DIRECTAIM

A QUARTERLY UPDATE FOR AIM COMPANIES | **Q2 2015**

DO THE BENEFITS OF AN AIM LISTING OUTWEIGH THE COSTS?

BDO

INTRODUCTION
TO DIRECTAIM Q2 2015

June marks the 20th anniversary of AIM which was established in 1995 to cater for new and growing businesses seeking the benefits of a public quotation along with a flexible regulatory approach. It has since become the most successful growth market of its type in the world.

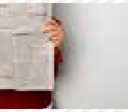
With over 1,000 companies currently listed and over 3,500 admissions during this 20 years period, AIM has become an international success.

BDO is proud to be closely associated with AIM, having helped many of those companies with their initial listing and their subsequent growth. Indeed over the last decade we having been the leading reporting accountant and we audit more AIM listed companies than anyone else.

In this edition of DirectAIM, as well as our usual look at the performance of the industry sectors in the last quarter, we have interviewed the CEO of Palace Capital, a commercial property investment company that bucked the trend for investing in London, a strategy that is helping them towards their target of £100m market capitalisation. We have also undertaken research, along with the Quoted Companies Alliance, into the costs of being listed on AIM and the desire of AIM companies to move to the main market.

I hope you find this a useful read.

SCOTT KNIGHT
Partner – BDO LLP
scott.knight@bdo.co.uk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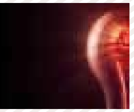
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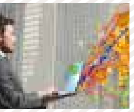
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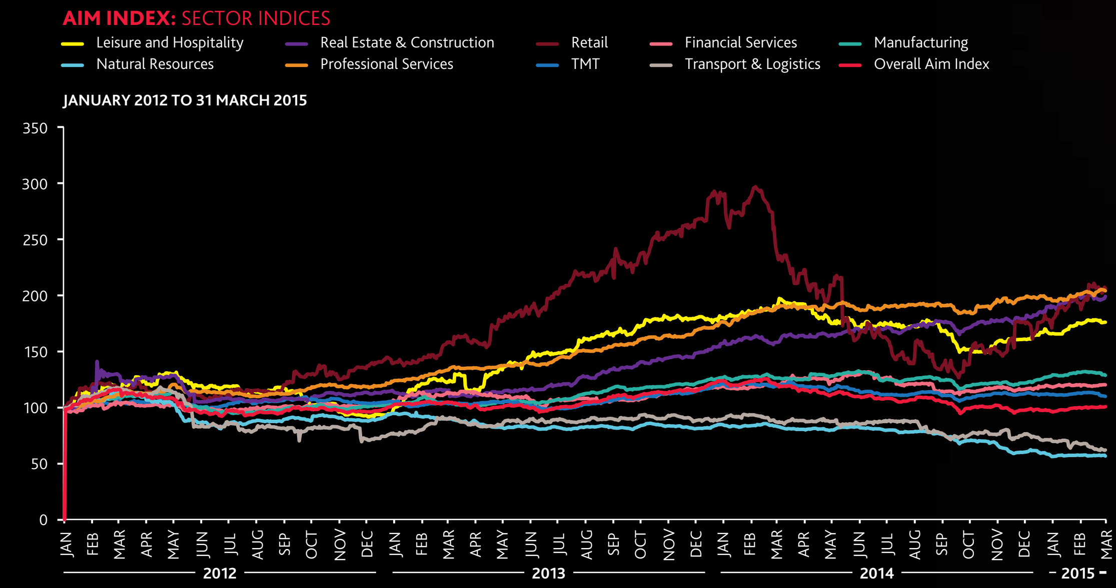
MARKET SPOTLIGHT

BDO AIM SECTORWATCH

The overall performance of the AIM index over the past quarter has been lacklustre at best with the index growing by just 2.02% over the previous quarter. Furthermore, after reaching a near-term high in Q1 2014, the index had lost 16% of this value by the end of Q1 2015. Whilst it could be argued that all small cap companies have been struggling over the past year, its closest comparable, the FTSE small cap index, saw its value grow by over 3% over the same period.

The index has undoubtedly been hit harder than the FTSE due to the number of natural resources companies on the index: indeed, if natural resources companies are stripped from the index, the performance of AIM looks more positive. Furthermore, AIM is gradually losing its reputation as being the incubator index for natural resources companies and is attracting more companies in the consumer and services sectors - some of which are seeing outstanding growth. High profile members such as ASOS and Vertu Motors are helping to drive the credibility of the index which saw £2.4bn worth of flotations in 2014 – the busiest year since 2007. The overall performance of the index is still heavily weighted by the natural resources sector – which accounts for 17% of companies on AIM – but significantly less than 2012 when they made up over 50% of the index.

However, AIM serves a purpose for smaller companies who are looking to raise capital, and is becoming increasingly attractive to foreign companies who regard AIM as a safer listing option than their home markets. There are individual pockets of success within the index: after being the strongest performer in the last quarter of 2014, the retail constituents of the index rose by a further 17.16% in Q1 2015. Retail and construction also saw a significant improvement this quarter with constituent companies rising by 9.21%. Transport and logistics continues to lie in the doldrums, seeing a fall of -18.75% over Q1; a greater fall than Natural Resources (-6.30%).



SOURCE: Bloomberg; Values rebased to 100 on 2 January 2012

MARKET SPOTLIGHT

BDO AIM SECTORWATCH
(continued)

BEST PERFORMING SECTOR INDICES ON AIM IN Q1 2015

RETAIL
+17.16%

REAL ESTATE & CONSTRUCTION
+9.21%

LEISURE & HOSPITALITY
+6.29%

WORST PERFORMING SECTOR INDICES ON AIM IN Q1 2015

TRANSPORT & LOGISTICS
-18.75%

NATURAL RESOURCES
-6.30%

TECHNOLOGY & MEDIA
-2.62%

RETAIL CONTINUES ITS OUTPERFORMANCE

Retail enjoyed a particularly strong quarter this year, with the retail constituents of the index improving by 17.16% over the previous quarter. The continued outperformance of retail comes as something of a surprise: the BDO High Street Sales Tracker has shown high street retailers' lack of widespread discounting this year has led to falling sales and also demonstrated that, despite widespread reports of consumers having more disposable income due to falling fuel prices and supermarket prices, the feelgood factor has yet to translate into better sales at shop tills.

However, the characteristic of AIM-listed companies – new, agile and a palpable search for growth – has meant they have managed to adapt their business strategies to help thwart declining consumer interest in the high street. ASOS plc, which famously saw its shareprice fall by half in 2014, has managed to successfully turn itself around: in the six months to the end of February 2015, it increased UK sales by 27% and international sales by 5%. It adapted its strategy to better match consumer needs and, crucially, got stock to its virtual shelves quickly. Despite pre-tax profits falling by 10%, due to increased international investment, shares jumped by nearly 7% in early trading after the results announcement. The company has just announced the appointment of Helen Ashton as the new CFO and investors will hope her deep financial experience, coupled with her significant knowledge of consumer-facing businesses, will help to take the company to the next level.

We also noted in the last quarter that Majestic Wines saw its share price dive by 17% after profit forecasts were cut, but it has now appeased shareholders by recently announcing it is buying online rival, Naked Wines, for £70m – a move which will help to thwart competition from wine discounting in supermarkets; the cause of its share price slide in 2014.

However, the competitive and ever changing retail market means retailers cannot afford to be complacent and the importance of a fluid and reactive strategy is crucial: Shoe Zone, which only floated on the AIM index in May 2014, recently issued a profit warning after lower sales of higher margin products such as knee-high boots due to warmer weather caused its share price to tumble by 28.3%.

BDO AIM SECTORWATCH

(continued)

REAL ESTATE AND CONSTRUCTION SEES RENEWED CONFIDENCE IN Q1

Real estate was the top performer in AIM in 2014, growing by 39%. Whilst not one of the top performers in Q4, it has continued its march in Q1 2015 showing growth of 9.21% over the quarter.

Although some investors may be reeling from the recent news that the largest company on AIM, Songbird Estates, is to be delisted following a hostile takeover, other companies on the index have seen a strong performance over the past quarter. Telford Homes plc, part of the AIM 100, recently announced that it expects to beat profit forecasts following consistently strong demand over the course of the year thanks to its strategy of developing properties in non-prime areas of London.

NewRiver Retail has also provided a boost to the AIM index: founded in 2009, the REIT was established to capitalise on investment opportunities created by the financial crisis. Its strategy of investing in retail space has proved hugely successful, and in the half year to September 2014 it made a total of £174m of acquisitions at an average yield of 8.2%. Since the 1 January this year, its shareprice has risen by 7.2% with analysts confident of a continued strong performance throughout the year.

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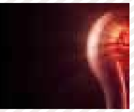
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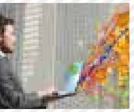
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(continued)

TRANSPORTATION AND LOGISTICS COMPANIES CONTINUE TO STUTTER

Transportation and logistics companies have continued to suffer this quarter. Interbulk Group, which we discussed in the last quarterly edition, recently saw its shares slide by a further 5% after it issued a warning that both profits and revenue will be lower in the first half of the year. The performance of the company, which is heavily reliant on demand from the European plastics market, shows the importance of ensuring a company's interests are diversified.

Many transportation and logistics companies have suffered recently due to poor economic performance within the Eurozone. However, with new figures showing that the Eurozone's GDP expanded by 0.3% in Q4 2014 and the European Central Bank projecting growth of 2.1% by 2017, the situation looks set to improve at long last.

NATURAL RESOURCES CONTINUES ITS DECLINE

Frequently blamed for the overall slump in the AIM index, the natural resources sector has had a far from comfortable ride over the year. During 2014, natural resources companies on the index saw an overall slump of 26% and, with a further decline of 6.30% in Q1 2015, there is little for investors to be happy about. 15 companies delisted in 2014, with challenging market conditions being blamed either fully or in part for the majority of these delistings. African Eagle Resources, which had its shares suspended in February 2014, had them removed entirely in February 2015 after the company failed to implement its investment strategy as required by the AIM rules.

Commodity price falls have been significant for natural resources companies - whilst the oil price decline has grabbed the headlines, base metal prices have also fallen sharply. A total of 27 companies delisted in Q1 2015 – the majority of which were natural resources companies. However, there are glimpses of hope: IronRidge Resources, a company which focuses on exploration and potential future development of iron ore resources in Africa, listed on AIM in February at 10p per share. The only commodities-focused company to list, it has already posted a narrowed pre-tax loss compared to the previous year and has received positive acclaim from the analyst community.

COMPANY FOCUS

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One hundred thousand to one hundred million in 5 years?

NEIL SINCLAIR

There is no denying it, the property sector is hot. However with yields coming down over the past year, particularly in London, managers are considering greater asset deployment outside of London and AIM listed Palace Capital is well ahead of the game.

Neil Sinclair, Chief Executive of Palace Capital, the property investment company that focuses on commercial property outside London, has the air of a man who is content but a brief read of his extensive and impressive biography soon shows he is happiest when driving and growing businesses.

Neil formed Sinclair Goldsmith in the West End of London in 1970, specialising in the acquisition, leasing and sale of commercial property and the business was successful even in the face of the economic climate at the time. As a member of the Royal Institution of Chartered Surveyors he was precluded from seeking outside shareholders but in 1986 this restriction was lifted and Sinclair Goldsmith was one of the first commercial firms to list their shares on the Official List of the London Stock Exchange. He has been involved in AIM and FTSE Main Board listed groups ever since.

Neil had four key aims on listing Sinclair Goldsmith:

1. RAISE THE FIRM'S PROFILE
2. RAISE MONEY
3. ENABLE THE COMPANY TO COMPETE WITH LARGER CONCERNS
4. INCREASE THE CHANCES TO GROW THROUGH ACQUISITIONS

COMPANY FOCUS

PALACE CAPITAL

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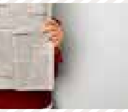
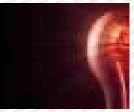
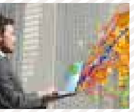
BUILDING A REGIONAL PORTFOLIO

Neil was involved in several companies following Sinclair Goldsmith before acquiring control of a listed shell company with Stanley Davis and Andrew Perloff in the summer of 2010. Their intention was to use the vehicle to buy secondary properties outside of London, believing that valuations there were on the verge of recovering after the financial crisis. They felt that they could improve rental yields and maximise asset value through careful management and building strong relationships with their tenants.

He looked at AIM companies with a market cap under £10m and found Leo Insurance. He called them up, met for a coffee the next day and the deal was done by lunchtime.

This firm was to become Palace Capital. Over the past 5 years Palace Capital has completed a few large deals with many more having fallen through, Neil often finding companies not having the assets they claimed to own. He is a stickler for due diligence and as part of the process of purchasing Quintain Estates & Developments' Sequel portfolio in 2013, Neil and his board made 5 separate trips to different parts of England.

They visited each of the 24 properties in the portfolio and listened to the tenants and letting agents who all said that things were picking up before concluding that there was potential in the portfolio. The board was convinced of its value and the deal was agreed with Quintain. However following the grant of a facility subject to credit committee approval by the existing lender Nationwide Building Society, they then needed to raise the equity.


COMPANY FOCUS

PALACE CAPITAL

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Neil approached eight brokers with six saying no immediately, feeling that they could not raise enough support for a regional property portfolio, and eventually only one said yes. After a week of due diligence, Palace Capital had a broker. They raised £23.5m of equity following 66 presentations to potential investors over a 3 week period, acquiring Sequel with a market capitalisation of £25m.

Neil believed that Sequel was lacking the intensive management needed with over £1m per annum in empty rates and with two properties in particular that were completely empty. By agreeing to pay the agents double their normal commission, both these properties were sold within three months. While Palace Capital made a profit on the sale, they also saved over £250,000 in annual rates.

They implement a different strategy for each property in their portfolio. For example, they decided to rent a 100,000 sq ft property on short term tenancies as it was 80% vacant. While the rentals were not initially strong, the saving in empty rates and void costs were significant.

Palace Capital made its second large portfolio deal in 2014 by raising another £20m to acquire the share capital of Property Investment Holdings Ltd. This company owned 17 properties which were valued at £32m. Here there were two vacant properties, one in Staines which was let within 3 months to produce a cash flow benefit of £250,000 per annum and the other in Burgess Hill where contracts have been exchanged to sell at £1.25m having been valued on acquisition at £690,000.

> Sitting across the table from Neil, it would surprise us if the next deal is not just around the corner.

Whilst Palace Capital does fast track the sale of certain properties, they have kept over 90% of the properties acquired and Neil has a strong belief that you need to keep your tenants but also, need to 'know your tenants'.

From a relatively shallow investor base in 2011, Palace Capital has attracted new shareholders such as Polar Capital European Forager Fund, Schroders Plc, Henderson Global Investors, Quantum Partners and Axa.

RELATIONSHIPS ARE CRITICAL

There are many instances of opportunities presenting themselves to Neil and Palace Capital as a result of long standing relationships and this is something that Neil feels is important. He invests much time in developing these, including speaking to local councils and is surprised that more groups do not take the time to understand what councillors are focussing on so that they can help them achieve their goals.

Although he continues to look for the next opportunity, Neil also lives by the old adage that "sometimes the best deals are those that I have walked away from".

There are still lots of potential for the firm with new developments and further portfolio deals including the recent acquisition of a 90,000 sq ft property in Leeds.

With a market capitalisation of around £80 million and with the group's history of transformative deals, Neil's goal of transforming Palace Capital from a £100,000 to a £100m company can't be far away.

BDO have been lucky to be part of Neil's career. Indeed, as we go to print, Palace Capital announced an agreement to acquire the entire issued share capital of O&H Northampton Limited, the owner of Sol Central, a mixed use leisure scheme in Northampton, for approximately £20.7m. We are acting as reporting accountants for this deal, helping Neil and his colleagues to achieve his initial objective for the group and break through the £100m market capitalisation mark. It will be helped considerably by another successful £20m fundraise.

BEING QUOTED ON AIM...

COMES AT A COST – BUT IS IT WORTH IT?

According to the results of our recent Pulse survey, which YouGov carried out on behalf of BDO and the Quoted Companies Alliance, the average cost of being quoted on AIM is around £220,000 per annum, whilst the average cost of maintaining a listing on the Main Market is more than 60% higher at around £360,000 per annum.

This total is made up of the costs of financial PR, investor relations, nomads, brokers, auditors, website maintenance, regulatory news service, registrars, annual general meeting, annual report production and the annual listing fees.

However, this captures only the external costs; the internal costs of time spent on investor relations and regulatory compliance will almost double this cost. Therefore, as a rule of thumb, the real annual cost for an AIM company is on average £500,000 and £750,000 for a Main Market listing.

Given the number of companies with a market capitalisation below £20m on AIM, this can make the cost of equity very expensive.

Nonetheless, despite these costs, being a public company does have benefits and AIM can provide a great platform for growing a company. In our survey, 54% of small and mid-cap quoted companies and 57% of advisers believe that the greatest benefit of being a quoted company is that the market provides a source of capital on a continuing basis. That is the obvious benefit, but a listing brings many other benefits that are more difficult to quantify.

BEING QUOTED ON AIM...

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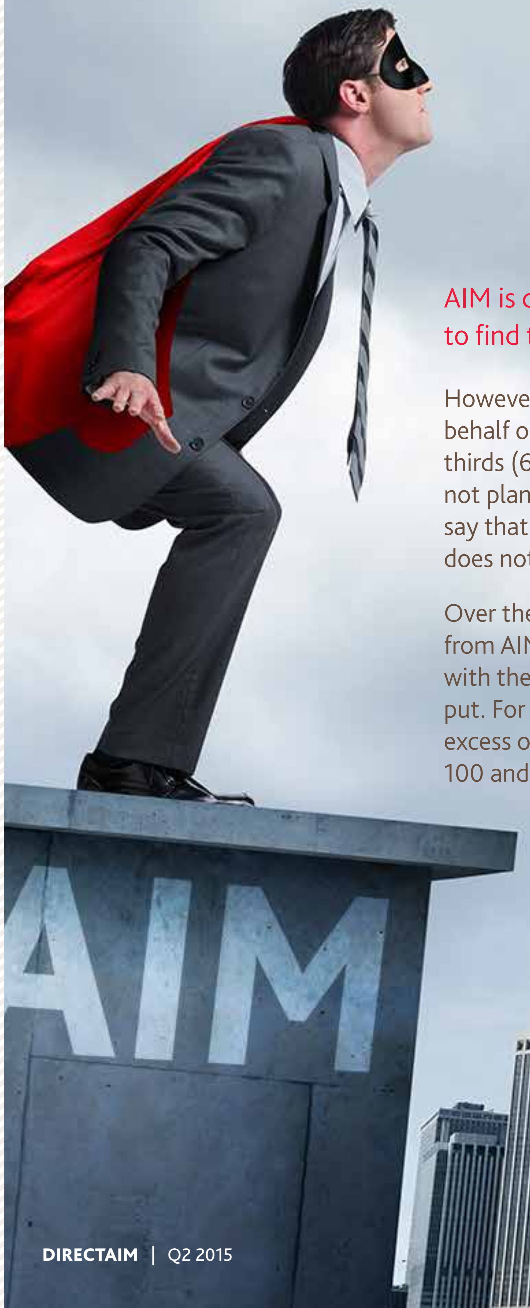
For example, an equity market listing brings the advantage of a kitemark – an endorsement that a company is fit and proper, with published information for all to see. Customers, suppliers and other stakeholders do not have to make lengthy enquiries as to the probity and financial health of a company; so in tendering situations and contract negotiations, being on AIM is a huge advantage. 29% of small and mid-cap quoted companies believe that this increased visibility is the biggest benefit of being a quoted company and more companies should recognise this benefit.

The regulatory environment for public companies will not get any easier. Most would agree that the London Stock Exchange, the Takeover Panel, the Financial Reporting Council and the Financial Conduct Authority have all become tougher than a few years ago and this trend is unlikely to reverse. 65% of small and mid-cap quoted companies and 74% of advisers believe that the greatest disincentive to being a quoted company is the high amount of management time spent complying with regulation.

The costs of falling foul of any of the above are highly significant. Increasingly, management teams may well need to look for savings to mitigate the time they spend on compliance issues, thus ensuring that the benefits of being on the market outweigh the costs.

View the full copy of our Pulse report here.

REPORTING AND GOVERNANCE



MAKING THE LEAP
TO THE MAIN MARKET

AIM is commonly viewed as a breeding ground for the Main Market, with companies using the junior market to find their feet before graduating to the more complex Main Market.

However, in research recently carried out by YouGov on behalf of BDO and the Quoted Companies Alliance, two thirds (66%) of AIM quoted companies state that they do not plan to move to the Main Market and a further 14% say that they are unsure. So, its status as a "feeder" market does not necessarily reflect reality.

Over the past 15 years, just 86 companies have graduated from AIM to the Main Market, and many of the companies with the largest capitalisation on AIM are choosing to stay put. For example, ASOS has a market capitalisation in excess of £2bn and would not look out of place in the FTSE 100 and the top 20 or so on AIM might well earn a place in the FTSE 250 if they were on the Main Market. This trend has continued in the past year with only 6 AIM companies moving to the Main Market which represents just 0.7% of the total companies on AIM.

The staying power of AIM demonstrates the attractiveness of the market. It remains a popular option for young, fast-growth companies looking to raise between £5m and £10m – an amount which is becoming significantly more prevalent now that more institutions systematically invest in companies on AIM. The lack of red tape, liquidity requirements and trading history together with ongoing tax incentives make AIM an attractive option. Our recent survey, Pulse, shows that the primary reason for companies wanting to stay on AIM is for these tax incentives, such as the inclusion of AIM shares in ISAs, the stamp duty exemption on the trading of these shares and Inheritance Tax relief. The extra financial cost of moving to the Main Market is also considered a barrier for 11% of AIM companies.

So perhaps that view of AIM being a breeding ground for the Main Market is simply not true and that AIM is a desirable place to be in its own right.

View the full copy of our Pulse report here

REPORTING AND GOVERNANCE

A BOMBSHELL FOR AIM

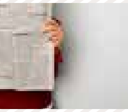
THE EUROPEAN COMMISSION CONSULTATION ON THE REVIEW DIRECTIVE

The European Commission's consultation document "Review of the Prospectus Directive" has the potential to have a major impact for future AIM admissions. Views are being requested by the European Commission on whether a prospectus should be required for admission of securities to trading on Multilateral Trading Facilities ("MTFs"), of which AIM is one.

At present, a company seeking admission to AIM prepares an Admission Document, the contents of which are set out in the AIM Rules for Companies, prescribed by the London Stock Exchange. There is currently no requirement for Admission Documents to be approved before admission. In contrast, however, the contents of a prospectus, as set out in the EC's review, would be determined by the Prospectus Directive ("PD") and, thereby EU regulation. All prospectuses would also have to be approved by the national competent authorities in the Member States, the Financial Conduct Authority in the case of the UK.

Such a major shake-up would clearly have major cost and resource implications for companies considering a listing on AIM and takes away one of the junior markets main attractions as an alternative to the FTSE. As such, the UK advisory community are responding to the consultation to express its concerns and to register its objections.

We have recently undertaken a survey of clients and advisers on the implications of this proposal with the views overwhelmingly in favour of retaining the status quo for both the AIM admission process and how the disclosure requirements of admission documents are determined.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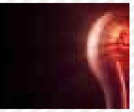
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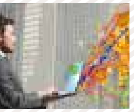
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In particular, there are strong opinions that:

- The information on an applicant in the current AIM admission document is sufficient enough to inform and protect investors
- It is a benefit to the market and investment community that AIM can draft, develop and adapt its own rules and that AIM can give derogations on its own rules in appropriate circumstances
- A company admitting to AIM should not be required to prepare a UKLA-approved prospectus rather than the current admission document
- There would be significant cost implications for a company admitting to AIM if a prospectus had to be prepared.

Our view is that AIM's lighter touch approach works for the UK capital markets and for investors. Although AIM bases its admission document requirements on the PD requirements we suspect that, if developed, an MTF prospectus would be considerably closer to a full prospectus than an admission document once the regulators got involved. Also, a benefit of AIM is that it can move relatively quickly to amend its AIM Rules to meet market and investor requirements – something that could never be said about changes to the PD.

AIM currently also has the ability to give derogations to its own AIM Rules where, for example, a disclosure in an admission document in a situation is particularly onerous (or impossible) but there is actually judged to be no detriment to investors in not strictly following the AIM Rules. Should the contents of an MTF prospectus be set out in law, the current ability to show discretion would go, and with it the element of flexibility that is so attractive to companies considering a listing on the junior market.

Companies and their advisers will continue to watch this issue with interest and concern.

CONTACT

For more details please contact:

LONDON AND SOUTH EAST

ANDY VINER Technology Media & Telecoms
t: +44 (0)20 7893 2373 | e: andrew.viner.co.uk

GERAINT JONES Real Estate and Construction
t: +44 (0)20 7893 3512 | e: geraint.jones@bdo.co.uk

DOMINIC STAMMERS Consumer Markets
t: +44 (0)20 7893 2471 | e: dominic.stammers@bdo.co.uk

VANESSA BRADLEY Financial Services
t: +44 (0)20 7893 2398 | e: vanessa.bradley@bdo.co.uk

SCOTT MCNAUGHTON Natural Resources
t: +44 (0)20 7893 2371 | e: scott.mcnaughton@bdo.co.uk

EAST ANGLIA

NICK BUXTON
t: +44 (0)1603 756 916 | e: nick.buxton@bdo.co.uk

EAST MIDLANDS

GARETH SINGLETON
t: +44 (0)115 962 9280 | e: gareth.singleton@bdo.co.uk

GATWICK & GUILDFORD

ANNA DRAPER
t: +44 (0)1293 848 952 | e: anna.draper@bdo.co.uk

MIDLANDS

TOM LAWTON
t: +44 (0)121 352 6372 | e: tom.lawton@bdo.co.uk

NORTH EAST

PAUL DAVIES
t: +44 (0)113 290 6144 | e: paul.davies@bdo.co.uk

NORTH WEST

PHILIP STORER
t: +44 (0)161 817 7510 | e: philip.storer@bdo.co.uk

READING

SIMON BROOKER
t: +44 (0)118 925 4488 | e: simon.brooker@bdo.co.uk

SCOTLAND

ALASTAIR RAE
t: +44 (0)131 347 0349 | e: alastair.rae@bdo.co.uk

SOUTH WEST

ANDREA BISHOP
t: +44 (0)117 930 1579 | e: andrea.bishop@bdo.co.uk

SOUTHAMPTON

MALCOLM THIXTON
t: +44 (0)23 8088 1895 | e: malcolm.thixton@bdo.co.uk

www.bdo.co.uk

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