

BROKER RATING: ● SELL ● HOLD ● BUY ● NOT AVAILABLE

Velocys to regain velocity

Fuel technology business close to commercial breakthrough

TOM SIEBER

Small scale gas-to-liquids (GTL) play **Velocys (VLS:AIM)** is on the cusp of demonstrating its technology is commercial. With the shares bumping around close to all-time lows there is an attractive entry point ahead of the commercial milestone and investors with an appetite for risk should buy now.

The £42 million cap's technology can convert neglected and otherwise sub-commercial deposits of gas into more valuable liquid fuels.

Velocys, backed by Russian oligarch and Chelsea FC chairman Roman Abramovich, recently announced (21 Sep) it had completed construction work on its most advanced project, the ENVIA Energy GTL plant in Oklahoma City.

ENVIA Energy is a joint venture between Velocys, **Waste Management (WM:NYSE)**, **NRG Energy (NRG:NYSE)** and Ventech Engineers.

Velocys gained greater operational control of the development after making available a \$9 million loan earlier this year to ENVIA, secured against the plant, and was granted additional equity in the venture. The company doesn't expect any further funding to be required and the plant is expected to be up and running before the end of the year.

House broker Canaccord Genuity reckons



a 'run period' of as little as six months 'will be enough to demonstrate the commercial viability of the process'.

Analyst Alex Brooks says the current market valuation pegs the company's other projects and intellectual property at less than \$15 million. Brooks has a price target of 110p and we share his optimism. Once the company has demonstrated its process works, other projects which are bubbling away in the background are likely to progress more rapidly.

LIQUIDS FROM GAS

GTL is the conversion of natural gas or other gas-based hydrocarbons into liquid synthetic fuels. GTL applications have, in one form or another, existed for the better part of a century but currently can only be commercially deployed at large plant sizes (30,000 barrels per day (bpd)) which can require upfront capital investment of \$3 billion or more.

Velocys' small scale GTL technology, based on the established Fischer-Tropsch (F-T) process, can operate efficiently at anywhere between 1,000 to 15,000 bpd.

STRATEGIC REVIEW

Velocys' current business model is based on licensing its technology for GTL reactor equipment and chemical catalysts but it is engaged in a strategic review to, in its own words, 'define the best way to deliver its world-leading technology to market'.

The company has more than 900 patents in force and has demonstrated willingness to defend its technology, winning a patent infringement case against rival CompactGTL in September 2014.

It has not all been plain sailing, reflected in a precipitous share price decline from highs above 230p two years ago. Delays in getting to the point of commerciality, the departure of previous chief executive Roy Lipski in August 2015 under something of a cloud and falling oil prices have all contributed to the weakness.

Canaccord notes the pricing for F-T products, which it describes as 'more akin to speciality chemicals than traditional liquid fuels', is 'resilient' and estimates unit revenue from Velocys' F-T process is in excess of \$100 per barrel at current crude oil prices.

The company's last reported cash position was £24.1 million with management guiding for burn of around £7 million in the second half of 2016.

VELOCOYS

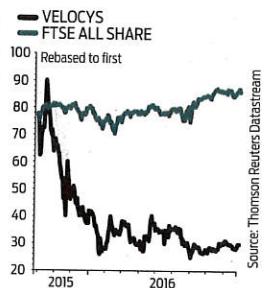
(VLS:AIM) 30p

Stop loss: 24p

▲ BUY

Market value:
£42 millionProspective PE Dec 2016:
n/aProspective PE Dec 2017:
30Prospective dividend yield:
n/aBid/offer spread:
0.6%Analyst price target:
110p*

Canaccord Genuity, 26 Sep 2016



Growth: HIGH

Velocys potentially has a highly scalable business model as it does not construct plants itself.

Risk: HIGH

The technology could fail to work on its first project which could scupper future plans and its share price.

Quality: LOW

Patented technology provides barriers to entry but the company is yet to turn a profit.