ValueStep

Emerging renewables companies could save us, but can we save them first?

1. Emerging renewables companies are being squeezed

With inflation abating only slowly, and interest rates persisting uncomfortably high, a troubling issue is appearing - the strangulation of emerging, pure-play, renewables and low carbon energy technology companies. This threatens a class of inventors and entrepreneurs who are seeking to bring their IP to market, and it could even deprive us of the next "big green idea".

Burdened by debt-loaded, 'zombie' balance sheets, a growing number of these firms, some listed on AIM, and others in pre-IPO funding rounds, are starting to look very sick (not least in share price terms). Frothy support from institutional and retail investors, who were previously clambering to be early backers, hungry for huge future returns with the side-benefit of 'doing their bit to help tackle climate change', seems to have totally evaporated.

For such firms, for the time being at least, the days of simply reaching-out for more, cheap cash to fund running and development costs before securing their order book and proving their concept to commercialisation with operational capability, appears to be over.

Worst still the current stuttering markets feel more alarming than the usual economic downside cycle, perhaps driven by anxiety over so many concurrent major global conflicts and uncertain times in geopolitical prospects.

2. View of the green investor

In such times, for any investor, cash remains king and a company that can demonstrate free cash generation, profit and regular shareholder distributions, is ever more desirable.

As the noose around the economy tightens (due to slow to fall inflation and higher for longer interest rates) anxiety is heightening. Markets are seeing illogical swings from herd behaviour patterns based on a single company report or a loose word from a member of central bank. These upswing and lows across global markets show emerging signs investors may not be quite as enthusiastic as they once were about backing good, potentially planet-saving energy concepts.

They are seemingly pushing the 'greener morals' priority down the list in pursuit of immediate returns (dividends) and assured paths to capital appreciation (share price growth).

3. Perspective for emergent business

Despite the "demand" for new green technology, the picture has blurred somewhat in the last 18 months and is very different for smaller, emerging companies that are focussed on renewable, sustainable, and low carbon energy solutions.

As economic times toughen companies need to be more rigorous about their strategic and business planning, marketing, R&D, and ruthless with cost control, and in order to stand a chance of 'reasonably affordable debt/ or modestly dilutive equity, must deliver firm sources and tangible progress to secured revenues.

Just because a company has a great idea, it doesn't mean that it will attract funds as easily as it would have done as recently as one year ago. Many a

Founder/ Inventor is getting a rude awakening around dilution in this cycle of economic turmoil. There are signs some are forced to decide on being stubbornly resistant to grasping the nettle, instead opting to remain perilously under-capitalised. It has become a tightrope walk between significant dilution or real threat to survival.

So, faced now with shrinking pool of available (or affordable) equity and debt, what lies ahead as they face brutal headwinds?

4. **The role for big oil**
Big oil and other major corporations must play their part. Perhaps the most recognised corporate behemoth, Shell, steeped in its rich fossil fuel history, started its diversification journey into renewables decades ago. Looking at a wide range of technologies it embarked on the journey toward net zero with serious levels of investment, multi-billions. Recently, however, its renewable ambitions are being scaled-back, and the focus of its new CEO is reversion to proven oil, and gas exploitation. Whilst Shell undoubtably will continue to develop renewable and sustainable lower carbon energy technologies, it seems that it will be less and slower than the planet needs.

There are though exceptions, and on the other hand, Total has recently changed its name to Total Energies (the clue is in the name), and it is doubling down on using its carbon profits to support its R&D and investment into its growing portfolio of new, green subsidiaries.

5. What can Government do?
Can and should humanity leave it up to corporations (big or small) and the 'markets' to deliver change? Surely, they can't be trusted alone.

Globally, Governments and regulators should show the leadership and set the ambitions and boundaries, backed with policy and legislation. If only Government could provide political stability and support consistency through long-term vision, improved regulatory clarity and an extended period of a beneficial taxation environment. Among much else, Government ought to set up long-term partnerships with: Big oil; green corporates; generators, and distributors, and establish a favourable business and regulatory environment for the emergent green technologies with perhaps matched funding. Innovation and delivery would then be undertaken by the marketplace and by those best placed to handle the risks.

6. The big corporate investor viewpoint

Shell and similar big, legacy corporates will thrive, for decades to come, seen as safe harbours for institutional investors, with a hope for steady share price growth and uninterrupted dividends. In the market, **Shell (SHEL.L),** oil, gas, and renewables technology, share price has (largely due to the post Covid 19 recovery in oil cost per barrel increases) remained around its all-time peak of £27.27 per share. During Covid, in October 2020 it was trading around £9.65. With a market capitalisation of £172bn it generates around £6bn a year in 'free cash flow' thus can satisfy hungry shareholders looking for dividends and special pay-outs.

7. Small and emergent players

The current enterprise value of smaller market cap listed players gives real cause for concern, and the question is how many of them have the balance sheet and the compelling story (source of revenues from their technology solutions) to survive until the economic upswing. Considering just a handful of smaller 'pure play' renewable solution companies, the storyline feels darker: -

- **AFC Energy (AFC.L).** Provides hydrogen power solutions, for charging EV's vehicles and more recently construction plant equipment. Share price peaked at close to 85p in late 2020, early 2021, now sits at 15p, with a market cap of £94m. This represents an enterprise value drop of around 85%.

- **Atome Energy (ATOM.L).** Only listed company to provide green hydrogen and ammonia products. Its share price peaked at 136p in April 2022, but since has dropped to 79p, leaving it with a market cap £32m, a lesser decline of 42%, perhaps underpinned by revenue generation becoming more consistent.

- **Eqtec (EQT.L).** Provides waste to energy solutions and proprietary gasification technology. Share price peaked at nearly 3p in late 2020 early 2021, now sits at a lowly 0.04p with a current market cap of £5m (a decline of 98%).

- **SIMEC Atlantis Energy (SAE.L)**. Tidal stream power solutions and waste to energy fuel technologies. Share price was 79p in September 2016, since it has rapidly reduced to trade at 0.9p, market cap of 6.7m a decline of 99%.

- **Velocys (VLS.L).** Developing sustainable airline fuels (SAF). Share price peak, 12p in November 2021 (although in its infancy back in 2013, shares were trading at 234p), currently trades at 0.275p, 99.99% and is subject to a discounted offer take over approach (it has admitted running out of cash).

This snapshot is by no means exhaustive, but there are common themes:

- The missions of these innovators are admirable, sharing a desire to develop sustainable, renewable, and low-carbon energy solutions.
- Nature is cruel and unforgiving, and investors are increasingly reverting to brutal financial assessment in lieu of green, moral investment.
- Not all such companies will survive the current economic storm.

8. Survival of the fittest - but at what price?

We can all agree that the world needs sustainable, renewable, and low carbon energy. We probably agree too that the big corporates don't own all the good ideas, although they may have the muscle to develop them. We operate in a world dominated by the concept of the survival of the fittest; not every company deserves to survive and that "you have to pay to play", so founders/innovators are going to have to consider the cost/ benefit of dilution to raise funds stand the chance to survive. The loyal, long-term investor in such ventures, has already seen staggering losses, in some cases, near total wipe-out.

Those backers are fatigued and less wealthy and becoming increasingly rare. Companies whose leaders are honest, courageous, and prepared to face reality, to make timely changes, might just ride the wave. Regardless of the strength of their products and solutions (and no matter the potential), some of these companies simply won't make it.

9. What could turn this situation around?

Reduced inflation and interest rates. Truth telling about the nature of the costs of acting and not acting on green issues and the proper understanding of the impact on the bill payer. A forty-year Government strategy for National Energy Security with concerted and sustained government sponsorship and intervention. Partnerships between Governments and the corporates (big and small). A business environment suitable to compliment and supplement emergent companies, including investment incentives and with the 'climate' valued at a premium to simple business economics. Improved performance of the emergent companies themselves, more rigorous about their strategic and business planning, marketing, R&D, and critically ruthless with cost control, all as should be needed to successfully secure funding.

10. How can ValueStep help?

We provide business critical assessment and intervention solutions to founders, shareholders and boards seeking to realise their next step change in enterprise value or to navigate and mitigate a serious threat or risk to it. Bringing perspective and experience from decades of leadership, company ownership and trusted advisory roles, we thrive in the most challenging situations.

Contact us to learn more.

James Leng, Director, Value Step Limited

UK: +44 (0) 7799 060674

International: +353 (0) 87 460 5484

www.valuestep.co.uk