



Taking AIM

Annual survey 2008

Executive summary

Meeting the challenge

This twelfth edition of Baker Tilly and Faegre & Benson's Taking AIM Survey comes at an uncertain time for global economies and markets. But while AIM's IPO volume has declined and its main share indices have fallen this year, our confidence in the market is undiminished. It remains a key source of capital and acquisition currency for fast-growing companies – both domestic and international – and continues to fully merit its unrivalled standing as the growth market for the world.



Undoubtedly, the market faces a very difficult external environment. The global credit crunch and resulting market volatility have increased risk aversion among investors to an unprecedented level. But this impacts smaller companies everywhere – not only on AIM.

We see AIM as undergoing an inevitable period of consolidation. To the extent that this may increase the quality of the market's new entrants (an abiding concern of investors, as our survey again highlights this year) and bring valuations to more sustainable levels, it may even be positive.

Consolidation challenge

Consolidation creates challenges in the nearer term, however. We do not share the pessimism of those who have already written off AIM's IPO prospects for all of 2008. But we (like the majority of the survey's 200 AIM companies, 50 institutional investors and 50 growing private companies) expect no substantial pick-up in new issues until the second half of the year.

While there is no shortage of funds available, most investors are likely to wait for more stable conditions before putting larger amounts of capital to work – especially in higher-risk opportunities.

IPOs are only one dimension of the market's capital-raising service for growth companies, however. The volume of secondary issues increased by two-thirds last year to reach a new record (£9.6 billion). This is clear evidence of investors' willingness to support strong AIM companies and underlines the market's maturity. Overall, we anticipate that capital raised on AIM in 2008 will be at around the same level as 2007.

Quartet of key themes

As last year, we structure this report around four key themes that emerged from interviews with internal and external experts on AIM: performance; regulation and legislation; advisers; and future outlook. Note that the third theme was not included last year, and the second has been modified.

Performance was robust in 2007. Although the number and value of IPOs fell sharply (by up to 50% over the year), AIM still surpassed its previous overall capital-raising high. This was due to the unmatched volume of secondary issues.

The value of IPOs in 2007 totalled £6.6 billion. This represented a fall on 2006, but still exceeded the figure recorded for 2005 - the market's record year by number of transactions.

Moreover, the main AIM indices mostly did rather better than in 2006 - although their performance still disappointed the majority of investors surveyed. The AIM 100 index, which tracks the market's largest domestic and international companies, even outperformed the FTSE 100. Having fallen 17% in 2006, it rose by 5% last year; this compares to the blue-chip benchmark's 2% gain.

The underperforming AIM All Share index did only marginally worse than in the previous year (-0.5% versus -0.2%).

Some individual stocks performed very strongly. The year's top 20 all rose by 150% or more; the best, ArgentVive, had a gain in excess of 2,000%. This reinforced AIM's standing as a market that rewards stock-pickers.

In addition, total turnover increased by as much as 30%. This growth (to some £75 billion) shows a notable increase in the market's liquidity.

Regulatory teeth shown

AIM has succeeded in balancing a commitment to upholding standards against the light regulatory touch that is one of its key assets. New rules introduced at the start of 2007 codified best market practice and imposed relatively high hurdles on nominated advisers (Nomads) and listed companies. With a series of fines and censures in recent months, the exchange has sent the AIM community a powerful reminder that the self-regulatory environment can be vigorous and vigilant.

Despite the lapses of a few, advisers generally continue to receive top marks from recently-listed companies. Some would like more help with investor relations; investors strongly echo the need for this.

Building with BRICs

Resources, one of the market's largest and best established sectors, is many experts' choice as a likely strong performer in 2008. The energy efficient technology sector should also see further new issues and price appreciation.

But AIM remains receptive to well-run smaller companies with clear prospects in any market. Equally, it continues to offer its listed companies a host of benefits: capital raising, acquisition currency, profile, credibility, low cost and liquidity. These support its longer-term outlook.

Emerging markets are likely to prove a particularly important source of new admissions. The emerging markets including Russia, India and China – and neighbouring areas such as Ukraine and Vietnam will be key. Some regulatory uncertainties over Chinese companies' ability to access foreign capital are unresolved, however.

Investors expect fewer UK admissions this year. Some survey respondents are sceptical towards their likely quality; the domestic growth outlook is also less positive than in emerging markets.

With AIM's corporate base so successfully internationalised (550-plus foreign companies), we continue to look for a comparable broadening of the investor base. Market conditions may be too volatile for much immediate progress. But, as we emphasised last year, increased investment in AIM shares by non-UK institutions will be important for AIM's growth over time.

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KEY FINDINGS

Performance of AIM

AIM in 2007 was a year of two halves. As the year opened, AIM fared strongly with more companies trading on it than the main market. In the second half of the year, however, AIM suffered from the macro forces that led to the 'credit crunch' which in turn affected most major economies and markets. Experts emphasise that market conditions led investor sentiment towards the relative safety of the larger cap stocks and this was to the detriment of AIM and other predominantly small cap markets. The differentiating opinions between companies and investors are a theme that most likely reflects the overall performance of the market and investors not picking stocks.

- Despite this, just over 60% of AIM companies said that the market's performance in 2007 was 'as expected', and most agree that the market is still meeting their needs. Furthermore, nearly two-thirds of the 50 growing private companies that participated in the survey consider AIM at least a 'fairly attractive' option for companies such as their own.
- The number of companies on the market continued to increase, albeit it at a slower pace, it continued to attract international companies and the total market capitalisation continued to increase.
- Investors were prepared for a more difficult year in 2007. Just over half (56%) said that the market's performance was 'worse' than expected; however, this is down on the 76% who thought 2006 was worse than they had expected.
- Nearly half of investors (44%) said they had increased the proportion of funds going into secondary funding, demonstrating AIM's ability to identify and nurture quality growth companies. Most investors and AIM companies alike see this trend as healthy.
- Nearly all recent AIM entrants surveyed (82%) said that the valuation of their company was as expected, and even more (88%) said that they had raised the expected funding.
- AIM companies continue to favour AIM's globalisation and investors are becoming more comfortable with it. Where most investors saw globalisation as detrimental in 2006, half of investors (50%) now see it as beneficial.

Regulation and legislation

Tighter regulation has been accepted by AIM companies and investors alike, although investors' calls for more regulation conflict with AIM companies, who find the continuing obligations increasingly time consuming.

- Most AIM companies and investors agree that the tightening of the AIM rules in early 2007 was beneficial to both the market's reputation and investor confidence (an average of 60% and 57%, respectively).

- Investor confidence was also increased by the rule changes according to 56% of companies and 58% of investors.
- The increased regulation has impacted investors' perceptions. A majority of investors (60%) surveyed said that the standard of corporate governance among new entrants was at least fairly good. This figure is double that of last year's survey.
- AIM companies are finding compliance more time consuming. 69% say their time and resource commitments have increased in the last 12 months. However, just over half of investors (54%) now support further increased regulation, up from 48% in the last survey.
- A large majority of investors (74%) disagree that low regulation means low performance. And the vast majority of AIM market participants are satisfied with self regulation. 85% of AIM companies and 72% of investors think self regulation is very or fairly effective.
- Most investors, AIM companies and private companies are against the proposed CGT changes and 64% of investors feel the effects will be detrimental to AIM. However, the majority of AIM and private companies (56%) said the changes would have no direct impact on their company or the actions of directors. Nearly all AIM companies (90%) said they would have still listed regardless of the planned tax changes.

Advisers

AIM companies old and new are pleased with the ongoing advice they receive from their Nomad, auditor and corporate lawyer.

- 84% of AIM companies are satisfied with the ongoing advice from their Nomad; 87% with their auditor and 95% with their corporate lawyer.
- Only a minority of AIM companies (39%) say they have noticed any change in the relationship with their Nomad, since the rule tightening. That said around one in ten has since changed their Nomad.
- AIM companies need more support in Investor Relations (IR) with little more than half (56%) admitting that they had IR instruction as part of their IPO process. However, 58% thought the effort spent did lead to a better understanding of their businesses by the City. But investors remain unimpressed by AIM companies' IR – only half (48% down from 51% last year) deem company activities effective.
- Fewer than one in four investors feel it is important for AIM companies to have a Big Four auditor. And only 4% consider it 'very important'.

Looking forward

AIM companies and investors approach AIM in 2008 with some nervousness. But experts agree that, while AIM will be challenged, the second half of the year should see improvements.

- Nearly two-thirds (64%) of investors predict a further drop in the number of IPOs during 2008. Experts consider, however, that better quality companies are likely to come to market.
- Experts observe that the flight to bigger stocks should not detract from successful AIM companies who are able to ride the ebbs and tides of a challenging economy.
- As in 2007, secondary funding seems set to be a major feature, with 71% of AIM companies saying they have considered this for the next 12 months.
- AIM companies (23%) cite competition from other markets as a possible threat over the next 12 months, but experts dismiss this, stressing that AIM has firmly established its model on the world stage that will be increasingly hard to replicate elsewhere.
- Nevertheless, more AIM companies than in previous surveys (and particularly those overseas) highlight the possibility of moving to another market in the future (50% overseas versus 23% of UK companies).

For a complimentary copy of the full report, please contact takingaim@bakertilly.co.uk or call +44 (0)20 7413 5418.

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We have advised on over 250 AIM transactions

We have over 160 AIM listed clients

We have acted on transactions in over 25 jurisdictions

We specialise in the Venture Capital Trust and Enterprise Investment Scheme legislation which can assist with fundraising

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