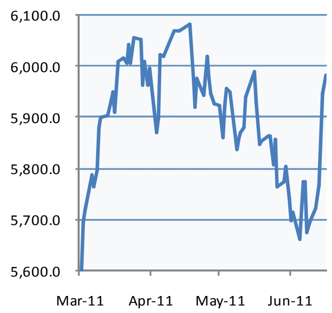
Tuesday, 5 July 2011

The next M&A wave

HB Markets

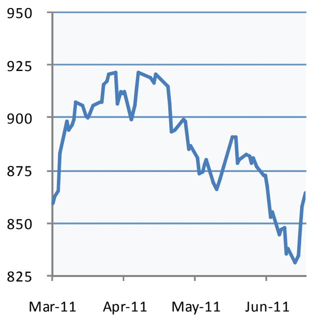
The recovery: punctured and now repaired?

FTSE-100 since mid-March



Source: Bloomberg

AIM all-share since mid-March



Source: Bloomberg

Note: *Prices and index levels in this document are taken as at close of business on Friday 1st July 2011*

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Choosing stocks for bid potential

In this note, we highlight some stocks where we think there is a better-than-evens chance of a company attracting a bid. A company can be bid for because the sector in which it operates is undergoing a series of global re-alignments; perhaps the company itself has reached the point in its cycle where its growth potential is better served inside a larger group; it may be occupying a unique niche, or it may be operating just too close to the patch of a larger, hungrier, and better-capitalised aggressor. Investors who wish to add some zest to a portfolio may find it useful to gain speculative exposure to some of the stocks where a bid might be on the cards.

- As markets seem to be emerging from a "soft patch" in this uncertain recovery cycle, one feature of global equity markets seems to be clear: conditions are right for a new wave of mergers and acquisitions to kick in.
- Potential acquirers are cash-rich: in the US alone, the corporate sector had US$1.84 trillion of uncommitted cash at the end of March, according to the Federal Reserve. With low interest rates across the developed world, debt is still cheap. Valuations of targets are still inexpensive compared to historical norms.
- For the first half of this year, global M&A deal volumes are up by almost a third relative to the same period in 2010 (measured in US dollar terms). But the number of deals struck is actually down, and in the UK the deal count so far this year is 786, compared to 952 in H1 2010.
- In recent weeks, though, old-fashioned corporate bids are beginning to surface again in the UK: the bid for Northumbrian Water by the Chinese acquirer Li Ka-shing; an approach for software firm Misys; a failed defence against a bid by the LSE; and Vedanta getting its way to take over a slice of Cairn Energy.
- It's too early to say that a trend is developing, but we do suggest that portfolios include some stocks with a dose of speculative appeal.

Top ten "bid stocks"

Large- and mid-cap stocks	Ticker	Price (p)	P/E 2011 (e) (x)	Yield 2011(e) (%)	Mkt. Cap. (£m)
BG Group	BG.	1428	17.3	1.0	48,380
Imperial Tobacco(1)	IMT	2117	11.3	4.5	21,534
Premier Oil	PMO	443	13.8	0.2	2,073
Severn Trent (2)	SVT	1494	16.6	4.4	3,549
Shire	SHP	1947	18.7	0.5	10,949
Xstrata	XTA	1389	8.7	1.5	41.180
Small-cap stocks					
Gulf Keystone Petroleum	GKP	143.3	-	-	1.092
Medgenics	MEDG	175	-	-	22
Minco	MIO	4.5	-	-	16
Noventa	NVTA	42.3	-	-	11

Note: All figures based on calendar years (end-December) except for (1) yr to Sep. and (2) yr to Mar. with actual 2011 figures.

BG Group

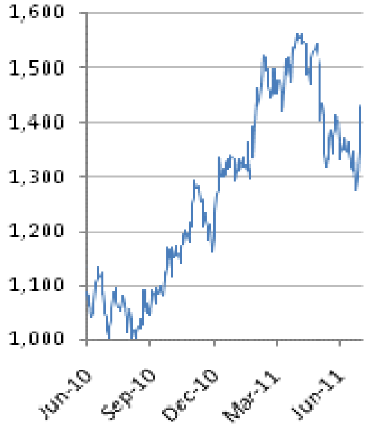
Buy (1428p)

Target:
1650p

Market Cap:
£48.4bn

Sector:
Oil & gas

Ticker:
BG.



Source Bloomberg

The case for a bid:

- **Speculation first hit the price of BG Group in August 2010, when it was thought by some commentators that a bid was in the offing. Rumours have re-surfaced from time to time, but the share price has only a modest premium relative to other oil companies, reflecting its speculative potential.**
- **The assets could be worth around £55bn on a break-up, according to some market estimates. BG has a number of particularly attractive assets, including offshore fields in Brazil and projects in Australia, that could well appeal to the majors like Shell and Exxon.**
- **Royal Dutch Shell, Exxon Mobil and Petrobras have all been reported as possible buyers of BG in the past, but no bids have ever been made.**
- **BG was formed as part of the demerger of British Gas in 1997. Partly as a result of its history, the group has the size and scope to be of interest to a major bidder, but of course it will never grow fast enough organically to reach the scale of a major global oil company itself: its nearest British counterpart, BP, has almost exactly twice the size of BG Group, having a market capitalisation of £87bn vs £43bn for BG.**
- **Stable oil prices above US$100/bl (currently US$111.80) will make acquisition strategies more appealing for the majors.**

The company fundamentals:

- BG Group is a global energy business with interests in more than 25 countries across five continents. It is engaged in the exploration, development, production, transmission, distribution and supply of natural gas. It is the sixth largest oil and gas group in Western Europe (measured by market capitalisation).
- On fundamental criteria, the stock is rather more expensive than BP or Royal Dutch Shell. With a 2012(e) P/E of 14.6x and a yield of only just over 1%, it looks at first sight to offer poor value compared to BP's ratios for the same period of 5.9x and 3.8% respectively. But the risks are arguably lower, the growth prospects considerably brighter and the sum-of-the-parts valuation is around 1700p per share – some 19% higher than the current share price.
- We believe there is already some speculative premium in the BG share price, but a full bid would need to come close to the true asset value. Though not a yield play like other oil majors, we think the shares may be bought at current levels.

Forecasts

Yr to Dec (£bn)	11(e)	12(e)
Sales	12.7	14.2
Pre-tax	5.12	5.85
EPS (p)	82.7	97.7
P/E (x)	17.3	14.6
Div. (p)	14.8	16.2
Yield (%)	1.0	1.1

Source: Consensus estimates

Imperial Tobacco

Buy (2117p)

Target:

2400p

Market Cap:

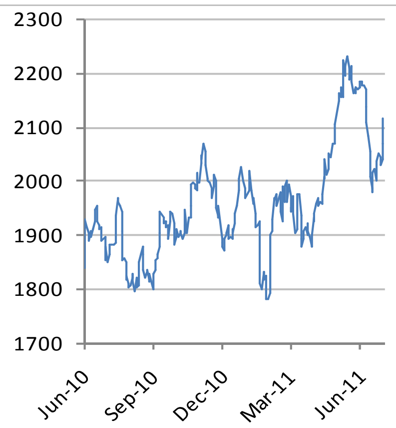
£21.5bn

Sector:

Tobacco

Ticker:

IMT



Source Bloomberg

The case for a bid:

- **Consolidation through mergers and takeovers has been a feature of the tobacco sector for well over a decade. Well- known names such as Rothmans and Gallaher were absorbed respectively by BAT in 1999 and Japan Tobacco in 2007, while Philip Morris took over the Rothmans and Benson & Hedges brands in North America. Altadis, itself the product of a merger between France's Seita and Spain's Tabacalera, was bought by Imperial for £11bn in 2008.**

- **A few years ago, there were seven global majors in the tobacco industry. Now there are four. And quite possibly, we think, there will one day be only three.**

- **BAT could be an acquirer of Imperial. It had cash of £2.3bn at the end of its last fiscal year, and like all the tobacco companies, it has very strong cash flow. It has capacity to increase its borrowing to finance a take-over of Imperial, and of course the stock market could easily absorb a capital issue if it were to fund a take-over through an issue of equity.**

- **Tobacco is a growing business across emerging economies, and professional investors sometimes regard the tobacco companies as a play on the growth of consumer spending across the developing markets of Africa, Asia and Latin America. An enlarged BAT, taking in Imperial brands such as Lambert & Butler, Embassy and John Player Special, could enhance its global appeal and generate further economies of scale.**

- **BAT is smaller than its major US counterpart with a market cap of £52bn. In contrast, Philip Morris is worth US$116bn (£73bn). Arguably, it needs greater scale to stay close to the forefront of the sector: the acquisition of Imperial would be the obvious growth route.**

The company fundamentals:

- Imperial Tobacco is a major global tobacco company, with products across all tobacco categories, including brands such as *Davidoff, Gauloises Blondes, Rizla, Golden Virginia*, and many others. The Group has a presence in over 160 countries worldwide, operates 51 manufacturing sites, and has around 38,000 employees.

- Investment fundamentals are attractive, irrespective of the speculative appeal. This is a high-yielding stock with a high pay-out ratio, with defensive properties particularly because sales tend to be largely uncorrelated with the consumer economy.

- Although there have been some concerns for this year because of pricing issues in Spain, a key market, the longer-term trend for growth in earnings is in the range of 7% to 8% per annum.

Forecasts

Yr to Sep (£bn)	11(e)	12(e)
Sales	8.01	8.28
Pre-tax	2.55	2.73
EPS (p)	188	206
P/E (x)	11.3	10.3
Div. (p)	94	106
Yield (%)	4.5	5.0

Source: Consensus estimates

Premier Oil

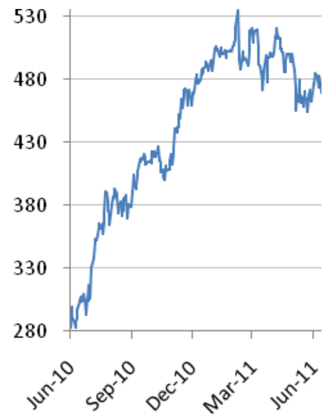
Buy (443p)

Target:
620p

Market Cap:
£2.1bn

Sector:
Oil and gas

Ticker:
PMO



Source Bloomberg

The case for a bid:

- **It was in 2006, when bid chatter had taken Premier's shares to an all-time high, that the company first admitted it was in takeover talks with an unnamed party, believed to be Dubai Energy. The bid came to nothing.**
- **More recently, several brokers have commented that Premier – nowadays less risky and more asset-rich - could be attractive to a bidder at current levels.**
- **As Premier has shifted its activity away from exploration and more directly into production, it becomes more realistic to consider it a target for an oil major. It has a rapidly growing production profile, which has been estimated by some analysts to reach 135,000 barrels a day by 2015.**
- **Premier has a solid core asset base, and a number of near-term developments are set to come on stream over the next year. Its net asset value is estimated at around 640p per share**
- **On the exploration side, Premier is focused on three core areas: the North Sea, Indonesia, and Vietnam. There could be a significant increase to the asset value as the drilling proceeds on prospects in these areas.**
- **Premier has a sound balance sheet and is well funded. It recently issued bonds for US$350m, giving it the financial resources to accelerate new development projects or acquire new interests in exploration blocks.**

Forecasts

Yr to Dec. (US$bn)	11(e)	12(e)
Sales	1.02	1.56
Pre-tax	0.41	0.69
EPS (¢)	51.7	85.5
P/E (x)	13.8	8.3
Div. (¢)	1.5	-
Yield (%)	0.2	-

Source: Consensus estimates

The company fundamentals:

- Premier Oil plc is a FTSE-250 listed oil and gas exploration and production company, with current interests in eight countries around the world. In 2009 it acquired the company Oilexco, which strengthened its base in the North Sea, and it has major assets in Indonesia, Pakistan, and Vietnam. It produces 100,000 barrels of oil per day and has around 400 million barrels of reserves.
- The strong growth expected in revenue and profits derives from the number of assets which are expected to move into production over 2011 and 2012. Longer-term growth could be achieved from recently awarded exploration blocks in Egypt and Kenya.
- The company's balance sheet had relatively modest gearing of 26% at end 2010, and should be able to fund further growth without fresh capital.
- The value case lies in the discount of more than 30% to estimated net assets, which could be as high as 640p per share.

Severn Trent

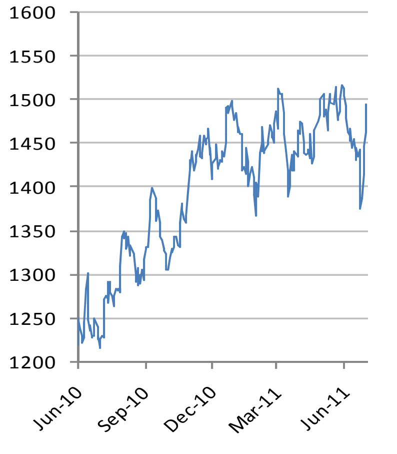
Speculative Hold (1494p)

Target:
1600p

Market Cap:
£3.5bn

Sector:
Water

Ticker:
SVT



Source Bloomberg

Forecasts		
Yr to Mar (£m)	11(a)	12(e)
Sales	1,720	1,801
Pre-tax	280	314
EPS (p)	89.8	97.9
P/E (x)	16.6	15.3
Div. (p)	65.4	70.0
Yield (%)	4.4	4.7

Source: Consensus estimates

The case for a bid:

- **Severn Trent was seriously considered as a bid target as long ago as 2006, when rumours were reported in the press that private equity groups Kohlberg Kravis Roberts and Apollo were considering a £5 billion bid. It was around the same time that Thames Water, Anglian, and South East Water all changed hands.**

- **Now the water utilities are back in the limelight. Water utilities are primarily attractive to a bidder because they have stable, long-term and predictable cash-flows, currently yielding more than long-term treasury bonds and with risks which are low for equities.**

- **Water utility companies are attractive opportunities for sovereign wealth funds, and private equity bidders. Kelda, (formerly Yorkshire Water) went to a consortium of funds in 2007. However, another bid for a water company by a major European utility group is not to be excluded: Thames Water passed initially to RWE (Germany), before being sold on, while Veolia, the French group, has numerous assets in the UK water sector.**

- **Of the three remaining independent water companies, Severn Trent looks the likeliest to be bid for. Pennon is a more complicated mix of waste treatment and disposal companies, while United Utilities is larger and possibly less digestible – at least from the standpoint of funds or private equity buyers. United is also the most heavily affected by the costs of recent regulatory changes requiring the adoption of private sewers.**

The company fundamentals:

- Severn Trent Water provides water and sewerage services to over 3.7 million households and businesses in the Midlands and mid Wales. Between 1991 and 2006 the company also owned Biffa, a waste management group which was subsequently demerged.

- From October 2011, Severn Trent (along with all UK water companies) will be obliged by new legislation to adopt all privately-owned sewers and drains, which will generate additional requirements for capital expenditure and increase overheads.

- In addition to this negative factor, we believe that a significant bid premium is already built into the price of Severn Trent's shares. The upside from a bid may be less than in other take-over situations.

- Nevertheless, the stock has defensive properties and an adequate yield, as well as speculative appeal. We recommend it as a Speculative Hold.

Shire

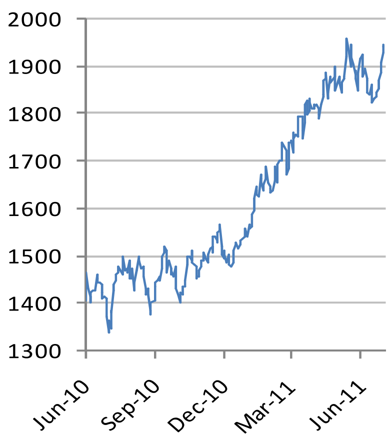
Buy (1947p)

Target:
2200p

Market Cap:
£10.9bn

Sector:
Pharmaceuticals

Ticker:
SHP



Source Bloomberg

Forecasts		
Yr to Dec. (US$m)	**11(e)**	**12(e)**
Sales	4,002	4,447
Pre-tax	1,212	1,404
EPS (¢)	168	192
P/E (x)	18.7	16.3
Div. (¢)	16.0	18.5
Yield (%)	0.5	0.6

Source: Consensus estimates

The case for a bid:

- **The pharmaceutical industry and its related sector of medical technology have given rise to two of the largest deals of 2011 so far. France's Sanofi acquired Genzyme Corp., a major US biotech company, for US$19.6bn in February, while Johnson & Johnson bought Synthes, which makes medical devices for trauma victims, for US$19.6bn.**

- **Patent expiries on some of the world's best-selling drugs are a major threat to the world's largest pharmaceutical companies, and several will be seeking to replace profit margins by acquiring new portfolios of drugs. Some US$33bn of drug sales in the USA alone will be exposed to generics when their patents expire in 2012. The most affected are Eli Lilly and Pfizer.**

- **As Britain's third largest pharmaceutical company, Shire is vulnerable to a takeover. GlaxoSmithKline (£75bn market capitalisation) and AstraZeneca (£43bn) are probably too large for a bidder from within the industry, but Shire could be financed by an asset-hungry acquirer without the need for a massive issue of shares by the buyer, and without causing significant dilution.**

- **Shire has itself been an acquirer this year, purchasing Advanced BioHealing (ABH) for US$750m. This company's lead product is Dermagraft, a treatment for diabetic foot ulcers. The acquisition is expected to enhance Shire's earnings from 2013 onwards.**

- **Shire is a high-growth stock (earnings are estimated to grow by around 24% a year to 2015) with a valuable portfolio of patents. It looks like an attractive target at the current share price.**

The company fundamentals:

- Shire is a mid-sized pharmaceutical company, founded in 1986 and first listed in 1996. Its main focus has historically been the mental abnormality Attention Deficit Hyperactivity Disorder, with other areas taking in gastrointestinal treatments, human genetic therapies and renal diseases.

- With an expected compound annual growth rate in excess of 20% for earnings over the period 2011-2015, the P/E is inexpensive even on a current year prospective of nearly 19x.

- Shire's recent acquisition of ABH appears to be positive, both in terms of the fit with the company's existing portfolio, and the potential to enhance earnings growth over the medium term.

- A sum-of-the-parts analysis of Shire's portfolio of drugs may give rise to a valuation in the range of £22 to £23 per share.

Xstrata

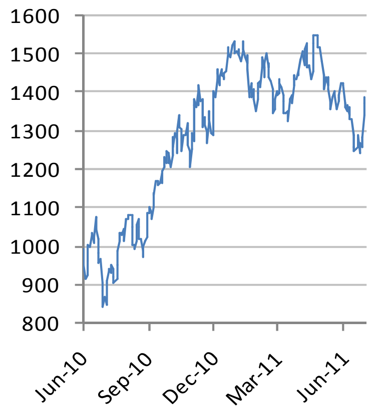
Buy (1389p)

Target:
1800p

Market Cap:
£41.2bn

Sector:
Mining

Ticker:
XTA



Source Bloomberg

The case for a bid:

- **The recent London listing of Glencore, a Swiss-based mining and commodities trading company, may well prove to be the trigger for a bid for Xstrata.**
- **Ivan Glasenberg, chief executive of Glencore, told the *Financial Times* (May 5th 2011) that "…there is good value in the two companies being together". The Swiss company already has a stake of more than 34% of Xstrata. He said that Xstrata wanted Glencore to go public and get a market price before entering into discussions.**
- **But the outcome is more complicated than it may at first appear. It has also been reported that senior executives from Brazil's Vale have met Glasenberg, to discuss a valuation at which Glencore might sell its stake to Vale, thereby triggering a full bid from the Brazilians.**
- **Several analysts have suggested that a fair value would be likely to value Xstrata at up to £53bn, but a take-over – especially if ownership were to be decided by competing bids – may well take the shares to a higher premium, possibly as high as 30%-40% above the current price.**
- **The group has assets of global importance in production of copper, coking coal, thermal coal, nickel, ferrochrome, vanadium and zinc. Control of these assets may also be attractive to buyers from China, where the issue of securing the resources to sustain economic growth and urbanisation for the coming decades is of critical national importance.**

Forecasts

Yr to Dec. (US$bn)	11(e)	12(e)
Sales	36.0	38.4
Pre-tax	10.9	12.4
EPS (¢)	256	285
P/E (x)	8.7	7.0
Div. (¢)	32.7	35.7
Yield (%)	1.5	1.6

Source: Consensus estimates

The company fundamentals:

- Xstrata was listed in 2002. It rapidly increased in size by making large acquisitions in Australia, Canada, and elsewhere. Today it has major operations or projects in eighteen countries, producing copper, coking coal, thermal coal, nickel, ferrochrome, vanadium and zinc. It has smaller-scale involvement in aluminum, gold, lead and silver. It also has interests in platinum through its 24.9% stake in Lonmin.
- Perceived demand for metals and other resources is the key driver to Xstrata's share price, alongside the discount to the real asset value.
- The stock should be bought for portfolios as a play on the industrialisation and long-term development of emerging markets, especially China and India. Valuation is not excessive even without the speculative angle on Xstrata's longer-term ownership, though yield support is relatively modest.

Gulf Keystone Petroleum

Speculative Buy

(143.3p)

Target:

220p

Market Cap:

£1.1bn

Sector:

Oil and gas

Ticker:

GKP

Source Bloomberg

Forecasts

Yr to Dec (US$m)	11(e)	12(e)
Sales	24.7	51.9
Pre-tax	(14.8)	15.2
EPS (¢)	(2.7)	2.7
P/E (x)	-	85.3
Div. (¢)	-	-
Yield (%)	-	-

Source: Consensus estimates

The case for a bid:

- **Bid speculation on Gulf Keystone first erupted almost two years ago, when newswires carried the spurious story that the company was in discussions with a joint venture comprising Indian Oil Corporation and Oil India for an eventual take-over. The story was denied in an official announcement from the company.**

- **Gulf Keystone is sometimes considered a take-over target because of the almost unique geography of its assets. It is one of 40 companies present in the Kurdistan region of Iraq, but virtually the only one focusing primarily on the region. Kurdistan represents a geological extension of the world's most abundant hydrocarbon resource (which extends overall from Saudi Arabia to Syria). Due to the war in Iraq, resources in Kurdistan have not been explored or drilled. It was only after the overthrow of Saddam Hussein that Kurdistan began to open itself to foreign investment.**

- **Gulf Keystone has stated that the range of oil in place for the Shaikan structure in the Kurdistan region is between 4.9bbo and 10.8bbo (billion barrels of oil), with a mean of 7.5bbo. This is a vast deposit, of sufficient scale to be of interest to one of the major integrated oil globals (such as Royal Dutch, Exxon, or BP) as a target for replacement of its own reserves.**

- **The likeliest buyers, however, would be those European companies which already have significant operations in the region (for example OMV of Austria or Mol of Hungary), or a private equity fund specialising in petrochemical assets.**

- **The company has to upgrade the status of its findings before it can truly realise its maximum potential for a take-over. But we would not rule out the possibility of a pre-emptive deal over the next twelve to eighteen months.**

The company fundamentals:

- Gulf Keystone is an independent oil and gas exploration and production company with operations in the Kurdistan Region of Iraq. It was listed on AIM in 2004 and is now the largest stock by market capitalisation on the AIM market.

- As an AIM-listed small-cap, share price movements are closely correlated to the news flow from the company itself rather than analysts' forecasts. A further upward revision to the estimates is expected as drilling proceeds to greater depths on the Shaikan-2 block, the second of four wells which Gulf Keystone is drilling.

- There have been numerous brokers' analyses of the total resource, including one which guessed a potential for at 18bbo at just one of the company's four blocks. Whether or not this is real, there seem to be good ground for taking a position in Gulf Keystone for its inherent asset potential.

Medgenics

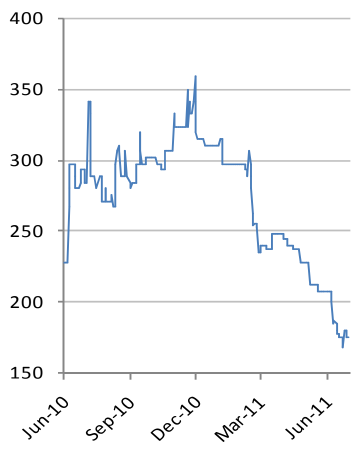
Speculative Buy (175p)

Target:
350p

Market Cap:
£21.9m

Sector:
Biotechnology

Ticker:
MEDG



Source Bloomberg

Reported figures		
Yr to Dec (US$ thou)	**09**	**10**
Income	327	2,577
R&D expenses	2,267	3.377
Pre-tax	(6,941)	(4,145)
EPS (p)	-	-
P/E (x)	-	-
Div. (p)	-	-

Source: Medgenics

The case for a bid:

- **Most of the biotechnology companies on AIM are working towards a definitive drug discovery or a therapeutic solution which can then be licensed out and eventually bought by a major pharmaceutical company. We have selected Medgenics from a number of possibilities for several reasons.**

- **Medgenics already has a major pharmaceutical partner (whose identity is undisclosed). Having signed a development agreement in 2009, this undisclosed partner has paid Medgenics US$4m to co-develop a further version of its Biopump for treating haemophilia. In November 2010, Medgenics took over the pre-clinical development as part of an extension to the agreement. The company now indicates that this work has gone well and the yields improved, so news that its partner has signed a definitive agreement could identify an eventual bidder.**

- **Medgenics is at a relatively late stage with the Phase I and Phase II clinical trial for Epodure, the version of Biopump which treats amnesia. Completion is expected this year, with the possible signing of a development partner and approval to start a more substantial US-based phase IIb study. This in turn could also lead to licensing out, an equity stake or a full bid.**

- **Medgenics is targeting the large and rapidly growing global US$50bn protein therapy market, which is expected to grow to some US$95 billion per year in the short term. The breadth of application for the products of Medgenics, combined with the current stage of development, has led at least one biotech analyst to identify the end-of-year fair value for the company in excess of £50m. This would imply an upside potential of 130% from current levels.**

The company fundamentals:

- Medgenics is a medical technology and therapeutics company focused on sustained protein therapies. Its proprietary technology, called the Biopump Platform, uses the patient's own skin to produce and deliver the patient's own protein therapy. It aims to treat a range of chronic diseases, including anaemia, hepatitis C, haemophilia, multiple sclerosis, arthritis, paediatric growth hormone deficiency, diabetes and other chronic diseases.

- Interim results will be announced in August, providing a further insight into the stage of development of the clinical trials and perhaps news of further agreements with the pharma partner.

- As with all biotech companies, risks of failure are high. However, we think that several important hurdles have been surmounted already, and the stock looks good value after recent price declines. We recommend as a Speculative Buy.

Minco

Speculative Buy (4.5p)

Target:
9.0p

Market Cap:
£15.8m

Sector:
Mining

Ticker:
MIO

Source Bloomberg

The case for a bid:

- **Minco is an AIM-listed mining exploration and development company engaged in zinc exploration in Ireland via a joint venture. It also has investments in base metal and silver projects in Mexico, through a 40% investment in Xtierra, which in turn is listed on the Toronto TSX exchange.**
- **The company is a bid candidate mainly because of its 23.6% of the Pallas Green exploration project, held through a joint venture with Xstrata Zinc.**
- **Although zinc has historically not been one of the most strongly-performing metals – at least since 2006 – some commentators believe that the world market for zinc will force prices higher. Many large-scale zinc projects under consideration are in inaccessible locations or are in economically and politically unstable countries (such as Burkina Faso and Indonesia). In addition exhaustion of existing mines will soon become an issue. The most notable example of this is Xstrata's New Brunswick mine in Canada.**
- **Since its low point in December 2008, the spot price of zinc has more than doubled, according to the S&P GSCI zinc index. It now stands at US$ 1.064/lb.**
- **Xstrata commented last year that "Pallas Green discoveries...continue to show encouraging signs of a world-class resource". It has indicated a potential start-up date of 2017 for the project, with an indicated annual production of 160,000 tonnes of zinc.**
- **We think that Xstrata itself is the most likely acquirer of Minco. But any of the major mining companies, including BHP Billiton, Rio, or Vedanta could eventually be seeking to extend their portfolios of zinc assets via acquisition.**

The company fundamentals:

- Minco and Xstrata have reported an updated JORC-compliant inferred resource estimate of 24 million tonnes of zinc at Pallas Green, suggesting that it may prove to be part of a world-class deposit. News flow from the 40%-owned affiliate Xtierra has indicated a resource estimate of 9.7 million tonnes of silver.
- Around 65% of Minco's market valuation is attributable to its 23.6% stake in its zinc and lead exploration joint venture with London-quoted Xstrata Plc, at Pallas Green, near Limerick, Ireland.
- We estimate that the assets of Minco could be valued at some £20m - £25m, allowing for significant upside potential as the newsflow accelerates. We rate the shares a Speculative Buy.

Reported figures

Yr to Dec (US$000)	09	10
Pre-tax loss	(4,998)	(1,957)
Net assets	23,710	18,974
Cash & equiv.	1,678	1,226
EPS (p)	-	-
P/E (x)	-	-
Div. (p)	-	-

Source: Minco

Noventa

Speculative Buy (42.3p)

Target:
80p

Market Cap:
£11.1m

Sector:
Mining

Ticker:
NVTA

Source Bloomberg

Reported figures

Yr to Dec. (US$ 000)	09	10
Revenue	5,709	2,301
Operating loss	(10,662)	(9,476)
Cash & equiv.	5,029	23,396
EPS (p)	-	-
P/E (x)	-	-
Div. (p)	-	-

Source: Noventa

The case for a bid:

- **Noventa was one of the small-cap stocks which stood out the most in June this year, for all the wrong reasons. Shares dropped by over 60% in a single day when it issued a warning of delays and spiralling costs at its Marropino tantalum mine in Mozambique. The company has burnt through its cash without achieving a suitable contract with an engineering company to build and manage its project. Noventa has already spent some £33m, but warned of an "urgent fundraising requirement".**

- **The company holds title to mining concessions at Marropino, Morrua and Mutala in the Zambezia province of Mozambique, and exploration licences over various adjacent areas. It is primarily a miner of tantalum, a key component in every mobile phone as well as a host of consumer electronics and aircraft engine blades.**

- **This is the territory of a rescue and recovery bid: the existing team of management has under-estimated, over-spent, and conspicuously failed to deliver. What is now required is a competent mining team to secure adequate funding, take the company over, and retire all of the top management. The underlying asset is a rare and valuable resource which in an under-supplied market could be valued at a multiple of Noventa's current market capitalisation.**

- **Tantalum prices have more than trebled over the last two years, as shortage of supply persists.**

- **Payback on Noventa's projects was anticipated at just 20 months, while the net present value of the two mines has been estimated at US$60m according to a report from Scott Wilson Roscoe Postle. The stock was sometimes referred to as a bid target when it traded as high as 285p earlier this year.**

The company fundamentals:

- Noventa is engaged in producing tantalum concentrate. Tantalum is a heavy metal that is used in the manufacture of electronic capacitors, turbine blades, medical applications, and industrial cutting tools. It holds title to mining in Mozambique.

- The mining licences have the capacity to supply up to 7% of total global demand for tantalum within a time frame of two years, according to original estimates.

- If mined successfully, even after allowing for further funding, the shares could appreciate by a multiple of their current value.

- However, investment in Noventa is not for the faint-hearted, as liquidation of the company and sale of its licences is a risk if it fails to attract a bidder.

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