reserves in the next quarter, with the percentage for March declining by 5% to 20% for the June 2016 quarter, the lowest since the September 2014 quarter. In previous quarters the downward trend has been attributable to exploration companies cutting back on expenditure in order to preserve cash reserves. Whilst this may still hold true for some companies, total exploration expenditure for the June 2016 quarter increased. Consequently, we primarily attribute the decline in the percentage of companies that would be unable to continue operations beyond the next period, to the significant increase in net financing cash flows, which have strengthened companies' cash reserves. This is evidenced by the increase in average cash balance of exploration companies increasing by $1.03 million to $5.85 million during the June 2016 quarter.
- In relation to administration expenditure, 22% of companies have only one or two quarters' of cash remaining (including companies with a negative cash balance) on current administration spend. This is a significant decline from the 27% identified in the March 2016 quarter and most likely a result of increased cash balances arising from successful financing activities during the June 2016 quarter.
- Dacian Gold Limited showed strong share price growth in the quarter increasing from $1.68 to $2.90, with a high of $3.05 reflecting a successful drilling program and progress of their feasibility study.

NUMBER OF COMPANIES LODGING APPENDIX 5B REPORTS: SEPTEMBER 2014 – JUNE 2016



- There has been a declining trend in the number of Appendix 5B lodgements over the review period, with the number of companies lodging Appendix 5B's decreasing to 713 in June 2016 from 737 in March 2016. This equates to a 3.4% reduction in the June 2016 quarter, the highest over the review period.
- The net decrease from the March 2016 quarter to the June 2016 quarter of 24 companies was a primarily a result of the following:
    - 14 companies were used as listing vehicles for backdoor listings, 12 of which were technology or biotechnology assets;
    - 7 companies were suspended from quotation on the ASX, 5 of which have entered administration and 1 where liquidators have been appointed;
    - 6 companies were delisted during the quarter; and
- These reductions in the number of companies lodging Appendix 5B's were partially offset by two new listings of exploration companies and two companies that had a late lodgement for the March quarter and therefore were not included in our March 2016 quarter dataset. There was also one company that was suspended during the March 2016 quarter but was reinstated following capital raisings and therefore lodged in the June 2016 quarter.

NET FINANCING CASH FLOWS



- The proportion of exploration companies with positive financing cash flows has increased in the June 2016 quarter to 51%, from 42% in the March 2016. Furthermore, total net financing cash flows have increased by $946 million from the March 2016 quarter, with the average per company increasing by $1.03 million. This indicates that there has been a resurgencein investor appetite for businesses demonstrating strong fundamentals and reasonable valuation levels.
- Furthermore, the significant increase in financing cashflows illustrates that explorers are finding it easier to raise equity funds. Consequently, we have observed a transition from a theme of cash conservation to explorers actively increasing expenditure across the board. This is a function of explores having some level of comfort in where the next dollar is coming from and is evidenced by the increase in both investing and exploration expenditure exhibited over the June 2016 quarter.

FUND FINDERS

The number of companies with nil financing cash flows for the quarter has decreased to 39% in June 2016, down from 46% in March 2016. The average net cash inflows for the period have also increased significantly, from approximately $560,000 in March 2016 to $1.9 million in June 2016. The number of companies that raised cash in excess of $10 million in the June 2016 quarter was 33, a significant increase from 7 in the March 2016 quarter. Of these, 10 were gold companies and 6 were oil & gas companies. Gold stocks have been particularly favoured by the market due to the increased economic uncertainty stemming from global political uncertainty, in particular uncertainty around the outcome fo the US Presidential and election and Britain's exit from the European Union. The companies that raised funds through either debt or equity are set out below:

- **Syrah Resources Limited** (graphite) - $194.32 million proceeds from issue of shares, exercise of options etc.
- **TerraCom Limited** (coal) - $156.30 million proceeds from borrowings.
- **Pilbara Minerals Limited** (lithium & tantalum) - $95.72 million proceeds from issue of shares, exercise of options etc.
- **Gold Road Resources Limited** (gold) - $73.95 million proceeds from issue of shares, exercise of options etc.
- **FAR Limited** (oil & gas) - $62.11 million proceeds from issue of shares, exercise of options etc.
- **CuDeco Limited** (copper) - $53.04 million proceeds from issue of shares, exercise of options etc and $8.48 million from proceeds from borrowings.
- **Wolf Minerals Limited** (tungsten & tin) - $47.04 million proceeds from issue of shares, exercise of options etc.
- **Champion Iron Limited** (iron ore) - $45.62 million proceeds from issue of shares, exercise of options etc.
- **Silver Mines Limited** (silver) - $36.32 million proceeds from issue of shares, exercise of options etc.
- **88 Energy Limited** (energy) - $24.87 million proceeds from issue of shares, exercise of options etc and $4.14 million proceeds from borrowings.
- **Finders Resources Limited** (copper & gold-silver) - $26.51 million proceeds from borrowings and other financing arrangements.
- **Samson Oil & Gas Limited** (oil & gas) - US$1.23 million proceeds from issue of shares and exercise of options etc and US$15.50 million from proceeds from borrowings.

- **Altura Mining Limited** (lithium & coal) - $22.38 million proceeds from issue of shares, exercise of options etc.
- **Elk Petroleum Limited** (oil & gas) – $21.19 million proceeds from issue of shares, exercise of options etc.
- **Doray Minerals Limited** (gold) $0.95 million proceeds from issue of shares, exercise of options etc and $20.00 million proceeds from borrowings.
- **Peninsula Energy Limited** (uranium) - $20.08 million proceeds from borrowings.
- **Blackham Resources Limited** (gold) - $2.09 million proceeds from issue of shares, exercise of options etc and $15.31 million proceeds from borrowings.
- **OreCorp Limited** (gold & nickel-copper) - $15.27 million proceeds from issue of shares, exercise of options etc.
- **Gascoyne Resources Limited** (gold) - $15.24 million proceeds from issue of shares, exercise of options etc.
- **Lucapa Diamond Company Limited** (diamonds) - $14.53 million proceeds from issue of shares, exercise of options etc.
- **Aurelia Metals Limited** (base metals) - $13.50 million proceeds from borrowings.
- **Skyland Petroleum Limited** (oil & gas) - US$9.67 million proceeds from issue of shares and exercise of options etc and US$0.59 million from proceeds from borrowings.
- **Dakota Minerals Limited** (lithium) - $12.96 million proceeds from issue of shares, exercise of options etc.
- **Capricorn Metals Limited** (gold) - $12.63 million proceeds from issue of shares, exercise of options etc.
- **Gateway Mining Limited** (gold and copper) - $12.63 million proceeds from issue of shares, exercise of options etc.
- **West African Resources Limited** (gold) - $12.50 million proceeds from issue of shares, exercise of options etc.
- **Alkane Resources Limited** (base metals) - $12.39 million proceeds from issue of shares, exercise of options etc.
- **Central Petroleum Limited** (oil & gas) - $11.73 million proceeds from borrowings and other financing arrangements.
- **Rum Jungle Resources Limited** (fertiliser & industrial minerals) - $11.56 million proceeds from issue of shares, exercise of options etc.
- **Xanadu Mines Limited** (copper-gold) - $11.27 million proceeds from issue of shares, exercise of options etc.
- **Austral Gold Limited** (gold) - $10.12 million proceeds from issue of shares, exercise of options etc.
- **Leigh Creek Energy Limited** (gas) - $10.06 million proceeds from issue of shares, exercise of options etc.
- **Oklo Resources Limited** (gold) - $10.04 million proceeds from issue of shares, exercise of options etc.

As noted in previous editions, the market continues to favour gold in times of economic uncertainty, a sentiment that has been exacerbated by global political uncertainties including Brexit. This is evidenced by the fact that 10 of the 33 major fund raisings came from gold exploration companies during the June 2016 quarter.

Commodity prices have increased over the quarter and provided the catalyst for companies with promising exploration assets to raise funds. Furthermore, increased commodity prices have improved the economic viability of many projects, which in turn has made it easier for companies with successful projects to attract capital.

The uncertainty stemming from Brexit and the outcome of the US Presidential elections and resultant investment in gold stocks, in conjunction with rallying commodity prices, have helped to improve the sentiment surrounding the mining and exploration industry. Consequently, exploration companies have been able to raise significantly increased levels of capital. However, it still remains to be seen the extent of this recovery and the extent to which explorers are ready to commit these funds to exploration and development of their projects. The next quarter will be very telling.

BDO INSIGHT

The sentiment at Diggers and Dealers in Kalgoorlie in August was far more positive than in prior years. The key messages that came across were that exploration spends are being carefully planned and increasingly using technology to gain more data. We are also aware that studies are more prevalent and boards are looking to be well informed before committing to the next steps. The improvement in corporate governance is not consistent across the board, however with the focus of the ASX and ASIC it should be firmly in the minds of boards, particularly Non-Executive Directors.

The June quarter has seen life return to the junior exploration space. Whilst much of the attention has been focused on Gold and Lithium, other commodities have attracted investment. One such Company was Lucapa Diamond Company which saw approximately $14.5 million raised through the conversion of options on the back of large diamond recoveries from alluvial mining.

We also note that despite the improving conditions, companies are taking a cautious approach to increasing administration expenditure which has been cut significantly over the past few years. This reflectsthe recent change in sentiment and perhaps lessons learned from the past. Now that equity capital markets have improved, these funds are flowing through to drilling programs and to other service providers who have faced difficult times. This transition is certainly beneficial for the industry and the economy.

We are also seeing an increase in M&A activities in the sector. With the value of most assets other than gold being reduced, many companies are looking to acquire, restructure or consolidate so that they are ready for the next phase of what may be an increase in the commodity cycle.

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