

DECEMBER 2010

AIM JOURNAL

THE ONLINE MONTHLY FOR THE ALTERNATIVE INVESTMENT MARKET

Government rules out AIM ISAs

The government has no intention of allowing AIM shares to be included in ISAs according to the response to an MP's question by Mark Hoban, financial secretary to the Treasury.

This appears to scupper the hopes of the London Stock Exchange and the Quoted Companies Alliance that inclusion of AIM shares in ISAs would help to improve their liquidity. The Association of Private Client Investment Managers and Stockbrokers (APCIMS) sent a letter to the Treasury at the end of October arguing this case.

Jake Berry, Conservative MP for Rossendale and Darwen, enquired in a written question if the government planned to introduce proposals to allow AIM shares to be held in ISAs. Hoban replied: "The government believes that ISAs are a trusted brand, and that it is important that this is maintained."

The government also believes that ISAs should be mainstream savings products. The government therefore do not intend to allow shares listed (sic) on AIM – which can be riskier and less liquid – to be qualifying investments for ISAs."

Hoban points out that AIM companies can benefit from other incentive schemes such as the Enterprise Investment Scheme and Venture Capital Trusts.

In a speech to the Tax Incentivised Savings Association conference prior to answering the question Hoban also said that AIM shares "carry a higher level of investment risk, and can be less liquid – and while that may be a risk worth taking for those who have knowledge and experience of investment, I'm not convinced that this is the right thing for ISAs more generally".

London & Stamford joins FTSE 250

Former AIM company London & Stamford Property is joining the FTSE 250 index in the latest quarterly index changes. This is within weeks of moving to a premium listing.

Two other AIM graduates, asset manager City of London Investment Group and Sinclair Pharma, are being included in the FTSE All-Share, while Hansteen and Raven Russia are on the reserve list for the FTSE 250.

Oil and gas firms Regal Petroleum and Volga Gas have both been dropped from the FTSE AIM UK 50 and FTSE AIM 100. Invista Real Estate, which is being wound down after it lost its contract with Lloyds, is also dropping out of the AIM 50. Miners Patagonia

Gold, Caledon Resources and Vatukoula Gold Mines are the replacements.

The other drop-outs from the AIM 100 are Datatec, Douglasbay Capital, Total Produce, Fyffes, and RCG. The additions to the AIM 100 include recently floated Indian call centre operator iEnergizer and Oakley Capital Investments, which has paid more than £20m for a 50% stake in listings magazines publisher Time Out. Xcite Energy, Discovery Metals, Hutchison China Meditech, Sandvine and Vatukoula are the other new inclusions.

The various index changes will become effective on Monday 20 December.

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general news

Manroy reverses into cash shell Hurlingham

Machine guns manufacturer Manroy Systems is reversing into cash shell Hurlingham and joining AIM on 22 December. Hurlingham is paying £3.1m in cash and shares and the quoted company will change its name to Manroy. The enlarged group is also raising £6m at 75p a share.

Glyn Bottomley, the chief executive of Manroy Systems, will take up the same role in the quoted company. He has warranted that Manroy Systems made a pre-tax profit of not less than £2.5m in the year to September 2010. Manroy Systems reported a pre-tax profit of £904,000 on revenues of £4.6m in the six months to March 2010. In the second half, Manroy delivered £6.2m of orders to the MoD.

Manroy's main product is the M2 HMG, which has been supplied to the MoD for 25 years. One thing

that investors need to be aware of is that the timings of large orders can make revenues and profits lumpy. Manroy believes that UK government spending cuts will not materially affect its business. Manroy intends to expand its product range and will tender for an MoD pistol contract.

Manroy markets the weapon mounting systems made by AEI. Bottomley owns 33.3% of AEI.

Hurlingham lost its AIM quotation at the end of September 2009 because it had not found a new business after it sold its hotel operations. It had £1.68m in the bank at the end of March 2010 and the original shareholders will own just over 22% of the enlarged company.

Most of the £5.2m after expenses raised by the placing will be used to pay off debt. Pro forma net debt will be £454,000.

Tokyo AIM debt market

Tokyo AIM, the joint venture between the London Stock Exchange and the Tokyo Stock Exchange, which has yet to attract any companies, is planning to launch a corporate bond market next March. The Tokyo Pro-Bond market is designed to attract foreign companies to issue bonds in Tokyo.

Tokyo AIM's chief operating officer, Yutaka Ito, believes that the new market "will account for several per cent of Japan's publicly traded corporate debt". Fees from debt issues are lower than for share issues but it will provide an opportunity to get the new market going. There are hopes that Tokyo AIM, which has been around for a year, could attract its first company early next year. A new nominated adviser from outside Japan is due to join the market and this could provide the impetus for the first company to gain a quotation.

Investors suffer Desire loss after water find

Desire Petroleum had to execute an embarrassing U-turn after it admitted that the oil it thought that it had discovered offshore of the Falkland Islands was water. The Desire share price halved on this news – it previously soared when Desire announced that the Rachel North 14/15-2 well had encountered hydrocarbons. There are rumours that AIM might launch an investigation into the announcements.

The fact that there were four days between the two announcements was particularly embarrassing for

Desire. It highlights the speculative nature of oil and gas exploration in the Falklands. Desire will certainly find it difficult to regain the confidence of the market after such a significant embarrassment and each well costs millions of pounds. Another well will be drilled on the Dawn/Jacinta prospect.

Panmure Gordon oil and gas analyst Peter Hitchens had been sceptical about whether the discovery would be commercial even if it had been oil. Writing before Desire discovered it had struck water he said: "We believe

that although there is a very significant pay zone we believe that reserves are likely to be modest and as such this is likely to be a marginal field at best".

Rockhopper Exploration, which has a 7.5% stake in the Rachel block, has been the most successful of the explorers in the region and has made a discovery at the Sea Lion prospect. However, the testing of that well did not go smoothly. There are around 200m barrels of oil on the Sea Lion prospect and there is scope for this figure to rise.

advisers

Seymour Pierce plans transatlantic merger

Seymour Pierce is planning a merger that could leave it with a NYSE listing.

The merger would involve Seymour Pierce, which has the largest number of AIM broking clients; Gerova Financial, a US insurance group; and Ticonderoga, a New York-based equities trader run by former Collins Stewart boss Joel Plasco.

The deal will be subject to approval by regulators but Plasco is expected to become boss of the enlarged broking business.

Seymour Pierce was bought by its management and Alchemy for £7.35m in July 2003. The deal is thought to value the broker at £40m.

Broker **Ambrian Partners** generated second-half revenues more than double those achieved in the first half. Fundraisings for AIM-quoted resources firms Nautical Petroleum and Archipelago Resources have helped, as has cutting costs. Ambrian Partners had built up its cost base by taking on analysts to help boost secondary trading. The benefits did not come through and Ambrian refocused on its core resources and cleantech sectors.

Astaire Group is close to selling private-client broker Rowan Dartington. This follows last month's sale of Astaire Securities to Canadian

broker NCP Northland Capital Partners for £2.45m. Rowan Dartington is Astaire Group's remaining operating business. A problem with Rowan Dartington's financial records was the catalyst for the break-up of Astaire.

AIM adviser **Liberum Capital** has opened an office in Leeds in order to attract northern clients keen on a locally based adviser. Liberum is already broker to Lancashire-based Daisy, the AIM-quoted telecoms services provider in the process of buying rival Spiritel.

US broker **Piper Jaffray** is pulling out of AIM, with its clients moving to new advisers.

ADVISER CHANGES – NOVEMBER 2010

COMPANY	NEW BROKER	OLD BROKER	NEW NOMAD	OLD NOMAD	DATE
Prime Focus London	n/a	Seymour Pierce	Grant Thornton	Seymour Pierce	01/11/2010
Canaccord Financial	Charles Stanley/Keefe, Bruyette & Woods	Macquarie	Charles Stanley	Macquarie	01/11/2010
Avia Health Informatics	Panmure Gordon	Merchant Securities	Panmure Gordon	Merchant Securities	03/11/2010
Plus Markets Group	Brewin Dolphin	Numis	Brewin Dolphin	Numis	03/11/2010
Vane Minerals	Allenby	Arbuthnot	Allenby	Arbuthnot	04/11/2010
Specialist Energy Group	FinnCap	Fairfax IS	FinnCap	Fairfax IS	05/11/2010
MobilityOne Ltd	Daniel Stewart / Allenby	Allenby	Allenby	Allenby	05/11/2010
Eckoh	Singer	Seymour Pierce	Singer	Seymour Pierce	08/11/2010
Parallel Media Group	Novus / Northland	Northland	Northland	Northland	09/11/2010
Real Estate Investors	Liberum	Singer	Smith & Williamson	Smith & Williamson	09/11/2010
Trading Emissions	Liberum	Cenkos	Liberum	Liberum	10/11/2010
GTL Resources	Cenkos	Arbuthnot	Cenkos	Arbuthnot	11/11/2010
Syntopix	XCAP	Zeus	Zeus	Zeus	11/11/2010
WH Ireland	Panmure Gordon	Oriel	Panmure Gordon	Oriel	12/11/2010
Kedco	SVS	Cornhill Capital	Deloitte	Deloitte	15/11/2010
Ortac Resources	Optiva / Beaumont Cornish	Beaumont Cornish	Beaumont Cornish	Beaumont Cornish	16/11/2010
Altitude Group	Merchant Securities	Daniel Stewart	Merchant Securities	Daniel Stewart	17/11/2010
Directex Realisations	Rivington Street	Libertas	Libertas	Libertas	17/11/2010
Hameldon Resources	Rivington Street	Hybridan	Strand Hanson	Strand Hanson	17/11/2010
Plethora Solutions	Daniel Stewart / Hybridan	FinnCap	Daniel Stewart	FinnCap	17/11/2010
D1 Oils	WH Ireland	Piper Jaffray	WH Ireland	Piper Jaffray	18/11/2010
Empyrean Energy	Shore Capital	Northland	Shore Capital	Northland	18/11/2010
Imagelinx	FinnCap	Seymour Pierce	FinnCap	Seymour Pierce	18/11/2010
Telit Communications	Investec	Northland	Investec	Northland	18/11/2010
Otium Ventures	Rivington Street / Daniel Stewart	Daniel Stewart	Daniel Stewart	Daniel Stewart	19/11/2010
Capital Pub Capital	Panmure Gordon	Altium	Panmure Gordon	Altium	19/11/2010
Kellan Group	Merchant Securities	Strand Hanson	Merchant Securities	Strand Hanson	19/11/2010
Minera IRL	FinnCap / Collins Stewart	Collins Stewart	Collins Stewart	Collins Stewart	23/11/2010
ZincOx Resources	Ambrian	Numis	Ambrian	Numis	23/11/2010
Coburg Group	Simple Investments	Merchant Capital	Grant Thornton	Grant Thornton	25/11/2010
IS Pharma	FinnCap	Piper Jaffray	FinnCap	Piper Jaffray	25/11/2010
Norish	Davy	NCB	Davy	NCB	25/11/2010
Public Service Properties	Arbuthnot	Evolution	Arbuthnot	Evolution	25/11/2010
Renewable Energy Generation	Evolution	Piper Jaffray	Smith & Williamson	Smith & Williamson	25/11/2010
Monitise	Evolution	Piper Jaffray / Evolution	Evolution	Evolution	26/11/2010
Griffin Mining	Panmure Gordon	Investec	Panmure Gordon	Investec	29/11/2010
Nexus Management	Rivington Street	Daniel Stewart	Merchant Securities	Merchant Securities	29/11/2010
Spitfire Oil	Panmure Gordon	Investec	Panmure Gordon	Investec	29/11/2010
Enfis Group	FinnCap	Execution Noble	FinnCap	Execution Noble	30/11/2010
Horizonte Minerals	Panmure Gordon	Westhouse	Panmure Gordon	Westhouse	30/11/2010
Karelian Diamond Resources	XCAP	City Capital	Merchant Securities	Merchant Securities	30/11/2010

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company news

Satellite successfully achieves orbit as Avanti prepares for next launch

Satellite operator

www.avanti-communications.com



Avanti Communications' first satellite, HYLAS 1, has been successfully launched and this has sent the share price soaring. Management believes that capacity will be sold out within three years. Avanti, which won the Best use of AIM award at the 2010 AIM awards, is on course to move into profit in the year to June 2011.

The Ariane 5 launcher took off from French Guyana on 26 November and HYLAS 1, which will provide coverage of most of

Europe, separated from the rocket after 34 minutes and went into its allotted orbit.

Broadband traffic will be put through the satellite in the New Year. Just after the launch Avanti signed a five-year agreement with BT to provide broadband services to Cornwall and the Isles of Scilly. There are a total of 62 customers.

Avanti has also signed a five-year contract worth \$15.5m with Iraq-based satellite service provider TigrisNet, which will provide internet-based services in Europe and the Middle East. This the first deal where the capacity will come from both the HYLAS 1 and HYLAS 2 satellites. HYLAS 2 is due to be launched in spring 2012 and will extend coverage to Africa and the Middle East. Avanti says that it is also talking to two mobile phone network companies that want to use the satellites to link remote

AVANTI COMMUNICATIONS (AVN)	700p
12 MONTH CHANGE % +59.3	MARKET CAP £M 562.3

base stations.

Avanti has secured the cash to fund HYLAS 2 from debt and an £89m share issue at 400p. At the end of June 2010, net debt was £15.4m. In July, Avanti raised a further £70m at 430p a share in order to repay debt. The business should be cash generative this year and then build up operational cash flow over the coming years. Net operational cash flow should total £135m in the three years to June 2014 and more than £320m in the subsequent three years, according to broker Daniel Stewart. The broker expects capital expenditure to tail off from 2012-13 onwards but HYLAS 3 has been designed and will require investment, so this is unlikely to happen.

Motion capture growth helps OMG treble profit

Motion capture software

www.omgplc.com

Motion capture software developer **OMG** almost trebled its underlying profit in the year to September 2010 as the Vicon motion capture business recovered strongly in the period.

Overall, revenues were 19% ahead at £31.2m, while the underlying profit improved from £1.1m to £3.2m. The latest figure excludes an intangible assets write-down of £1.92m.

The Vicon division's revenues grew from £10.6m to £14.1m even though there was a lack of spending

OMG (OMG)	39.5p
12 MONTH CHANGE % +116.4	MARKET CAP £M 27

on new software by entertainment customers. This did help the House of Moves animation services business but the main growth came from life sciences and engineering sectors.

The part of the business developing software for unmanned aircraft should benefit from the defence spending review because

spending in this area will not be cut. Loss-making Yotta uses the motion capture software to survey highways and pavements plus the assets related to them. The UK is winning new contracts but the US business remains weak and costs are being reduced.

Strong cash flow helped OMG to increase its net cash position from £2.78m to £6.2m by the end of September 2010. The full-year dividend was doubled to 0.3p a share.

company news

Western Coal merger creates major global coal producer

Coal miner

www.westerncoal.com

NYSE-listed hard coking coal producer Walter Energy is acquiring AIM-quoted and TSX-listed **Western Coal Corporation (WCC)** for C\$3.3m (£2.1bn). WCC is the biggest company on AIM and the merger will create a major global metallurgical coal producer.

Walter is offering C\$11.50 a share in cash or 0.114 of one of its shares for each Western Coal share. Alternatively, each shareholder can opt for a mixture of cash and shares but 70% of the total will be paid in cash and 30% in shares. WCC's largest shareholder, Audley European Opportunities Master Fund Limited, had already agreed to sell its holding of 54.5m shares to Walter at \$11.50 a share. Walter is seeking to borrow \$2.73bn to

Western Coal is the biggest company on AIM

finance the deal.

The bid valuation is based on the number of WCC shares in issue but excluding those held by its own subsidiaries – so it is based on 291.1m shares. In the past year or so, WCC has acquired fellow AIM-quoted coal companies Cambrian Mining and South Wales-based Energybuild. Cambrian had a large shareholding in WCC prior to that merger.

The merger with Walter creates one of the largest producers of metallurgical coal in the world, with mines in Canada, the US

WESTERN COAL CORPORATION (WTN) 721.5p

12 MONTH CHANGE % +428.6 MARKET CAP £m 2,100.3

and UK. WCC expects to produce 6.1m tonnes of coal in the year to March 2011, while Florida-based Walter should produce 6.6m tonnes of coal in 2010. Most of that is metallurgical coal. Combined coal reserves are around 385 million tons. The group expects to produce 20m tons of coal a year by 2012.

The deal should be completed by the middle of 2011. Walter says that the acquisition should be earnings enhancing in the first full financial year after completion. The WCC share price is well over five times the level it was one year ago.

SRG flotation delay hits Palmaris valuation

Investment company

www.palmariscapital.com

Scottish Resources Group, the largest surface coal miner in the UK, will not be floating this year because it was unable to secure the valuation that it wanted. This is a disappointment to AIM-quoted investment company **Palmaris Capital**, whose SRG stake is its only real asset.

A pre-new money valuation of around £200m was suggested for SRG when the pathfinder prospectus was issued in July. On top of that, SRG wanted to raise £25m as part of the listing on the Main Market. Palmaris owns 16.1% of SRG and that stake could have

PALMARIS CAPITAL (PMS) 8.75p

12 MONTH CHANGE % +32.1 MARKET CAP £m 13.6

been worth more than £30m. Palmaris might have sold some or all of its stake if SRG had floated. That is why during the summer the Palmaris share price jumped to 15.75p before falling back as the flotation was delayed.

Palmaris has been a shareholder in SRG, originally known as Mining (Scotland), since 1994. The stake is in the books at the end of June 2010 at 240p a share – or 96p a share following a five-for-two stock

split on 8 July. That is equivalent to a total market value of £96m for SRG – and £15.5m for the Palmaris shareholding.

SRG has nine opencast mines and its revenues grew 59% to £229.9m in the year to March 2010. SRG moved back into profit last year. Operating profit was £33.1m and post-tax profit was £16.5m.

Palmaris has a net asset value of 10p a share, so the shares are trading at a 12.5% discount to NAV. Net cash was £179,000 at the end of June 2010, which is similar to the operating cash outflow in the 12 months to June 2010.

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Lighting - The Third Revolution

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Infocus

www.cleantechinvestor.com

company news

Hamworthy's long-term order book starts to recover

Fluid handling systems

www.hamworthy.com

Marine and offshore fluid handling systems supplier **Hamworthy** continues to report lower revenues but the order book is showing signs of recovery. There is always a lag in orders turning into revenues so this augurs well for an upturn next year.

The order book was worth £186.7m at the end of September, thanks to big orders in China and Brazil. They were a £20m order from a Chinese shipyard and a £50m order from oil and gas company Petrobras.

The order book is well up on the figure at the end of March 2010 but it is still lower than one year earlier. It includes £75m of work that should be generated in the second half. Aftersales revenues are not included in the order book but they provide a regular and growing income.

Interim revenues fell 17% to £83.1m in the six months to September 2010.

The order book was £186.7m at the end of September

That led to a sharp drop in underlying pre-tax profit from £10.3m to £6.94m.

The lower sales mean that working capital requirements are also reduced. Net cash was £73.4m at the end of September 2010. In line with its progressive dividend policy, Hamworthy has increased its interim payout by 5% to 3.36p a share. The dividend is still well covered by earnings.

Water systems was the only division to generate a higher level of income in this period. Demand for water treatment systems from cruise ships is strong. However, the ballast water

HAMWORTHY (HMY)		381p
12 MONTH CHANGE %	+42.2	MARKET CAP £m 173

treatment business Greenship, which was acquired for its technology, has been a disappointment. The system needs further development and it will not be ready until 2012. That should be in time for the start of the retrofit market in 2013.

Ship exhaust gas cleaning technology developer Krystallon has proved more successful, with its product already launched. A £5m order has already been secured. Hamworthy is assessing other air emission control technologies.

Numis forecasts a fall in group profit from £19.9m to £11.2m in the year to March 2011, with a small recovery to £12.3m the following year.

Sutton Harbour offloads Air Southwest

Port operator, property

www.sutton-harbour.co.uk

Plymouth-based property developer and port operator **Sutton Harbour Holdings** has completed the sale of its loss-making airline, Air Southwest, for a total loss of £7.3m.

Eastern International Airlines is paying £1.5m for the airline but there will be an adjustment for unflown ticket revenues and working capital of £2.8m. That means that Sutton Harbour will be hit by a net cash outflow of £1.3m. The rest of the £7.3m loss will come from asset write-offs. This figure does not include trading losses in the

SUTTON HARBOUR (SUH)		39p
12 MONTH CHANGE %	-31	MARKET CAP £m 24.5

six months to September 2010, which will be shown after tax on the upcoming interims.

Air Southwest was started in 2003 but in the past couple of years it has struggled as oil prices increased and competition got fiercer.

Sutton Harbour had net assets of £43.1m at the end of March 2010 and that figure is likely to fall to below £36m plus any retained earnings in

the past six months. That indicates that the shares are trading at a discount to net assets of around 30%.

The third tranche of land at Plymouth Airport, which Sutton Harbour still manages and remains part of the group, will be sold later this year and this will release a significant contribution to profit. It underpins the £3.15m profit forecast for 2010-11.

The exact position will become clearer when Sutton Harbour announces its interims on 15 December.

dividends

CSF promises to pay out one-third of earnings

Data centre builder and operator

www.csf-group.com

Dividend

Malaysia-based **CSF** intends to build additional data centres in Malaysia and the surrounding countries but it has a specific dividend policy of distributing one-third of earnings to its shareholders each year. These earnings include any gains on the sale and leaseback of data centre properties. The plan is to pay one dividend each year.

CSF floated on AIM in March 2010, when it raised £25m net at 55p a share, so it has not yet paid a dividend as a quoted company. The first dividend is expected to be 1.7p a share, rising to 2.2p a share in 2011-12.

The cash raised at the time of the flotation can be used to double data centre capacity and CSF will also raise cash from sale and leaseback deals. The sale and leaseback of its first data centre generated £10.1m earlier this year and enabled CSF to pay off a £9.1m loan. The sale and leaseback and the flotation proceeds have left CSF with net cash of £26m, including restricted cash of £1.24m, at the end of September 2010.

CSF's earnings are forecast to grow steadily and this means that it can pursue a progressive dividend policy without holding back its expansion plans.

Business

CSF started out designing and constructing data centres for clients and it has been involved in the design and fit-out of more than 200 since it commenced trading in 1991. CX1, the company's first data centre, was built in 2003. The second, CX2,

CSF GROUP (CSFG)	
Price	69p
Market cap £m	110.4
Historical yield	nil
Prospective yield	2.5%

was completed in 2009 and is 72% occupied. The cash raised this year will help CSF to grow faster. CSF has four data centres in operation and CX5 is being built. The first phase will be completed by the end of 2011. One-third of capacity is already pre-sold, with contracts tending to last for three years.

CSF already holds a strong position in Malaysia, with more than one-third of the market, and it has 6% of the southeast Asia market. The company's fourth data centre is a joint venture in Vietnam. CSF plans to open a data centre in Singapore and is considering Thailand and Indonesia. There is still scope to grow in Malaysia and the government has offered CSF a site in Terengganu for the development of a 20,000 square foot data centre. The Malaysian government would take 30% of the space.

Total income jumped from £6.58m to £12.7m in the six months to September 2010, thanks to a £4.59m gain on the sale and leaseback of CX1. Underlying revenues improved from £6.58m to £8.08m. Pre-tax profit jumped from £942,000 to £6.65m but, even stripping out the disposal gain, the underlying profit more than doubled.

The shares are trading on 13 times prospective earnings for 2010-11, falling to 10 the following year.

Dividend news

Photonic products supplier **Gooch & Housego** has returned to the dividend list with a 2p a share final dividend. G&H reported a near doubled profit of £6m in the year to September 2010 and net debt was cut by 58% to £5.2m. The trading recovery and strong cash generation have given the board confidence to pay its first dividend for two years. G&H's products go into lasers and other capital goods and it is demand for this equipment from manufacturers of electronic consumer goods, such as iPads and iPods, that has led the company's recovery.

First Property Group edged up its interim dividend even though its pre-tax profit dipped from £1.56m to £1.32m in the six months to September 2010. The decline was due to its 60%-owned mechanical and electrical maintenance subsidiary falling into loss. Most of the profit comes from the property fund management division, although First Property also owns some properties itself. The interim dividend was increased by 3% to 0.32p a share, which indicates the company's optimism about its future prospects. Cash generation was strong, with net cash of £3.4m at the end of September 2010.

A 2p a share final dividend announced by toys supplier **Character Group** takes the total dividend to 4p a share for the year to August 2010. The dividend is covered more than six times by earnings. After an 18-month hiatus, Character restarted dividend payments the previous year with a 1p a share distribution. Character returned to profit in 2009-10 after it bounced back from the consequences of Woolworths going into administration in the previous period. Brands such as ZhuZhu Pets and Peppa Pig are selling well. Materials and freight cost increases plus the imminent VAT rise make the outlook uncertain.

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expert views

Expert view: The broker

Pharma cash machine

By DR KEITH REDPATH

Alliance Pharma's business is a deceptively simple one: it acquires or licenses rights to established branded pharmaceuticals that have been on the market for many years, and continues to sell them with little or no sales and marketing expense.

The business is readily scalable, as serial acquisitions have shown, and profitable. Generally the brands have been off-patent for many years. The

The portfolio is not dominated by any one major product, although Deltacortril, an oral formulation of the steroid prednisolone used for inflammatory and allergic disorders, accounted for nearly 20% of sales last year. Deltacortril was acquired from Pfizer in 2006 and it has been on the market since 1957. It has a market share of about 50%. Teva launched a generic product on 23 November 2010 and we have adjusted our forecasts for

gross margins of more than 55% and the low operating cost business model results in operating margins of about 30%. The company is very operationally geared and we believe additional products (and revenue) can be added to the business with little increase in operating cost.

Cash generation

Alliance has built the current portfolio predominantly through the use of term loans. However, we believe the company is sufficiently cash-generative that servicing the debt is not an issue. We estimate that the company will generate more than £10m in operating cash flow in each of our forecast years.

Maiden dividends totalling 0.3p a share were paid in the last financial year. We believe this is a demonstration of management's confidence in the future of the company, and we forecast

The average age of Alliance Pharma's portfolio is 37 years

average age of Alliance's portfolio is 37 years and if a generic was to have entered the market, it would have done so by now. The portfolio is generally not actively promoted, thereby keeping costs low.

Promotional resource may be directed in a campaign fashion to brands that management considers will react to such activity. This is outsourced and therefore does not represent a fixed cost. There is no significant R&D expenditure.

We do not believe that the investment community has woken up to the speciality pharmaceutical business model, continuing to position such companies in the 'biotech' bracket. The reality could not be further from the truth. Companies in this sector have recurring revenues, low overhead costs, are profitable and, in several cases, pay dividends. Alliance is such a company.

Acquisitive growth

Over the 12 or so years of Alliance's history it has completed 18 transactions to build its current product range. The portfolio consists of 57 individual products.

Deltacortril accordingly and assumed a one-third share of the UK market.

Of the 57 products in Alliance's portfolio, seven contribute sales greater than £2m per annum.

The key products in the portfolio are often the only drugs available for the

The low operating cost business model results in operating margins of about 30%

indication, with no generic alternative. Consequently we believe the risk of downward price pressure from the National Health Service is low.

A measure of the resilience of the sales of Alliance's products is that on average the portfolio of non-promoted products delivers growth of 3% per annum, according to management analysis.

In addition to the regular sales of drugs from the portfolio, Alliance is a supplier to the UK government of a tablet only referred to as a 'toxicology product'. This requires the servicing of a stockpile on a two-three year cycle for a contract worth up to £5-6m.

The portfolio of products provides

a progressive growth in the dividend.

Alliance Pharma is a profitable company, and we believe a comparison of earnings multiples to be the most appropriate valuation metric: in particular we consider EV/EBITDA to be the best comparator.

Alliance is trading at a discount of more than 25% to the average EV/EBITDA multiples of the comparator group of small pharma companies, and this leads us to the price target of 41p a share.



DR REDPATH is a research director specialising in health care and pharmaceuticals at FinnCap

 feature

Pay increases no longer the norm

AIM directors have shown relative restraint in their pay demands in the past year and non-executive chairmen have led the way, while finance directors have managed to get the best pay rises.

Directors of AIM companies have had to face the harsh realities of the economy over the past couple of years. Some companies have fallen by the wayside and the directors of the others have needed to be realistic in their pay demands.

Directors' Pay on AIM 2010, the annual survey published by Growth Company Investor, shows that pay rises have not been the norm in the past year. In fact, the median level of board pay has fallen from £490,000 in 2009 to just under £461,000 in 2010. It may be that this is more to do with companies reducing the number of directors in order to cut costs rather than pure pay restraint. Even so, 49% of boards were paid less last year and just over one-third of chief executives and finance directors took a pay cut.

The survey covers 1,093 AIM companies and uses all the data on directors' pay that those companies reveal. New AIM rules that have come into force mean that next year even more information will be published.

Nick Britton, head of research at the report's publisher, Vitesse Media, points out that the number of companies on AIM has fallen from 1,392 to 1,235 since the 2009 survey. Many of the companies that left were small and the average size of an AIM company has risen. As larger companies tend to pay more to their directors this could have an effect on the median pay levels, which makes the modest rises for most bosses even more significant.

Non-exec chairmen

There are 352 non-executive chairmen that remain in place from the previous year. Of those, 106 did

not have a pay increase last year and 97 had their pay reduced.

Pay rises do not tell the whole story when it comes to chairmen. The chairman of Coburg received a 2,784% increase in his pay last year but as he started out with annual pay of £208 his 2010 salary of £6,000 is not excessive.

Not all non-executive chairmen had to worry too much about their income, though. There were 25 that earned £100,000 or more. Some of those even had significant pay cuts but remain well remunerated. The chairman of wood treatment technology company Accsys Technologies was paid £337,000, down 2.3% on the year. The company has subsequently had to write off expected payments that had been taken to profit in previous years but are unlikely to be paid.

There are four chairmen who were

Chief executives

Chief executives' median total pay was £190,300 in 2010, barely changed from the £190,000 figure in the 2009 survey. Basic pay showed a decline from £169,000 to £165,000. Bonuses and other benefits increased, although only one in five of the chief executives received a bonus.

There were still some chief executives that got large pay packets. The number making more than £500,000 a year moved up from 56 to 64, while those earning more than £1m a year jumped from five to 14.

Those chief executives that run larger companies generally get higher pay. The median pay below £5m market capitalisation is £130,000, whereas for companies worth more than £200m it is £392,000.

A comparison of the pay of chief executives of profitable and loss-

The median level of board pay has fallen from £490,000 in 2009 to just under £461,000 in 2010

the highest-paid directors in their company but none of these was among the highest-paid chairmen. The chairman of East Balkan Properties was paid the most of these four people at £75,792, which was more than double the previous year's figure. The Sportswinbet chairman was paid £42,000, which is a lot considering that it had closed its online gaming business and fallen into loss – but he was good enough not to take a pay rise. The chairman's pay accounted for 15% of the company's expenses last year.

making companies reveals that it does not seem to make much difference to a chief executive's pay if a company is making money or not and it is making less difference with every year.

In 2010, chief executives of profitable AIM companies were paid a median of £200,897, while the loss-making companies paid £181,677. The pay of the chief executives of profitable companies fell from £216,013 in 2009 yet loss-making companies increased their chief executives' pay from £171,835.

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That means that in 2009 profitable companies paid their chief executive 1.26 times what a loss-making one paid but that ratio has fallen to just over 1.1 times in the past year. In 2007 and 2008, profitable companies paid their chief executive 1.4 times the pay the loss-making ones did, so

Chief executives' median total pay was £190,300 in 2010, barely changed from the £190,000 figure in the 2009 survey

there is a definite downward trend.

It may be that some companies fell from profit to loss in the latest period and that boosted the median for the loss-making chief executives' pay. Even so, that is unlikely to account for relatively large increases in the pay of loss-making company chief executives. They appear less flexible in their pay than the chief executives of profitable companies. The willingness to hold back their pay levels may have helped some chief executives to keep their companies' profitable.

The highest paid chief executive was Raymond Chu, who has subsequently stepped down to a non-executive role at Asian biometrics supplier RCG. Chu was paid a basic salary of £3.8 million. RCG also had the highest-paid board on AIM, absorbing a total of £5.7 million. RCG is a profitable business, though, even if cash flow has not been very good.

Todd Kozel of Kurdistan-focused oil and gas explorer Gulf Keystone Petroleum is the fourth-highest paid AIM chief executive and receives the most pay at a loss-making company – if the fact that property company Conygar Investment, whose chief executive was paid £2.87m, only made a profit because of exceptional gains is ignored.

Kozel's pay almost quadrupled to £1.68m, with most of that in the form of a bonus. Kozel's basic salary has not changed since 2005.

Even though it is losing money, Gulf Keystone has been successful in finding oil in Kurdistan and that has also boosted the share price, making the company one of the largest on AIM. That provides a strong argument that Kozel deserves to receive a significant bonus although

the company is still a long way from generating revenues from its discoveries.

The tenth-highest paid chief executive on AIM was Soumo Bose of loss-making Gasol, which is involved in the liquefaction of natural gas (LNG) in Africa and the sale of the LNG around the world. Admittedly, nearly one-half of his total pay of £1.13m was payment for the termination of his job. A further £408,000 came from share-based payments. Gasol is currently capitalised at around £10m.

There is little difference between the median pay of chief executives of profitable and loss-making companies

Finance directors

Finance directors are there to make sure that the cash comes in and costs are kept under control but they seem particularly good at making sure that they do not lose out in pay terms. The research was started in 2003 and they have never failed to have a pay rise. Median pay has increased by 63.5% over that period – an annualised increase of 7%. In 2010, the median pay rise was more modest, at 4.2%, taking the pay to £139,000, but this was still more than the median pay rise for chief executives.

Chief executives still get more money but the gap in monetary terms has narrowed slightly over the past four years. In 2010, chief executives' median pay is 37% higher than finance directors'. Back in 2007 chief executive pay was 48% higher.

The highest-paid finance director was Rachel Rhodes of London Mining. She was paid nearly £785,000 including bonuses. That is nearly 25% more than Ivan Dittrich, the finance director of Datatec, who was paid £628,000. IT services firm Datatec and former cement manufacturer Prosperity Minerals have both their chief executive and finance director in their respective top five pay lists.

Surprise

Bill Cohen, partner of executive remuneration at report sponsor Deloitte, says he was "quite surprised by the results". He points out that on the Main Market there was a period when pay was held back but bonuses have started shooting ahead again. He reckons that the link between pay and performance is greater on AIM

than on the Main Market and believes AIM companies are "more flexible on how bonuses work".

Cohen warns that the new AIM guidelines on reporting pay could lead to "pay ratcheting" where the remuneration committee of a company looks at the median pay levels and bases their pay awards on that figure. That would be an unwanted consequence of providing additional information.

Directors' Pay on AIM 2010 is available for £295 plus VAT by either calling 0207 250 7039 or emailing samantha.hay@vitessemedia.co.uk.

statistics

Market Performance, Indices and Statistics

AIM SECTOR INFORMATION		
SECTOR NAME	% OF MARKET CAP	% OF COMPANIES
Oil & gas	21.5	9.4
Financials	20.8	23.7
Basic materials	19.4	13.2
Industrials	10.7	18.9
Technology	8.3	10
Consumer services	7.5	12.1
Health care	5.6	5.3
Consumer goods	3.8	5.2
Telecoms	1.6	1.2
Utilities	1	1.1

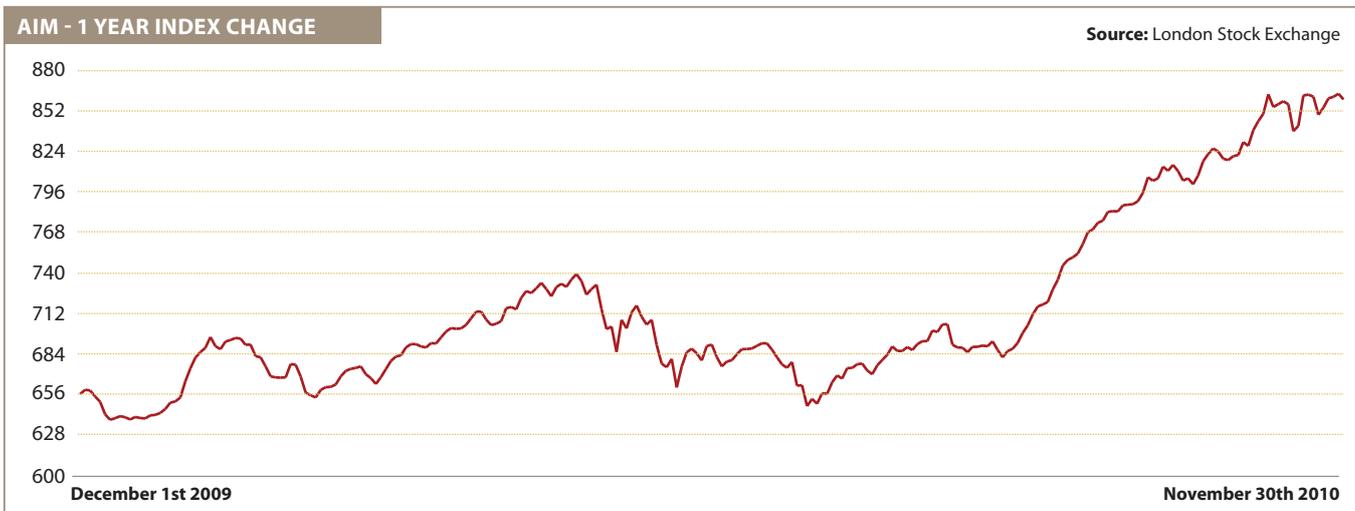
KEY AIM STATISTICS	
Total number of AIM	1,198
Number of nominated advisers	63
Number of market makers	50
Total market cap for all AIM	£67.6bn
Total of new money raised	£69.92bn
Total raised by new issues	£33.94bn
Total raised by secondary issues	£35.98bn
Share turnover value (2010)	£25.23bn
Number of bargains (2010)	3.05bn
Shares traded (2010)	112.44bn
Transfers to the official list	151

FTSE INDICES		
INDEX	PRICE	ONE-YEAR CHANGES % CHANGE
FTSE AIM All-Share	881.88	+33.9
FTSE AIM 50	3481.28	+29.7
FTSE AIM 100	4088.54	+37.3
FTSE Fledgling	4459.55	+12.4
FTSE Small Cap	3060.04	+11.6
FTSE All-Share	2974.74	+9.7
FTSE 100	5745.32	+8.1

COMPANIES BY MARKET CAP	
MARKET CAP	NO.
Under £5m	275
£5m-£10m	167
£10m-£25m	270
£25m-£50m	197
£50m-£100m	125
£100m-£250m	107
£250m+	57

TOP 5 RISERS OVER 30 DAYS			
COMPANY NAME	SECTOR	PRICE (p)	CHANGE (%)
Northwest Investment Group	Financials	160	+611.1
Verdes Management	Financials	1.23	+226.7
Regency Mines	Mining	7.25	+225.8
HaiKe Chemical Group	Chemicals	41	+221.6
Bahamas Petroleum Co	Oil and gas	16.5	+161.9

TOP 5 FALLERS OVER 30 DAYS			
COMPANY NAME	SECTOR	PRICE (p)	CHANGE (%)
Aurum Mining	Mining	2.62	-83.6
European Convergence Properties	Property	€ 0.01	-67.5
ACP Capital	Financials	3	-66.7
Central African Gold	Mining	0.45	-64.7
Amphion Innovations	Financials	3.25	-63.9



Data: Hubinvest Please note - All share prices are the closing prices on the 3rd December 2010, and we cannot accept responsibility for their accuracy.


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finnCap is already ranked as a top-ten AIM adviser and broker and occupies leading positions in several sectors. In technology it is No. 1 ranked by number of AIM clients,

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finnCap works with over 65 corporate clients and raised just over £90m for clients in 2009. It is a Nominated Adviser (NOMAD) for AIM companies and a Corporate Adviser for Plus Markets.

In 2007, private client stockbroker

JM Finn transferred its corporate finance, research and institutional broking business into a new subsidiary, JM Finn Capital Markets (finnCap). The management team and employees of finnCap took a significant equity stake in the business.

In 2010, finnCap employees and non-executive chairman Jon Moulton acquired the outstanding 50% of the company that was previously owned by JM Finn. The company name has changed to finnCap Ltd, in line with the trading name.



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PUBLISHED BY:	Hubinvest Ltd,	Mobile:	07849 669 572
ADDRESS:	1C Beaufort Road, Kingston-upon-Thames, Surrey. KT1 2TH.	EDITOR:	Andrew Hore
TELEPHONE:	020 8549 4253	DATA:	Andrew Hore
		PRODUCTION & DESIGN:	David Piddington

SPONSORSHIP & ADVERTISING editor@aimmicro.com
or telephone 020 8549 4253

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