

AIM: Waste & Disposal Services

27 November 2009

Nature Group

CORPORATE*

Initiation: Cleantech solid growth

22p#

Year-end December	2008A	2009E	2010E	2011E
Gross Turnover (£m)	3.38	5.56	8.61	8.97
EBITDA (£m)	0.87	2.05	2.70	2.93
Adj. Pre-tax Profit (£m)	0.51	1.44	1.99	2.18
Adj. EPS (p)	1.8	3.4	4.6	5.1
DPS (p)	0	0.5	0.62	0.68
Net Cash/(Debt) (£m)	0.40	0.78	1.69	2.78
P/E (x)	12.2	6.5	4.8	4.3
Dividend yield (%)	0%	2.3%	2.8%	3.1%
EV/EBITDA (x)	9.3	3.8	2.5	2.0

Source: Astaire Securities estimates

*Priced at market close, 26 November 2009

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Nature's businesses grew strongly in H12009 boosted by the first time 100% consolidation of Gibraltar operations as well as organic growth. PBT at £0.628m comfortably exceeded that for the whole of 2008. A US\$4.2m contract to design and build a ship sullage and sludge treatment plant at Duqm Port in Oman, provides a public showcase for Nature's cleantech capabilities and boosts growth further. Trading on 6.5x and 4.8x forecast 2009 and 2010 earnings, Nature represents good value in the sector.

- **Contract win:** The recent mandate win in Oman is indicative of more to come. We think the letter of intent should be viewed as a positive assessment of Nature's overall position in the market place. Increasingly, port waste operators are outsourcing complex water treatment, in favour of specialist providers. Such compliance-driven niche markets provide protection from competition and drive future growth.
- **Port profits:** The stand out Gibraltar operation Nature Port Reception Facilities (NPRF) is growing steadily but has capacity, the necessary licenses, and the convenience of location on one of the world's busiest shipping lanes to earn additional revenues by marketing its services to tanker operators and receiving waste from nearby ports that lack the necessary treatment capability.
- **Growth potential:** Nature's Offshore Treatment Unit (OTU) meets offshore rig operators' need to comply with minimal discharge policies and contain costs by treating waste water in situ. With as yet no sign of a proven competitor offering, this business should show strong revenue growth and high margins from 2010 onwards.
- **Cash flow is strong** and, with increased activity levels in Gibraltar, deployment of OTUs and the Oman contract, growth should accelerate in future. Nature intends to pay a dividend of 0.5p per share out of 2009 earnings in 2010. Forecast strong cash flow should allow a progressive dividend policy and provide funds for future growth.

Key Data	
Ticker	NGR.L
Shares in issue	38.9m
Market cap	£8.5m
12-mth price range	8.5p - 23.75p
Net cash	£0.4m
Next event	May Prelims

Company description

Nature Group is a waste treatment business specialising in treatment of vessel slops and oily wastes, recovery of oil from those wastes and the discharge of clean water at sea. It serves increasingly regulated customer groups.

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Contents

Investment Appraisal	3
The business	3
Technology	3
Key value drivers	3
Port operations, Gibraltar	4
Treatment operations	5
Nature Environmental Solutions Ltd	6
Forecasts	7
Risks	8
Competition	8
Currency	8
Commodity risk	8
Regulatory & political	8
Environmental	8
Key data	9

Investment Appraisal

The business

Nature Group Plc is the ultimate holding company for five businesses specialising in complex water treatment, including vessel slops, tanker washings, oily waste and other waste water.

Waste water and complex water treatment

Nature Group Companies	
Nature Port Reception Facilities	Gibraltar, collection, treatment of waste oil, vessel slops
Nature Environmental Solutions Ltd	Wastewater engineering projects,
Nature Technology Solutions AS	Norway, Technologies and engineering for treatment of complex oily water
Northern Treatment AS	Offshore treatment units for slop and wastewater
SAR Treatment AS	40% JV, Tananger, treatment and reception of liquid waste from the oil industry

Source: Company

Technology

Constant-flow polluted water treatment utilising small-footprint hydraulically engineered modules is a core proprietary skillset of the Nature Group. Combinations of bio and other water treatments are utilised worldwide in many industries, and from a number of suppliers. However, the ten year record of Nature Group subsidiaries in small scale and larger projects, onshore and offshore, positions Nature amongst the leaders in hydrocarbon-polluted wastewater treatment.

In Norway, patents are held over a key "green" hydrocarbon adsorbent. Marine wastewaters typically require only two phases of hydraulic/engineered flow treatment, whereas more complex wastewaters with higher Chemical Oxygen Demand (COD) from the oil industry may require more stages of treatment and also need to operate at a lower flow rate to achieve greater retention time under treatment.

Key value drivers

Nature Group's two main customer groups are the shipping industry and the oil industry, both subject to mounting levels of regulation. The core business is therefore essentially compliance driven and this underpins the growth profile of Nature Group.

Compliance driven

Marpol; The International Convention for the Prevention of Pollution From Ships requirements, reinforced by local legislation in the EU¹, drives revenues. In essence the regulations lay down standards for vessel waste management, including vessel slops, tank washings and waste water discharge. The required

¹ e.g. Directive 2000/59/EC of 27 November 2000 on port reception facilities for ship-generated waste and cargo residues, which provides for compulsory disposal of oil, oily mixtures, ships' waste and cargo residues at EU ports and enforcement of the rules on this subject; or other signatories to Marpol.

level of compliance and standards are increasing. The group has a strong Marpol skill set to help customers meet their compliance obligations.

Minimal discharge best practice; The oil industry is also subject to growing regulatory requirements worldwide as the focus on negative environmental impacts from the oil industry increases. Focus on offshore wastes and adoption of a minimal discharge policy, particularly in Norway, is a key driver of Nature's business.

Many of the group's businesses also have a dual revenue stream; fee based for the reception and treatment of waste, and a supplementary revenue stream from oil recovered. As a result, the group's revenues and earnings also have some sensitivity to crude oil prices.

Finally levels of activity in both the marine industry and the oil industry will drive revenues, as will increased marketing of the group's services.

Port operations, Gibraltar

Nature Port Reception Facilities (NPRF), formerly SORT, (Slop Oil Reception & Treatment) operates an oil slops, tanker washings and wastewater treatment facility in the port of Gibraltar under a long term agreement with the Government of Gibraltar. This business has a number of specific characteristics;

- Regulatory and legislative drivers, MARPOL/EU – all EU ports are required to provide waste reception facilities and ships are required to discharge waste unless they have sufficient capacity to reach the next port of call without discharging;
- Gibraltar has specific limitations in that waste water cannot be returned to the municipal system and must be discharged to sea and therefore has to be treated;
- Nature is the nominated waste contractor for the Port of Gibraltar;
- In addition NPRF has a Port waste management contract to provide EU compliant waste management procedures at the Port for all ships entering Gibraltar.

Nature has a 250,000 tonne annual throughput capacity bio treatment plant at the port and provides a barge service to receive oil slops from ships at anchorage and transport them to the treatment plant. The business has grown consistently and 2009 will be the eight consecutive year of growth.

Revenue streams for the Gibraltar business comprise the already mentioned port management contract, charges to ships for waste reception and treatment, and revenue from the sale of recovered oil from the treatment process. Another source of developing revenues is tanker washings, collection of which is negotiated with tanker operators transiting the Straits or with their agents, which provides a more valuable recovery of oil.

Future growth for this business depends ultimately on the ability of management to market its services effectively, to make use of its spare capacity. Nature can

Nature is the nominated waste contractor for the Port of Gibraltar

Excess capacity in Gibraltar

Growth depends on effective marketing

handle 250,000 tonne annually at its Gibraltar terminal and currently processes about 70,000 tonne. We expect growth to come from;

- Tightening up the enforcement of legislation;
- Receiving oily waste from other ports, e.g. the Spanish ports in the Canaries, and Cueta, and it recently acquired a 1,000 tonne double-hulled coastal tanker to facilitate this growth;
- Marketing its services to tanker operators to increase the portion of tanker washings - an estimated 5,000 tankers pass through the straits annually;
- Increase the number of vessels visiting Gibraltar that use its slops discharge services, currently about 4%, and market these services to ships transiting the Straits, estimated to be around 80,000 annually.

We estimate that NPRF should be capable of delivering a growth rate of about 15% p.a. for the next couple of years.

Treatment operations

The group's other operations are based in Norway, and comprise SAR Treatment (SART), Nature Technology Solutions (NTS) and Northern Treatment.

SART is a joint venture with Norwegian waste management group SAR. SAR Treatment (SART) is 40% owned by Nature Group and receives and treats waste water at the NorSea supply base in Tananger in the Stavanger area of South West Norway. This business receives waste water primarily from North Sea rigs for treatment and is licensed by the Norwegian Pollution Control Authority (SFT) to receive waste and discharge treated water to sea. The JV will treat about 30,000m³ this year, and has annual capacity to treat 60,000m³. SART contributed £0.44m as joint venture revenue to the group in H1.

Reception and treatment of oily waste and complex water in Stavanger area

NTS designs, supplies and operates on-site waste water treatment units, for the treatment of drilling fluids, oily waste and sludge and low level radioactive wastewaters primarily for the oil industry. 2009H1 revenue was NOK7m (£0.7m). NTS has an extensive blue chip customer base including Halliburton, Grundfos, Shell and Statoil and has been involved in projects such as water treatment in rig decommissioning, refinery decommissioning and treatment of waste water in oilfields.

Northern Treatment (NT) was established in 2005 based on an identified need for a small footprint, mobile unit, for treatment of slops and other wastewater offshore, which due to increasingly tighter regulation of offshore drilling rigs can no longer be discharged at sea if they contain more than 30ppm of hydrocarbons and the Norwegian target is to reach a level of 10ppm. Without an on-rig treatment solution, the wastewater has to be collected by a supply vessel and taken to an onshore reception and treatment facility such as Tananger, which is both costly for the rig operator and environmentally harmful as the activity involves burning fossil fuel to ferry large quantities of water back to land.

In situ slops treatment solution for offshore rigs

NT has developed an Offshore Treatment Unit (OTU), built into a 20ft container that can be delivered to the rig and hoisted aboard to treat slops and wastewater in situ. The unit meets the Norwegian target of less than 10ppm and Nature has a

License to discharge treated water at sea

license to discharge the treated water at sea. The unit has operated successfully this year on rigs contracted by Statoil.

The drivers for this business opportunity are compliance with minimal discharge best practice and elimination of transportation costs for slops. Regulatory pressures are rising, and, while activity levels in the North Sea are stable, cost inflation is ever present and the cost saving potential of treating waste water in situ will be hard to pass up.

The business model is to supply the OTU and operator to the rig operator on a typical budgetary day rate pricing of NOK30,000 (£3,150) per day. There are significant advantages for the rig operator, including;

- Lower costs through reduced transport of wastewater to shore;
- Lower risk of production shutdown due to full slop tanks – each day of lost operations can cost anything in the region of US\$1,000,000 and upwards.

NT intends to have 4 units operating by H2 2011. Based on recent tenders these units could be rented at NOK30,000 (£3,150) per day and the EBITDA margin for the unit is estimated at about 70%. Each unit could theoretically be generating revenue of NOK11m (£1.2m) assuming 100% capacity utilisation, with EBITDA of NOK7.7m (£0.8m) p.a.. The units cost roughly NOK5m (£0.5m) each. In 2009 the first unit will have generated about £250,000. Our forecasts are based on the units achieving NOK30,000 per day but operating for 180 days to allow for maintenance and transfers between rigs. NT will however need to increase its operational costs and offshore staffing levels to support an increased number of units. Typically staff deployment offshore is at best 50% on, 50% time off plus all normal family and leave entitlements. NT will also need to market this service.

At present NT is concentrating on opportunities in the North Sea but it has been in discussions with potential partners to help widen its operations. The benefits of these OTUs should appeal to rig operators anywhere, regardless of geography. The major oilfield service companies have all been trying to develop similar OTUs and to offer a similar service to rig operators as part of their fluids contracts but as yet none appear to have a proven solution.

Nature Environmental Solutions Ltd

NESL handles European and International wastewater engineering projects for the group. A consulting and engineering business, NESL designs systems for wastewater treatment for ports and remote locations.

NESL has received a letter of intent dated 25 November 2009 from the Unique Maritime Group (“Unique”) and Tile Marine Emirates Environmental Joint Venture which has been awarded the contract by the Oman Tender Board for the overall site construction of tankage and waste treatment facilities at the Oman Dry Dock, Duqm Port in the Sultanate of Oman. The joint venture has contracted Nature to fulfil the plant and technical services element of the contract. The letter of intent and the anticipated contract have expected gross revenues for NESL of approximately US\$4.2m. Revenues will be recognised on a percentage of completion basis and Nature expects to recognise £1.78m in 2010. Planned completion is currently estimated to be mid 2011. Typically Nature earns margins

Rental model

Broader geographical opportunity

Letter of intent for US\$4.2m for plant and technical services in Oman

on these contracts of about 20%. It is also likely there will be a tail of revenues from ongoing support services once the facility is commissioned.

Unique offers a wide array of integrated support and construction services to the maritime and offshore construction industries. Richard Eldridge (a director and substantial shareholder of Nature Group) is also a director of Unique Maritime Group in which his family have potential beneficial minority interests.

Although the Oman contract is both large and high profile, management expects NESL to be able to generate ongoing project revenues of around £1m p.a.. The Oman contract is also a good showcase for NESL's capabilities. The principal contractor selected Nature on the basis of its experience with NPRF's treatment facility and the Oman facility is an opportunity to improve on the technology.

The Oman contract is a good showcase for Nature's capabilities

Forecasts

The first-time 100% consolidation of NPRF, following the acquisition of the outstanding 50% at the end of 2008, will bring a significant increase in revenue and earnings for the full year. Organic growth of 34% in that business in the first half is also contributing to the overall growth of revenues and earnings. After reaching £1.34m in H1 we expect a full year figure for NPRF of £3.1m.

SART has shown a marked turnaround from 2008, contributing £0.44m to revenues in H1 and we expect full year revenue contribution to be £0.99m.

We expect NTS to contribute revenue of £1.22m and NT £0.25m giving total revenue for the group for 2009 of £556m. 2010 revenues are also expected to include a percentage of the Oman contract, amounting to £1.78m at current exchange rates. We have summarised our revenue and growth assumptions for 2010 and 2011 in the table below.

Forecasts and assumptions

(£m)	2008A	2009E	2010E	2011E
NPRF Sales	(50%) ¹ 1.13	3.10	3.52	4.05
% growth rate		n.a.	13.5%	15%
SART (40%) - Sales	0.48	0.99	1.04	1.09
% growth rate		106%	5%	5%
NTS - sales	1.30	1.22	1.28	1.35
% growth rate		(5%)	5%	5%
NT- Sales	0.47	0.25	0.99	1.98
% growth rate		(47%)	296%	101%
NESL revenue	n.a.	n.a.	1.78	0.50
Total group sales	3.38	5.56	8.61	8.97

Source: Nature Group, Astaire Securities estimates

¹ NPRF was 50% owned in 2008

The group has a small long-term loan in Norway of £0.2m and had net cash of £0.4m as at the end of 2008. Nature has taken out a seven year marine mortgage of £0.4m to finance the purchase of the Humber Mist. With all group subsidiaries profitable, reported net profits in the first half exceeded those for the whole of 2008 and operating cash flow has increased sharply. The group intends to pay a maiden 0.5p dividend for FY09. Cash flow will increase again in 2010 and we expect the dividend policy to be progressive.

Risks

Competition

Nature is insulated from competition in the Port of Gibraltar by virtue of being the nominated waste contractor for the Port. However in its drive for growth from attracting ship operators to use its services for tanker washings, de-bunkering etc and in attracting business from nearby ports without treatment facilities, Nature will be competing with other port operators that do have the requisite facilities. This can be mitigated by securing long-term contracts and ensuring the service is competitive, which Gibraltar's location and Nature's spare capacity helps. SART is also offered a measure of protection by its location at Tananger Norsesea base and its discharge licenses. The fledgling NT business is a small business operating in a niche area of an industry dominated by a handful of big players but, as none of these players have a workable solution yet, NT currently enjoys an advantage. It could also mitigate this risk by partnering with one of the major players in oilfield services.

Competition is the biggest risk but operating in specialist niches mitigates this

Currency

Nature Group is an international business and conducts almost all its business overseas, such as Norway or offshore, and as such its transactions are conducted in several currencies, such as NOK and USD, while its reporting currency is GBP. There is therefore a degree of translation risk. The core slops and waste business in Gibraltar is billed in GBP while recovered oil is billed in Euros. As Nature Group has always been an international business, currency risk is well understood and considered to be low.

Commodity

Nature both provides a service to the oil industry and generates a revenue stream from oil recovered from vessel slops and tanker washings; it does therefore have some sensitivity to the oil price in that it is a measure of activity in the oil industry and determines the price Nature receives for recovered oil. This risk is mitigated in several ways: 1) oil recovered from waste is just one of several revenue streams, not the core, and its price is less volatile than crude; 2) the long-term trend price of oil is expected to be upwards as economic activity levels recover; and 3) Nature is afforded a degree of protection by the specialist nature of the niches it operates in.

Regulatory and political

As compliance with regulation and legislation drives Nature Group's growth, there is a political and regulatory risk present, albeit one we consider very low. We consider it extremely unlikely that regulations governing the treatment of marine and oil industry wastes will be relaxed. Indeed all current evidence points to the opposite, namely a greater degree of compliance being required in the future.

Environmental

While in theory there is an environmental risk, Nature's business is ensuring its customers' compliance with environmental legislation. therefore it deals with this risk continuously. All its treatment units are monitored continuously and records of treated water discharged maintained.

KEY DATA: Nature Group

Company Description

Nature Group is a waste treatment business specialising in treatment of vessel slops and oily wastes, recovery of oil from those wastes and the discharge of clean water at sea. It serves increasingly regulated customer groups.

Website

www.investnature.com

Management

Richard Eldridge	Chairman
Darren Laguea	CEO
Peter Snell	FD

Major Shareholders

Darren Laguea	29.99%
Richard Eldridge	10.51%
C.P.Fairweather	8.56%

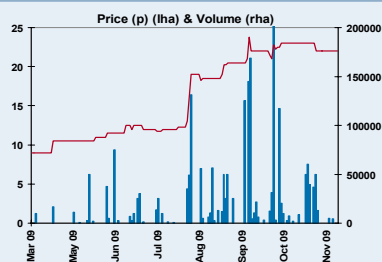
Recent News

27 November	Letter of intent for plant and technical services for Duqm Port, Oman
28 July	Grant of options and directors dealing

Financial Diary

28-May 2010	Prelims
30 September 2010	Half yearly results

Share Price & Volume Chart



Year-end December Key Profit & Loss Data (£m)	2008A	2009E	2010E	2011E
Turnover	3.38	5.56	8.61	8.97
Operating profit	1.51	3.15	3.91	4.20
<i>Operating profit margin (%)</i>	<i>44.7%</i>	<i>56.7%</i>	<i>45.4%</i>	<i>46.8%</i>
EBITDA	0.87	2.05	2.70	2.93
<i>EBITDA margin (%)</i>	<i>25.9%</i>	<i>36.9%</i>	<i>31.3%</i>	<i>32.7%</i>
PBT (adjusted)	0.51	1.44	1.99	2.18
Tax rate (%)	(11.4%)	(7.6%)	(10.0%)	(10.0%)
PAT (adjusted)	0.45	1.33	1.79	1.97
Adj. EPS (p)	1.8	3.4	4.6	5.1
DPS (p)	0	0.5	0.62	0.68
Key Cash Flow Data (£m)	2008A	2009E	2010E	2011E
EBITDA	0.87	2.05	2.70	2.93
Gross operating cash flow	0.50	1.72	2.57	2.88
Net operating cash flow	0.50	1.61	2.37	2.66
Capex	(0.18)	(1.20)	(1.29)	(1.35)
Free cash flow	0.32	0.41	1.08	1.31
Cash flow from investing	0.00	0.00	0.00	0.00
Cash flow from financing	0.03	0.34	(0.23)	(0.27)
<i>Incr/(Decr) in net cash</i>	<i>0.35</i>	<i>0.75</i>	<i>0.85</i>	<i>1.05</i>
Key Balance Sheet Data (£m)	2008A	2009E	2010E	2011E
Fixed assets	4.17	4.84	5.41	5.99
Current assets	1.58	2.76	4.28	5.40
Current liabilities	(0.84)	(1.19)	(1.79)	(1.83)
Net current assets/(liabilities)	0.74	1.57	2.49	3.57
Total assets less current liabilities	4.91	6.41	7.91	9.55
Long-term liabilities	(0.22)	(0.58)	(0.53)	(0.47)
Closing net assets	4.69	5.83	7.38	9.08
NAV per share (p)	12.1	15.0	19.0	23.4
Valuation	2008A	2009E	2010E	2011E
P/E (x)	12.2	6.5	4.8	4.3
Div. yield (%)	0.0%	2.3%	2.8%	3.1%
EV/EBITDA (x)	9.3	3.8	2.5	2.0
FCF Yield (%)	3.7%	4.7%	12.7%	15.4%

Source: Company, Astaire Securities estimates, Proquote International





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