

- BG Group – Solid Full Year Results & Improved Outlook.
- Low & Bonar – Preliminary Results.
- M&G Strategic Corporate Bond – Update.

	Previous Close	Change
FTSE 100	6051.03	0.89%
FTSE 250	11811.07	1.24%
Dow Jones	12161.63	0.57%
€ per £	€1.186	0.00c
\$ per £	\$1.611	0.00c
Oil (Brent)	\$99.25	-\$0.58
Gold	\$1,351.30	\$2.45
UK 3m LIBOR	0.800	0.008

	Last (10am)	Change
FTSE 100	6045.20	-0.10%
FTSE 250	11824.4	0.11%
Dow Future	12128.00	-0.28%
€ per £	€1.185	-0.12c
\$ per £	\$1.612	0.09c
Oil (Brent)	\$99.62	\$0.37
Gold	\$1,355.35	\$4.05

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Share prices are quoted as at last night's close

*Indicates a covered stock / fund

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UK Large Company News

This morning's full year results¹ from BG Group (BG..L, 1,440p) are broadly in line with expectations at the headline level. Full year revenue rose by 11% to \$17.4bn (versus consensus of \$17.8bn) and operating profit rose 9% to \$6.9bn, slightly higher than the consensus number of \$6.8bn. The rise in revenue and operating profit primarily reflected higher commodity prices. Management's confidence in the outlook is reflected in a 10% increase in the full year dividend (FY 2012 prospective yield of 1.1%).

In the fourth quarter, the group generated revenue of \$4.4bn (versus a consensus number of \$4.5bn) and operating profit of \$1.8bn (modestly above expectations). This represented an increase of 1% (revenue) and 3% (operating profit) compared to the fourth quarter of 2009. Although production volumes fell in both the Exploration & Production (54% of operating profit) and Liquefied Natural Gas (LNG, 35% of operating profit) divisions, higher realised prices helped to deliver higher revenues and profitability.

BG is an integrated global energy company, engaged in the exploration, development, production, transmission, distribution and supply of oil and natural gas. The group has built up an enviable portfolio of projects that will deliver strong growth over the next decade. At a time when many of the oil majors are growing production in the low single digits, BG is aiming to increase production volumes by a CAGR of 6-8% to 2020.

The group also issued the key points of its annual strategy update due to be delivered today². The group reaffirmed its E&P long-term average growth range of 6-8% out to 2020, with the 7% mid-point now achievable from existing discoveries alone. In particular, we would highlight the acreage offshore Brazil where production recently started and the estimate of gross reserves for the Tupi, Iracema, and Guar fields were increased 34% to 10.8bn barrels. In time, as the group becomes more familiar with the acreage, we would expect this estimate to move higher for an asset which management believes is economic at an oil price of \$35-\$40 a barrel. Management now expects around 70% of group revenue to be oil or oil-related by 2015, up from c. 50% in 2010.

The group has raised its estimate of net production from the Santos Basin (Brazil), by 37%, from 400,000 barrels oil equivalent per day (boed) to more than 550,000 boed by 2020. US shale gas net production estimates are being raised by 90%, from 100,000 boed to 190,000 boed by 2015. LNG profit guidance is increased to \$1.9-\$2.2bn per annum for 2011-12, from \$1.8-2.0bn a year ago.

In Australia, BG has a very attractive asset position in the LNG market and has recently taken the Final Investment Decision for the first phase of the Queensland Curtis project. Exports are due to commence in 2014 and are underpinned by 20-year purchase agreements with China, Japan and Singapore. Following the \$950m acquisition of US shale gas assets from its JV partner EXCO, the group has strengthened its unconventional gas portfolio.

Comments on the medium and long-term outlook for the group are very encouraging and we reiterate our positive stance on the shares. We believe the attraction of BG is the long-term growth prospects for the business, especially in

relation to the oil majors.

BG remains financially strong, with net debt of £4.3bn (Enterprise Value of £53.2bn) and gearing of 20% at the end of 2010. This provides firepower to make acquisitions, invest in capex and to continue to pay a progressive dividend. We expect the oil and gas sector to undergo a period of consolidation in the medium term, and, in this respect, BG's portfolio of growth assets would make an attractive fit for any one of the oil majors, all of which are struggling to grow production. Proved reserve replacement (i.e. a measure of the amount of proved reserves added to the reserve base during the year relative to the amount of oil and gas produced) was 224% compared to 129% in the case of BP.

Although the shares are trading at a premium to the oil majors (2012 PE of 16.1x, pre-upgrades), we believe a higher rating is justified by the above-average growth prospects and the value tied up in assets which are expected to generate strong returns beyond the forecast period. The chart illustrates the performance versus the UK market and the Oil & Gas sector over the last five years. **The shares have had a strong run into these results and may be due a pause for breath. However we remain buyers of this long term, high quality, resource story.**

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COMPARATIVE RETURNS

1825 Day Period

Securities	Crcncy	Prc	Appr	Total Ret	Difference	Annual Eq
1 BG/ LN Equity	GBp	133.20 %		145.85 %	117.07 %	19.71 %
2 ASX Index	GBP	7.62 %		28.78 %		5.19 %
3 FAOILG Index	GBP	13.26 %		37.95 %	9.17 %	6.65 %

(* = No dividends or coupons)



UK Small Company News

Mike Savage, Peter Bate and Stephen Timoney provide Killik & Co clients with recommendations on UK small companies housed within a virtual portfolio of preferred ideas. For more detail on any of the stocks mentioned please contact your broker.

This morning Low & Bonar (LWB.L,58.3p) , the international performance materials group, released a strong set of preliminary results³. Revenue grew by 13% to £344.6m (versus consensus estimates of £341.5m), driven by recovery in many of the groups' end markets, innovative new products and an increasing proportion of sales to higher growth emerging markets. Operating margins were also stronger, growing 20bps to 7.5%, despite the adverse impact of the timing lag in adjusting selling prices to the significantly higher raw material prices seen in the year. Headline PBT was £10.2m (broadly in line with expectations), and the group also slightly increased the full year dividend to 1.6p.

Divisionally, the Performance Technical Textiles division (comprising Colbond, Technical Fabrics, Yarns and Yihua Bonar) saw sales growth of 13%, however, adjusting for adverse foreign exchange movements, underlying sales improved by 15%. Within this division, Carpet sales were a particularly strong vertical, with 25% sales growth, driven by recovering markets, strong growth in China and positive substitution effects. The key focus for this division going forward however will be on the restructuring of the loss-making yarns business, which shifted its manufacturing base to Abu Dhabi in December. Management highlight that the relocation is going to plan, and that this will lead to an improvement in divisional margins.

The Technical Coated Fabrics division saw revenue growth of 14%, however, after adjusting for foreign exchange impacts, the improvement was 16.5%. The sales pattern in this division is reported as improving after a slow first quarter, with growth in emerging markets augmenting recovery during the year. By vertical, the trailer, leisure & agriculture markets are reported as improving, however print markets and the replacement trailer markets remain weak.

The shares trade on a prospective P/E of 10.8x 2011E and yield c. 3.0%. We continue to view LWB as a cyclical recovery play, which is also driven to a degree by environmental regulation. Today's results highlight sustained trading momentum, with the inherent operational gearing in the business positively impacting earnings. Unlike other ways of gaining exposure to the continued economic recovery, we feel that the market leading positions the group has in many of its end markets, combined with the recent refinancing, significantly de-risks the investment proposition.

Specialist Energy Group (SEGR.L, 78p) has announced another £5.9m of contract wins this morning⁴, with sales to India, China and Norway. The shares have had a great run since the recent 48p placing but they were anomalously cheap at that time. In the meantime the Indian civil engineering group McNally Bharat has continued to build its stake (which now stands at c.16%). Current market forecasts for 2011 are now more than under-pinned, meaning that at 77p the shares trade on 13x FY11. We feel that 100p feels fairer value given the operating momentum in the business and the growing interest from McNally Bharat.

Renovo (RNVO.L, 70.5p), the AIM-listed biopharmaceutical group, this morning issued an IMS⁵. As expected, there is little new information in this statement. However the key EU PIIa trial for the scar healing product Juvista is highlighted as remaining on track to report results in H1 2011. The cash balance at the group as of 31st December remains robust at £46.1m, which is in line with the management target of having a cash balance of £30m at the time of reporting the Juvista data.

Funds^a

Richard Woolnough, manager of the **M&G Strategic Corporate Bond Fund* (Buy)**, presented his latest thoughts on the fixed interest market at M&G's recent investor conference. Over the last 12 months, the fund continued its long term record of delivering returns (+5.8%) over and above that of the gilt market - FTSE All Stocks Index (+3.4%) – and the peer group - IMA £ Corporate Bond (+4.1%). The fund retains the number one performance rank in the IMA sector over three years, five years and since inception.

Woolnough believes the UK economy will recover comparably slower than the US over the next 12 months. He points to the still subdued capacity utilisation rates. The latest Bank of England Inflation Report signalled that utilisation remains well below pre-recession levels, especially in the Services sector. The manager believes UK unemployment is likely to rise in 2011 and that the domestic housing market still looks fragile. This morning the Royal Institution of Chartered Surveyors announced their January survey results showing that almost a third more estate agents and surveyors reported a fall in house prices in England and Wales rather than a rise. The survey showed a reduction of the pace of decline from the previous month but this was due in large part to reduced supply coming onto the market. The manager cannot see how the BOE Monetary Policy Committee could increase interest rates in the near future.

Woolnough is wary of the potential effect that a major shift from bonds into equities, by asset allocators, could have on the debt market. However, he notes that investment grade debt issuance is expected to be very low in the coming year which he expects will mute the impact of this move. January has been the lightest month for new issuances he can remember and the manager believes near term net issuance could in fact be negative in the investment grade space. Many companies have recently initiated tender offers on their debt, taking the opportunity to buy back high coupon bonds in the current low interest rate environment. Kingfisher, owner of DIY retailer, B&Q, was one of the latest companies to carry out this process in order to “reduce gross debt and improve the return on the cash held on its balance sheet”.

The manager has been increasing exposure to high yield names (now 7% of the portfolio), where new issuance is strong in contrast to investment grade. Woolnough believes the risk premium is now more attractive on high yield debt. The modified duration (a measure of the price sensitivity of the bond to a change in interest rates) of the portfolio is currently c.7 years (v 5.9 years in January 2010) reflecting his expectations on interest rates.

Although our view on government debt is less positive than this manager's, we see a case for having some exposure to bonds and a preference for corporate over government. **We continue to rate this manager's ability to make consistently good macro and credit calls and maintain our BUY recommendation for exposure to the sterling corporate bond asset class. Please contact your broker for a copy of our recently updated research note.**

In the Press

Reuters – Cellphone security threats rose sharply last year as a proliferation of Internet-enabled mobile devices like smartphones and tablets provided new opportunities for cybercriminals, security software maker McAfee said. In its fourth-quarter threat report, McAfee said the number of pieces of new cellphone malware it found in 2010 rose 46% over 2009's level.

Financial Times – For the first time since the onset of the credit crisis, Moody's has recorded a month in which not a single company defaulted on its debt. The ratings agency said on Monday that January was the first month since June 2007 when no default was recorded among the companies whose debt it rates. In comparison, eight companies defaulted in January 2010 and there were five defaults per month on average last year.

Financial Times – A majority of hedge fund investors are eschewing traditional offshore funds in favour of tightly regulated onshore vehicles – a sign of the lasting impact of the Madoff scandal and 2008 liquidity crisis. According to a comprehensive industry survey,

55% of hedge fund investors would now prefer to allocate money in onshore so-called UCITS funds compared with just 21.7% in traditional offshore Cayman Island funds.

Director Dealing

Richard Burns, a Director at **JPMorgan Indian Investment Trust** has **bought** 10,000 shares at 407.1p.

Mike Muller, Chief Technology Officer at **ARM Holdings**, has **sold** 350,000 shares at 579.94p.

Killik & Co Personal Account Holdings

One or more members of Killik & Co, who contributed to writing this note, have a personal position/holding in Low & Bonar, Specialist Energy Group and Renovo.

References

1. BG Group – Final Results.
2. BG Group – Annual Strategy Update.
3. Low & Bonar - Final Results.
4. Specialist Energy Group - Hayward Tyler Contracts Update.
5. Renovo - Interim Management Statement.

Disclosures

^a Killik & Co may receive trail commission (typically a rebate of up to 50bps of the fund manager's Annual Management Charge) on a number of open-ended funds and on certain closed-ended funds. Some of these funds may be subject to a Killik & Co Research recommendation. Further details of the trail commission terms are available upon request.

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Daily Note	ETFs Bulletin	Thematic
A summary of the day's newsflow and an update of opinion on covered stocks.	Focusing on London-listed Exchange Traded Funds (ETFs) and Exchange Traded Commodities (ETCs).	A number of direct equity and fund ideas that are well positioned to exploit a key investment theme.

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