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AIM JOURNAL

QCA urges action to help AIM companies

"Government must have a policy to direct cash flows into small firms," says Quoted Company Alliance chief executive Tim Ward, be it "through force, encouragement or incentives".

The government clearly sees the banks as one stumbling block, but the small quoted company lobby group boss says there are other areas where a bit of cajolement from Whitehall could be equally as effective.

"Pension funds need to demonstrate they are investing in small caps," Ward says, even going as far as to suggest a small proportion of pension fund money should have to be directed towards the small end of the market.

The attitude of the UK regulator, currently the FSA, in steering private investors away from AIM-quoted firms also needs to be looked at, suggests Ward. "Private client brokers should be allowed to recommend small stocks," he says. "The aim should not be investor protection but investor enablement and not to keep investors away from investing in small firms." This could include better tax incentives, possibly for a new debt/equity instrument to be quoted on an AIM debt market, "anything that will help small firms raise finance."

Ward believes that the government is in listening mode and intends to take advantage of this to change the environment for smaller companies for the better.

Autumn flotation for green firm

Green technology commercialisation firm Novo Energies International (NEI) plans to float on AIM this autumn. Hong Kong-based NEI has worldwide rights, excluding the Americas, for multi-stage hybrid gasification (MSHG) technology, which converts plastic and tyre waste into a synthesis gas (syngas) that is used to generate electricity.

Montreal-based Novo Energies Corporation was granted the worldwide rights to the technology by Colorado-based Precision Pipe and Vessel. The Canadian company evaluated other technologies but felt that MSHG was best because there are no toxic emissions, it produced consistent syngas and it has a low production cost. Novo Energies Corporation kept the rights to the Americas and assigned the rights to the rest of the world to NEI, in which it has a 12.5% stake.

NEI's intention to join AIM was announced when it entered its commercialisation agreement with Novo Energies Corporation in June. Novo Energies Corporation reaffirmed NEI's goal in its latest shareholder update. NEI plans to raise £3m to spend on the first international MSHG plant. Sites in Australia, Thailand and South Africa have been assessed. The company's website is www.novoenergiesint.co.uk.

In this issue

HubInvest publishes AIM Journal

www.hubinvest.com

general news

Investors get taste for DP Poland

DP Poland, the Domino's Pizza master franchise owner in Poland, joined AIM in July and it has proved popular with investors. The company raised £6.5m gross at 50p a share and was valued at £9.9m. The share price reached 69p on 9 August. However, this is a start-up business and investors will need to be patient if they are expecting the same type of profitable growth achieved by former AIM company Domino's Pizza UK & IRL.

DP Poland is very different from its UK counterpart both now and when it originally floated on AIM more than 10 years ago. Domino's Pizza UK was already profitable when it joined AIM in November 1999. The company acquired the master franchise for the UK and Ireland in 1993 but there had been outlets in the UK since 1985, so the underlying business had been operating for 14 years when it floated. That meant that it was able to generate the cash it needed to finance expansion.

This is important to understand when looking at DP Poland. Domino's Pizza UK is a cash-generating machine but that is down to economies of scale.

Switzerland-based Domino's Pizza master franchisee Global Brands has shown it is not as easy as some might think to make the franchise work. Global had branches open when it joined AIM in September 2005 at a placing price of 185p a share. Management problems held back progress and Global has been consistently loss-making. The current share price is 2.75p but management is showing some success in turning the loss-making business around.

DP Poland does have a management team that understands the Polish market. Executive chairman Richard Worthington and marketing director Peter Shaw ran Polish coffee bars operator Coffeeheaven International, which was acquired by Whitbread's subsidiary Costa Coffee at the beginning of 2010 for £36m.

Coffeeheaven probably provides a better indication of the time it could take DP Poland to prosper. Coffeeheaven joined AIM in December 2001 and raised an initial £750,000. More cash was raised later. Coffeeheaven did not move into profit (before share based payments) until the year to March 2007. The operations moved into profit one year earlier but they were not covering corporate overheads.

The Domino's brand might mean that DP Poland could move into profit more quickly than Coffeeheaven but it will still take time. Regional differences need to be taken into account so DP Poland is tweaking the formula in Poland. The menu will be tailored to the Polish market and will include Polish sausage, regional cheeses and local vegetables as well as variations on the standard pizzas.

The strategy is to open at least 50 stores in Poland by 2015. The initial focus will be on Warsaw. Poland's population is two-thirds the size of the UK's.

Alexander David seeks to snare Hoodless Brennan

AIM broker Alexander David Securities Group is in talks to acquire broker Hoodless Brennan, whose merger with broker Astaire fell through because of accounting problems at Astaire's Rowan Dartington subsidiary.

Astaire was offering 0.9403p in cash and 4.4665p of convertible loan notes for each HB share. Astaire's own broker Fairfax IS valued the convertible loan notes at 55p in the pound and the conversion price was to be 6p per Astaire share. The deal valued HB at £3.61m.

Alexander David is based just down the road from HB in London. Both have private client stockbroking activities and HB would take Alexander David into market making.

HB's corporate finance operations were spun off last year and are now known as Allenby Capital. HB still owned 9.9% of Allenby at the time of the Astaire bid and, under certain circumstances, is allowed to increase the stake to 50%.

HB shareholders might prefer cash to shares which would mean a large fundraising. Alexander David also needs to make sure it has enough regulatory capital.

Talks continue for what would be a reverse takeover of Alexander David and any deal is subject to due diligence. At the suspension price of 0.45p a share, Alexander David is valued at £2.25m.

advisers

Busy summer for many AIM brokers and advisers

It has been a busy summer in the AIM broking sector and there is more to come. Brokers are changing management and owners and there is even a new entrant in the form of Mayfair-based **Jendens Securities**, whose employees include Dru Edmonstone.

Belgian financial services firm KBC has sold broker **KBC Peel Hunt** to its staff for £74m. Most of the 136 staff at the broker will have a stake in the firm, which is 21 years old. There has been uncertainty over the ownership of the broker for some time and it should benefit from a more certain future. Staff, led by chief executive Simon Hayes, own 75% of the buyout vehicle and external investors the rest.

Meanwhile, **Astaire**'s future remains uncertain with the requisition of a general meeting in order to obtain votes on proposals to return spare cash to shareholders, force the company to put itself up for sale and remove finance director Chris Roberts from the board. Astaire is still talking to potential investors/buyers of its subsidiary, Astaire Securities.

Former Collins Stewart capital markets boss Paul Compton is taking over as chief executive of WH Ireland from Richard Ford. Compton joins at a time when **WH Ireland** is finding trading tough, with declining revenues and a swing from a profit of £137,000 to a loss of £518,000 in the six months to May 2010.

AIM adviser **Merchant Securities** returned to profit in the year to March 2010 and it has rebranded all of the subsidiaries, including broker John East, under the Merchant Securities name. Lindsay Mair, formerly of Daniel Stewart and Astaire, will become head of UK small cap sales and research in September.

AIM broker **Westhouse** has raised £3.5m from a subscription for a perpetual convertible loan by Bermuda Commercial Bank and it will use the cash to expand its operations in the investment trust, agribusiness, cleantech and technology sectors. Westhouse already had £1.7m in the bank at the end of July 2010 and it still has non-core investments to sell.

First half trading has been difficult but M&A work has picked up since the end of June. The interim figures will be published towards the end of September.

ADVISER CHANGES - JULY 2010

COMPANY	NEW BROKER	OLD BROKER	NEW NOMAD	OLD NOMAD	DATE
Geong International	Evolution/Evolution China	Seymour Pierce	Evolution	Seymour Pierce	01/07/2010
Highams Systems Services	Seymour Pierce	Charles Stanley	Seymour Pierce	Charles Stanley	01/07/2010
Cyprotex	Singer	Execution Noble	Singer	Execution Noble	02/07/2010
Newmark Security	Seymour Pierce	Astaire	Seymour Pierce	Seymour Pierce	06/07/2010
Highland Gold Mining	Matrix/JPMorgan Cazenove	JPMorgan Cazenove	JPMorgan Cazenove	JPMorgan Cazenove	06/07/2010
Scientific Digital Imaging	FinnCap	Astaire	FinnCap	Grant Thornton	07/07/2010
Probability	Daniel Stewart	Collins Stewart	Daniel Stewart	Collins Stewart	07/07/2010
China Private Equity Inv.	Shore/SVS	Shore	Shore	Shore	08/07/2010
UKR	Metropol/WH Ireland	WH Ireland	WH Ireland	WH Ireland	09/07/2010
Charles Street Capital	Allenby	ZAI/Rivington Street	Allenby	ZAI	12/07/2010
Ipso Ventures	Allenby	Ambrian/Old Park Lane	Allenby	Ambrian	12/07/2010
Indian Energy	Execution Noble/Arden	Arden	Arden	Arden	13/07/2010
Coms	XCAP	Astaire	Astaire	Astaire	13/07/2010
Media Corporation	XCAP/Astaire	Astaire	Astaire	Astaire	14/07/2010
Nyota Minerals	Mirabaud/Ocean	Ocean	Ambrian	Anbrian	14/07/2010
GoIndustry-DoveBid	WH Ireland	Cenkos	WH Ireland	Cenkos	15/07/2010
IQ Holdings	Rivington Street	Rivington Street	Libertas	Grant Thornton	16/07/2010
Obtala Resources	ZAI	Fox-Davies	ZAI	ZAI	20/07/2010
Acta	Altium	Charles Stanley	Altium	Charles Stanley	20/07/2010
Amino Technologies	FinnCap	KBC Peel Hunt	FinnCap	KBC Peel Hunt	21/07/2010
Argo Real Estate Opportunities	FinnCap	Oriel	FinnCap	Oriel	22/07/2010
ToLuna	Numis/Cenkos	Cenkos	Merchant Securities	Merchant Securities	23/07/2010
Avingtrans	FinnCap	KBC Peel Hunt	FinnCap	KBC Peel Hunt	26/07/2010
Connemara Mining	Optiva/Smith & Williamson	Smith & Williamson	Smith & Williamson	Smith & Williamson	26/07/2010
Evolve Capital	Allenby	Fairfax IS	Allenby	Fairfax IS	26/07/2010
Digital Marketing Group	FinnCap	Cenkos	FinnCap	Cenkos	27/07/2010
Conroy Diamonds & Gold	XCAP	City Capital	Merchant Securities	Merchant Securities	27/07/2010
Rapid Realisations Fund	Singer	Cenkos	Grant Thornton	Grant Thornton	28/07/2010
Avisen	Strand Hanson	Brewin Dolphin	Strand Hanson	Brewin Dolphin	29/07/2010
Accumuli	Zeus	Arbuthnot	Zeus	Arbuthnot	30/07/2010

company news

Australian tax changes will not dent prospects for Skywest Airlines

Airline *www.skywest.com.sg*

Skywest Airlines generates more than half of its revenues from flying workers to mines in Australia, so the share price was hammered during May because of the proposed mining super tax in Australia. That was knocked on the head when Prime Minister Kevin Rudd was deposed in June but the share price has not fully recovered.

The Mineral Resource Rent Tax has replaced the previous proposals. There is still uncertainty about the details of the MRRT, which would only apply to iron ore and coal resources, but it should not prevent investment in new mines. Activity levels drive business for Skywest and they could have been severely reduced by the previous proposals. As it is, a number of iron ore projects could come into production over the next few years.

Skywest also generates revenues

from holiday routes to Bali and parts of Western Australia. The freight business is being built up as well with medical supplies an area where revenues could grow.

A reduction in capacity and an increase in passenger kilometres travelled helped improve the load factor from 51.6% to 54.3% in the year to June 2010. Charter services increased 9% to 2,835 over the year.

Skywest has leased an Airbus A320 for three years at a rate of

SKYWEST AIRLINES LTD (SKYW)	18.5p		
12 MONTH CHANGE %	+184.6	MARKET CAP £M	36.9

$190,000 a month. This is the company's seventeenth plane but it is much larger than the others, which are Fokker 100 and Fokker 50 jets. During the week it will enable Skywest to handle charters that require more seat numbers and at the weekend it will be used for holiday and leisure flights.

Skywest joined the ASX last December and it hopes that this will improve liquidity. Executive chairman Jeff Chatfield believes that Australian institutions might start to take a closer interest in the company when Skywest publishes its full-year figures. House broker WH Ireland forecasts earnings per share of more than 3p for the year to June 2010.

Kopane agrees to merger with Firestone

Diamonds miner *www.firestonediamonds.com*

Firestone Diamonds has launched a recommended bid for Kopane Diamonds. Kopane's main asset is the Liqhobong diamond project in Lesotho, which is thought to be the third largest undeveloped kimberlite resource in terms of carats. Firestone believes that it could produce more than 1m carats a year from the enlarged portfolio of diamond interests.

Firestone is offering 0.4657 of one of its shares for each Kopane share. Based on a Firestone share price of 36.5p, the bid values Kopane at 17p a share, or £52.7m. Firestone

FIRESTONE DIAMONDS (FDI)	26.75p		
12 MONTH CHANGE %	-2.7	MARKET CAP £M	34.2

shareholders will own roughly 52% of the enlarged company.

Liqhobong, which is 75% owned by Kopane and 25% owned by the Lesotho government, is around 20 times larger than Firestone's BK11 mine in the Orapa region of Botswana where production recently commenced. BK11 was in production within nine months of the decision being made. Firestone believes that it can use the cash generated from BK11 to develop Liqhobong.

Liqhobong's resource contains 31m carats. There have been 350,000 carats produced but production was stopped in 2008 because of the weak diamond price. The diamond price is recovering and it is returning to 2008 levels. A definitive feasibility study is being undertaken and the initial indication is that the main pipe will support a long-life mining operation. Next year small-scale production should recommence at Liqhobong.

company news

Ebiquity broadens its media reach through Xtreme Information acquisition

Media monitoring and analytics *www.ebiquity.com*

Media monitoring and analytics business **Ebiquity** has increased its size, widened its range of services and broadened it geographic coverage through the purchase of Xtreme Information Systems.

Ebiquity enables advertisers to analyse whether or not they are getting value for money from their spending. It reported an improved profit in the year to April 2010 thanks to a strong performance from its analytics business and a 17-day contribution from media intelligence group Xtreme.

Revenues grew from £18.4m to £21.2m in the year to April 2010. Underlying profit rose from £2.11m to £2.5m.

Ebiquity acquired Xtreme for £17.9m in cash, shares and convertible loan notes. Private equity firm Veronis Suhler Stevenson took a 24.7% stake in Ebiquity via the acquisition. Ebiquity also bought the remaining 50% of its existing subsidiary in Germany for £800,000 in cash and shares.

Edison Investment Research believes Ebiquity can grow at 15% a year

Xtreme reported revenues of £18m and EBITDA of £2.3m in 2009. Around 90% of the revenues are based on subscriptions. The integration of the business is well underway and this will yield cost savings.

The enlarged group's business covers 70 countries. Group revenues are expected to reach around £42m in the year to April 2011. Analytics will account for two-fifths of those revenues, with the rest coming from advertising and editorial monitoring. A profit of £4.2m is forecast for 2010-11 but earnings per share will be flat at 5.9p a share.

EBIQUITY (EBQ)	63.5p		
12 MONTH CHANGE %	+16.5	MARKET CAP £M	35.5

A share placing raised £770,000 at 56p a share at the time of the recent acquisitions. Net debt was £2.4m at the end of April 2010, although that excludes the £9.4m of convertible loan notes.

Edison Investment Research believes that Ebiquity can grow at 15% a year over the medium term.

Recovery gains pace at Gooch & Housego

Optical components manufacturer *www.goochandhousego.com*

Five weeks after releasing its interim figures optical components supplier **Gooch & Housego** revealed that trading is even better than it said in its interim statement. A sharp recovery in demand for Q-switches had already helped profits recover in the six months to March 2010 and next year G&H could get back to the peak profitability of £6.5m reported in 2006-07.

The order book was worth £19.8m at the end of the half year and it had risen to £22.1m by the end of June. Aerospace and defence sectors are particularly strong.

G&H has managed to increase its capacity so it is better placed to fulfil those orders. Additional staff are being employed and some lower-margin work is being outsourced so that better-margin work can be done in-house.

GOOCH & HOUSEGO (GHH)	287.5p		
12 MONTH CHANGE %	+177.8	MARKET CAP £M	55.4

Q-switch demand is back to past levels and G&H has been taking on more people at its main factory, where employee levels are back to pre-rationalisation levels. Revenues grew from £18.8m to £20.4m at the interim stage. The underlying interim profit jumped from £909,000 to £2.2m as overheads were cut. Underlying earnings per share more than doubled to 7.9p.

Analysts forecast a recovery in underlying full-year profit from £3.1m to more than £5m in 2009-10, with a further rise to more than £6m the following year. There could even be a return to dividend payments this year although the need to invest in capacity will have to be taken into account when the board makes the decision.

Net debt nearly halved to £9.3m at the end of March 2010. It could come down sharply again this year but it will depend on the level of capital expenditure needed to further increase capacity in order to satisfy the continuing growth in orders.

company news

Strong order book points to long-term growth for DQ Entertainment

Animated programming producer *www.dqentertainment.com*

India-based **DQ Entertainment** has continued to grow even in the tough times and its strong order book suggests that the animated programming producer could grow even faster in the next few years. Despite that, DQE's stake in its Indian subsidiary is worth more than its own market value.

DQE's order book is worth $136m and stretches over a period of up to 30 months. In the year to March 2010, DQE increased its revenues by 14% to $36.8m and pre-tax profit by one-quarter to $6.46m. Revenues grew even faster in rupee terms. The shares are trading on 12 times historical earnings.

DQE specialises in animations that include established characters with a ready-made audience rather than new, and therefore inherently risky, characters and properties. The characters include Lassie, Casper the Friendly Ghost, Charlie Chaplin and Little Prince. Some, such as Iron Man are co-productions with the rights owners, while others are owned 100% in perpetuity by DQE. The latter includes the Jungle Book and Peter Pan animated series. DQE also undertakes some third-party animation – the latest is forthcoming feature film *The Prodigies*.

DQE's order book is worth $136m and stretches over 30 months

DQE raises more than 90% of the budgets of the animations through pre-sales. It has raised €9m in pre-sales for its animated series of Iron Man. DQE's library comprises 450 hours of animated programmes and it also generates income from merchandising rights. DQE has a strong balance sheet and had net cash of $21.6m at the end of March 2010.

X DQ ENTERTAINMENT (DQE)			115p
12 MONTH CHANGE %	+32.9	MARKET CAP £M	41.4

DQE floated its Indian subsidiary, DQ Entertainment (International) Ltd, on the Bombay Stock Exchange on 29 March 2010. The flotation raised rupees 1,530m (£22.75m) at rupees 80 a share (119p) a share, and this offering was heavily oversubscribed. The closing price on 29 March was rupees 118.55 a share, equivalent to 161p a share. The share price has fallen back but is still trading at around the closing price on the first day's trading. DQE's 75% stake in its Indian subsidiary is worth just under £100m, which is more than the market value of DQE itself.

Port deal boosts Eredene's long-term prospects

Indian infrastructure investments *www.eredene.com*

Indian infrastructure investor **Eredene Capital** has four revenue-generating projects and it has just won a highly lucrative tender for a new container terminal.

Eredene is part of the successful consortium that tendered for the container terminal at Ennore Port, which is near to Chennai. The project will cost $325m (£207m) and Eredene will contribute around £23m of that over a 48-month period. The life of the licence is 30 years and it will take 36 months to construct the terminal.

EREDENE CAPITAL (ERE)			20p
12 MONTH CHANGE %	-3.8	MARKET CAP £M	56.1

Eredene has 22% of the consortium and because this is less than 25% it means that it can sell its stake whenever it wants. That will make it much easier to unlock value and generate cash to reinvest in other projects.

The Ennore Port terminal should move into profit in 2017-18 and could be generating post-tax profit of £34.1m by 2019-20. Eredene's share would be £7.5m, making the stake highly valuable.

Eredene's stated NAV was 23p a share at the end of March 2010. This was before the winning of the tender and the acquisition of a 8.2% stake in port and marine services provider Ocean Sparkle. Ocean Sparkle might eventually float on the Bombay Stock Exchange.

Eredene had net cash of £21.8m at the end of March 2010. Eredene raised £7m during the last year and if it needs extra cash it will raise it from another placing.

dividends

IDS passes test as AIM growth success

Diagnostic testing *www.idsplc.com*

Dividend

Diagnostic testing kits producer **Immunodiagnostic Systems Holdings** increased its dividend by 21% to 2p a share in the year to March 2010. Although the yield on the shares is not high there is scope for further significant increases in the dividend payment. The dividend is more than 14 times covered by earnings per share. Earnings are forecast to grow rapidly over the next few years and they could double by 2012-13 and there is no reason why the dividend could not increase as fast, or even faster. This year's dividend costs less than £600,000. Cash generation is strong and the company's cash pile could be significant in the next few years even if the dividend payment is much higher. A 3p a share dividend is forecast for 2010-11, rising to 4p a share in 2011-12.

Business

IDS joined AIM on 24 December 2004 at a placing price of 51p a share. That means that the investors in the flotation have enjoyed an increase in their investment of more than 1,300%.

The basis for this growth is vitamin D testing, which generates around three-fifths of IDS's revenues. Vitamin D is important in the development of bones and cells so if a patient has low levels of vitamin D they could become ill or suffer bone diseases, such as osteoporosis. There is increasing awareness of vitamin D deficiency and demand for tests continues to grow. The main fear is more competition in the vitamin D market. IDS is adding additional tests in order to broaden its range.

IMMUNODIAGNOSTIC SYSTEMS HOLDINGS (IDH)	
Price	720p
Market cap £m	200.9
Historical yield	0.3%
Prospective yield	0.4%

Longer-term growth is going to come from the automation of testing through the IDS-iSYS system. IDS will make money from selling the machines and regular revenues from consumables. The system can handle up to 120 samples at one time. So far, 91 of these machines have been built and manufacturing capacity has been increased to 24 a month.

IDS has made strong progress in the past year even though the US approvals for the IDS-iSYS instrument were delayed until July. Revenues grew 49% to £37.2m in the year to March 2010. Pre-tax profit more than doubled from £4.78m to £11m.

Net debt was £6m at the end of March 2010. Cash generation is expected to be strong and IDS should be cash positive by March 2011 and there could be net cash of more than £20m by March 2012.

It may take until the second half of this financial year before there are significant sales of IDS-iSYS in the US. House broker Brewin Dolphin forecasts a further jump in profit to £16m in 2010-11, and then to £19.3m the following year.

Roger Duggan is moving from chief executive to head business development and Ian Cookson will take over Duggan's former role. Growth will come from new products and a wider geographic spread of sales.

Dividend news

Vimto owner **Nichols** increased its interim dividend by 10% to 4.45p a share after it reported a 39% increase in pre-tax profit to £6.01m in the six months to June 2010. Nichols grew sales of its soft drinks in the UK by 19.3% compared with market growth of 5.1%. The launch of Cherry Vimto is boosting sales. International sales grew by 39% but this was helped by the earlier timing of Ramadan, which meant that Vimto sales in the Middle East were brought forward. A total dividend of 13.4p a share is forecast for this year, which is likely to be twice covered by earnings. The prospective yield is 3%.

Asset management performance software provider **Statpro** grew revenues 7% to £16.6m in the first half of 2010, while underlying profit edged up from £3.19m to £3.36m. The interim dividend rose 17% to 0.7p a share. The new Revolution portfolio analysis software is being beta tested. Statpro capitalised £1.4m for its development and expensed a further £1m. This spending is set to increase. House broker Cenkos believes Revolution will make a profit contribution by 2013. The broker forecasts flat underlying profits of £6.9m in 2010, rising to £8m in 2011. A full-year dividend of 2.4p a share is forecast giving a yield of just over 2%.

IT services firm **Maxima** reported a slump in adjusted pre-tax profit from £7.1m to £4.9m in the year to May 2010. Maxima reduced its total dividend from 4.5p to 3p a share, which is in line with the drop in profit and provides a yield of 3.6%. The dividend is covered nearly 4.5 times by underlying earnings. Analysts forecast a profit of £5.1m for 2010-11, which leaves little scope for an increase in the dividend unless the cover is reduced.

expert views

Expert view: The broker

Smaller E&P companies provide upside potential

By WILLIAM ARNSTEIN

Following a strong recovery during the past two years valuations in the oil and gas exploration and production (E&P) sector now look relatively stretched. As such, we initiate coverage of the sector with a neutral rating but differentiate our view favouring smaller caps to the larger listed E&P companies.

While the sector as a whole has done well the larger-cap E&P companies now trade at or close to record highs, benefiting from M&A activity, increased risk tolerance, exploration success and continued disillusionment with the integrated oil companies. In addition, these stocks were able to leverage reserves and production to refinance earlier and on relatively attractive terms.

In contrast, some of the smaller E&P companies suffered substantial dilution, although few went out of business despite the brutal impact of the credit crunch. This is in part reflected in the more flexible than expected business models and the short duration of the crisis. A more sustained period of lower oil prices and a lack of financing would have caused many more casualties.

Our coverage universe as a whole has emerged well from the crisis with business models effectively intact. Only one company (fully listed Salamander Energy) avoided issuing new equity, although fully listed Premier deserves credit for issuing equity opportunistically to acquire the assets of Oilexco out of administration. All have refinanced or secured new debt facilities and as such we see no need for new financing except in response to successful exploration and appraisal.

Macro view

We set our macro assumptions based on the futures curve for oil prices and UK gas prices. Oil prices are expected to rise sharply in the next few years before slowing to 2% year-on-year growth per annum. This effectively implies a real $85/bbl oil price.

Gas prices remain pretty weak but have recovered from lows. Prices are expected to recover strongly over the next two years, with longer-term growth about twice that of oil prices. That suggests a gas price of $7.90/mcf in 2012. Because of the lack of data further out the curve, we align gas price growth with that of oil.

Our two favoured AIM-quoted E&P companies are Aurelian Oil & Gas and Northern Petroleum.

AIM favourites

Our two favoured AIM E&P companies are Aurelian Oil & Gas and Northern Petroleum. Aurelian and Northern are both trading at a discount to core NAV.

Core NAV in itself only gives us a base valuation, and trading at a discount provides a strong value indicator. However, focusing on core NAV tends to penalise companies with discoveries under appraisal and significant exploration potential. As such, total NAV gives a fairer benchmark across the group. This shows that Northern is the cheapest. However the discount is partly explained by a lack of exploration activity and development delays in the Netherlands.

Building on this we consider the unrisked values – ie, what would the company be worth if every opportunity targeted is successful. In reality this is unlikely as outcomes rarely come in line with pre-drill expectations and it takes time to fully de-risk a prospect as it progresses from discovery to appraisal and then to development and production. In addition, it does not take into account how priorities change, exploration potential not ready for drilling, follow on potential and financing (farm-outs lower the upside). Putting these issues aside shows that Aurelian offers the highest upside.

Aurelian has secured funding for a multi-well programme targeting a large tight gas field in central Poland and high-risk, high-impact exploration prospects in southern Poland and Slovakia. While the stock has done well following a restructuring, it remains on a discount to core NAV of 56.8p a share despite having the largest unrisked upside. We have a 65p price target.

Following a disappointing 12 months for Northern that have seen development projects and drilling plans delayed, investor sentiment is now at rock bottom. The UK assets are for sale and we expect future exploration activities to focus on the Netherlands, Italy and French Guiana. The shares are trading well below core NAV of 102.6p a share and a clear value play has emerged. Investors should look to buy ahead of a recovery. A strong balance sheet and attractive acreage positions provide the means and the opportunity to regain lost ground.

WILLIAM ARNSTEIN is a research director at FinnCap.

feature

AIM's Chinese successes

Chinese companies moving from AIM to the Hong Kong Stock Exchange is a reflection of the junior market's success.

Negative noises have been made about Chinese companies switching from AIM to the Hong Kong Stock Exchange (HKEx) but this misses the important point of how successful these companies have been on AIM. If there is a market that should come under scrutiny when it comes to Chinese companies leaving London then it is the Main Market.

Cement manufacturer West China Cement (WCC) and pharmaceuticals supplier China Medical System Holdings (CMS) are both on the brink of making the move to a HKEx listing. These companies have reached a point where they need to decide what market will be best for them. It is not surprising that a local market where investors have greater knowledge of the business and their customers is attractive.

These companies would not have been able to float on the HKEx or another regulated market at the point they joined AIM. What could be a better affirmation of the success of AIM than a company using the junior market to grow big enough to switch to a regulated exchange?

Tim Metcalfe, co-head of corporate finance at AIM adviser Westhouse Securities, says that he tells clients that they can use AIM as a stepping stone to a regulated market. He is still seeing Chinese companies that are keen to quote on AIM.

Success stories

WCC had one cement plant on flotation in December 2006, when it raised £22m at 105p a share. Joining AIM helped WCC to finance its growth and build new plants but it also gave it an improved standing in its market.

The WCC share price has risen to 695p in less than four years. There will be a 50-for-one share split at the time of the HKEx listing as well as a global offer. The offer price range is HK$1.21-HK$1.69 a share. At the middle of the range this offer will raise $1.0 9bn (around £89m) to help finance expansion of capacity and the repayment of loans.

WCC is more than happy to acknowledge the help it has received from AIM. Chairman and chief executive Zhang Jimin praised AIM in a press release for the fundraising. "AIM has given West China Cement an excellent platform for our growth from a 1.5m ton cement company into one of the largest producers in Shaanxi Province with capacity of over 12.5m tons by early 2011," he said. "Although we are sad to be leaving AIM, we are glad that our shareholders are willing to follow us to Hong Kong to pursue our growth opportunities in western China."

WCC is not moving because it was unhappy but because of a promise it made when it entered into a $60m loan facility with warrants in May 2008. Part of the deal was a promise to relist on a recognised stock exchange within 30 months – by the end of 2010.

WCC always said it would take into account the views of its investors when making the decision on moving markets. One of its choices could have been a move to the Main Market in London but the board decided against this.

CMS joined AIM on 26 June 2007 so it has spent just over three years on AIM. At that time it raised £10m at 138p a share (equivalent to 6.9p after the 20-for-one share split in June 2010) and was valued at £65.2m.

CMS is currently valued at £373m at 40p a share. That is after the demerger of Healthlink at the end of 2009. Shareholders in CMS could choose to take one Healthlink share for each CMS share they owned or a cash alternative of 23.2 cents a share (14.5p a share, or 0.725p a share post-share split).

That means that an investor in the original flotation could have posted a 490% gain in little more than three years.

> There are even signs that more Chinese companies are considering floating on AIM

Cost of AIM

There are companies, such as orange grower Asian Citrus and biometrics technology supplier RCG, that have gained a HKEx listing but kept their AIM quotation. This is relatively costly and causes additional work for the company because of differing regulations. AIM is just as rigorous as many of the regulated exchanges so it is not a question of complying with a listing and having to do little more to comply with AIM regulations.

That is why many companies do not continue with a quotation on

feature

AIM when they obtain a listing. Although solar wafer company Renesola is not moving to the HKEx it is asking shareholders to vote to cancel its AIM quotation so that it can concentrate on its New York Stock Exchange listing. Renesola joined AIM in August 2006 and subsequently obtained a listing of its ADSs on the NYSE in January 2008. The company says that an increasing amount of the trading is on the NYSE and it will save a significant sum of money by dropping the AIM quotation.

Fashion

A lot of Chinese companies have left AIM and not all of them have as good a record as the likes of WCC and CMS. Many have not even moved to another market.

There tend to be fashions on all junior markets. For example, there were a lot of oil and gas companies that floated on the USM when it started because of the boom in the North Sea.

AIM has certainly been a market where fashion has played a big part, whether it relates to a sector such as mining or a more niche area such as personal insolvency and IVAs. The latter is a good example of a sector that boomed and investors were keen to get involved but many of the companies are no longer even quoted.

China was effectively a fashion in the middle of this decade. Investors understood that China was growing rapidly and wanted exposure. Some of the early valuations were a bit racy to say the least. The quality of the companies varied and too many floated at once. Some of these companies never raised the amounts of cash that they wanted at the time of their flotation but still joined AIM in order to raise it later. That did not always prove possible.

A lot of the Chinese companies that have left AIM were very small. It is difficult enough being a small UK company on AIM but there are additional costs for overseas companies. It was not economic for them to continue with the quotation.

> China was effectively an investment fashion for AIM

That has meant that there has been negative sentiment towards all Chinese companies.

Generally, the larger, more soundly based Chinese companies have been successful. WCC started trading in 1977 and the current chief executive, Zhang Jimin, took over the running of the business in 1989 – 17 years before the flotation.

Of course, there are exceptions. China Real Estate Opportunities is a relatively large company but its share price has declined and in June the renamed Treasury China Trust chose to switch to the Singapore market. In some ways CREO was part of two fashions. When it floated investors were interested in Chinese companies and overseas-focused property companies. This interest waned in subsequent years.

New entrants

Even though the fashion has ended, there are Chinese companies considering floating on AIM. They are likely to be fewer in number but they should generally be of better quality.

Asia Ceramics plans to join on 25 August. The company distributes ceramic wall and floor tiles, and other home improvement products to the domestic Chinese market. It will be valued at £6.81m at an introduction price of 66p a share. Chief executive Dr Dingxin Pu owns 73.4% of the company.

MiLOC Group is the holding company of a traditional Chinese medicine business launched in 2009. The focus of the business will be developing and selling traditional medicines and it also wants to develop clinics and hospitals in China. There is no indication of a valuation or how much MiLOC wants to raise but it is due to join AIM on 24 August.

It could be argued that these companies are relatively small so they do not have the same profile as the more successful Chinese companies. Hopefully, they will prosper. The fact that Asia Ceramics will be so tightly held is certainly a worry, though.

Ultimately, no one market can fulfil the needs of every company. Some may only provide what the company needs for a certain time until it matures. AIM has helped to develop a number of Chinese companies and there is no shame that they want to move on.

It is not all positive. AIM certainly has its problems and liquidity is probably the most significant of these. Even the more successful Chinese companies have had problems stimulating trading in their shares at some times.

> These companies would not have been able to float on the HKEx or another regulated market

Macau Property Opportunities Fund decided to switch from AIM to the Main Market in London rather than a local market but this is unusual. The London Stock Exchange should look into why other China-focused companies are not moving from AIM to the Main Market rather than to other regulated markets.

statistics

Market Performance, Indices and Statistics

AIM SECTOR INFORMATION

SECTOR NAME	% OF MARKET CAP	% OF COMPANIES
Financials	24.8	24.2
Oil & gas	19.9	9.1
Basic materials	18.3	13
Industrials	11.3	18.9
Technology	7.9	10
Consumer services	7.2	11.8
Health care	4.2	0.5
Consumer goods	3.9	5.1
Telecoms	1.6	1.4
Utilities	1	1.1

FTSE INDICES

ONE-YEAR CHANGES

INDEX	PRICE	% CHANGE
FTSE AIM All-Share	685.68	+27.2
FTSE AIM 50	2824.01	+26.6
FTSE AIM 100	3124.39	+28.8
FTSE Fledgling	4047.35	+15.5
FTSE Small Cap	2782.43	+17.3
FTSE All-Share	2715.36	+15.0
FTSE 100	5258.02	+13.5

COMPANIES BY MARKET CAP

MARKET CAP	NO.
Under £5m	221
£5m-£10m	189
£10m-£25m	273
£25m-£50m	178
£50m-£100m	125
£100m-£250m	99
£250m+	50

KEY AIM STATISTICS

Total number of AIM	1,235
Number of nominated advisers	62
Number of market makers	49
Total market cap for all AIM	£58.89bn
Total of new money raised	£68.14
Total raised by new issues	£33.46
Total raised by secondary issues	£34.68bn
Share turnover value (2010)	£14.46bn
Number of bargains (2010)	1.67bn
Shares traded (2010)	70.37bn
Transfers to the official list	146

TOP 5 RISERS OVER 30 DAYS

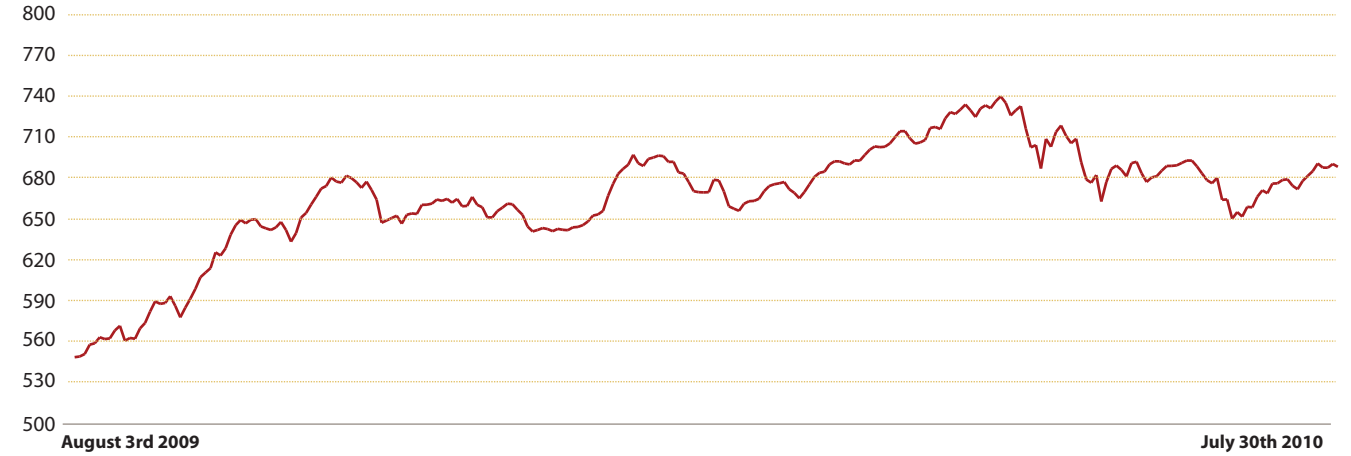
COMPANY NAME	SECTOR	PRICE (p)	CHANGE (%)
Weather Lottery	Leisure	2.375	+458.8
Petro Matad	Oil and gas	144	+242.9
Leo Insurance Services	Shell	4.12	+175
Karelian Diamond Resources	Mining	3	+161.9
Northacre	Property	72	+118.2

TOP 5 FALLERS OVER 30 DAYS

COMPANY NAME	SECTOR	PRICE (p)	CHANGE (%)
Deo Petroleum	Oil and gas	30	-62
Avisen	Software	3.75	-58.3
IQ Holdings	Shell	0.042	-53.3
Falkland Oil and Gas	Oil and gas	123.25	-49.5
MDM Engineering	Support services	90	-49.3

AIM - 1 YEAR INDEX CHANGE

Source: London Stock Exchange



Data: Hubinvest Please note - All share prices are the closing prices on the 30th July 2010, and we cannot accept responsibility for their accuracy.

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finnCap

finnCap is a client focused institutional broker and corporate advisor, with a strong track record in advising and raising capital, providing research and after-market care for both growing and established smaller companies. The institutional broking team provides a dedicated, bespoke agency broking service to fund managers and private client brokers.

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, and no 2 in life sciences. finnCap's 45-strong team has established leading positions in the small cap consumer, industrials, insurance, support services, financials and mining sectors. The finnCap research team was shortlisted at the 2009 AIM awards.

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 August 2007, private client stockbroker JM Finn transferred its corporate finance, research and institutional broking business into a new subsidiary, JMFinn Capital Markets (finnCap). The management team and employees of finnCap took a significant equity stake in the business.

In August 2010, finnCap employees and 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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