VELOCYS

# News release

## Velocys plc

("Velocys" or "the Company")
This announcement contains price sensitive information.

**26 September 2016**

## Interim results for the six months ended 30th June 2016

Velocys plc (VLS.L), the company at the forefront of smaller scale gas-to-liquids (GTL), is pleased to announce its interim results for the six months ended 30th June 2016.

**Highlights**

- Good progress at ENVIA Energy's GTL plant in Oklahoma City (in H1 and post period end):
  - Construction complete.
  - On-site loading of Fischer-Tropsch catalyst complete.
  - Highly experienced Velocys commissioning team deployed on site in July 2016.
  - Pre-commissioning activities substantially complete.
  - Robust commissioning plan in place and early commissioning steps begun.
- US$3 million equity and US$9 million secured loan facility (10% coupon) made available to ENVIA in February 2016. Greater influence in the commissioning, start-up and operations of the plant for Velocys.
- Other existing opportunities progressing:
  - Preliminary engineering studies completed, including for a GTL project in Central Asia (post period end).
  - Air permit granted on a third party project in the US (post period end).
- Strategy review underway. Update will be provided in Q4 2016.
- Velocys pilot plant completed its comprehensive demonstration of the Company's technology.
- Revenue of £0.5 million (H1 2015: £0.1 million).
- Cash* at period end £24.1 million (31 December 2015: £37.7 million).
- H2 2016 cash outflow to be materially lower than H1 (excluding the drawdown on the loan to ENVIA).

**David Pummell, CEO of Velocys, said:**
"Successful commissioning and operational start-up of the ENVIA plant is now within sight and its steady state operation will represent a seminal milestone for Velocys. Planned progress is being made week by week towards this goal by our operational team on the ground in Oklahoma City. Our significantly increased operational involvement in the ENVIA project has allowed the Company to assure the plant's successful operation and has further enhanced our core competences and real-world GTL project execution, commissioning, start-up and operations capabilities.

"In addition I am very pleased with the progress made recently on a number of other fronts, including a detailed review of the Company's strategy, advancement of future project opportunities and maintaining a continued focus on prudent cost management across the Company."

* Defined as cash, cash equivalents and short term investments.

**Corporate Broker**
On 23 September 2016, Canaccord Genuity Limited was appointed as Joint Corporate Broker to Velocys to work alongside Numis Securities who remains Joint Corporate Broker and Nominated Adviser.

**– Ends –**

## For further information, please contact:


| | |
|---|---|
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## Notes to editors

About Velocys
Velocys is the company at the forefront of smaller scale gas-to-liquids (GTL) that turns natural gas or biomass into premium products such as diesel, jet fuel, waxes and base oils. Smaller scale GTL adds value to a range of gas and biomass resources, and makes stranded or flared gas economic – an untapped market of up to 25 million barrels per day.

Velocys technology, protected by several hundred patents in over 30 countries, is specifically designed for smaller scales, combining super-active catalysts with intensified reactor systems. The Company's standardised modular plants are easier to ship and faster to install, at lower risk, even in the most remote or challenging locations. Together with world-class partners, Velocys works flexibly to unlock gas resources of 15,000 to 150,000 mmbtu per day, allowing more companies to take advantage of more opportunities.

Velocys plc is listed on the AIM market of the London Stock Exchange (LSE: VLS). The Company has a strong, multi-disciplinary staff operating from its commercial centre in Houston, Texas, USA and technical facilities near Oxford, UK and Columbus, Ohio, USA. Construction is complete at its commercial reference plant, which is located adjacent to Waste Management's East Oak landfill site in Oklahoma City.

www.velocys.com

**Think Smaller™. Velocys is changing the way fuels are made.**

# Chairman's statement
**Pierre Jungels, CBE**

There is a great sense of anticipation within Velocys, as well as externally, as the start-up of the ENVIA Energy GTL plant in Oklahoma City approaches. Velocys' on-site team is playing a number of key roles in this process; we have every confidence in the plant's successful operation and we fully expect this to develop the smaller scale GTL market and drive our business forward. The platform for success is strong – the manufacturing supply chain has delivered commercial reactors and catalyst, the Velocys pilot plant has completed its comprehensive demonstration of the technology, and the Company's intellectual property remains well protected.

Velocys continues to work through this challenging period of low and volatile oil prices and limited availability of capital, in particular for new upstream projects. For this reason, the Board has initiated a strategic review that will both determine the strategic plan to commercialise our technology and grow the business, and ensure we are best prepared to withstand the ongoing uncertainty in the sector. The review of strategy is discussed further in the CEO's report. It is a testament to the strength of our business that both the ENVIA project and a number of third-party projects continue to make tangible progress during this period.

The Company knows it cannot rely on a swift return of oil prices to higher levels, even though there have been some encouraging signs of positive oil price movements in 2016. However, natural gas remains an abundant, low cost and under-utilised resource, and there are numerous situations where opportunities remain attractive and financially robust.

Wider political and socio-economic factors increasingly favour the adoption of GTL. The flaring of associated gas is becoming increasingly unacceptable. Momentum is building for the Global Gas Flaring Reduction Partnership's "Zero routine flaring by 2030" initiative, with the US, Canada and Nigeria all pledging their support for this programme run by the World Bank in the first half of 2016.

The acceptance of alternative fuels continues to grow. United Airlines became the first US airline to begin use of commercial-scale volumes of sustainable aviation biofuel for scheduled flights, and the European Committee for Standardisation (CEN) has approved a new European Standard for synthetic paraffinic diesel. The new standard will help the GTL industry by increasing the acceptance of and sale of Fischer-Tropsch (FT) diesel.

David Pummell joined the Company as CEO in January 2016. He is bringing significant commercial challenge to what we do and has a management style that is inclusive, positive and fresh. I would like to congratulate him on the way he has stepped into the leadership of what is an established and effective senior management team, bringing a new perspective and his considerable experience of deal creation.

Earlier this month Jan Verloop retired from his role as Non-executive Director. The technical and GTL expertise that Jan has brought to the Board has been pivotal in guiding the Company's technology development from an innovative idea to a fully validated system with steel in the ground at its commercial reference plant. I thank him for his 10 years of valued service.

Although the focus of the Company is currently very much on the ENVIA plant, it continually reviews opportunities to enter new markets and projects. For example, in the first half of 2016 the Company explored an opportunity to acquire, in partnership with other parties, certain GTL assets of a US-located company that had gone into Chapter 11 bankruptcy. Velocys entered into discussions with the company's debtors, but was not ultimately able to secure the acquisition of the assets with favourable terms. David Pummell and his team cost-effectively pursued this opportunity with great energy, handled its complexities rigorously, and responded positively to the Board's scrutiny and challenge. To me this was a clear sign of a team working effectively together, and with their Board.

## Outlook

Velocys remains confident in the successful start-up, commissioning and operation of ENVIA Energy's GTL plant. In parallel, Velocys is pursuing a broad review of its strategy, which will define the best way to deliver its world-leading technology to market. We expect that having a commercial reference plant up and running will greatly enable our commercialisation and value growth.

# Chief executive's report

**David Pummell**

## Introduction

In the first half of the year I have been enormously impressed and encouraged by the advances made at ENVIA Energy's GTL plant in Oklahoma City; construction is now complete and early commissioning steps have begun. Velocys and its partners are working together in a high-performing professional collaboration and I have confidence that we shall continue to build on this progress and deliver a safe, successful start-up of the plant and the production of in-specification product. Looking beyond ENVIA, in the short term we plan to complete our review of strategy and define the high level plan for commercialisation that will be implemented over the coming months and years. We shall also keep focused on the prudent management of our cash expenditure.

## Market conditions

In its 2016 Annual Energy Outlook Early Release, the US Energy Intelligence Agency (US EIA) predicts a slow upturn in oil prices to around $48 per barrel in 2018. A return to levels of $90 per barrel is not to be expected over the short or medium term. Despite that, plant economics remain favourable for smaller scale GTL projects that access low price feedstocks, exploit local situations in isolated areas where the cost of fuel is high, or target high value speciality products. Prices for wax are decoupled from oil; the price for some cuts of Fischer-Tropsch (FT) wax is as much as US$300 per barrel and the US supply of wax for use in-country has decreased by 66% since the late 1990s. The outlook for wax pricing, and the wax market in general, is positive.

In the longer term, the market for smaller scale GTL remains substantial; 50% of stranded gas fields worldwide are of a size that could be unlocked by smaller scale GTL, and 140 billion cubic meters of associated gas is currently flared each year around the world. Meanwhile, diesel demand continues to be strong; for example, the US EIA predicts that between 2011 and 2040 the total transportation fuel demand in the US being met by diesel will increase appreciably. Furthermore, the FT process (starting with syngas derived from biomass) is one of a very small number of options that could deliver a sustainable drop-in replacement to conventional jet fuel with an energy density high enough for use in aviation. Thus, the fundamentals exist for a large market for smaller scale GTL, subject to economics appropriate to each location.

## Strategy

The review of the Company's strategy and commercial opportunities is now underway. The start of this review was delayed in order to focus on the potential acquisition of certain GTL assets in the US from bankruptcy. During that process it emerged that the deal available to Velocys was not in the Company's best interests and so it was decided not to pursue it to completion. From my perspective, this initial period in the Company enabled me to accelerate my learning regarding our technology, our capabilities, our competition, and the market dynamics around the world. It also allowed me to start shaping my thoughts about what we must do to accelerate the commercialisation of our technology and leverage the considerable capabilities and experience of the Company.

The review of strategy will provide a clear direction for Velocys in terms of the markets (geographic, feedstock and product) on which the Company will focus, how we will participate in those markets and leverage our assets and capabilities.

My approach is that the strategy adopted shall be simple, realistic and implementable. Significant market data, projections on market dynamics and market intelligence on key stakeholders have all been inputs to the review process. We will provide shareholders with an update with regard to this process before the end of 2016.

## Commercialisation

Commercial reference plant

Construction of ENVIA Energy's GTL plant in Oklahoma City is now complete. This is a major milestone for Velocys and a significant step for the smaller scale GTL industry. I congratulate the team for their hard work and their dedication over many years that have enabled us and our partners to reach this point.

Over the spring and summer all of the modular process units, including those incorporating the Velocys reactors, and all other major packaged equipment skids, including the steam methane reformer, cooling towers, landfill gas inlet and syngas compression units, product storage tanks and motor control centre were set in place on site. Piping, electrical and instrumentation installation progressed at an accelerated pace during that period; at the height of which 170 personnel were working on site. Loading of catalyst into the FT reactors has been completed by Velocys with support from its internationally-recognised partner, Mourik.

Photographs of recent progress on-site are available at www.velocys.com/media_image_library.php.

Pre-commissioning work, including hydro-testing of the lines and vessels, and a rigorous inspection process, is substantially complete. The team has made extensive and detailed preparations; operating manuals and procedures have been fully completed and robust commissioning and start-up plans are in place. In line with best practice, the commissioning plan will ensure that each process system in sequence is working robustly, safely, and within specification, in order to best assure a successful, safe and uneventful plant start up. Early commissioning steps have begun.

In February 2016, as part of a stakeholder capital contribution, Velocys made available to ENVIA a senior loan of US$9 million, secured on the project. Additional equity ownership units and voting rights were granted to the Company as part of the terms of the loan agreement and Velocys sought and gained greater operational management involvement in the project.

Velocys has been supporting the EPC contractor, Ventech, in leading and executing the planning for the commissioning, start-up and operation of the plant. For example, the Company has provided, under contract, an operability review, operating procedures and commissioning management.

Additionally, under a secondment agreement with ENVIA, Velocys' team of experienced GTL operations managers, operators and engineers have been on site in Oklahoma City since their deployment began in July. This Velocys operations team, which is serving under the ENVIA Plant Manager, will bring essential support to the ENVIA team through commissioning, start-up and early stage operations, until the permanent operations team is phased in over a planned period. The Velocys team brings a wealth of operational GTL plant expertise including commissioning and plant performance optimisation, drawing on experience gained at a number of large scale commercial GTL projects as well as from the Velocys pilot plant.

Drawdown on the loan to ENVIA will begin in Q4 2016, with the final drawdown expected in Q1 2017. The majority of the drawdown will fall in the current financial year. Velocys will endeavour to pursue options for the early repayment of the loan once the plant is operational. The Company does not currently anticipate any additional funding needs from Velocys for the project.

US Congressman Steve Russell and his Energy Legislative Assistant toured the plant this summer and pledged their ongoing support for H.R. 2412, a bill that would establish tax parity for methane conversion technologies such as GTL with LNG and CNG. The Congressman, a Republican, represents the 5$^{th}$ District of Oklahoma, the district in which ENVIA's plant is located.

Evaluation continues, with our partners, on future ENVIA projects using learnings from the Oklahoma City project.

Pipeline of projects

Successful operation of ENVIA's GTL plant will facilitate progress with third-party sales opportunities for Velocys technology. It will establish a commercial reference site for the Velocys technology, providing commercial-scale performance data for stakeholders to analyse, and a physical site where they can see our technology in action.

In addition, the construction of the commercial reference plant has naturally brought many learning points that the Company can and will use in future projects. These include plant-wide integration design improvements that will increase the efficiency and economics of future GTL plants incorporating Velocys technology.

Velocys has also demonstrated competence in a broader set of roles through its involvement in the ENVIA project, as part owner, commissioning contractor as well as technology licensor. Velocys is building on its solid technology background, and growing into a company with real-world commercial GTL project execution, commissioning, start-up and operations capabilities beyond the Fischer-Tropsch section of a plant.

The further analysis of the wax market in North America that was carried out by Velocys in H1 confirmed that the projected plant economics remain attractive for a 5,000 barrel per day (bpd) GTL plant that Velocys has been developing in North America, focused on the production of waxes and other speciality products. Given the challenges in raising equity for capital projects of this nature at present and in order to defer costs, Velocys has put its development of Ashtabula on hold, pending reassessment as part of the broad review of the strategy of the business that the Company is currently undertaking.

Meanwhile, projects being developed by third parties that are pursuing independent sources of funding, and where Velocys acts purely as technology licensor and supplier of reactors, catalysts and services, make up most of the Company's current sales pipeline, as in previous years. In the first half of 2016, new, attractive opportunities have emerged and existing projects have progressed.

Red Rock Biofuels, which is developing a biomass-to-liquids plant of over 1,100 bpd using forestry waste as feedstock in Lakeview, Oregon, USA, continues to make progress on permitting, financing and offtake agreements. Elsewhere, the opportunity with a major fuels player in the US remains active; recent progress includes the issuing of the air permit for the plant.

Two engineering studies previously announced were completed recently by Velocys and its project partners:

- The project being developed on behalf of a national gas company in Central Asia that is seeking to develop its stranded gas reserves. Velocys' project partner will present the findings of the study to the project sponsor shortly.
- The development of a new waste-to-liquids project in the UK. Velocys is reviewing options with potential partners.

Pilot plant, technology and intellectual property

The Velocys pilot plant (VPP) has been one of the Company's most significant assets used in the validation of its technology, to aid client-specific business development activities, to optimise plant economics and to refine operating procedures at ENVIA and for future commercial plants.

As outlined in the 2015 annual report and accounts, the VPP was placed into standby mode in Q2 2016. It remains available for specific client-supported studies if needed. The VPP operators and engineers currently form the core of the commissioning and operations team at ENVIA's Oklahoma City plant.

Meanwhile, a third-party independent engineering firm has validated Velocys' design for larger FT reactors, use of which will allow the substantial simplification of larger plants using our technology. Modular designs for the complete FT "island" have been developed, both with the existing four-core reactors with a capacity of around 175 bpd, and with larger reactors with 700 bpd capacity. This positions Velocys well to respond cost-effectively to the needs of customers developing projects with a wide range of plant capacities.

Velocys remains committed to developing and protecting its intellectual property (IP) to optimise its competitive position, primarily through patents, trade secrets, and trademarks. Velocys' IP portfolio includes several hundred patents worldwide, including twenty cases that were granted during the first half of 2016.

## Financials

Total revenues for the period were £0.5m (H1 2015: £0.1m). This was mostly engineering fees from a number of design studies, but also included the first revenue from the secondment of employees to the ENVIA site. Revenue from reactor sales to ENVIA was recognised in 2015 and revenue from the lease of catalyst to ENVIA will be recognised once the plant is operational.

Operating loss was reduced to £9.5m before exceptional items (£9.4m after exceptionals) (H1 2015: £12.5m (no exceptionals)). Exceptional items, which are explained in more detail in note 3, included:

- Net expenses of £2.4m incurred during the pursuit of the opportunity to acquire certain GTL assets of a US-based company in administration.
- Remaining £2.5m income from a lapsed contract for Velocys reactors that had been deferred after receipt of upfront payments.
- £3.4m income (not included in the operating loss) arising from the accounting treatment of the investment in ENVIA.

The Company continues to take prudent measures to control expenditure and preserve cash given the market environment and while it seeks to secure further commercial orders. These measures have included, but are not limited to, putting the development of Ashtabula GTL on hold and placing the VPP into stand-by mode. In selecting measures to take with regards to its capital discipline, a primary concern of the Company has been to ensure they will not impact Velocys' ability to deliver its commitments at ENVIA or its readiness to implement a new strategic plan. With regard to orders, a small number of the projects in Velocys' sales pipeline that are being developed by third parties could provide cash in-flow to the business in the next 12 months.

Cash (including short term investments) at period end stood at £24.1m (31 December 2015: £37.7m), while cash outflow (excluding share issues) was £13.3m (H1 2015: £13.6m). The increased outflow from H2 2015 (£8.4m) was largely as a result of the incurrence of exceptional expenses mentioned above. H2 2016 cash outflows (excluding drawdown on the ENVIA loan) are expected to be materially lower than in H1 at around £7m.

The Company incurs much of its expense in US dollars and has exposure to the US dollar exchange rate. This is hedged to the extent possible by holding cash reserves in US dollars and taking out forward contracts to cover future foreign exchange exposure. In addition, the majority of the Company's income is invoiced in dollars.

# Consolidated income statement

for the six months ended 30 June 2016

| | Note | **6 months ended 30 June 2016 (unaudited)** £'000 | **6 months ended 30 June 2016 (unaudited)** £'000 | **6 months ended 30 June 2016 (unaudited)** £'000 | 6 months ended 30 June 2015 (unaudited) £'000 | Year ended 31 December 2015 (audited) £'000 | Year ended 31 December 2015 (audited) £'000 | Year ended 31 December 2015 (audited) £'000 |
|---|---|---|---|---|---|---|---|---|
| | | Before Exceptional items | Exceptional items (note 3) | Total | | Before Exceptional items | Exceptional items (note 3) | Total |
| **Revenue** | 4 | 509 | - | 509 | 120 | 2,002 | - | 2,002 |
| Cost of sales | | (443) | - | (443) | (20) | (1,275) | - | (1,275) |
| **Gross profit** | | 66 | - | 66 | 100 | 727 | - | 727 |
| Research and development costs | | (5,323) | - | (5,323) | (6,036) | (13,199) | - | (13,199) |
| Share-based payments | | (472) | - | (472) | (1,513) | (2,142) | - | (2,142) |
| Administrative expenses | | (4,042) | (2,428) | (6,470) | (5,092) | (10,142) | (1,204) | (11,346) |
| **Total administrative expenses** | | (9,837) | (2,428) | (12,265) | (12,641) | (25,483) | (1,204) | (26,687) |
| **Other income** | | 263 | 2,496 | 2,759 | 12 | 2,009 | 1,763 | 3,772 |
| **Operating income (loss)** | | (9,508) | 68 | (9,440) | (12,529) | (22,747) | 559 | (22,188) |
| Finance income | 5 | 1,943 | - | 1,943 | 389 | 1,155 | - | 1,155 |
| Finance costs | 6 | (17) | - | (17) | (244) | (53) | - | (53) |
| **Income (loss) before income tax** | | (7,582) | 68 | (7,514) | (12,384) | (21,645) | 559 | (21,086) |
| Share of profit of investments accounted for using the equity method | | (207) | 3,431 | 3,224 | - | - | - | - |
| Income tax credit | | 396 | - | 396 | 341 | 1,035 | - | 1,035 |
| **Income (loss) for the period attributable to the owners of Velocys plc** | | (7,393) | 3,499 | (3,894) | (12,043) | (20,610) | 559 | (20,051) |
| **Loss per share attributable to the owners of Velocys plc** | | | | | | | | |
| Basic and diluted loss per share (pence) | 7 | (5.18) | | (2.73) | (8.49) | (14.52) | | (14.13) |

The results from the periods shown above are derived entirely from continuing operations. There were no exceptional items for the six months ended 30 June 2015.

# Consolidated statement of comprehensive income

for the six months ended 30 June 2016

| | Note | **6 months ended 30 June 2016 (unaudited)** £'000 | **6 months ended 30 June 2016 (unaudited)** £'000 | **6 months ended 30 June 2016 (unaudited)** £'000 | 6 months ended 30 June 2015 (unaudited) £'000 | Year ended 31 December 2015 (audited) £'000 | Year ended 31 December 2015 (audited) £'000 | Year ended 31 December 2015 (audited) £'000 |
|---|---|---|---|---|---|---|---|---|
| | | Before exceptional items | Exceptional items (note 3) | Total | | Before Exceptional items | Exceptional items (note 3) | Total |
| Income (loss) for the period | | (7,393) | 3,499 | (3,894) | (12,043) | (20,610) | 559 | (20,051) |
| **Other comprehensive income** | | | | | | | | |
| **Items that may be reclassified subsequently to profit or loss if certain conditions are met** | | | | | | | | |
| Foreign currency translation differences | 8 | 3,944 | - | 3,944 | (276) | 1,869 | - | 1,869 |
| **Total comprehensive income (expense) for the period** | | (3,449) | 3,499 | 50 | (12,319) | (18,741) | 559 | (18,182) |

# Consolidated statement of financial position

as at 30 June 2016

| | Note | **30 June 2016 (unaudited) £'000** | 30 June 2015 (unaudited) £'000 | 31 December 2015 (audited) £'000 |
|---|---|---|---|---|
| **Assets** | | | | |
| **Non-current assets** | | | | |
| Intangible assets | | 31,394 | 28,086 | 28,378 |
| Property, plant and equipment | | 5,608 | 5,418 | 5,507 |
| Investments | 9 | 9,122 | 2,563 | 3,375 |
| | | 46,124 | 36,067 | 37,260 |
| **Current assets** | | | | |
| Trade and other receivables | | 491 | 821 | 911 |
| Current income tax asset | | 1,176 | 1,140 | 780 |
| Inventories | | 1,517 | 1,421 | 1,393 |
| Derivative financial instruments | | 985 | - | 156 |
| Short term investments – funds held on deposit | | - | 23,998 | 3,000 |
| Cash and cash equivalents | | 24,141 | 22,154 | 34,736 |
| | | 28,310 | 49,534 | 40,976 |
| **Total assets** | | 74,434 | 85,601 | 78,236 |
| **Liabilities** | | | | |
| **Current liabilities** | | | | |
| Trade and other payables | | (3,162) | (10,138) | (7,380) |
| Borrowings | | (320) | (265) | (288) |
| | | (3,482) | (10,403) | (7,668) |
| **Non-current liabilities** | | | | |
| Trade and other payables | | (1,497) | (318) | (1,327) |
| Borrowings | | (682) | (855) | (759) |
| Deferred tax | | - | (269) | - |
| | | (2,179) | (1,442) | (2,086) |
| **Total liabilities** | | (5,661) | (11,845) | (9,754) |
| **Net assets** | | 68,773 | 73,756 | 68,482 |
| **Capital and reserves attributable to owners of Velocys plc** | | | | |
| Called up share capital | | 1,419 | 1,419 | 1,419 |
| Share premium account | | 148,966 | 149,238 | 149,197 |
| Merger reserve | | 369 | 369 | 369 |
| Share-based payment reserve | | 15,834 | 14,732 | 15,362 |
| Foreign exchange reserve | | 3,662 | (2,427) | (282) |
| Accumulated losses | | (101,477) | (89,575) | (97,583) |
| **Total equity** | | 68,773 | 73,756 | 68,482 |

The financial statements were approved by the Board of Directors on 23rd September 2016, and were signed on its behalf by:

Susan Robertson
Chief Financial Officer

# Consolidated statement of changes in equity

as at 30 June 2016

| | Called up share capital £'000 | Share premium account £'000 | Merger reserve £'000 | Share-based payments reserve £'000 | Foreign exchange reserve £'000 | Accumulated Losses £'000 | **Total** £'000 |
|---|---|---|---|---|---|---|---|
| **Balance at 1 January 2015** | 1,419 | 149,225 | 369 | 13,220 | (2,151) | (77,532) | 84,550 |
| **Comprehensive income** | | | | | | | |
| Loss for the year | - | - | - | - | - | (20,051) | (20,051) |
| **Other comprehensive income** | | | | | | | |
| Foreign currency translation differences | - | - | - | - | 1,869 | - | 1,869 |
| **Total comprehensive income (expense)** | - | - | - | - | 1,869 | (20,051) | (18,182) |
| **Transactions with owners** | | | | | | | |
| Share-based payments – value of employee services | - | - | - | 2,142 | - | - | 2,142 |
| Employee benefit trust reimbursement | - | (28) | - | - | - | - | (28) |
| **Total transactions with owners** | - | (28) | - | 2,142 | - | - | 2,114 |
| **Balance at 1 January 2016** | 1,419 | 149,197 | 369 | 15,362 | (282) | (97,583) | 68,482 |
| **Comprehensive income** | | | | | | | |
| Loss for the period | - | - | - | - | - | (3,894) | (3,894) |
| **Other comprehensive income** | | | | | | | |
| Foreign currency translation differences | - | - | - | - | 3,944 | - | 3,944 |
| **Total comprehensive income (expense)** | - | - | - | - | 3,944 | (3,894) | 50 |
| **Transactions with owners** | | | | | | | |
| Share-based payments – value of employee services | - | - | - | 472 | - | - | 472 |
| Tax payment on exercise of options | - | (311) | - | - | - | - | (311) |
| Issuance of holdback shares from acquisition of Velocys Project Solutions | - | 80 | - | - | - | - | 80 |
| **Total transactions with owners** | - | (231) | - | 472 | - | - | 241 |
| **Balance at 30 June 2016** | 1,419 | 148,966 | 369 | 15,834 | 3,662 | (101,477) | 68,773 |

# Consolidated statement of cash flows

for the six months ended 30 June 2016

| | **6 months ended 30 June 2016 (unaudited)** £'000 | 6 months ended 30 June 2015 (unaudited) £'000 | Year ended 31 December 2015 (audited) £'000 |
|---|---|---|---|
| **Cash flows from operating activities** | | | |
| Operating loss | (9,440) | (12,529) | (22,188) |
| Depreciation and amortisation | 674 | 513 | 1,277 |
| Loss on disposal of property, plant and equipment | - | - | 5 |
| Loss on disposal of intangible assets | 91 | 123 | 383 |
| Impairment of intangible assets | - | - | 1,473 |
| Write-down of deferred consideration and deferred tax liability | - | | (2,032) |
| Share-based payments | 472 | 1,513 | 2,142 |
| Tax payment on exercise of options | (311) | - | - |
| Loss on derivative financial instruments | - | 435 | 279 |
| Changes in working capital (excluding the effects of exchange differences on consolidation) | | | |
| -Trade and other receivables | 454 | (76) | (301) |
| -Trade and other payables | (4,480) | (444) | (975) |
| -Inventory | (14) | (1,150) | (1,066) |
| Interest paid | (14) | (18) | (33) |
| Tax credits received | - | 978 | 2,031 |
| **Net cash used in operating activities** | (12,568) | (10,655) | (19,005) |
| | | | |
| **Cash flows from investing activities** | | | |
| Purchases of property, plant and equipment | (159) | (1,874) | (2,262) |
| Purchases of intangible assets | (205) | (219) | (395) |
| Investment in ENVIA | (1,805) | (901) | (1,535) |
| Interest received | 84 | 85 | 401 |
| Decrease in funds placed on deposit | 3,000 | 4,085 | 25,083 |
| **Net cash generated from investing activities** | 915 | 1,176 | 21,292 |
| | | | |
| **Cash flows from financing activities** | | | |
| Issuance of equity shares (including Trust payments) | - | 13 | (28) |
| Decrease in borrowing | (147) | (135) | (271) |
| **Net cash used in financing activities** | (147) | (122) | (299) |
| **Net (decrease) increase in cash and cash equivalents** | (11,800) | (9,601) | 1,988 |
| Cash and cash equivalents at the beginning of the period | 34,736 | 31,693 | 31,693 |
| Exchange gains on cash and cash equivalents | 1,205 | 62 | 1,055 |
| **Cash and cash equivalents at the end of the period** | 24,141 | 22,154 | 34,736 |

# Notes to the accounts

for the six months ended 30 June 2016

## 1. Basis of preparation and accounting policies

The unaudited interim financial statements have been prepared in accordance with International Financial Reporting Standards as adopted by the European Union (IFRSs as adopted by the EU), IFRS IC Interpretations and the Companies Act 2006 applicable to companies reporting under IFRS and Article 4 of the IAS Regulation including those applicable to accounting periods ending 31 December 2016 and the accounting policies set out in Velocys plc's annual report for the year ended 31 December 2015. These unaudited interim financial statements have been prepared in accordance with International Accounting Standard 34 "Interim Financial Reporting". They do not include all the statements required for full annual financial statements, and should be read in conjunction with the consolidated financial statements of the Company as at 31 December 2015.

In preparing these condensed interim financial statements, the significant judgements made by management in applying the Group's accounting policies and the key sources of estimation uncertainty were as stated within the consolidated financial statements for the year ended 31 December 2015.

The Directors have concluded that it is appropriate to prepare the financial statements on the going concern basis. Management have prepared financial forecasts to estimate the likely cash requirements of the Company over the next twelve months. These forecasts include certain assumptions with regard to the costs of ongoing development projects, overheads, commitments to funding ENVIA, and the timing and amount of any funds generated from commercial revenues. The projections demonstrate that when reasonable sensitivities are applied the existing funds cover the Company's cash requirements for at least the next twelve months.

The nature of Velocys' commercialisation programme means that the timing of funds generated from future sales is difficult to predict and so the Directors will continue to review other sources of finance as appropriate.

## 2. Publication of non-statutory accounts

The financial information for the six month periods ended 30 June 2016 and 30 June 2015 has not been audited or reviewed and does not constitute full financial statements within the meaning of Section 434 of the Companies Act 2006.

The financial information relating to the year ended 31 December 2015 does not constitute a full financial statement within the meaning of Section 434 of the Companies Act 2006. This information is based on the Company's statutory accounts for that period. The statutory accounts were prepared in accordance with IFRS, received an unqualified audit report, did not include a reference to any matters to which the auditors drew attention by way of emphasis without qualifying the report and did not contain a statement under section 498(2) or (3) of the Companies Act 2006. These accounts have been filed with the Registrar of Companies.

## 3. Exceptional items

Items that are material because of their size or nature, and/or that are non-recurring are considered as exceptional items and are presented with the line items to which they best relate. Exceptional items, as detailed below, have been included in the consolidated income statement.

Exceptional items were as follows:

| | **6 months ended 30 June 2016 (unaudited)** | 6 months ended 30 June 2015 (unaudited) | Year ended 31 December 2015 (audited) |
|---|---|---|---|
| | **£'000** | £'000 | £'000 |
| Costs of unsuccessful acquisition | (2,428) | - | - |
| Recognition of deferred income | 2,496 | - | - |
| Excess of the entity's share of the net fair value of the associate's identifiable assets and liabilities over the cost of the investment | 3,431 | - | - |
| Impairment of intangible assets | - | - | (1,473) |
| Deferred tax liability write down | - | - | 269 |
| Deferred consideration write down | - | - | 1,763 |
| | 3,499 | - | 559 |

In 2016, the Company sought to acquire certain assets of a US-based GTL company that had gone into administration but did not complete the acquisition. The Company received a partial reimbursement by the acquirer of the plant. The Costs of unsuccessful acquisition in the table above represents the amounts spent on the activity net of the related reimbursement.

The Company released £2,496,000 of deferred revenue in respect of the cancellation of the Ventech contract. The deferred income arose on receipt of upfront payments, and, under the terms of the contract, is not refundable to Ventech. The full amount was recognised as other income.

The excess of the Company's share of the net fair value of ENVIA's identifiable assets and liabilities over the cost of the investment relates to negative goodwill arising at the point that the Company acquired an additional share of the business and therefore started to account for its investment in ENVIA on an equity basis. This is further explained in note 9.

The impairment of intangible assets in 2015 relates to the full impairment of customer contracts. Customer contracts represented the discounted value of expected future income, which the Company had expected to receive in 2015 upon obtaining a final investment decision (FID) by outside investors in the Ashtabula project. Since FID was not reached in 2015, this balance was written down to £nil. In addition, the related deferred tax liability was written down to £nil.

The deferred consideration arrangement required the Company to issue shares in Velocys plc to the former owners of Velocys Project Solutions contingent upon the achievement of FID on the plant in Ashtabula in a specified time frame. In 2015 the deferred consideration was written down to £nil through Other income as the FID was not achieved.

## 4. Segmental information

Business segments
At 30 June 2016 the Company is organised as a world-wide business comprising a single segment.

Geographic segments
The Company's business operates in three main geographical areas. Revenue is allocated based on the country in which the customer is located.

| | **6 months ended 30 June 2016 (unaudited)** | | | 6 months ended 30 June 2015 (unaudited) | | |
|---|---|---|---|---|---|---|
| | Europe £'000 | Americas £'000 | Asia Pacific £'000 | Europe £'000 | Americas £'000 | Asia Pacific £'000 |
| Revenue | 273 | 236 | - | - | 107 | 13 |

## 5. Finance income

| | **6 months ended 30 June 2016 (unaudited)** | 6 months ended 30 June 2015 (unaudited) | Year ended 31 December 2015 (audited) |
|---|---|---|---|
| | **£'000** | £'000 | £'000 |
| Interest income on bank deposits | 76 | 173 | 329 |
| Net fair value gains on forward foreign exchange contracts | 1,116 | 216 | 381 |
| Foreign exchange gains | 751 | - | 445 |
| | 1,943 | 389 | 1,155 |

## 6. Finance costs

| | **6 months ended 30 June 2016 (unaudited)** | 6 months ended 30 June 2015 (unaudited) | Year ended 31 December 2015 (audited) |
|---|---|---|---|
| | **£'000** | £'000 | £'000 |
| Unwinding of discount on deferred licence payments payable | - | - | 20 |
| Interest on finance leases | 3 | 5 | 9 |
| Interest on borrowings | 14 | 13 | 24 |
| Foreign exchange losses | - | 226 | - |
| | 17 | 244 | 53 |

## 7. Loss per share

The calculation of loss per share is based on the following losses and number of shares:

| | **6 months ended 30 June 2016 (unaudited)** | | | 6 months ended 30 June 2015 (unaudited) | | | Year ended 31 December 2015 (audited) | | |
|---|---|---|---|---|---|---|---|---|---|
| | Loss | Number of shares | Pence per share | Loss | Number of shares | Pence per share | Loss | Number of shares | Pence per share |
| | £'000 | '000 | | £'000 | '000 | | £'000 | '000 | |
| Basic & fully diluted | (3,894) | 142,748 | (2.73) | (12,043) | 141,910 | (8.49) | (20,051) | 141,915 | (14.13) |

## 8. Foreign currency translation

The foreign currency translation differences included in the Consolidated statement of comprehensive income primarily related to differences arising on the translation into pounds sterling of a) the Company's net investment in Velocys, Inc. whose assets and liabilities are denominated in US dollars, and b) goodwill and fair value adjustments arising from the acquisition of Velocys, Inc. in 2008 which are also denominated in US dollars.

## 9. Investments

| | **6 months ended 30 June 2016 (unaudited)** | 6 months ended 30 June 2015 (unaudited) | Year ended 31 December 2015 (audited) |
|---|---|---|---|
| | **£'000** | £'000 | £'000 |
| Investment in ENVIA: | | | |
| At 1 January | 3,375 | 1,711 | 1,711 |
| Investment | 1,805 | 901 | 1,535 |
| Share of loss | (207) | - | - |
| Negative goodwill | 3,431 | - | - |
| Foreign exchange | 718 | (49) | 129 |
| | 9,122 | 2,563 | 3,375 |

Velocys' holding in ENVIA is the one item in Investments. In 2014 the Company entered into a joint venture with other partners to develop GTL plants using a combination of renewable biogas (including landfill gas) and natural gas. At 31 December 2015, the investment was recorded at cost, which was also considered to be fair value. At this date, the investment was considered to be an investment held for sale.

On 29 January 2016, Velocys entered into an additional financing arrangement with ENVIA under which the Company committed to provide loan financing. Under the terms of this arrangement, Velocys was awarded additional voting rights in ENVIA, which was recognised by an additional allocation of equity capital in ENVIA to Velocys. As a result of this additional equity, Velocys' share in ENVIA voting rights exceeded 20% and from this point, the investment has been recognised as an investment in an associate and accounted for under the equity method of accounting. The additional equity allocation gave rise to a negative goodwill balance of £3,431,000, which has been treated as an exceptional item in the income statement. Velocys share of losses of ENVIA since 29 January 2016 have been reflected in the consolidated income statement. These losses arise from administration costs incurred by ENVIA ahead of the start-up of its first GTL plant. The investment is denominated in US dollars.

Under the terms of the loan agreement, Velocys has committed to provide up to US$9,310,000 to ENVIA through a senior loan note bearing a 10% interest rate due on 31 December 2019 with an optional extension to 31 December 2020 with prior notice. As at 30 June 2016, no draw down on this facility had been made by ENVIA.

## 10. Post-financial position events

Significant progress was made on the ENVIA project between the end of H1 2016 and the date of this announcement. Completion of construction of the plant was announced on 21 September. Readers can refer to the business update of 7 July 2016 for a summary of the status of the ENVIA project (and other projects) at the end of H1 2016.

Non-executive Director Dr Jan Verloop stepped down from the Board on 20 September 2016.