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AIM Bulletin INSIGHT

Stuttard wants shorting disclosure rules

Marcus Stuttard, the new chief of AIM, welcomes hedge fund activity on the junior market but believes the disclosure rules on short-selling should also apply to AIM stocks.

Stuttard, who became the new chief of the AIM market following the surprise departure of the previous head Martin Graham, told AIM Bulletin Insight that hedge funds have been good supporters of AIM and did not want to see them banned.

But he wants short-selling disclosure rules that apply to the main market to also apply to AIM. At present, any main market short position over 3% has to be revealed.

The 39-year-old also admitted that liquidity has been an issue on AIM but said there are initiatives in place to address the problem

The recent changes in the tax regimes, such as CGT, have hit the market but Stuttard believes that investors should make investments based on the merits of individual companies and not on tax breaks.

Stuttard, who has spent 15 years at the LSE, the last three as deputy head of AIM, says AIM's recent underperformance is due to the general global conditions, which have affected all markets.

He also blames the tough conditions for the recent rise in the number of companies delisting from AIM but adds cancellations are just a natural feature of a public market, not a specific trend on the junior market.

The one part of AIM that has impressed in recent months is the secondary market. Stuttard says despite the tough market conditions, it has seen £670m raised by AIM companies so far in 2009. He also predicts an uptick in IPOs by the end of the year and the beginning of next year.

The full interview is on page 3.

Max looks to recreate Leslau magic

Max Property is set to be AIM's first major IPO this year, but the listing of the distressed property investor has already raised eyebrows over the scale of fees involved for Prestbury Investments, one of its principal backers.

Prestbury, the vehicle of property industry and AIM company veteran, Nick Leslau, is set to pull in £18.75m in fees as apart of a 7½ year deal to advise Max on where to invest the £200m it raises.

According to the admission document, Prestbury will get an annual fee of 1.75% with a minimum fee set at £625,000 a quarter. Hedge fund Och-Ziff, which is also backing Max, will receive a cut of the fees. Both get a share of any profits over and above an annual return over 11%.

Prestbury is putting in £25m with Och-Ziff stumping up £35m. The rest will come from other investors, who are reportedly very keen to back another venture set up by Leslau.

He is still best known for rollercoaster ride that was Trocadero-owner Burford Holdings in the nineties. That was followed by the first incarnation of Prestbury, which was listed on AIM between 1997 and 2000.

This time Max has a set shelf life. Leslau intends to wind it up after the 7½ years.

He believes that the property cycle is close to bottom. Max's plan is to buy commercial properties and add value by restructuring the tenancies, or refurbishing them and selling them on.

Morgan Stanley is nomiated advisor

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general news

Not a poisoned chalice for Stuttard

Marcus Stuttard takes over as AIM's new chief executive at a tough time for the junior market, but he remains upbeat over the prospects.

Hedge funds have been blamed for a lot of the global economic ills over the past year, but that cuts little ice with Marcus Stuttard, the new chief executive of AIM.

Like many markets, the junior market could hardly have endured a worse year than it saw in 2008. Stuttard, though, believes AIM's underperformance is due to general global market conditions, which has affected all markets.

"Clearly, there was in some cases a flight to cash across the investment community. Not just on AIM but also main markets and other markets globally.

Other have cited hedge fund activity as a prime cause of last year's problems, but not Stuttard. Rather, he sees hedge fund activity amongst stocks in the junior market as a positive and believes they improve liquidity in the market.

"We want to make sure a wider set of market participants are using the market because it all adds to a vibrant and liquid market," he says. "Hedge funds have been good supporters of AIM and good providers of liquidity and capital. I'm not looking to try and ban hedge funds."

But he says the same disclosure that applies to the main market should also apply to AIM. "It's all about disclosure not about banning. Our own figures have demonstrated that short-selling is an absolutely legitimate activity and a very good source of liquidity."

Stuttard accepts that liquidity is a fundamental issue for AIM and says the market has introduced measures of its own to address the issue.

"The last six to nine months has shown that liquidity has definitely been an issue and we've known about that. We will continue to look at ways we can provide companies to increase their visibility to a wider set of investors."

To increase liquidity, AIM has been very active in public policy and lobbying activities. After the budget, it submitted a report focussing on SME's and small caps and proposed changes in the VCT legislation, one of which is to allow VCT's to invest in the secondary market. Investor days and a new research initiative have also been introduced.

Stuttard is also careful in his comments over recent changes in the tax regime, such as CGT. They have hit the market hard, but Stuttard points out that investors should make investments based on the merits of individual companies and not on tax breaks. "No market should be driven by tax breaks. They are there to support natural market activity."

But he adds that there have been areas identified where it would be helpful to have modification to the tax regime. "Those areas will be consistent with the wider government policy of supporting SMEs and stimulating funding for those companies.

"The proposed changes relate to a set of companies that would be appropriate for VCT funding. It's not a change that would impact right across the market," he adds.

A lot of commentators have said that the rising numbers of cancellations on AIM is a shake-up the market needed to weed out companies that should have not been listed in the first place.

Stuttard again says the current market conditions have played a part in the rise in delistings but he does not accept the charge that inherently bad companies were allowed to list.

"Statistics show over 4/5 years that percentage of cancellations has remained broadly static. But because now we don't have the same level of IPOs, the number of cancellation have become more visible," he says, adding that he is not concerned about cancellations as it is just a natural feature of a public market.

The one part of AIM that has impressed in recent months is the secondary market. Stuttard says despite the tough market conditions, it has seen £670m raised by AIM companies so far. He adds that there is a tendency amongst many commentators to gauge the health of a market - not just AIM - simply by looking at IPO numbers.

"We said very clearly for a long time that we are not playing a numbers game, in relation to IPOs. Clearly IPO conditions are exceptionally tough globally. Not much is taking place in small or large-cap markets anywhere," he says.

"They (investors) would rather now put money into an existing business, where they are already invested, rather than put money in new business. It's a natural response to current market conditions."

But Stuttard does see signs that confidence is returning, especially in relation to IPOs. "We are starting to hear of an increased number of advisors working with companies to prepare them for IPOs at the end of this year and next year."

news

Evolution snaps up Dresdner staff

Dresdner Kleinwort is no longer a nominated adviser after requesting its name be removed from the register of nomads. The move follows the takeover of Dresdner by German rival Commerzbank.

Separately, Evolution moved to beef up its equities team by taking on 45 staff previously employed at Dresdner Kleinwort. The new staff will boost Evolution's equity trading staff by 30%.

The new staff will work for the securities subsidiary, Evolution Securities Limited, in research, sales, sales trading and trading, Evolution said in a statement.

Meanwhile, a battle for control has broken out at broker Panmure Gordon. A proposed cash injection from private equity group BlueGem Water was trumped by a better offer from French hedge fund billionaire Bertrand des Pallieres.

The French tycoon's vehicle, SPQR Capital, offered to subscribe for shares equivalent to 43% of Panmure at 28p each, compared with the proposal from BlueGem, which was at a price of 24p per share and for a 40% stake.

To complicate the situation further, reports have suggested that a third party is also interested in some form of deal with Panmure, though the name of this group has not been disclosed.

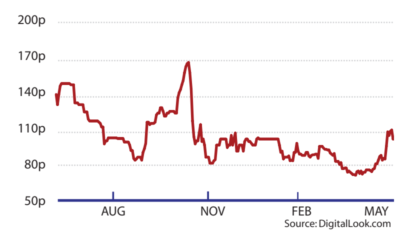
ADVISER CHANGES - APRIL 2009

COMPANY	NEW BROKER	OLD BROKER	NEW NOMAD	OLD NOMAD	DATE
Portrait Software	Singer	Teathers	Singer	Teathers	01/04/2009
Cambrian Mining	Singer/Seymour Pierce	Teathers/Seymour Pierce	Singer	Teathers	01/04/2009
Andor Technology	Singer	Teathers	Singer	Teathers	01/04/2009
CW Residential	Singer	Teathers	Singer	Teathers	01/04/2009
Augean	Singer	Teathers	Singer	Teathers	01/04/2009
Principle Capital Holdings	Singer	Teathers	Singer	Teathers	01/04/2009
Hightex Group	Singer/Old Park Lane	Teathers/Old Park Lane	Singer	Teathers	01/04/2009
Lipoxen	Singer/Noble	Teathers	Singer	Teathers	01/04/2009
City of London Investment Group	Singer/Evolutions	Teathers/Evolution	Singer	Teathers	01/04/2009
Ebiquity	Numis	Teathers	Numis	Teathers	01/04/2009
Trikona Trinity Capital	Arden/Evolution	Evolution	Evolution	Evolution	01/04/2009
Physiomics	WH Ireland	Dowgate	WH Ireland	Grant Thornton	01/04/2009
HaiKe Chemical	Hanson Westhouse	Evolution China	Hanson Westhouse	Evolution	01/04/2009
Nautical Petroleum	Evolution/Ambrian	KBC Peel Hunt	Evolution	KBC Peel Hunt	01/04/2009
Intercede	FinnCap	KBC Peel Hunt	FinnCap	KBC Peel Hunt	01/04/2009
Beowulf Mining	Alexander David	Alexander David	Strand	Ruegg	02/04/2009
LonZim	WH Ireland	Beaumont Cornish	WH Ireland	Beaumont Cornish	03/04/2009
Lonrho	Beaumont Cornish	Collins Stewart	WH Ireland	Collins Stewart	03/04/2009
Northern Petroleum	Jeffries/Blue Oar	Blue Oar/Investec	Investec	Investec	06/04/2009
LiDCO Group	FinnCap	Panmure Gordon	FinnCap	Panmure Gordon	06/04/2009
Speymill	Lewis Charles	Lewis Charles	Smith & Williamson	Nabarro Wells	07/04/2009
Eatonfield Group	Orbis/Evolution	Evolution	Evolution	Evolution	08/04/2009
Airsprung Furniture	Smith & Williamson	Blue Oar	Smith & Williamson	Blue Oar	08/04/2009
Central China Goldfields	Alexander David/Hanson Westhouse	Hanson Westhouse	Hanson Westhouse	Hanson Westhouse	09/04/2009
West Pioneer Properties Ltd	Evolution	Libertas	Evolution	Libertas	14/04/2009
Keenair Systems International	WH Ireland	Hybridan	WH Ireland	Blomfield	15/04/2009
D1 Oils	Piper Jaffray	Dresdner Kleinwort	Piper Jaffray	Dresdner Kleinwort	15/04/2009
Kubera Cross-Border Fund Ltd	Numis/LCF Edmond de Rothschild	LCF Edmond de Rothschild	Grant Thornton	Grant Thornton	15/04/2009
GEM BioFuels	Shore	WH Ireland	Shore	WH Ireland	15/04/2009
Amteus	Daniel Stewart	Daniel Stewart	Strand	Daniel Stewart	16/04/2009
White Star Energy	OLd Park Lane/First Equity	First Equity	Strand	Strand	17/04/2009
Freedom4 Group	Liberum	Collins Stewart	Liberum	Collins Stewart	21/04/2009
Sirius Exploration	Rivington Street/SP Angel	SP Angel	Beaumont Cornish	Beaumont Cornish	21/04/2009
ContentFilm	Throgmorton Street	Evolution	Grant Thornton	Grant Thornton	22/04/2009
Elephant Capital	Seymour Pierce/Fairfax IS	Fairfax IS	Seymour Pierce	Seymour Pierce	23/04/2009
System C Healthcare	Charles Stanley	Collins Stewart	Charles Stanley	Collins Stewart	23/04/2009
Business Systems Group	Singer	KBC Peel Hunt	Singer	KBC Peel Hunt	24/04/2009
Island Gas Resources	Brewin Dolphin	Brewin Dolphin/Libertas	Brewin Dolphin	Brewin Dolphin	27/04/2009
Zeehan Zinc Ltd	Alexander David	Libertas	Grant Thornton	Libertas	27/04/2009
Hollywood Media Services	Merchant Capital	IAF	Dowgate	KBC Peel Hunt	28/04/2009
Volga Gas	Oriel/Renaissance	Renaissance/KBC Peel Hunt	Oriel	KBC Peel Hunt	30/04/2009
Vitesse Media	Seymour Pierce	KBC Peel Hunt	Seymour Pierce	KBC Peel Hunt	30/04/2009

NWF profits bloom

Support Services

NWF GROUP (NWF)			100.00p
12 MONTH CHANGE %	- 27.01	MARKET CAP £M	46.89
TURNOVER £M	361.20	FORECAST P/E	13.80



Good business through its distribution arm helped Cheshire-based **NWF** maintain its improved first half performance into early spring, with results for the year to May 2009 now forecast to be significantly ahead of previous expectations.

Underlying profits will be approaching £6m against previous expectations of nearer £5m. Grocery distribution has experienced strong volumes and its recently enlarged capacity is already being used. Efficiency is improving and service levels are good enough for the company to receive bonuses from customers.

The feeds market is getting tougher and feed volumes are down. The vast majority of NWF's animal feed goes to dairy cattle and milk prices and output have all fallen. The feeds division benefited in 2007-08 from one-off gains related to rising cereal prices. That will not be repeated this year so the division's profit contribution will be lower.

The fuel distribution division enjoyed what the management describes as "perfect trading conditions". The cold winter and volatile oil prices created the conditions to improve margins.

NWF chief executive Richard Whiting says that the fuels division has achieved an "outstanding performance through the period".

Net debt will fall to around £25m by the end of May 2009. The disposal of the garden centres business helped but there has also been strong cash generation from operations.

Longer-term, NWF wants to set up a base for the grocery distribution business further south. That is likely to be via an acquisition or a joint venture with an existing distribution operation. There are also consolidation opportunities in the feeds and fuels sectors.

Cyril Sweett on course

Support Services

CYRIL SWETT (CSG)			27.50p
12 MONTH CHANGE %	- 71.79	MARKET CAP £M	15.56
TURNOVER £M	62.71	FORECAST P/E	5.60

Cost cutting will enable construction and property consultancy **Cyril Sweett** to hit expectations for the year to March.

Market conditions tightened during the second half of the year. Annualised cost savings of £11m have been made through job cuts and salary reductions to bring the cost base into line with activity levels in the current financial year.

The company has a strong balance sheet with net cash in the bank. A number of significant new projects have been secured over the past year. The UK experienced strong demand in the public sector, whilst overseas there was encouraging growth in the Middle East, including Abu Dhabi and Saudi Arabia.

Full year figures will be announced on 1 July. Broker Brewin Dolphin expects profits of £6m but forecasts a fall in profits to £4m in 2009-10.

EPE seeks distressed companies

Investment Entities

EPE SPECIAL OPPORTUNITIES (ESO)			6.25p
12 MONTH CHANGE %	- 88.32	MARKET CAP £M	2.04
TURNOVER £M	1.30	FORECAST P/E	N/A

EPE Special Opportunities is raising £5m to take advantage of the low corporate valuations at the moment. A placing and 3.0574-for-one open offer at 5p a share will raise up to £5m, which is more than the company's current market value.

EPE is targeting small quoted companies with market capitalisations of between £1m and £10m. Any deals will probably be done with a mixture of cash and shares. EPE, which used to be known as Epic Reconstruction, believes that even strong businesses are facing difficulties and some are very short of working capital. EPE admits that there are others looking at potential distressed investments but it believes that there are plenty of opportunities to go round.

EPE is currently valued at well below its NAV of £15m (46p a share), which includes cash of £1.6m. EPE will sell some existing investments to further boost its cash pile. Net proceeds will be £4.7m assuming full take up of the open offer.

Renewable Energy offloads its wave power business

Electricity

RENEWABLE ENERGY HOLDINGS (REH)	35.50p		
12 MONTH CHANGE %	- 28.28	MARKET CAP £M	23.27
TURNOVER £M	5.31	FORECAST P/E	N/A

Renewable Energy Holdings has sold the intellectual property to its wave energy operations to ASX-listed Carnegie Corporation in return for £30m in shares. The deal should be completed in September.

REH has invested up to £6m in the CETO wave power technology and planned to invest a further £1m to complete its technical development.

REH will receive 252m shares in Carnegie at a price of 24c a share, which will give it 35% of Carnegie. REH intends to be a long-term holder. Boss Michael Proffitt and fellow director Alan Burns are both on the Carnegie board and REH has the right to appoint another director.

This transaction is subject to due diligence on CETO and the agreement of Carnegie shareholders. Carnegie also needs to show that it has the cash to continue to develop CETO.

REH had previously sold the Southern Hemisphere rights to CETO to Carnegie. Carnegie had paid £3.54m to REH but the auditors decided that this payment has to be spread over the 30 year life of the deal. Another £1.2m was due by the

REH had previously sold the Southern Hemisphere rights to CETO to Carnegie.

end of 2009 but this is covered by the latest deal. EdF is the joint venture partner in the Northern Hemisphere and this will continue after Carnegie takes control of CETO.

REH still has wind and landfill power assets. Most of the 2008 revenues of £5.31m come from 40.5MW of German wind power assets with an additional contribution from landfill gas in Wales. There are 99MW of wind power projects being developed in Poland and Wales.

Longer-term, REH is interested in building up solar power assets. Italy is an attractive area at the moment because of its high prices for solar energy.

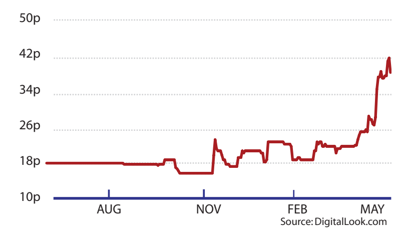
There is cash of £6.45m in the 2008 balance sheet. Although REH reported a £1.99m loss in 2008 it did generate cash. That was before capitalised development spending on CETO.

There is enough cash to finance the short-term expansion of wind power assets but not enough for additional expansion into solar or for additional wind power projects.

Advanced snaps up BSG

Software & Computer Services

ADVANCED COMPUTER SOFTWARE (ASW)	37.50p		
12 MONTH CHANGE %	+ 117.39	MARKET CAP £M	71.60
TURNOVER £M	7.33	FORECAST P/E	N/A



Advanced Computer Software is acquiring fellow AIM company Business Systems Group for £15.5m as part of its strategy to build up its primary care centre product range. BSG will help ACS develop hosting and managed services.

ACS is offering 19.11p for each BSG share. BSG had £8.1m in cash in the balance sheet at the end of September 2008 so the net cost of the business will be much less than £15.5m.

BSG's founder and chief executive Nick Gerard is swapping 40% of his holding for shares in ACS. His trust will receive 14m shares in ACS at an issue price of 25p each, which will give him 6.8% of ACS. Gerard will continue to run BSG as a division of ACS.

Smart meter boost for Bglobal

Support Services

News that the government is pushing for the installation of smart meters should be good for supplier **Bglobal**. The government wants 49m smart meters installed by 2020. Bglobal has installed smart meters in 55,000 businesses and public sector sites.However, the withdrawal of one of the main meter asset funders has hampered these installations.

BGLOBAL (BGBL)			13.50p
12 MONTH CHANGE %	- 53.45	MARKET CAP £M	10.00
TURNOVER £M	4.50	FORECAST P/E	N/A

Management believes that it can secure new funding arrangements but until that happens installations will remain lower than hoped.

Charles Stanley estimates that Bglobal still has cash of around £750,000. The broker forecasts a loss of £4.3m in the year to March 2009.

news

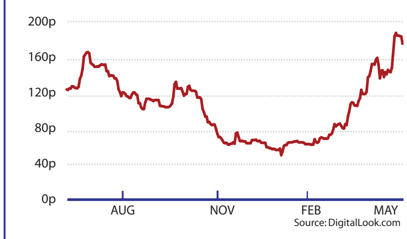
West China Cement benefits from AIM experience

Construction & Materials


WEST CHINA CEMENT - PUCHENG PLANT

Joining AIM helped WCC to finance its growth but it also gave it an improved standing in its sector.

WEST CHINA CEMENT (WCC)			173.50p
12 MONTH CHANGE %	+ 42.21	MARKET CAP £M	111.48
TURNOVER £M	86.60	FORECAST P/E	2.50



West China Cement continues to take advantage of the demand for its cement in a growing region of China.

WCC had one cement plant when it floated in December 2006 and raised £22m at 105p a share. This cash was used to build a cement plant at Lantian in 2007, which more than doubled annual capacity to 3.5m tonnes of cement.

Joining AIM helped WCC to finance its growth but it also gave it an improved standing in its sector. The business started trading in 1977 and the current chief executive Zhang Jimin took over the running of the business in 1989.

Cement is too bulky to transport long distances so WCC holds strong market positions in the areas of Shaanxi Province around its plants. WCC is the second largest cement producer in Shaanxi Province.

The Ankang plant was completed at the end of 2008 and it has been building up its production and sales since March.

Two more plants, either side of Hanzhong city, will be complete by the end of 2010.

That will increase capacity to 7.3m tonnes. There is still scope to win business from plants that use old technology that is inefficient. These are likely to close over the next few years.

WCC made a net profit of £24.6m (RMB246m) in 2008, up from £10.7m (RMB150m) the previous year. Turnover more than doubled from £36m to £86.6m, although in terms of RMB the growth was slower – from RMB526m to RMB866m- but still impresssive. Turnover increased by 264% between 2005 and 2008. WCC sold 3.44m tonnes of cement in 2008 at a higher average price than in 2007.

The Lantian site has a waste heat recycling plant which is producing electricity for the site. It started producing electricity in August 2008 and still saved WCC RMB2.9m in electricity costs during 2008.

It could save up to one-quarter of electricity costs in a full year. Another waste heat recycling plant is planned for Ankang. WCC also uses desulphurised gypsum, which is a by-product of power stations, and it also recycles rubble.

WCC has successfully passed on increased costs and demand remains strong around the area of the Sichuan earthquake. Coal prices have fallen back helping to reduce costs, while cement prices remain relatively high.

WCC will be a beneficiary of the Chinese government's RMB4 trillion infrastructure investment package.

Net debt was £59.5m at the end of 2008. The business is cash generative and even with the investment in new capacity WCC is expected to be in a net cash position by the end of 2011. There is no intention to raise any money via a share issue.

WCC has enough cash and existing facilities to build its additional capacity and it may even consider paying a dividend in 2009. WCC entered into a $60m loan facility with warrants in May 2008.

The annual interest rate is 13.5%. WCC has to repay 50% of the loan after two years – in June 2010 - and the rest one year later. There are 7.8m warrants to subscribe for shares up to 36 months after they were issued.

Part of the deal is a promise to relist on a recognised stock exchange within 30 months – by the end of 2010.

The Hong Kong Stock Exchange seems a possible home for the company but it is in no hurry to move to another market just yet. WCC will take into account the views of its investors when making any decision on moving markets.

Nominated adviser NCB forecasts net profits of around £36m in 2009, rising to £54m in 2010. The current share price does not take into account that potential to grow profits. The shares have risen by 65% since flotation but remain modestly valued.

expert views

THE INSIDE TRACK

Expert view: The lawyer

Corporate Governance Under Review

By NICK JENNINGS

In March 2009, the Financial Reporting Council (FRC) announced its review of the impact of the Combined Code on Corporate Governance ("Code"). At the time of making this announcement, Sir Christopher Hogg, Chair of the FRC, stated that although there was no assumption that the Code was fundamentally flawed, "the time is now ripe for testing the Code's content and application against the fresh thinking that the financial crisis must provoke."

Although there is no corporate governance regime that AIM companies are formally required to comply with (there is no obligation in the AIM Rules to make a "comply and explain" statement in their annual report), the relevance of the FRC's review of the Code for AIM companies is that corporate governance standards typically adopted by AIM companies are broadly derived from the Code (in the form of the corporate governance guidelines published by the QCA and NAPF respectively), hence any changes to the Code or the regulatory framework for corporate governance will inevitably filter down to the AIM Market.

For AIM companies, like others, the theoretical value proposition, as outlined in the NAPF Corporate Governance Guidelines for AIM Companies, is that by encouraging higher standards of corporate governance, companies will be able to manage their growth better and attract a greater institutional following, thereby enabling them to raise fresh capital more easily and on potentially more advantageous terms.

While many AIM companies continue to provide levels of reporting which are close to those of full list companies, in practice and against the background of a voluntary as opposed to a regulated environment, governance structures adopted by AIM companies vary greatly. In addition, size and economic clout does not necessarily produce a higher level of compliance with the Code, even though the market capitalisation of the larger AIM companies is on a par with smaller cap main list companies.

It is a common argument that the light-touch regulatory framework is the cornerstone of AIM's popularity and previous successes. Some commentators now contend that this is its weakness, particularly in the context of corporate governance. Corporate governance in the voluntary arena therefore provides an opportunity for AIM companies to differentiate themselves from competitors and the regulatory environment fosters this. Or so the theory goes.

For the majority of AIM companies, the economic burden of compliance is very real and nowadays ever more keenly noted. Resources are committed to areas of the business where they are most needed. Often in the case of development and exploration companies, who may be fighting the negative cash-flow curve, corporate governance comes well down the list of priorities and sometimes is simply not relevant. The reason for this is that the benefits that may be gleaned from achieving exemplary compliance in corporate governance are largely unknown and intangible. The cost of compliance is however quite easy to measure.

Although experience dictates that financial crisis and scandal often produces a knee-jerk regulatory response, raising the regulatory bar may not provide the right sort of encouragement to improve and focus standards across the board. However, the key should be to enable companies to concentrate on aspects of governance that are real and relevant to their business structures and relationships. Any changes to the Code and their impact on AIM regulation and expectation should therefore be considered in the context of what is necessary or relevant in order for the company in question to conduct its business so as to maximise returns for shareholders in keeping with simple principles of corporate governance.

Responses to the consultation paper are requested by 29 May 2009. The FRC will publish its findings before the end of 2009. If any changes are proposed to the Code or the way in which it operates they will be subject to further consultation.

NICK JENNINGS is an associate in the London office of international law firm Faegre & Benson LLP. He specialises in corporate finance transactions, including main market and AIM IPOs and fundraising, public and private mergers & acquisitions and private equity deals. He can be contacted on +44 (0)20 7450 4551 or at njennings@faegre.com.

expert views

Expert view: The broker

Input pressure eases for AIM's food groups

By CHARLES PICK

Input cost pressures have been a serious issue for all UK food manufacturers over the last 18 months, both for the industry giants and Finsbury Food, Glisten and Zetar from AIM.

This pressure has necessitated varied actions to prevent margin pressures and has often also had adverse ramifications for individual companies' cash flows and balance sheets.

The problems preceded UK recession and have exacerbated the pressures on UK consumer incomes, but input cost pressures are now easing, which bodes well for margins in the second half of 2009.

> The pound's weakness should have mainly filtered through in 2009.

The causes of the higher input prices were varied, but included stocking levels by several leading cereal producing nations, extreme weather in 2005-2008 (including drought and floods) and a sharp rise in oil prices which boosted fertiliser costs.

In addition to this, demand picked up with economic growth and urbanisation in China and India, rising biofuels investment and speculative interest by financial investors.

Food inflation easing

Historically food prices have lagged inflation and UK food inflation is now subsiding. Retail Price Index numbers peaked at 12.8% last August, but averaged 10.5% in the first quarter of 2009.

This downward trend has continued with most companies now citing 5-8% rises for input cost rises in 2009, though the impact of the weak pound must be considered.

Sterling's plunge has been an inflation booster in many areas, but the general UK macro-economic situation is tending to 'squeeze out' inflation. As prices for many items peaked in August of 2008, comparatives in the second half of 2009 will become far more favourable.

It seems unlikely, therefore, many input cost rises for individual items will top 10% in 2009, though retailer resistance to price rises will grow and they will demand lower input costs are passed on quickly.

There will be positives for cash flow and positives for margins assuming lag effects, especially for second half comparisons with the same period in 2008.

Prices to fall further

Barring another oil price or bad harvests input shock, input cost growth for food manufacturers could subside to 2-4%. The pound's weakness should have mainly filtered through in 2009.

It is also possible that one or both of the key average £/$ and £/€ rates will be slightly improved in 2010 so there will be less need for food manufacturers to engage in debates with retailers to recoup higher costs via higher pricing.

Top line growth among the food producers will largely reflect their individual volumes and product mix. Margins should stabilise relative to the second half of 2009 and could even edge higher if trading down (from premium to value products) reverses.

From an individual company perspective, following the November profits warning cakes and breads specialist Finsbury Food has been looking somewhat boxed in on the debt front although revised banking facilities totalling £49m were successfully secured from 26 March 2009. It looks cheaply rated but a catalyst is needed for a re-rating.

Confectionery maker Glisten also reported poor interims in March (along with a passed dividend) but the shares had been heavily over-sold previously. They have since almost doubled as the market rally extends to smaller companies. A pause for breath now looks warranted.

Snacks group Zetar has also rallied following the sale of The Baked Snack Company on 1 May. It was Zetar's fifth purchase out of six and easily the worst. With circa £1.6m of annual losses eliminated via the sale, profit should rebound strongly in the current financial year. The 8 May trading update was also positive on a number of counts.

Overall, though, the decline in input pressure must be good news for all three AIM companies. It should mean less scope for profit warnings from food producers, while the defensive attributes of the sector reassert themsleves.

CHARLES PICK is finnCap's food company analyst. He started work as a research analyst in 1979 and has since worked predominantly for Williams de Broe and WestLB Panmure. Sectors researched over the years have included chemicals, conglomerates, mining, other industrial materials, support services, transport and tobacco, plus more recently food manufacturing and waste management.

feature

Merger activity off to a slow start in 2009

M&A activity was expected to come to the fore in 2009 but the number of completed takeovers so far this year is lower than in the first four months of 2008. The recent rise in AIM share prices may spark more takeovers.

When there is little in the way of new issues activity, corporate financiers have to look elsewhere for business. This year was expected to mark an upturn in mergers and acquisitions activity. Consolidation was thought to be needed at the smaller end of AIM in particular. There has continued to be a steady level of takeover activity but, if anything, it has been at a lower level than in recent years.

Weak share prices leaving companies with a devalued currency for takeovers has not helped. Even so, many companies are still finding deals worth doing.

In reality, takeover activity has been at relatively high levels for more than two years. Companies valued at a total of more than £10bn were taken over in 2007, which was four times the level the previous year and remains the peak for takeovers in any one year.

The number of takeovers completed dipped from 75 in 2007 to 68 in 2008. There was no repeat of the billion pound takeovers that happened in 2007 but there was still a steady flow. These tended to be at the smaller to medium-sized end of the spectrum.

However, there were some larger buys. For example, African oil explorer First Calgary, which was at one point a few years ago the largest company on AIM, was acquired by Italian oil company Eni. The bid valued Canada-based First Calgary at C$923m (£529m) in cash, which was less than one-third of its value four years ago. There were at least six takeovers worth more than that in 2007.

In the first four months of this year, there have been 11 completed takeovers, against 16 by the end of April 2008. Completed takeovers refers to bids that have been declared unconditional and where the AIM quotation has been cancelled. There are a number of ongoing bids, some of which are well on the way to success, but the quotations have not been cancelled.

Advanced Computer Software is buying cash rich hosting and managed services company Business Systems Group. ACS is a major software provider to the primary health sector and wants to use BSG's expertise in hosting. Broadcast scheduling software developer Pilat Media is being acquired by a rival, while Hong Kong Stock Exchange-listed Shui On Construction and Materials is bidding for property investor China Central Properties, where it already holds a substantial minority interest.

There have even been contested takeovers. Local radio broadcaster UKRD and Hallwood Finance fought over Local Radio Company. Both the bidders increased their bids twice after their initial offers. UKRD passed the 50% acceptances point with its 4p a share bid - double the original 2p a share offer - even though Hallwood's final bid was 5p a share.

There are also a number of AIM companies talking to potential bidders. They include technology PR firm Next Fifteen Communications, Syndicate Asset Management and skin care treatments developer York Pharma. A significant number of bid discussions that are revealed to the stock market do not lead to a bid, though.

The AIM broking community is a sector that is rife for consolidation yet little has happened that has not been forced on a company because of its poor financial position - i.e. Singer snapping up the rump of Teathers.

> This year was expected to mark an upturn in mergers and acquisitions activity.

Nearly all of the AIM-quoted brokers have been in merger talks with another firm yet they can never agree on terms. Blue Oar is currently talking with Dowgate, which previously pulled out of talks with Daniel Stewart. Blue Oar itself has had unsuccessful merger talks with WH Ireland on more than one occasion.

Egos and inability to agree on price appear to be a major factor in the broking sector. It would be wrong to assume that this is not the case in other

feature

sectors as well. While consolidation may seem the sensible thing for a sector it may prove difficult without willing parties.

Past experience

Looking back to 2003, which marked the previous bottom of the FTSE Aim All-Share index, there were 36 takeovers completed and that was the record number until 2006. There were a significant number of companies acquired by their managements in 2003. This appears to be due to the low valuations placed on the companies at that time.

Many valuations are just as low now or possibly even lower. However, management buy outs are not such a feature of takeovers at the moment. That appears to be mainly down to the difficulty in raising finance under the current tough banking environment.

One of the main reasons given for an AIM flotation by many companies is the ability to use shares for acquisitions. That is all very well but low valuations make this much more difficult.

K3 Business Technology chief executive Andy Makeham would like to purchase related enterprise software businesses but he has found it difficult to make an earnings enhancing acquisition with the company's share price at a low level. The share price has risen by 47% in the past month, which should make it easier, but it is still difficult when the shares are trading on five times prospective earnings.

Many companies believe that there is still room for further reductions in valuations and are holding off on buying. Owners of unquoted businesses, in particular, can take time to adjust their expectations. CBG has been built up from scratch through the acquisition of insurance brokers in the North West. It is still looking to buy insurance brokers in the region but management thinks that price expectations may start to reduce over the coming year. Penna Consulting chief executive Gary Browning also believes that the bottom has not been reached yet.

Integration

Broker Daniel Stewart recently published an AIM M&A Survey. This survey is based on the responses of 98 AIM executives, the majority of which were chief executives or finance directors. They come from a wide range of different businesses and sectors.

One of the most interesting aspects of the survey relates to the ranking of success factors in acquisitions. Experience of M&A transactions came surprisingly well down the list.

Many companies believe that there is still room for further reductions in valuations and are holding off on buying.

Post-merger integration was ranked the most important factor. The more successful purchasers think about the integration process well before the deal is finalised.

Alan Bonner of Pinnacle Telecom sets a lot of store by his ability to integrate acquisitions. Pinnacle, formerly known as Glen Group, offers voice, mobile and data services and has a buy and build strategy. He believes in quick integration and says that in most cases it can be achieved in 90 days.

Pinnacle has strict limits on what it will pay. That includes EBITDA multiples of two to six for companies or up to 24 times gross profits for customer bases. After five years Pinnacle wants annual revenues of £50m.

The next most important things in the rankings were due diligence - both financial and non-financial. Keeping the client relationships and linking the M&A with the corporate strategy were also rated in the top five.

NUMBER OF COMPLETED TAKEOVERS OF AIM COMPANIES

YEAR	NO. OF COMPANIES
2001	15
2002	14
2003	36
2004	20
2005	35
2006	44
2007	75
2008	68
2009 - to end April	11

The survey also shows that 61.9% of the respondents expect to make acquisitions in the next 12 months, with a further 18% unsure whether they will or not. The vast majority will pay for the deal with a combination of cash and shares.

Higher share prices and recent fund raisings indicate that there may be increased scope for takeovers in the coming months. EPE Special Opportunities is raising £5m and is looking to acquire quoted companies valued at between £1m and £10m. EPE would need to use its shares to do that but they are trading at a discount of more than 80% to the last stated NAV.

Daniel Stewart points out that pressure on chief executives to achieve growth could spark deals. That is not necessarily a good thing. Making acquisitions for the wrong reasons can prove costly in the future.

AIM shares are an important currency in financing takeovers, whether the target is quoted or unquoted.

Further improvement in share prices will give AIM companies a more valuable currency to fund acquisitions – either through the issue of shares to the seller or by raising cash through a placing.

AIM is a market ripe for consolidation and, if companies can find the finance, there is likely to be increasing acquisitions activity as the year goes by.

market performance, indices and statistics

AIM SECTOR INFORMATION

SECTOR NAME	AS % OF AIM MARKET CAP	AS % OF AIM COMPANIES
Mining	14.67	10.75
General Financial	11.64	12.59
Oil & Gas Producers	10.41	6.37
Equity Investment Instruments	9.34	4.24
Real Estate	8.50	6.37
Travel & Leisure	5.61	4.31
Support Services	5.56	8.90
Food Producers	4.31	1.64
Software & Computer Services	4.01	7.39
Media	2.94	6.43
Construction & Materials	2.85	2.26
Electronic & Electrical Equipment	2.75	3.35
Pharmaceuticals & Biotechnology	2.19	3.83
General Retailers	2.07	1.51
Electricity	2.02	0.96
Health Care Equipment & Services	1.28	2.46
Nonlife Insurance	1.03	0.89
General Industrials	0.90	1.44
Industrial Engineering	0.83	1.98
Technology Hardware & Equipment	0.75	1.92
Chemicals	0.70	1.85
Industrial Transportation	0.66	0.82
Mobile Telecommunications	0.57	1.10
Oil Equipment & Services	0.55	0.75
Food & Drug Retailers	0.54	0.55
Life Insurance	0.53	0.07
Banks	0.44	0.14
Fixed Line Telecommunications	0.39	0.41
Household Goods	0.29	0.89
Industrial Metals	0.28	0.41
Forestry & Paper	0.24	0.27
Gas Water & Multiutilities	0.23	0.21
Aerospace & Defence	0.23	0.21
Personal Goods	0.20	1.10
Beverages	0.20	0.21
Automobiles & Parts	0.16	0.75
Leisure Goods	0.08	0.48
Nonequity Investment Instruments	0.04	0.07
Investment Entities	0.01	0.14

KEY AIM STATISTICS

Total number of AIM companies:	1461
Number of market makers:	49
Total market cap for all AIM:	£44572.98m
Total of new money raised:	£60813.70m
Transfers to the official list:	130

AIM COMPANY PERFORMANCE

Statistics for April 2009

No. of shares rising:	969
No. of shares falling:	314
No. of shares unchanged:	178
Advance/Decline Ratio:	3.09
Market Volatility:	46.50

FTSE INDICES

ONE-YEAR CHANGES

INDEX	30/04/2009	30/04/2008
FTSE AIM All-Share	479.60	977.50
FTSE AIM 50	2070.12	5009.70
FTSE AIM 100	2142.24	4964.10
FTSE Small Cap	2212.27	3154.40
FTSE All-Share	2173.06	3099.94
FTSE 100	4243.71	6087.30
FTSE 250	7528.95	10122.30

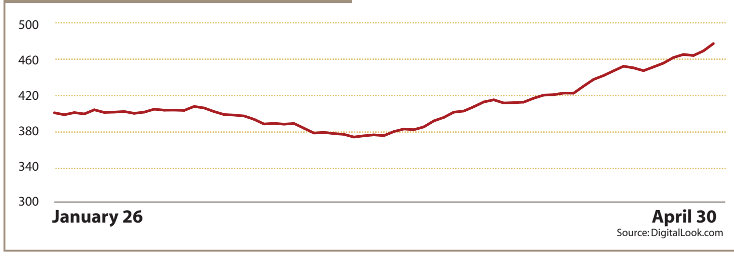
COMPANIES BY MARKET CAP

MARKET CAP	NO.
Under £5m	499
£5m-£10m	227
£10m-£20m	248
£20m-£50m	261
£50m-£100m	130
£100m-£250m	73
£250m+	23

RISERS

COMPANY NAME	SECTOR	PRICE (p)	CHANGE (%)
Everfor Diamonds	Mining	5.00	640.74
European Nickel	Mining	9.32	296.60
Solomon Gold	Mining	10.75	290.91
Premier Management Holdings	Support Services	0.20	233.33
Red Leopard	Equity Investment Instruments	0.10	233.33
Pangea DiamondFields	Mining	1.80	213.04

AIM - 13-WEEK INDEX CHANGE



Top Director Dealings in April

TOP DIRECTORS' DEALINGS

COMPANY NAME	TICKER	VALUE (£)	BUY/SELL	TRADE	TITLE	SURNAME	FIRST NAME	DATE
Climate Exchange	CLE	£4,163,300	Sell	527000 x 790.00p	Dr	Sandor	Richard L	07-Apr-09
Prosperity Minerals Holdings	PMHL	£2,415,000	Buy	6900000 x 35.00p	Mr	Wong	David	28-Apr-09
Birmingham City	BMC	£2,034,419	Buy	9462414 x 21.50p	Mr	Gold	David	07-Apr-09
Birmingham City	BMC	£2,034,419	Buy	9462413 x 21.50p	Mr	Gold	Ralph	07-Apr-09
Helius Energy	HEGY	£570,000	Sell	3000000 x 19.00p	Mr	Worrall	Alex	16-Apr-09
Prosperity Minerals Holdings	PMHL	£526,000	Buy	2000000 x 26.30p	Mr	Wong	David	23-Apr-09
London Capital Group	LCG	£420,000	Buy	200000 x 210.00p	Mr	Denham	Simon David	24-Apr-09
Maple Energy	MPLE	$520304	Buy	121283 x 429.00c	Mr	Canon	Rex W	23-Apr-09

Source: Digital Look Please note - All share prices are the closing prices on 30th April 2009, and we cannot accept responsibility for their accuracy.

Faegre & Benson

Faegre & Benson LLP is an international law firm which offers an integrated team of more than 525 lawyers in Europe, the US and Asia. In the UK, Faegre & Benson focuses on advising middle market and high quality emerging companies meeting their legal needs, both domestically and internationally, in corporate finance, mergers and acquisitions, dispute resolution, employment, commerce and technology and commercial property.

With lawyers who have been advising companies and nomads since the AIM market began, the firm provides sophisticated advice and practical experience in flotations and fundraisings, takeovers and reverse takeovers, mergers and acquisitions, corporate governance and regulatory issues.

Lawyers at the firm are at the forefront of the AIM market and have strong relationships with the major players in the AIM community. Members of the team serve at the highest levels with the Quoted Companies Alliance, which lobbies for the interests of smaller quoted companies, and have made significant contributions to legal and regulatory reforms which have shaped the market.

For further details about the firm and its legal services for AIM companies please contact Donald Stewart on +44(0)20 7450 4586 or dstewart@faegre.com.

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 employs 39 members of staff and is 50% owned by JM Finn, an independent private client stockbroker founded in 1945. In 2008, FinnCap won 14 new clients and has a total of 47 clients. FinnCap is a Nominated Adviser (NOMAD) for AIM companies and a Corporate Adviser for Plus Markets.

In August 2007, 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 have taken a significant equity stake in the business, meaning they have made a substantial financial commitment.

About J M Finn & Co

JM Finn is an independent private client stockbroker with approximately £4bn under management as at June 2007. Its 260 staff are based in London, Bristol, Leeds and Suffolk.

JM Finn was founded as a partnership in 1945, incorporated as a private limited company in 2006 and has been a member of the London Stock Exchange for over 60 years.

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PUBLISHER Andrew Yates
EDITOR Philip Whiterow
DEPUTY EDITOR Jamil Hussein
SENIOR CONTRIBUTOR Andrew Hore
DATA Angela Barham, Shane Ryan

PRODUCTION AND DESIGN David Piddington
SHARECAST TEAM Lee Wild, Jana Weigand, John Harrington, Rory Gallivan

SPONSORSHIP & ADVERTISING aimbulletin@digitallook.com or telephone +44 (0)20 7743 0050