



How a £67 million small cap is set to lead the UK “Green Recovery”

Sam Volkering, Editor



Dear reader,

It's been 203 days since I last was on a plane.

I was thinking about my last trip which was out to Australia and back over the space of a week. I was there on business, so it was a short trip.

I left for Melbourne exactly one week after I had got back from another trip. This was to Las Vegas, also for a week, also for business – the huge CES tech trade show and conference.

Little did I know that under two months later the entire global aviation industry would be brought to its knees.

But thinking about my Aussie and

US trips just in January, I wondered how many miles I had covered in total. I did a rough calculation and discovered that I covered around 24,312 miles in total over the space of just three weeks.

That's a lot of air time, a lot of miles covered, a lot of jet fuel and a lot of carbon emissions that these days need to be offset.

Seeing the ongoing theme of green and clean energy being so dominant in the market at the moment, I asked myself a simple question, was I bothered about my part in contributing to the emissions that are apparently so damaging to our world?

I'm not sure I have a definitive answer on this one. And usually I'm pretty sure of my view on a lot of these topics.

On one hand, yes, I realise that in flying those distances, I'm effectively contributing to the emissions that do damage to our natural ecosystems. I contribute by driving to the airport. I contribute by sitting in that seat and flying all that way.

I am conscious of this fact. But I'm also not sorry about it. I'm not sorry because I need to travel back to Australia. I need to travel to the US. I need to travel to all parts of the world in order to be effective at what I do.

I also need to travel to Australia because I have family there. While I'm conscious of my contribution to emissions, what would the eco-warriors have me do otherwise? Never see my family again? Travel by electric power to Australia? Travel by train? By carbon fibre sail boat?



Of course none of those are feasible options. And here's the thing...

They never will be.

If I need to get from the UK (an island) on one side of the world to Australia (an island) right on the other side of the world, there is only one effective way to get there. Plane.

There is *no other effective and efficient way* for any of us to travel around the world outside of a plane.

Cars are too time consuming and also don't go everywhere you think they can. Trains are also

it will come.

Airlines already operate on thin margins, with some in the US explaining, "For every dollar of revenue we take in, we keep just under a nickel in profits."

However, in terms of economic viability many airlines (which already run on thin margins) are going to need to adopt ways to make their planes more efficient and most cost effective. They also need to ensure their planes are more environmentally friendly.

This has been an area of focus for airlines for a number of years now. And most new aircraft

Airlines.org explained in a post about the new system,

Aircraft consume a great deal of fuel and fuel costs eat up a huge amount of airlines' operating costs. By reducing delays and allowing for more efficient ATC operations, NextGen will help reduce fuel consumption and related emissions by 12 percent per year. That's the equivalent of removing 2.2 million cars from the road for a year.

Still, that's not enough.

In the years since NextGen, the importance of efficiency, particularly fuel efficiency and clean fuel, has been one of the most important issues in aviation.

... there's really only one outcome here for airlines and manufacturers: develop more environmentally friendly engines and fuels.

limited by the rail networks they exist on. Boats are too slow, and equally as polluting as a plane.

To fly is actually the best way for us to get around the world.

As I say, that is not going to change in a hurry. While the world might be on lockdown and people think the airline industry is going to radically change, you're wrong... to an extent.

Plane travel isn't going to disappear. It will return and it will return at the levels and passenger volumes we are used to and have seen in the years before this global pandemic hit.

It's hard to conceive that now, but

that roll off the shop floor from Boeing or Airbus employ new technologies such as composite materials and more fuel efficient engine systems.

But it's not just the airlines and plane manufacturers that are needed to make the airline industry more economically viable, sustainable and "green" in the years that come as they recover from this current crisis.

For example, in 2014 the US airlines, manufacturers and the Federal Aviation Administration (FAA) rolled out NextGen, an all-new air traffic control system to help aircraft operate more efficiently.

Add to the growing social pressure on airlines to become more "green" and there's really only one outcome here for airlines and manufacturers: develop more environmentally friendly engines and fuels.

In the US, it's already become one of the most pressing issues. And there's already action underway to tackle the problem head on.

Airlines for America released a "primer" report in August 2019 titled, "Deployment of Sustainable Aviation Fuel in the United States".

In its executive summary it notes,

The U.S. aviation industry has taken a leadership role in the development and deployment of sustainable aviation fuels (SAF). We remain committed to advancing



the commercialization and deployment of these fuels to help the industry meet its emissions reduction goals, diversify fuel supply and enhance energy security.

There's no doubt this is an important area of development in global aviation moving forward. And it presents a unique opportunity for one particular UK-listed, UK-based company that's developing new, more sustainable fuels for transport and in particular the aviation industry.

Introducing your latest Frontier Tech Investor recommendation...

Velocys plc (LSE:VLS) is your latest *Frontier Tech Investor* recommendation. Velocys is a technology company that has developed processing technology that's able to turn waste into sustainable fuels for heavy goods transportation and aviation industries.

It is listed on the London Stock Exchange with offices in Oxford, and Ohio and Houston over in the US. The stock is currently trading at a price of around 6.12p with a market capitalisation of around £65 million.

Velocys has been in the news of late and has seen wild volatility in its stock because of its involvement in developing new sustainable fuels for aviation. However, it was an announcement on 12 June by the UK government which really sent a rocket up the backside of this small-cap star.

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During the Covid-19 daily briefing on 12 June, Grant Shapps, secretary of state for transport, announced a new "Jet Zero Council". The Jet Zero Council will try to figure out how to,

... decarbonise the aviation sector while supporting its growth and strengthening the UK's position as a world leader in the sector.

The members will look at how to work across their sectors to achieve these goals, including through brand new aircraft and engine technologies. These could include using new synthetic and sustainable aviation fuels as a clean substitute for fossil jet fuel, and eventually the development of electric planes.

It was in the 12 June briefing however that Shapps said,

"Our goal – within a generation – will be to demonstrate flight across the Atlantic, without harm to the environment.

"And today we're backing a company called Velocys who are building a plant for aviation biofuels in Lincolnshire."

This sent the Velocys stock price into overdrive. It went from around 5p to a high of 16.64p in a matter of days.

Thankfully for us, in the weeks

since, the stock price has wound off a lot of that excitement and the stock has now achieved a level where we're ready to bring it into the portfolio for the huge potential its technology holds long term.

As mentioned earlier, the airline industry isn't going to pack up and go home. It's here to stay and is a fundamental part of the fabric of modern society. However, it needs to undertake significant change to be sustainable, viable and "green" long term.

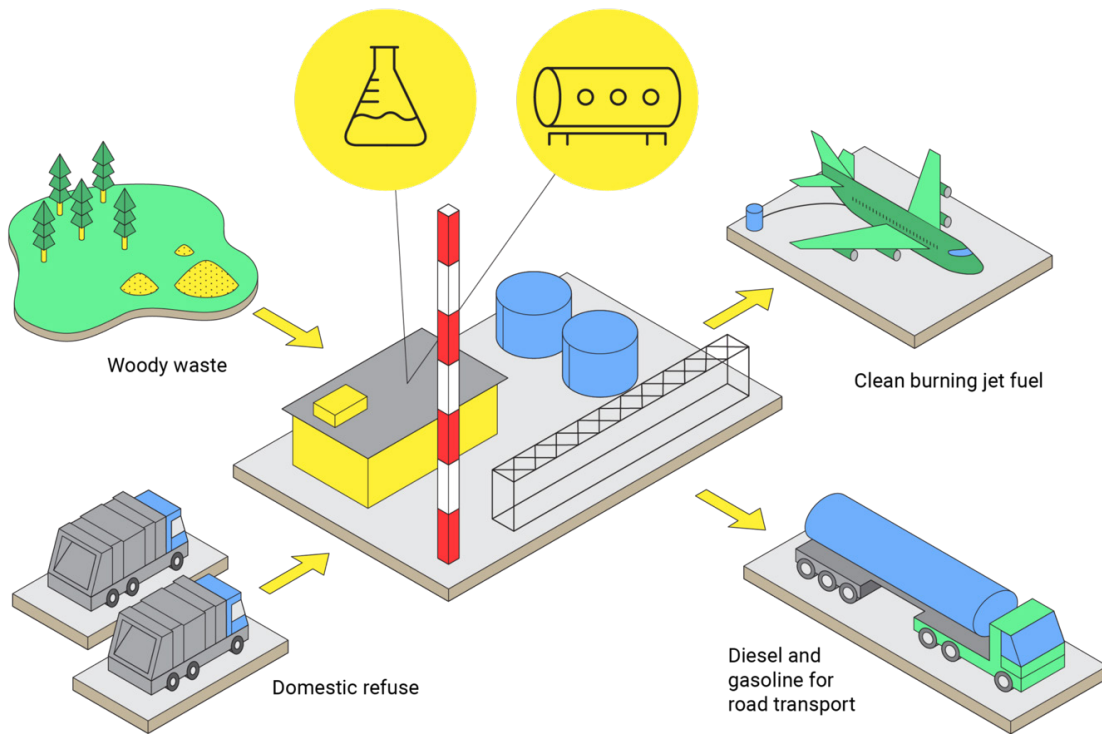
The measures that are being put into place by global governments like the UK are a key step in making that happen. But it's also companies like Velocys that will deliver it.

Velocys use a process known as the Fischer-Tropsch process in their reactors to turn synthesis gas into liquid transport fuels. It describes the whole process as, "an integrated end-to-end process that converts solid wastes, first to synthesis gas and then to liquid transport fuels."

This isn't some overnight success. The company was founded in 2001 and its first pilot plant in Australia was launched in 2010.

Furthermore, the plans for a proposed waste-to-jet fuel plant in North East Lincolnshire were only submitted in August 2019. The good news, however, is that on





Source: Velocys

20 May approval was given and then on 12 June, in conjunction with the statement from Shapps, the company also announced the following formal notice:

... formal notice of the decision to grant planning permission for the Altair Immingham plant has now been issued by North East Lincolnshire Council (NELC).

That means its full steam ahead to develop this pioneering plant.

The plant itself isn't solely on the shoulders of Velocys either. It's a Joint Development Agreement project with British Airways and Shell.

This small-cap £65 million company working on a pioneering waste-to-jet fuel plant in North East Lincolnshire with £94 billion giant Shell and the UK's major airline (owned by £4

billion giant IAG) British Airways.

It's a huge project, which I believe will be the catalyst for bigger things to come long term for Velocys.

What's important here is that we see this as the first of potentially many plants that Velocys will develop.

One of the important pieces of news from Velocys, which has gone largely under the radar, was its attendance in October 2019 at the AIREG Berlin SAF Conference. It was there to discuss the potential for sustainable jet fuel produced from solid and waste biomass residues.

CEO Henrik Wareborn noted in the news release that,

A key benefit of the Velocys SPK fuel produced is that it meets the

ASTM D7566 specification, so it is a "drop-in" fuel at up to 50% blend into Jet A1 that requires no adaptation by the end user.

This ability to "drop in" is key to ensuring that these new synthetic fuels don't require the complete overhaul of existing aircraft systems.

In the earlier mentioned sustainable fuel report from Airlines for America, it identifies the number one "Core Enabler for Airline Deployment of Sustainable Aviation Fuel" as,

Equally safe and effective as petroleum-based jet fuels, meeting criteria so it may be "dropped in" to existing aviation fuelling infrastructure and aircraft. This is addressed through jet fuel specification ASTM D7566 and application of



procedures to assure fuel quality is maintained.

With Velocys able to meet this criteria, it opens the entire global aviation industry for its technology process and sustainable fuels.

That's what gives this small-cap UK pioneer such big long-term potential. It's at the precipice of disrupting the entire global aviation fuel industry and it's only just started its run.

Financials and risks

Now it's important to recognise this is all pioneering technology and things are only just getting started now.

The Lincolnshire plant has only just received approval and will still need to be built and tested before going into actual production. That's why when commenting about the announcement from the government on 12 June, Wareborn made note the company and the plant, "...could be producing sustainable aviation fuel in commercial scale by the middle of this decade."

We see this as a long-term play but the gear in motion now could lift the company, and the stock price, in further anticipation of what's coming in the next few years.

And should it announce further development of other plants, for example in the US, it could see the stock price lift off (so to speak) again.

With this being a long-term play,

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with pioneering technology and early-stage development of the commercial fuel plants, the financials aren't of the most critical importance right now. Nonetheless, it's still worth considering to ensure that the company can deliver on this ambitious projects and go from being a small cap to a major player in the UK market.

Its most recent numbers are from its 2019 annual report released just this week. And it doesn't make for the most enticing reading.

Revenues of £300,000, operating loss of £9.6 million, cash at end of period (31 December) of £4.8 million.

As I say, it's not a fundamental financial story here. It's a company that's going from research and development to tangible projects and development (with global players like Shell and BA). This transition phase isn't going to necessarily deliver financial riches, but the anticipation is it will, which is why I'm bringing in the stock now.

Both BA and Shell are contributing towards the Lincolnshire plant (£2.8 million in 2019 and another £1 million May 2020) and it's received funding from the Department of Transport via the way of a grant for £500,000. So we're not anticipating there will be issues in

getting this built and operational.

At the end of June the company was able to raise £20 million (upped from £10 million due to demand) so is quite heavily funded for what we would anticipate to be around two years considering the £9.8 million operating loss from 2019.

From a financial perspective, I'm happy with the current position of the company. However, you should be aware that due to the transition from R&D to a commercially viable company, there still may be a situation where the company looks to the market again for another capital raise.

We wouldn't expect one soon considering one just completed. But it's possible and as shareholders it has the potential to dilute your holdings should it again issue more stock for a raise.

While our view is long term, it's quite obvious that due to the coverage in June of the stock, it's now somewhat of a more known stock around the market. This brings volume, which is great to get a position, but also brings the wider market volatility.

We would expect that volatility will continue here. Ongoing news flow is important to keep the stock moving along – absence of developments or positive news may see a number of newer



shareholders looking to exit that aren't taking a long view on this one as we are.

Expect volatility and market risk while being in the stock.

Still, considering the position of the company, its technology and the current push from industry and from government for a "Green Recovery", Velocys is primed to ride this opportunity and I think deliver tremendous upside to shareholders.

Buying instructions

As noted, **Velocys plc (LSE:VLS)** is listed on the London Stock Exchange. The stock is currently trading at a price of around 6.12p with a market capitalisation of around £65 million.

Average volume in the stock is around 16 million – which equates to roughly £1 million traded per day. I wouldn't say it's illiquid, but again our recommendation may shift the price of the stock a little higher

after recommendation.

As a reminder, we recommend sticking within our buy-up-to limits and not over bidding for the stock. Should it trade over the buy-up-to I'd suggest again being patient for an opportunity to enter the stock once the dust settles.

I also recommend using a trailing stop-loss order to limit downside risk and to help lock away profits should we get to that point.

Buy Velocys plc (LSE:VLS) the stock is currently trading at 6.12p with a market cap of £65 million. Buy up to 7.5p and set a trailing stop-loss order at 50% below entry price.

Regards,

Sam Volkering
Editor, *Frontier Tech Investor*

Action to take:

Ticker:

Price as of 13.08.20:

Buy up to:

Market cap:

52-week high/low:

Buy Velocys

VLS: LN

6.12 GBp

7.5p

£65.08 million

16.64p/0.94p



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