

Taking AIM

Annual survey 2010

Executive summary

Restoring confidence in AIM

AIM in 2009 – culling the weak, keeping the strong, coming of age

Although 2009 was a year of continued economic hardship and investor caution, a significant delisting of many of its smallest companies saw AIM end the year a stronger, but significantly streamlined, entity.

Indeed, with the benefit of hindsight, we may ultimately come to regard 2009 as the year that AIM came of age, showing its ability less for the volume of its IPOs, and more for its continued support of existing quoted companies.

The contrast between the size of AIM's membership and its strength may be summarised in two statistics. Whilst the AIM population at 31 December 2009 was below 1,300 for the first time since August 2005, the average market value of an AIM company at that date stood at £44 million, compared with only £24 million at the end of 2008.

The attrition rate was not, in fact, significantly higher than in the previous year (293 delistings in 2009, compared with 259 in 2008), but, with investors naturally keener on more proven secondary stocks, rather than untested start-ups, only 13 companies joined the market by IPO.

The good news is that AIM has revealed itself to be a market of maturity and strength, not to mention durability, and one with a role to play for companies advancing beyond their infancy and seeking to develop further. The most substantive proof of this is that secondary fund raisings increased from £3.2 billion in 2008 to £4.8 billion in 2009.

AIM also has the popular vote: our survey shows that the vast majority of current AIM-quoted companies (71%) support the market, saying that, if they had known about the recession, they would still have joined. Now that the dust has settled on 2009, one can see that AIM's aggregate membership is undoubtedly of a higher quality than before. This can only be good news for the market as it has responded to concerns about the merit of the companies in its previously long tail.

Cautious optimism for the second half of 2010

With the average AIM-quoted company in a reasonably strong position, and secondary funding seemingly available, our attention turns to IPOs and the likelihood of their return in significant numbers.

A substantial appetite for AIM IPOs will require an amount of economic certainty. Early 2010 sees a general election and the likelihood of two budgets, which is not the best recipe for a return of investor confidence. Of course, IPOs will still happen, but probably only for the highest quality companies – another way in which the recession will, ironically, strengthen the market's overall quality.

In the context of the future of AIM, we are delighted to see that, in the March 2010 Budget Report, the Government has, at last, announced plans to consult on allowing AIM shares to be eligible for inclusion in ISAs and on the possible relaxation of the VCT rules to make it easier for VCTs to invest in small cap companies. If implemented, these proposals will provide a real boost for the market and should provide its companies with access to valuable additional sources of capital.

As worldwide economic stability returns, and the UK economy benefits in the post-election period, there is cautious optimism for AIM's primary market expansion in the second half of 2010.

Resilience, re-establishment, readiness

The resilience of AIM's performance in 2009 should not be underestimated. Its weathering of that year's particular economic storm has re-established the market's credibility and world position after the severe difficulties of 2008. With a slimmer and stronger membership, AIM is ready both to welcome high quality entrants and to play its unique role in nurturing the further development of its existing companies.

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Performance in 2009

Whilst the speed and severity of the economic downturn – and its impact on AIM – may have taken many by surprise in 2008, so AIM's resilience and its bounce back, principally in terms of market valuations, came as welcome relief in 2009. In the view of our experts, AIM silenced its critics, re-established its credibility, reasserted its position in world markets and ended the year leaner and fitter.

- With many investors retrenching to safer positions in 2008, the beginning of 2009 saw bargains to be had on AIM as soundly based companies continued to perform well. Investment stabilised and the 66% increase in the Index over the year – more than making up the losses of the previous year – flagged up a good year for investors. Nearly two-thirds of those in our survey said that AIM's performance during the year had a positive effect on their own funds.
- With few IPOs, investors' continued support for secondary issues confirmed their faith in the market and support for its companies. This support was welcomed by the companies, for whom, with bank debt and private equity capital scarce, raising finance was a major concern.
- With some outflow of – particularly smaller – companies, those that remain on AIM are, in the main, happy with their position. Nearly three quarters of those who listed before the current downturn say that, even if they had known about it, they would still have listed. Most of these companies have stayed with AIM because of the access to capital and to institutional investors that listing brings.
- The weeding out of some of the weaker companies and the general uplift of the market over the year has reinforced many of the benefits that AIM companies have realised. Around three-quarters have seen some benefit from the access to capital, and more than one in three say this has been a major benefit (36%, up from 22% last year). 90% say that they have realised benefits in profile and credibility, two-thirds in facilitating exit for investors and in liquidity, and more than half in facilitating strategic acquisitions, and these benefits have generally strengthened since the last survey.

Looking forward

With a strong performance in 2009, both companies and investors faced 2010 with greater confidence, expecting further recovery from AIM as world markets pick up. Its premier position as a market for growing companies will encourage its recovery and growth, providing growth opportunities for investors and access to capital and investor support for AIM companies.

Both companies and investors believe that the market will be buoyed by the general upturn in world markets and renewed investor interest, with investors looking for some strong growth stories and successful IPOs to underline the market's recovery.

A majority of both institutional investors (63%) and AIM companies (53%) anticipate an improvement in AIM's performance over the next 12 months, with many expecting a full recovery in market valuation and levels of activity. Investors are perhaps a little more cautious than companies, anticipating that full recovery may not be seen until 2011 or later.

In particular, investors and our experts believe that there will only be a slow recovery in IPO activity, as investors continue to favour known companies with an established track record until confidence fully returns. However,

secondary issues are likely to continue to be well supported, and two-thirds of the UK AIM companies surveyed say that they have considered or would consider AIM for further funding in the next 12 months.

With few IPOs anticipated, it is expected that there may still be some contraction in AIM over 2010. Some smaller AIM companies may reconsider the cost and viability of remaining on AIM while they find it more difficult to attract investor attention. 60% of investors still believe that some smaller companies should consider de-listing, although the proportion of AIM companies seeing any likelihood of going private in the next 12-18 months has fallen from 22% in last year's survey to only 8%. Most investors also support further consolidation, particularly at the smaller end of the market. More than 40% of UK AIM companies see some likelihood of making acquisitions in the next 12-18 months, although the proportion seeing any likelihood of being acquired has fallen from 34% to 19%.

Investors cite a strong balance sheet, a good track record, good management and realistic valuation as the most important criteria. However, our experts underline that AIM is even more a stockpickers' market.

There may be some return to a higher level of risk in investments, with investors looking for the best growth opportunities. In last year's survey, they were staying close to home, seeing the best, safest opportunity in UK companies. However, with the UK expected to lag other markets in recovery, they see opportunities in UK companies with good overseas earnings and in overseas companies from strong growth markets. Investors believe that interest will be particularly high in China (37%) and India (23%). Sectors most favoured are mining, resources, oil and gas (37%), which has a high overseas focus, and technology and IT (33%).

Regulation

AIM's relatively light regulatory touch has always been a key feature in its success. However, the formalisation and tightening up of the rule book over the past two or three years is seen as a contributory factor in the market's resilience during the downturn and to retaining its international reputation. This has largely silenced its critics and reduced the call for further regulation.

AIM companies and experts continue to believe that AIM's self-regulation is working well (86% of companies say that it is effective), that the level of regulation is about right and that it would be a mistake to impose additional regulation on the market.

It may be that companies already feel constrained by regulation – around one in three say that the most time – and resource-consuming aspects of being an AIM listed company are regulatory compliance (37%) and reporting requirements (33%).

Whilst there is still some support among investors for further regulation, the strong market performance of the past year has perhaps eased their demands in this respect. A majority of investors now say that self-regulation is at least fairly effective (60%, up from 47% last year), and only half support the view that further increases in regulation are still required (50%, down from 67% last year).

Similarly, some pressure may also have eased on corporate governance. Nearly three-quarters of investors say that good corporate governance is more important in the current difficult environment (73%, down from 91%), and most believe the standards of corporate governance in AIM companies to be at least acceptable. Little more than one in three now believe that they are not good enough (37%, down from 58%).

Advisers and IR

The stronger performance of the past 12 months may also have relieved a little of the pressure on investor relations (IR). Nevertheless, nearly three-quarters of investors (70%, down from 76% last year) and a majority of companies (59%, down from 76%) still say that IR is more important in the current difficult environment.

There is some suggestion that companies may be putting a little less senior management time into investor relations now than they were a year ago. However, in an improved market, they believe that they are getting a better return on this investment. A majority believe that their efforts are reasonably well reflected in the City's understanding of their company (58%) and in the level of interest in their company and its shares (59%, up from 46% last year).

Most investors (60%) see companies' IR activities as at least fairly effective (no change from last year). They look for full, clear, honest and timely communication from companies, and some call for more personal communication and better web-accessible information.

Companies remain most satisfied with the quality of advice that they get from their corporate lawyers, although that from their nomads and auditors is a little more highly rated this year than last year. 92% of companies are generally pleased with the advice from their nomads (up from 86% last year), 88% with their auditors (up from 81%) and 94% with their corporate lawyers (up from 92%).

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