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THE ONLINE MONTHLY FOR THE ALTERNATIVE INVESTMENT MARKET

AIM JOURNAL

Octopus hails AIM importance

Investment manager Octopus argues that AIM is "one of the UK's most important assets" in the Octopus High Growth Small Business Report 2015. Octopus adds that, over two decades, AIM has provided a platform for high-growth smaller businesses and no other country has a market like it.

One in four of the high-growth smaller businesses surveyed find it difficult to obtain the funding they need. Octopus offers recommendations that could make it easier for smaller businesses to gain the funding they require and this includes a part for AIM. "We propose that the government dedicates resources towards ensuring that the regulatory and tax environment encourages UK businesses to list on AIM, and encourages both UK and overseas investors to invest in smaller companies."

Another recommendation is raising the profile of existing financial initiatives including the British Business Bank, the Angel CoFund, VCTs and the Enterprise Investment Scheme (EIS). A large number of smaller companies are still unaware of many of these initiatives and incentives. Octopus also believes that pension funds and corporations should be given access to the same tax incentives as individuals via VCTs and EIS.

Airship flotation plans

Airship developer Hybrid Air Vehicles is planning to raise cash ahead of a potential AIM flotation. At the end of October, Hybrid's Airlander aircraft, which is 92 metres long and can be used to carry cargo or passengers, was filled with helium and floated for the first time – although this was inside its hangar.

Bedfordshire-based Hybrid raised £2.37m via a crowdfunding campaign earlier this year, according to the company's website (www.hybridairvehicles.com). That took funding from investors to more than £12m. In February, Hybrid was awarded a £3.4m regional growth fund grant.

The engines and other parts of the aircraft will be added over the coming months and the first flight is expected in the first quarter of 2016. The Airlander has the capacity to carry up to ten tonnes of cargo and Hybrid believes that it could travel halfway around the world on one tank of fuel. There is also potential for passenger services, surveillance operations and movie-making uses. Hybrid is building the order book for trials and sales.

This business is not entirely new to the London market. Hybrid founder Roger Munk, who died in 2010, also founded Airship Industries, which developed the basis of the technology. Airship Industries was quoted on the Unlisted Securities Market and subsequently the Third Market in the 1980s and at one point Alan Bond was a backer.

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Malta seeks smaller company Prospects

Malta Stock Exchange is planning a new smaller companies market called Prospects. Although the main focus is Maltese smaller companies there are also plans to attract overseas entrants. It is most likely to attract companies that are not big enough for AIM so this should not provide any concerns for the London Stock Exchange. The rules are still being finalised and Prospects could be launched in the first quarter of 2016.

Admission to Prospects will be granted by the Malta Stock Exchange (www.borzamalta.com.mt) rather than the regulatory authorities. This means that unlike the existing companies quoted in Malta the shares are not passportable within the EU. There will be no minimum percentage of shares required to be in public hands.

The new market is designed for companies that want to raise between €1m and €5m. This is because €5m is the highest figure that can be raised without the need to publish a full prospectus, according to current EU regulations. Instead, a business plan will be required. If the company is a start-up, it will be need to be up and running within 12 months.

Each company requires a corporate adviser, which will conduct due diligence and owe a duty of care to market participants. The cost of floating on Prospects could be as little as £100,000, depending on the size of the company.

As with any small companies market, liquidity after the flotation is important; if it is lacking it can hamper the market. The current two-tier market has limited liquidity. Malta Stock Exchange is currently promoting itself and this could help to improve overall liquidity.

Globo fraud

Greece-based mobile technology company Globo has been placed in administration following the uncovering of fraudulent accounting. This was triggered by the publication of a report into the company by Quintessential Capital Management. Globo chief executive Costis Papadimitrakopoulos has resigned, but not before selling 42 million shares – two-thirds of his stake. He was followed out of the door by other directors, including the finance director. The administrator is FTI Consulting and it will investigate the books in order to understand the true financial position. There are also likely to be investigations by the authorities in the UK, Greece and Cyprus. Globo previously reported growing profits but it always seemed relatively short of cash. Although there was cash in the balance sheet this was supplemented by share issues.

UHY Hacker Young's prospectus warning

Accountant UHY Hacker Young says that the European Commission (EC) consultation on the Prospectus Directive could diminish one of AIM's important advantages over the Main Market. The consultation includes the possibility that AIM companies might be required to comply with the same prospectus rules as the Main Market. That would mean that the UK Listing Authority would be required to assess each AIM prospectus – currently the company's nominated adviser fulfils that role. That would make gaining an AIM quotation much more costly. UHY Hacker Young says that market participants should make sure that their voice is heard during the consultation so that any changes do not hamper AIM.

UHY's AIM review 2014/15 says that the economic recovery is renewing companies' desire to raise cash in order to grow. In 2014, the average cost of gaining a quotation on AIM was 7.4% of funds raised, which is a sharp decline from 9.4% of funds raised in 2013. This is the lowest average cost level since 2010.

UHY Hacker Young believes that there has been a renewed focus on corporate governance on AIM. This has led to fewer flotations from countries where there are concerns about corporate governance. There has been a noticeable move by AIM itself to tighten up controls. The systems and controls of some Chinese companies are being reviewed, although China Rerun Chemical Group was not willing to pay for an independent review and its nominated adviser Cairn resigned.

The accountant argues that a tighter focus by nominated advisers on their clients' corporate governance will help to reinforce investor confidence in the market and make AIM even more attractive to high-quality companies.

HubInvest publishes AIM Journal

www.hubinvest.com

AIM brokers return cash to shareholders

AIM advisers Cenkos Securities and Shore Capital are both returning cash to shareholders via tender offers. The two companies have been strong cash generators in recent times.

Cenkos had £48.2m in the bank at the end of June 2015 and intends to use up to £8m to buy back 7.28% of its share capital at 180p a share, which is above the market price at the time of the announcement. A general meeting will be held on 24 November to enable the tender to go ahead. Cenkos has already returned £10.8m to shareholders at 188p a share at the beginning of 2015. Cenkos declared an unchanged interim dividend of 7p a share, which is payable on 5 November. The shares have already gone ex-dividend.

Shore had £37.4m in the bank at the end of June 2015 helped by the proceeds of the disposal of radio spectrum licences. Shore gained shareholder approval to buy back up to 9.91% of its share capital at 417.5p a share, which is worth £10m. Shareholders were able to tender more than their entitlement and the tender was over-subscribed.

In contrast, Daniel Stewart Securities does not have the luxury of large cash balances. The broker is still trying to secure a funding package. Trading in the shares has suspended since 1 October because the accounts for the year to March 2015 have not been published. Daniel Stewart says that it requires additional funds before it can publish the accounts. This is despite the fact that £1.2m was raised at 3.35p a share in June. Daniel Stewart has already admitted that it made a pre-amortisation loss of £1.36m last year as the bad-debtors provision was raised by £500,000. Non-executive Peter Dicks will resign when the accounts are published.

ADVISER CHANGES - OCTOBER 2015

COMPANY	NEW BROKER	OLD BROKER	NEW NOMAD	OLD NOMAD	DATE
Minds + Machines	N+1 Singer	N+1 Singer	N+1 Singer	Beaumont Cornish	02/10/15
Ceres Power	Zeus	N+1 Singer	Zeus	N+1 Singer	05/10/15
Cloudbuy	Arden	Westhouse	Arden	Westhouse	05/10/15
Stellar Resources	Optiva	Cairn	Cairn	Cairn	05/10/15
Flowgroup	Cenkos	Cenkos/Investec	Cenkos	Investec	07/10/15
Sirius Minerals	JPMorgan Cazenove/ Liberum/WH Ireland	Liberum/ WH Ireland/Macquarie	Liberum	Macquarie	07/10/15
Polar Capital Holdings	Peel Hunt/ Canaccord Genuity	Canaccord Genuity	Canaccord Genuity	Canaccord Genuity	12/10/15
TomCo Energy	SP Angel	Shore	SP Angel	Shore	12/10/15
Northamber	Cantor Fitzgerald	Charles Stanley	Cantor Fitzgerald	Charles Stanley	16/10/15
Conviviality	Investec/Zeus	Investec/Zeus	Investec	Zeus	19/10/15
Inspired Energy	Panmure Gordon/Shore	Shore	Shore	Shore	19/10/15
Staffline	Berenberg/Liberum	Liberum	Liberum	Liberum	19/10/15
Abzena	N+1 Singer/Cenkos	Cenkos	Cenkos	Cenkos	21/10/15
Cyan Holdings	Cantor Fitzgerald/ Beaufort	Allenby/Beaufort	Cantor Fitzgerald	Allenby	26/10/15
Eden Research	Shore	WH Ireland	Shore	WH Ireland	26/10/15
Scholium Group	WH Ireland	WH Ireland/ Whitman Howard	WH Ireland	WH Ireland	26/10/15
Action Hotels	Zeus/Investec	Investec	Investec	Investec	29/10/15
Metminco Ltd	SP Angel/RFC Ambrian	RFC Ambrian	RFC Ambrian	RFC Ambrian	29/10/15
Treveria	Allenby/Peterhouse	N+1 Singer	Allenby	N+1 Singer	29/10/15
URU Metals Ltd	SVS/Northland/ Beaufort	Northland/Beaufort	Northland	Northland	30/10/15

HubInvest publishes AIM Journal
www.hubinvest.com

company news

Online investment and growing product range underpin growth prospects at Gear4music

Musical instruments retailer *www.gear4musicplc.com*

GEAR4MUSIC (G4M)			145p
12 MONTH CHANGE %	N/A	MARKET CAP £M	29.2

Online musical instruments retailer **Gear4music** reported a reduced first-half loss and is on course for a strong second half. Gear4music still has a modest market share of 2.5% in the UK and 0.6% in Europe but it is becoming a significant player in the market and it continues to add customers.

In the six months to August 2015, revenues grew 43% to £12.5m, while the loss excluding flotation costs halved from £914,000 to £450,000. The fastest growth came from branded instruments but the growth of higher-margin own-brand sales should accelerate in the second half as more stock becomes available.

There is continued investment in the website, with plans for other European country specific websites. Recent improvements have enabled Gear4music to increase website traffic from continental Europe by 46% to 1.83 million people in the first half. Conversion rates have also improved but they remain below UK levels. Non-UK sales are running at around one-quarter of the total.

There is continued investment in the website

Gear4music joined AIM in June when it raised £9m at 139p a share. That cash has gone towards paying off borrowings and building up stock levels. There is still some international trade finance debt on the balance sheet and net cash was £613,000 at the end of August 2015. Gear4music is considering opening a London showroom. It already has one at its York base, but management is still seeking a suitable London site.

House broker Panmure Gordon believes that Gear4music can make a profit of £660,000 in the full year, rising to £1.51m in 2016-17. The shares are trading on 24 times prospective 2016-17 earnings. That rating reflects the growth potential now that Gear4music has a strong online base and an expanding product range.

US distribution costs hold back ASOS profit growth

Online fashion retailer *www.asos.com*

ASOS (ASC)			3261p
12 MONTH CHANGE %	+22.8	MARKET CAP £M	2,750

Online fashion retailer **ASOS** continues to grow its revenues fast but it is where some of that growth is coming from that is hitting operating margins. Although the US has the highest gross margin the difference is more than swallowed up by the high distribution costs in the region.

US gross profit grew by 38% last year, which is faster than any other region. The US gross margin was 60.2%, compared with 46.8% in the UK and around 50% for the EU and rest of the world. However, US distribution costs were 51.4% of the region's gross profit, down from 53.4% the previous year. UK distribution costs are much lower at 23.1% of gross profit, while the figures for the EU and the rest of the world were 27.7% and 29.7% respectively.

US operating margin before central costs was 29.3%, up from 26.7%, while the group figure was 35.3%. The US warehouse already fulfils more than a quarter of orders. Admittedly, the US is only 11% of revenues and 9% of operating profit before group overheads but it is a market with large growth prospects.

The balance sheet includes £119.2m of cash but there is significant investment planned in the new Eurohub warehouse. Further investment in US distribution will have to wait until this is completed. Peel Hunt forecasts a rise in underlying profit from £41.3m to £54m. The shares are still trading on a heady rating of 63 times 2015-16 but it will be difficult for ASOS to grow fast enough in the medium term to warrant this.

OMG!
OPPORTUNITY 4
MATERIAL
GAINS

company news

Private equity-backed bidder Orca mops up minorities in OpSec Security

Anti-counterfeiting products *www.opsecsecurity.com*

Minority shareholders have agreed to a 55p a share offer for anti-counterfeiting technology developer **OpSec**, having turned down a 50p a share bid in 2011. The bid price is at a 69% premium to the market price before the potential bid was announced. Bidder Orca has the backing to cancel the AIM quotation even if shareholders do not accept the bid.

The bid values OpSec at £66.7m, which is more than twice the £28m valuation of the 2011 offer. This is because there have been two significant share issues in the intervening period. In March 2012, £7.8m was raised at 45p a share to finance the acquisition of Delta Labelling, whose original shareholders invested £2m in OpSec at 75p a share. In March 2014, a further £7m was raised at 33p a share, with Herald Investment Trust subscribing for one-third and Orca the rest, although a small number of the shares were clawed back by other minority shareholders via an open offer. This cash was needed to finance growth.

OpSec is involved in a consolidating sector

OPSEC SECURITY (OSG)			54.5p
12 MONTH CHANGE %	+70.3	MARKET CAP £M	55.2

OpSec is involved in a consolidating sector and it has been growing its transaction cards revenues on the back of the move to chip and pin in North America - the region that generates the majority of group revenues. Orca believes it will be easier for OpSec to take advantage of growth opportunities as an unquoted business. Orca and its owner Investcorp Technology Fund III are seeking complementary acquisitions that can be combined with OpSec and they are prepared to provide the cash required. A business with higher revenues and profit than OpSec has already been identified but there is competition for the purchase.

Stratex proves self-financing is possible

Mining *www.stratexinternational.com*

One thing that can normally be assumed when it comes to junior explorers on AIM is that they will require regular fundraisings, probably at a significant discount to the market price. **Stratex International** is different in that it has not raised cash from shareholders since March 2012, when it raised £7.9m at the then market price of 7.625p a share. Sales of projects in recent years have helped to raise £17m and there will soon be cash generated from the Altintepe gold project in Turkey.

Stratex owns 45% of Altintepe and the first gold pour was at the beginning of November. All of the pre-production capital costs have been funded by Stratex's partner, Bahar. Altintepe will generate cash to at least help Stratex to cover overheads, and there is a 1% net smelter royalty (capped at $20m) expected from the Oksut project from the middle of 2017. Next year, the 30%-owned Muratdere copper/gold project should commence construction and although Stratex will have to contribute its share of costs, much of this will come from debt.

STRATEX INTERNATIONAL (STI)			2.08p
12 MONTH CHANGE %	-9.4	MARKET CAP £M	9.72

If there is cash flowing in from operations, Stratex could retain higher stakes in its projects. Outside Turkey, the main focus is Senegal with other west African assets in 33.5%-owned, AIM-quoted GoldStone Resources. The east African exploration assets have been placed in the Thani Stratex Resources joint venture.

There was still £2.53m in the bank at the end of June 2015. The share price is well below the 2012 placing price as junior mining companies remain out of favour. There should be no need for any dilutive fundraising unless there is a large opportunity that requires significant investment.

OMG! Opportunity 4 Material Gains

Greenko sells Indian power generating assets to its major financial backer

Power generator *www.greenkogroup.com*

Greenko has agreed the sale of its Indian wind and hydro electricity generating assets and says that it will be able to make an initial distribution of 98p a share following completion of the deal. The installed capacity is 838MW and Greenko is on course for achieving its 1,000MW target by the end of the year. However, the financial performance of the assets has been disappointing.

An affiliate of sovereign wealth fund GIC has set up Greenko Energy Holdings (GEH) to buy Greenko Mauritius, which owns some of the generating assets and development projects, and other assets for £162.8m. This should be enough to pay up to 100p a share to shareholders. Greenko's NAV (after minority interests) was $168.3m at the end of June. In the first half of 2015, power generation increased by 49% to 904GWh. There was $34.5m of cash generated from operations in the six months to June 2015. Net debt was $1bn.

Three Greenko non-executive directors have been buying shares

Greenko chief executive Anil Kumar Chalamalasetty and joint managing director Mahesh Kolli will continue to be involved in managing the operations and a company associated with them will invest in GEH. They have not been involved in the board's recommendation of the disposal. The bondholders owning a majority of the 8% senior loan notes 2019 in issue have agreed to amendments the rules of the notes in return for a consent fee.

GREENKO (GKO)			92p
12 MONTH CHANGE %	-35.2	MARKET CAP £M	141.6

Greenko joined AIM in November 2007 when it raised €45m at €1.40 a share – 97.6p a share at that time. That valued Greenko at €95.2m (£66.4m). In January 2010, £72m was raised at 140p a share. In 2013, GIC invested £100m in Greenko Mauritius and this was convertible into Greenko shares at 260p each between July 2015 and 2017.

Three Greenko non-executive directors have been buying shares at between 87p and 90p each.

Hayward Tyler plans to improve Brotherhood

Pumps and motors *www.haywardtyler.com*

Specialist pumps and motors supplier **Hayward Tyler** has widened its product range and boosted its earnings per share by acquiring the business of Peter Brotherhood, which became part of Siemens after it acquired Dresser Rand. Peter Brotherhood was a non-core asset and it makes steam turbines, gas compressors and CHP units, with an installed base of 1,500 units in total.

Hayward Tyler is paying $15m (£9.87m) for the acquisition, which is similar to net assets. In 2014, Peter Brotherhood made an underlying operating profit of $3.2m on revenues of $46.7m. Operating margins could be improved to 10% in the coming years. There is also scope to cross-sell to the two customer bases.

HAYWARD TYLER (HAYT)			97p
12 MONTH CHANGE %	+22.8	MARKET CAP £M	44

The deal is funded by debt so pro forma net debt is expected to be £22.6m at the end of March 2016. There is potential to sell and lease back the acquired company's 11.5 acre Peterborough site for around £6m.

The deal is forecast to enhance earnings by 14% to 10p a share in 2016-17 – the first financial year following the acquisition. That puts the shares on ten times prospective 2016-17 earnings.

Hayward Tyler holds a strong market position and it continues to prosper even though oil and gas markets are difficult. The construction of new test beds, which is part of the investment in the facilities at Luton, has just started and the project should be completed by July 2016. Capacity should double and working capital requirements will be lower.

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OPPORTUNITY 4 MATERIAL GAINS

Consistent NAV growth proves attractive at BP Marsh

Insurance investments *www.bpmarsh.co.uk*

Dividend

Insurance-focused investment company BP Marsh has in the past paid dividends to shareholders when it has spare cash but it has reached the point where it can make regular payouts. BP Marsh did not initially pay a dividend after floating on AIM in early 2006 and the maiden dividend was 1p a share in the year to January 2010. However, there was no dividend for the next two years until a 1p a share dividend in 2012-13. An interim dividend of 1.25p a share and a final dividend of 2.75p a share were paid the following year. Last year's dividend was 2.75p a share. BP Marsh says that it will pay a dividend of 3.42p a share for 2015-16, costing £1m, and pay at least that much for 2016-17.

Company

BP Marsh has been quoted for more than nine years. At the end of January 2006, the NAV was £31.2m which had more than doubled to £65.5m by the end of July 2015 – the company having paid out more than £2.5m in dividends and £133,000 on share buy-backs. The share capital has barely changed.

The company has been in existence since 1990 and the average NAV annual compound growth rate has been 11.2%. More than doubling the NAV since 2006 is also impressive given that this period includes the global financial crash.

In 2013, BP Marsh sold four-fifths of its stake in Hyperion Insurance for £29.2m, which has helped to finance dividends as well as further investments. Hyperion has been in the portfolio since 1994. The rest of the shareholding will be sold for £7.3m in July 2016.

There was £6m in the bank at the end of January 2015, although £2.8m of this has been committed for follow-on investments. On top of this there are long-term investment funds of £3.55m, which can be used when additional opportunities arise, although management is highly selective.

BP MARSH (BPM)	
Price (p)	149.5
Market cap £m	43.7
Historical yield	1.8%
Prospective yield	2.3%

The company chairman, Brian Marsh, has more than three decades of experience in the insurance sector, particularly in insurance broking and underwriting in Lloyd's. His core team is also experienced and has been working with him at the company for a number of years.

The portfolio currently includes 14 companies. Insurance broker Besso Insurance is the largest investment and this stake is valued at £13.9m. The 34.9% stake in independent financial adviser LEBC is valued at £8.45m, while the Hyperion stake is the third largest investment.

Helium Special Situations has increased its stake by more than 50% to 6.13%, while executive director Daniel Topping has added 2,606 shares at 152.5p each to his holding. The attraction of the shares is the one-third discount to the NAV of 225p a share. The dividend and share buy-backs are designed to reduce the discount but most of the portfolio is unquoted businesses so a discount is warranted, although the current level appears high given the track record.

Dividend news

Acquisitive vehicles distributor **Vertu Motors** reported another strong set of figures for the six months to August 2015. It says that the full-year results will be better than expected. Interim revenues grew 14% to £1.24bn (like-for-like growth of 5%) and pre-tax profit by 28% to £16.4m. Service revenues generated like-for-like growth of 6% and gross margins improved. The interim dividend was increased by 29% to 0.45p, while the total dividend for the full year is expected to improve from 1.05p a share to 1.25p a share. Since the end of the interim period, Vertu has acquired SHG, which operates three VW and Audi outlets, for £12.8m with a further £1.5m payable if certain conditions are achieved.

Panmure Gordon has upgraded its earnings forecasts for pet medicines and accessories supplier **Animalcare** due to expectations of a bigger contribution from R&D tax credits. Even so, pre-tax profit is likely to be flat at around £3m and the total dividend will remain at 6.1p a share – covered nearly two times by earnings. Animalcare is investing in its pipeline of animal drugs and this will take time to show through in the figures. Net cash was £5.8m at the end of June 2015 and this could fall slightly over the next couple of years as more is invested in drug development.

Furnishings supplier **Walker Greenbank** continues to benefit from its investment in manufacturing operations and expansion of its brand portfolio but it can still afford to increase its interim dividend by a quarter to 0.44p a share. Net debt was down to £571,000 at the end of July 2015, following an improvement in underlying profit from £3.28m to £3.68m. Cash generation is stronger in the second half and a 2015-16 profit of £8.7m is forecast. A full-year dividend of at least 2.5p a share is expected.

Expert view: The broker

More flip than flop at Shoe Zone

By ROGER TEJWANI

Shoe Zone is a leading UK specialist footwear retailer, offering low-price footwear for all the family. We initiate coverage with a target price of 236p and a buy recommendation. We think the sell-off post profit warning was overdone, although we appreciate that the valuation was frothy and trust needs to be regained.

However, at 179p, we think the forward 2016 PE multiple of 9x undervalues the achievable 7% EPS CAGR, 6% prospective yield and potential for further capital returns.

Shoe Zone sells about 20m pairs of shoes pa (£167m in revenue) through a network of 536 stores across the UK and the Republic of Ireland plus multiple online channels. The average retail price per pair of shoes sold was £9.77. The company is able to maintain low retail prices due to high volumes, direct sourcing from factories and by maintaining a low product line count.

The Shoe Zone business was acquired in 1980 by Michael and Christopher Smith (father and uncle respectively of the current CEO and COO). The retailer's online offering (www.shoezone.com), combined with its extensive store portfolio, enables its customers to shop via multiple channels.

We think the scalability and higher relative margins of online sales offer an opportunity to drive more volume online. Average basket size is 50% higher than in-store, and net margins are 2x store. Online sales can 1) expand the reach internationally 2) capture marketing data 3) test market more fashionable ranges which, if commercially viable, can be launched in-store. The large store estate can be used to underpin an increase in click & collect, removing costly last-mile delivery.

Shoes market

We estimate Shoe Zone's market share has declined over the past couple of years. Part of this is due to store closures which have clouded the picture, but we also suspect that growth rates among specialist footwear retailers have underperformed the multiples and more fashionable participants, and estimate that like-for-like sales growth has been in a range of -1% to +1% over the past three years.

> There is potential for further capital returns

Verdict estimates the size of the UK footwear market at £7.5bn, 40% of which comprises specialist providers such as Shoe Zone, which has an estimated 6% share by volume and 3% by value. The top ten retailers accounted for 46% of total sales value in 2012, according to Mintel, and Shoe Zone was the only specialist value retailer in the top ten. Mintel forecasts 3.8% CAGR for the UK footwear market between 2013 and 2018.

Households are seeing strong increases in purchasing power, and growth in real household spending of over 4% is expected for 2015. Growth of between 2% and 2.5% is forecast for 2016 and 2017.

We are pencilling in broadly flat turnover over the medium term, expecting average price points to remain static and trading space and density to stabilise. A focus on core product (shoes are 95% of the mix), low price points and a high proportion (85%) of mature, own label brands makes revenues defensive, in our view.

We forecast 120bps accretion to operating margin over the medium term through 1) increasing direct sourcing from 60-65% and cutting out the 10-20% intermediary margin 2) closure of the 50 remaining loss-making stores 3) relocation to larger stores to widen the product range while decreasing cost ratios and 4) lower rental renewal costs, which are down 24% on average in each of the past three years and continue to fall due to low average outstanding lease length.

We expect the impact of the National Living Wage on Shoe Zone to be broadly neutral, with the £0.5m additional annualised wage charge from next April to be largely offset by an uplift in disposable income among the C,D,E target customer base. While management estimates the gross impact of the Living Wage at £1m by 2020, the net impact will be minimised by a shift towards a younger workforce (60% are currently over 25 years).

We expect the balance sheet to remain ungeared and excess cash to be generated annually. Current low yields on cash make retention harder to justify and lack of deployment could depress returns on equity and capital. This gives management the flexibility to make capital returns, and while the 60% payout ratio is generous, the forecast dividend yield is more than twice covered by FCF yield.

We think the sell-off after the profit warning was overdone, although we appreciate that 1) the valuation was getting frothy 2) management needs to regain investor trust and 3) the high earnings base set in 2014 may weigh on the price in the short term.

ROGER TEJWANI is a research director at finnCap

feature

AIM plans tougher investing company rules

AIM is tightening the rules for shells and investing companies and plans to make them raise at least £6m to gain a quotation.

AIM is proposing changes to its rules relating to investing companies and shells. These will make it more difficult to float on AIM and for existing companies that change their strategy to maintain their quotation.

In 2005, AIM changed the rules so that new shells had to raise at least £3m in order to join AIM. Prior to that there had been a flood of shells with little or no money and vague plans to make an acquisition at some point.

The latest proposal is that shells and investing companies will have to raise at least £6m of new money in order to gain admission to AIM. The cash should not be raised from "related parties unless the related party is a substantial shareholder only and an authorised person". New shells and investing companies will still have 18 months to complete their strategy and then will have to get shareholder approval each year in order to continue the policy.

If a company sells its business or control of its operations, it becomes a shell. AIM plans to change the rules so that it will have six months, rather than 12 months, to make an acquisition or face suspension. AIM is concerned about the number of companies with little in the way of cash maintaining their quotations. There will still be a six-month suspension period before the quotation is cancelled.

This is intended to encourage shells with little prospect of making an acquisition within that time period to ask shareholder permission to leave AIM when they make the disposals rather than hang around on the market.

AIM also says that the nominated adviser must inform it if a company becomes a shell or even if there is a possibility that it will happen.

Changes

AIM is keen to avoid companies with limited liquidity floating and making little progress with their strategy. If there is limited liquidity, the share price can be pushed up on little buying activity, thereby inflating the valuation of the company.

Gate Ventures, whose chairman, Geoff Morrow, is a songwriter whose songs have been sung by Elvis Presley, provides one example of what AIM is likely to want to avoid through these rules.

Gate joined AIM on 10 March 2015 and intended to seek acquisitions in theatre production and the music industry. At that time, £3.24m was raised at 10p a share from a limited number of shareholders.

Shells and investing companies will have to raise at least £6m in order to gain admission to AIM

A lack of available shares and a limited number of large shareholdings meant that the share price shot up after trading commenced. Gate left AIM in July because Beaumont Cornish resigned as nominated adviser in June and a replacement could not be secured within one month.

When trading in the shares was suspended during June, Gate had £2.82m in the bank and little else in the way of assets yet it was capitalised at more than £103m. That is the equivalent of paying £1 for less than 3p.

Gate is still going and has moved to the Britdaq trading platform. It has invested in a couple of theatre productions but the main investment has been in Infinity Creative Media, a UK-based television production company headed by Lord Grade. There was a £2.6m investment for a 20% stake in Infinity plus an option over a further 5% stake.

Gate has had share splits since leaving AIM and its market capitalisation is £1bn, according to Britdaq. It is difficult to come up with a rational argument for this valuation.

ISDX

ISDX tightened the rules of the ISDX Growth Market relating to shells and investing companies earlier this year so any companies despatched from AIM are not likely to be able to immediately switch to ISDX.

The ISDX Growth Market does not admit cash shells. If an existing quoted company disposes of its business and becomes a cash shell with no business activity it is given six months to find a new business before trading in the shares is suspended. The company is encouraged to consider returning any remaining cash to shareholders.

The alternative is to reapply to the market as an investment vehicle. A condition of the admission of an investment vehicle is that it raises at least £500,000, which is net of the costs of raising the cash and joining the market.

An investment vehicle has to implement its stated investment strategy in one year and if it has not

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feature

then it requires shareholder approval for a further 12 months. If, after two years, the company has not made a reverse takeover or substantially implemented its strategy by investing the majority of funds, trading in the shares will be suspended. The company should then consider returning cash to shareholders. As with AIM, the quotation will be withdrawn after the shares have been suspended for six months.

Many standard list shells are illiquid

There is a fast-track route to an ISDX Growth Market quotation for companies with an existing quotation on another market. Four AIM companies have already taken advantage of this, with UK Oil & Gas Investments about to obtain the additional quotation. All of these companies were previously trading businesses that became investment companies. These can all be called investment vehicles but they appear to have implemented, or be near to implementing, their strategy.

However, ISDX is not just going to accept shells and investment companies that are looking to move purely because they do not meet AIM rules so it is unlikely to provide a haven for companies that have been kicked off AIM.

Standards

Shells are not allowed on the premium list of the Main Market but when the standard list was launched it enabled shells to gain a Main Market listing, albeit a lower-quality one.

Existing AIM shells are likely to find it difficult to move to a standard listing, but many of the new shells that would have come to AIM may find their way onto the standard list, where ongoing requirements for the companies are generally more lax than on AIM.

For example, standard list shell Non-Standard Finance (NSF), which raised £102m at 100p a share when it floated in February, has completed the acquisition of Loansathome4u, the home credit division of S&U. Because NSF is standard listed it did not require shareholder approval for the deal, although premium-listed S&U had to gain shareholder approval for the disposal. An AIM company, whether a shell or not, would be required to obtain shareholder approval if the acquisition were classed as a reversal.

There have been a number of standard list shells in recent years and many of them have raised relatively small amounts of money. There is no limit on the time that these shells have to make an acquisition. The latest is oil and gas shell Upland Resources, which joined the standard list and raised £1.3m at 1p a share. That is much lower than would be required to float a shell on AIM even under the current AIM rules.

Derbyshire-based Upland has already applied for UK onshore exploration blocks and is seeking acquisitions. Chief executive Dr Stephen Staley previously founded AIM companies Fastnet Oil & Gas and Independent Resources.

Many standard list shells are illiquid and there can be significant share price rises in early trading. They go to significant premiums within days although they do not tend to maintain all the increase.

Challenger Acquisitions floated at 10p a share in February and the price rose to 78.5p in the first few weeks, although it fell back to 38.5p prior to suspension in June ahead of publication of a prospectus for a deal involving investment in an observation wheel being built in New York. At the suspension price Challenger is trading at well over five times its net cash position.

This suggests that the problem is already shifting from AIM to the standard list.

Some shells use the standard list as a way to gain access to AIM after a deal. Standard list shell Cleeve Capital floated in December 2014 and in May, Satellite Solutions Worldwide completed its reversal into Cleeve and a move to AIM. Mithril Capital, which floated last September, has announced plans to acquire Agenda 21 Digital and move to AIM. Mithril has common backers with Satellite Solutions Worldwide.

Come-backs

Just because the investing companies will be forced to leave AIM does not mean that they will not be back. Investing and trading companies have had their quotations cancelled and returned – sometimes in a matter of months and other times after a number of years.

The latest example is Cambridge Mineral Resources (www.cambmin.co.uk). Cambridge's AIM quotation was cancelled on 5 March 2009 following the resignation of Ruegg as its nominated adviser, after it breached a prepayment funding agreement with its lender by failing to deliver enough gold by the end of 2008. It has taken more than six years to sort out the business and start to develop a new project - the 40% owned Masa Velverde zinc and copper metals project in Spain. Cambridge wants to rejoin AIM in the first quarter of 2016 and is currently trying to raise up to £500,000 via an open offer to existing shareholders at 5p a share to finance the costs of the flotation.

The consultation on the proposed new rules ends on 12 November. The results of the consultation and the finalised rules will be announced after that.

The new proposals are likely to lead to a further reduction in the tail of small AIM companies and could mean the number of companies falling below 1,000. That is not a bad thing and it should help to refocus attention on the better companies on AIM.

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statistics

Market Performance, Indices and Statistics

AIM SECTOR INFORMATION

SECTOR NAME	% OF MARKET CAP	% OF COMPANIES
Financials	22.1	18.3
Industrials	15.9	16.8
Consumer services	15	11
Healthcare	14.1	7.7
Technology	9.7	10.7
Consumer goods	8.1	5.9
Oil & gas	6.1	11.5
Basic materials	5.8	15.2
Telecoms	1.9	1.4
Utilities	1.1	1.3

FTSE INDICES

ONE-YEAR CHANGES

INDEX	PRICE	% CHANGE
FTSE AIM All-Share	737.91	+3.3
FTSE AIM 50	3926.21	+14.5
FTSE AIM 100	3398.47	+9.5
FTSE Fledgling	7802.97	+16.8
FTSE Small Cap	4599.28	+7.5
FTSE All-Share	3484.6	+0.7
FTSE 100	6361.09	-1.6

COMPANIES BY MARKET CAP

MARKET CAP	NO.
Under £5m	254
£5m-£10m	116
£10m-£25m	210
£25m-£50m	165
£50m-£100m	132
£100m-£250m	119
£250m+	67

KEY AIM STATISTICS

Total number of AIM	1063
Number of nominated advisers	35
Number of market makers	50
Total market cap for all AIM	£73.7bn
Total of new money raised	£93.9bn
Total raised by new issues	£40.1bn
Total raised by secondary issues	£53.8bn
Share turnover value (2015)	£23.6bn
Number of bargains (2015)	4.36m
Shares traded (2015)	301.8bn
Transfers to the official list	176

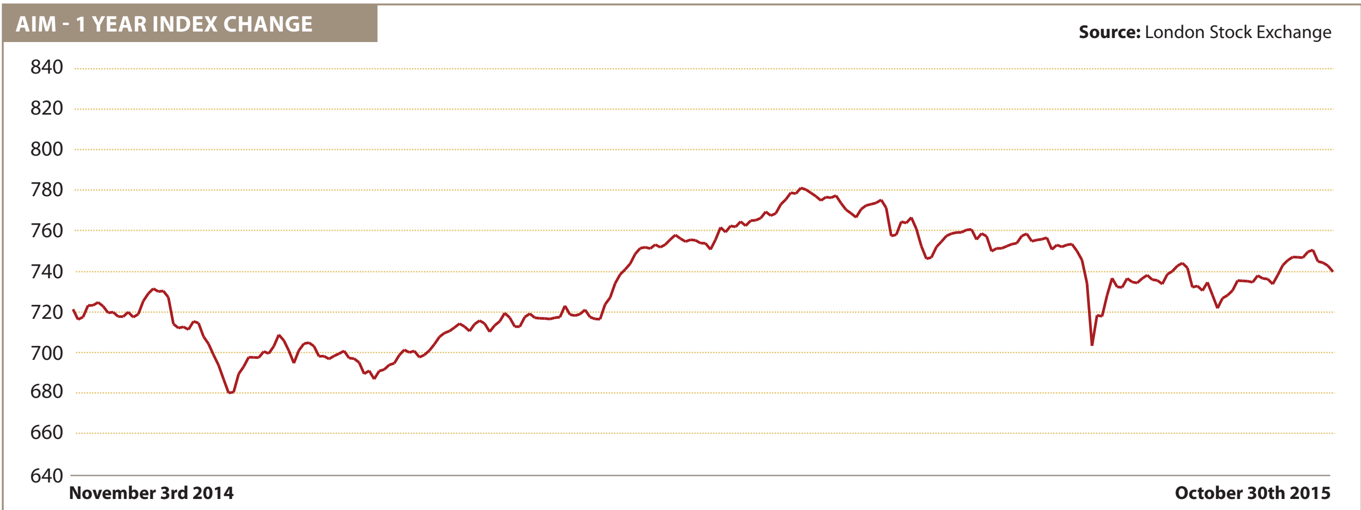
TOP 5 RISERS OVER 30 DAYS

COMPANY NAME	SECTOR	PRICE (p)	CHANGE (%)
Mobile Streams	Mobile	19	+347.1
Sovereign Mines of Africa	Mining	0.75	+188.5
Pantheion Resources	Oil and gas	75.5	+166.1
China New Energy Ltd	Cleantech	1.78	+150
Mporium Group	Mobile	9.88	+92.7

TOP 5 FALLERS OVER 30 DAYS

COMPANY NAME	SECTOR	PRICE (p)	CHANGE (%)
Sefton Resources Inc	Oil and gas	0.02	-75
Adgorithms Ltd	Media	36	-71.4
Cloudbuy	Software	6.62	-64.7
Cambria Africa	Financials	0.52	-54.4
Northbridge Industrial Services	Support services	66	-50.8

AIM - 1 YEAR INDEX CHANGE



Data: Hubinvest Please note - All share prices are the closing prices on the 31st October 2015, and we cannot accept responsibility for their accuracy.

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finnCap, whose chairman is Jon Moulton, is 95% employee-owned and is the top AIM broker by overall client numbers, according to research compiled by financial website Morningstar. The broker is also the number one adviser in the technology, industrials and healthcare sectors, number three broker in the oil and gas sector and in the top five in the basic materials sector.

In 2013, finnCap commenced market making and launched fAN Club, a new offering aimed at providing specialist support to ambitious small private businesses seeking pre-IPO funding.

finnCap was presented with the Best Research award at the 2015 AIM Awards, while finnCap's corporate broking and sales trading teams have achieved Extel Top 10 rankings for three years running. finnCap is a sponsor of the AIM Awards, the plc Awards and the UK tech Awards.

In the year to April 2015, finnCap's reported revenues were 4% higher at £16.1m, while pre-tax profit was £2.2m. The finnCap 40 Mining index, finnCap 40 E&P index and finnCap 40 Tech index were all launched during 2014.

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