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FORTUNES

Two exponential energy stocks to buy now



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Two exponential energy stocks to buy now

By James Allen
Editor, *Exponential Energy Fortunes*

Here are three things I don't know to be true and one thing I do.

Firstly, I don't know exactly when, or how, the coronavirus crisis will end. No one does.

It's very difficult to model, which means we don't really know how bad it's going to get – which, of course, is part of the problem.

When and how the coronavirus crisis ends will largely depend on the number of people who end up getting infected and the virus's still-largely-unknown mortality.

Secondly, I – along with everyone else – don't know what life will look like when coronavirus does finally pass.

Already societal norms are being dropped and, who knows, perhaps won't be picked up again.

How commonplace will handshakes, meetings and conferences be when the pandemic ends? The global shift from the analogue to digital might just have shunted from third gear into fifth.

Thirdly, I don't know what the financial markets will do while the world waits for a vaccine to be developed. Again, no one knows for sure.

Markets are already down by a third since the virus reached British shores nearly two months ago. Will they fall further? It seems unlikely to me that we have already found a bottom to the market, but then who knows?

When you look at liquidity, volatility, fund structure, the assumptions of bond-equity anti-correlation, debt levels, interest rates, valuations pre-crash, the oil shock and market psychology, it seems likely that there is much more to unwind.

Although it's never good to be too sure of these things, it *does* seem likely that, for long-term investors, this could well turn out to be a great investment opportunity. After all, every pound, dollar or euro invested today buys many more shares than it would have done just a few short weeks ago.

Which brings me on to something I *do* know to be true.

That is, the great megatrend towards cleaner energy, which has been underway over the last decade or more, certainly won't be derailed by coronavirus.

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It is going too fast, with too much intensity and far too much momentum to see off any challenge posed by the economic fall-out of Covid-19, which include lower oil prices.

In fact, I believe renewables investment is the best way we can turn the financial narrative surrounding coronavirus on its head, from threat to opportunity.

The reality is that decarbonisation is the single biggest investment opportunity on the planet right now and, arguably, ever has been in peacetime.

The numbers – potentially up to \$110 trillion to create a fully climate-safe system by 2050 – eclipse any other possible investment opportunity out there today by an order of magnitude.

As we emerge from the post Covid-19 wreckage, investors will see that climate change – backed by ambitious global climate change targets – provides perhaps the only long-term structural growth opportunity in the markets, one that has the potential to make life-changing returns.

From threat to opportunity

Certainly, once the dust settles – if not before – it's likely that fiscal stimulus will be necessary.

And where better – to get green points and support new projects, skills and jobs – than for governments to invest in the renewable energy industry?

High-capex solar and wind could be an ideal post-corona stimulant and tonic for the global economy. Certainly, there will be few better vehicles for public money than renewable energy infrastructure.

A massive increase in spending by governments will help the energy transition, as it climbs back to the top of priority lists in the aftermath of the current mayhem.

The International Energy Agency (IEA) has already recognised the opportunity, demanding that clean energy is put “at the heart of stimulus plans to counter the coronavirus crisis”.

Boosting deployment of technologies including wind, solar, and battery storage provides “twin benefits” of stimulating economies and moving to cleaner energy, IEA executive director, Dr Fatih Birol, said in a [LinkedIn post on 14 March](#).

“Governments can use the current situation to step up their climate ambitions and launch sustainable stimulus packages focused on clean energy technologies,” Birol said.

“The coronavirus crisis is already doing significant damage around the world. Rather than compounding the tragedy by allowing it to hinder clean energy transitions, we need to seize the opportunity to help accelerate them.”

As Gregor Macdonald, one of the top energy experts in the world says, in our current zero-interest rate environment, it is almost inevitable that the private market – “capitalists” – will pour money into clean energy.

“Renewable energy was already a lay-up because its sticker price is so attractive, but when you start discounting future cash flows through a much lower interest rate environment then you’re looking at very favourable conditions indeed,” he said.

Remember, low interest rates are great for renewables investment as they make financing easier to get for companies looking to build infrastructure up front.

In the long term, they make renewable assets – solar and wind farms – incredibly attractive (especially to pension funds) as these assets offer long-term, predictable cash flow with great operating margins (the marginal cost of energy is zero so operating and maintenance costs (opex) in minimal).

Certainly, renewable sources such as wind and solar will offer a far safer investment in a world of unstable oil prices.

Unlike oil and gas, nearly all of the costs of wind and solar energy are in the infrastructure required to capture it – capital costs that have been plummeting over the past half-decade or so.

Oil price crash no impediment

Although oil prices have seen a coronavirus-induced crash, I don’t think we’ll see a flood of capital flowing into the oil sector.

The generous dividends coveted by oil investors are already [starting to disappear](#), while we might find that low oil prices are the perfect opportunity for governments to remove subsidies for fossil fuel and/or raise taxes on carbon dioxide emissions, since consumers would be less likely to feel the impact.

Certainly, the popular narrative surrounding lower oil prices and renewables investment – that low prices incentivise greater use of oil and squeeze the budgets of oil companies, putting clean-energy projects in doubt – needs to be challenged.

While lower oil prices certainly used to correlate with struggles for the renewables and clean tech, that correlation has been broken for upwards of a year now.

In 2012 and 2016, we saw low fossil fuel prices correspond with falls in green stocks. But since the beginning of 2019, as oil prices have fallen slowly and then all at once, renewables have performed brilliantly.

Why might this be?

Well, firstly, this time around, the economics have certainly changed. Solar, wind, and storage are all dramatically cheaper than they have ever been, and the trend continues. Efficiency is improved, economies of scale are kicking in, demand is higher and supply chains are well established.

Although fossil fuel giants may have to lower their capital expenditure on green investments, many clean tech and renewable energy business are already cash-flow positive, and have the money to invest themselves.

Therefore, the renewable sector is vastly more competitive and competent now than it was before.

Secondly, it's worth remembering that, for the most part, renewable energy doesn't compete directly with oil, but with coal and gas.

Oil competes with renewably produced electricity primarily in transportation, where electric vehicles (EVs) are taking market share from petrol vehicles.

The uptake of EVs is the real challenge of renewables to the oil industry. It creates increasing demand for electricity, not for oil. That increasing demand is only being met by the rapid growth of renewables.

Given that every doubling of renewable capacity reduces the price of wind or solar by 10-20% depending on the mode of production, then the halving of oil prices in 2020 so far will be dwarfed by the decimation of wind, solar and EV lifetime prices. They've already fallen by 50% (wind) and 85% (solar) in the last decade alone – and show no sign of slowing down.

And when comparing costs of renewable generation to coal- and gas-fired power plants, over half the world can already be said to have cheaper renewables on offer than their dirtier predecessors.

While cheap oil has often depressed sales of electric cars, nowadays, a large share of EV sales is being driven by regulations in places like China, Europe and California. These measures will continue to accelerate the electrification of transport regardless of oil prices.

Battery costs are plunging, too, meaning EVs are steadily becoming more competitive with conventional cars, even if you ignore fuel costs. As long as battery prices continue falling, depressing the high upfront cost of purchasing an EV, electric vehicle adoption will keep going up.

With electrification here to stay, the old rules just don't apply any more.

Indeed, the chaos in the oil market could end up being good news for renewable energy.

As Wood Mackenzie's Valentina Kretzschmar explains, one reason for oil and gas companies not to invest in renewable energy has been that the returns in solar and wind projects have offered much lower rates of return than upstream oil and gas. At today's crude prices, be clear, that is no longer true.

“Capital allocation is no longer a one-way street for Big Oil,” she writes. “Renewables projects suddenly look as attractive as upstream projects at \$35 a barrel.”

As per a 16 March article in the Financial Times:

The current volatility in oil markets does not change the fundamental point: from now on, oil will increasingly be competing with the deflationary dynamics of renewable energy...

In short, dramatic as the events of the past week have been, in this age of energy disruption they might ultimately prove a passing zephyr across the sand dunes compared with the prolonged dust storm to come as the end of the petroleum age draws into view.

The long-term trajectory is unchanged

Of course, an economic slowdown could dent the demand for clean energy or reduce the amount of finance available, meaning the renewables and EV revolution might slow down, but it won't be for long.

The longer-term trajectory remains unchanged.

Already Mark Carney, the former Bank of England chief who is now advising prime minister Boris Johnson on climate finance, has said Britain's commitment to cutting carbon emissions remains undimmed amid the coronavirus pandemic.

"We don't see there would be any modification of those objectives," Carney said before the House of Lords' European Union Financial Affairs Sub-Committee on 18 March.

The shift to cleaner energy and electrification is a megatrend, after all.

(The thing with megatrends is that they don't come around often. In fact, there's only be one – the birth of the online world – in my lifetime.)

Remember, the last time we ramped up our energy capacity and infrastructure was for oil, almost 100 years ago.

To be watching and participating in the current megatrend is a massive long-term opportunity, one that cannot be undone by a halving of the oil price, coronavirus or even a full-blown recession.

The climate imperative is too strong; the economics of renewables too powerful. Change is coming and investors who keep their heads could pick up some life-defining bargains if this market capitulation continues.

Indeed, right now, this megatrend is seeing a fire-sale as it's been hit along with every other sector out there. Some of the winners of the next decade, the next cycle, are being offered at huge discounts.

But while all stocks get knocked during times like these, investors need to focus on what is likely to lead the rebound.

My view is that renewables will soar out of the ashes of the oil crash.

Since coronavirus hit British shores, we've seen a [raft of good news emanating from the green energy sector](#), which have been largely buried under the deluge of panic-inducing headlines.

I suspect one day we will look back on these weeks and months as a symbolic turning point in the global transition away from fossil fuels and towards a clean, sustainable future.

For me, renewable energy and the new technologies driving the energy transition are a one-way bet. If you're not staking at least a small amount of your capital into this market, you are turning down perhaps the single biggest investment opportunity of the last 30 years.

Green may be just one slot on the roulette wheel but, in the long run, it's the best choice for investors.

On that note, I would now like to introduce you two must-own stocks that will be on the frontlines of this green growth.

The fuel cell truck manufacturer that is set to out-Tesla Tesla

I'm recommending you invest in a company called VectoIQ Acquisition Corp. (VTIQ), a publicly traded special purpose acquisition company that's backed by investors including Fidelity and ValueAct.

But I'm not actually interested in VectoIQ, per se.

That's because, up until early March, VectoIQ was a company that didn't really do anything. It was actually formed for the sole purpose of effecting a merger with another company that does do something.

A company such as Nikola Corporation.

In March, you see, Nikola Corp said it plans to list on the Nasdaq by merging with VectoIQ.

Nikola is developing a family of battery electric vehicles (BEV) and hydrogen fuel cell electric vehicles (FCEV). It's also developing hydrogen station infrastructure to support its FCEV vehicles.

In particular, Nikola wants to make electric "class 8 semi-trucks" that might compete with the electric semi-truck that Tesla announced in 2017. Nikola and not VectoIQ is the company we're really interested in here.

Nikola is the Tesla of FCEVs

We've written about Nikola before in *Exponential Energy Fortunes*. Indeed, we mentioned Nikola when we recommended Norwegian hydrogen company Nel. The two companies are partners.

In fact, in the [recommendation](#), we described Nikola as "the Tesla of FCEVs"...

One immediate catalyst that makes this such an exciting time for investors right now is Nel's partnership with a company called Nikola Motor, which is trying to be the Tesla of hydrogen fuel cell vehicles.

Nel is already an investor in Nikola, having ploughed \$5 million into its C-funding round in late 2018. Nikola's valuation has since tripled, so Nel is already doing well on its investment in the company, but the even better news is what Nel is working on with Nikola.

Hydrogen applications in transport are varied, but Nikola focuses on heavy-duty trucks predominantly. It has just ran its first delivery for Ab InBev (which has ordered 800 Nikola trucks in total), and has \$14 billion in pre-orders for its next-gen semi-truck, the "Tre". That's the highest ever pre-order book for a truck in American history.

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This just goes to show how fast the transition to hydrogen is happening in certain parts of the transport sector, and Nel is very much a part of that.

You see, Nikola has committed to building 700 hydrogen fuelling stations across the US by 2028, and has selected Nel as its primary supplier for the electrolyser units with associated refuelling and storage units for this extraordinary, multi-billion dollar project.

It's the largest electrolyser and fuelling contract ever awarded, and here we can really see the value of Nel's diversified product offering.

Providing the full range of products, from production to distribution and storage, allowed Nikola to select Nel as its one partner for this project, rather than splitting it between two or three companies. This is really where you can see Nel's competitive advantage paying off.

Nikola is doing this as it also plans to roll out its hydrogen trucks over the same time frame, and it can't do so without a refuelling network to match.

A bright future for Nikola means a bright future for Nel, as its key supplier of hydrogen technology, and as an investor too.

After the merger with VectoIQ, the combined company will be named Nikola Corp and be valued at more than \$3.3 billion, Nikola said.

The transaction will be funded by VectoIQ cash in trust and a \$525 million private placement of common stock at \$10 per share, led by institutional investors including Fidelity Management & Research Company and ValueAct Spring Fund.

The transaction, which is expected to close in the second quarter of 2020, has been approved by the boards of both companies.

Upon completion of the merger, VTIQ stockholders will automatically become stockholders of Nikola Motor Company (NKLA). The firm is expected to remain Nasdaq-listed.

This deal will accelerate Nikola's production of zero-emissions vehicles

To my mind, this merger will surely speed up Nikola's production of zero-emissions commercial vehicles. The proceeds of the transaction will accelerate production, allow Nikola to finance the building of its state-of-the-art manufacturing facility in Coolidge, Arizona, as well as its hydrogen station infrastructure rollout.

The company expects to generate revenue by 2021 with the rollout of its battery electric heavy-duty truck, followed by its fuel cell electric class 8 sales starting in 2023 and the initial build-out of hydrogen fuelling stations to serve Nikola customers' fleets, such as Anheuser-Busch, Nikola said.

The companies say they have "more than 14,000 pre-orders" on the books already, "representing more than \$10 billion in potential revenue and two-and-a-half years of production" work.

“We are on a roll. You couldn’t ask for better news for the energy and tech industry,” Trevor Milton, founder and CEO of Nikola, said in a release.

“The world is transitioning to zero-emissions platforms and Nikola is the leader for heavy-duty vehicles. We believe we have a differentiated business model built on economics, not government subsidies. We now need to double down and speed up the timelines and get to market.”

The boards of directors of both VectoIQ and Nikola have unanimously approved the proposed transaction. Completion of the proposed transaction is subject to approval of VectoIQ and Nikola stockholders and other customary closing conditions, including a registration statement being declared effective by the US Securities and Exchange Commission, and is expected to be completed in the second quarter of 2020.

Once approved, Milton will serve as executive chairman of the combined company, continuing to lead the vision and forward-looking strategy.

Risks

To be perfectly honest, one of biggest risks here is hidden from view.

The nature of the merger has been chosen because, for whatever reason, Nikola couldn’t pursue a listing by normal means. Stockmarkets impose some strict regulations on would-be public companies, and Nikola has likely fallen short somewhere.

For the Nasdaq, where VTIQ is listed, these regulations are:

- Shareholders’ equity of at least \$2,000,000
- At least 100,000 shares of public float
- A minimum of 300+ shareholders
- Total assets of \$4,000,000
- At least two market makers
- \$3 minimum bid price of the company stock
- Public float market value of \$1,000,000.

We don’t know where, but all we know is that this is an unusual route to market – though it is growing in popularity. It’s likely that listing shares via VectoIQ will generate funds faster than through a conventional IPO. What’s more, doing it via a company that’s already trading on Nasdaq is also likely to be cheaper.

When the merger happens in a couple of months’ time, the ticker will change and a private placement for \$525 million will be issued, but essentially, as of the announcement on Tuesday 3 March, the stock is already trading as Nikola Motor.

But it is unknown how many shares of Nikola will be included in the merger, and how many current owners will keep theirs private. So although the stated enterprise value of the merger gives Nikola a \$3.3 billion valuation, we don’t know what percentage of the company will be issued as shares.

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This is probably the biggest risk, as we simply don't know what percentage of the company will be issued as shares.

But because this is a rushed move, there hasn't been a long build-up with a big prospectus, lots of material on the workings and numbers of the company, and public sector scrutiny.

Instead, much of what we are forced to go off is based on the company's claims about itself. For example, it claims that it has the largest ever pre-order pipeline of any truck in US history at USD\$12 billion for the Nikola Tre hydrogen truck, but we don't have evidence of the contracts or details on how Nikola will meet its obligations to fulfil those contracts.

Milton, its founder, is a slightly eccentric, Mormon entrepreneur whose Twitter account reveals both his similarities to, and his dislike for, Elon Musk.

He is a fan of calling out his future competitor for his attitude to hydrogen vehicles amongst other things, but shares his love for big promises and aggressive hype of his own company.

For example, last year he announced that Nikola had made an incredible breakthrough in battery technology. Apparently, the company has developed a battery with twice the energy density, only 40% of the weight and half the cost of a Tesla battery. Many scientists and experts are sceptical though, and we are yet to see any examples of the product itself.

As a result, it's hard to be sure about claims such as those mentioned above.

So the risk mainly is a lack of visibility into the company's workings, financials, and contracts. It's perhaps a bit of a leap of faith, but if it's even close to the truth then it will be one easily worth taking.

That's why I'm recommending you BUY VectoIQ Acquisition Corp. (VTIQ) soon to be Nikola Motor Company (NKLA) stock, the Tesla of FCEVs.

Action to take: buy VectoIQ Acquisition Corp.

Ticker: VTIQ US

Price as of 28.04.20: \$14.35

Market cap: \$425.3 million

52 week high/low: \$16.25/ \$9.92

Buy-up-to price: \$16



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A critical hydrogen market supplier primed for “double growth”

“The technology of the future.”

That’s how Prime Minister Boris Johnson once described hydrogen. It’s easy to see why.

Hydrogen is a superfuel. It is the universe’s most abundant element. And it can be used to power almost anything you like. It can replace natural gas to heat the home. (In fact, the gas grid was originally built to use hydrogen.)

Hydrogen fuel cells can power cars, trucks and buses. (As the great-grandson of Henry Ford and executive chairman of Ford Motor Company said: “I believe (hydrogen) fuel cells will finally end the 100-year reign of the internal combustion engine.”) They can even fuel planes and rocket ships.

Wilhelm Ostwald, a Nobel Prize winner, said that the hydrogen fuel cell “is a larger invention for the civilisation than the steam machine.”

And remember: so-called green hydrogen is 100% emissions free.

So why isn’t hydrogen already the lifeblood of the world economy?

That’s easy.

For decades, enormous amounts of cheap oil has outcompeted hydrogen.

But as you know... the world is turning against oil.

Greta Thunberg and the Extinction Rebellion is just one part of this. Yes, the world is moving away from fossil fuels to help combat climate change.

But global dependence on oil was never a good thing.

Oil is scarce. Some countries have it, others don’t. It’s volatile. It’s dirty.

Hydrogen is none of those things. It is clean, abundant and versatile.

That’s why the world is turning towards hydrogen in a BIG way.

Indeed, right now, before our very eyes “the new oil” – hydrogen – is being deployed at breakneck speed.

Last year, Angela Merkel pinpointed it as playing a central role in “rebuilding” Germany’s energy strategy.

Following that, the biggest pilot project in history went live in Austria.

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Then, Europe's biggest gas infrastructure firm announced it was ploughing one fifth of its revenues into hydrogen.

And since then, we've seen the trend accelerate.

The good news keeps on coming

First off, a Fortune 100 company just placed what is to my knowledge the biggest commercial order in the history of the industry, worth \$172 million.

Second, the world's richest oil company Saudi Aramco took the major step of joining the "Hydrogen Council". That isn't surprising – as a former Saudi Arabian oil minister put it,

"The day they use hydrogen for transportation, this is the day that oil disappears."

Third, European Commission's upcoming vice president for the Green Deal said hydrogen has a "pivotal" role to play in meeting Europe's climate goals.

And perhaps most urgent of all for British investors, on 2 January 2020 hydrogen was deployed for the very first time in Britain, as part of a major government-backed project in Staffordshire.

Mark my words: the hydrogen revolution will hand early investors extraordinary profits. Just consider this... In the second half of last year, a new index of hydrogen stocks made investors 5x more than gold... 6x more money than oil... and 12x more money than the FTSE 100.

But we're just at the beginning.

In fact, I think if you select the right hydrogen stocks, you can expect to make at least 10x your money as economies around the world move away from fossil fuels and towards clean, green hydrogen.

Expert forecasts predict hydrogen is set to grow globally into a new \$2.5 trillion market as the so-called "hydrogen economy" develops.

The three hydrogen-focused companies we have recommended Although hydrogen is still a nascent industry, there are already numerous firms so far are involved across a wide range of applications, from electrolyzers that will produce abundant emissions-free hydrogen from surplus renewable electricity to fuel cells that use that same green hydrogen to power our cars and trucks.

The potential markets the firms are involved in – from industry and power to shipping and transport – are all huge and disruptive in their own right, together forming perhaps the single biggest piece of the great decarbonisation puzzle.

After all, hydrogen produced via green energy has huge potential to help phase out fossil fuels, whilst minimising reliance on mining metals such as cobalt and lithium.

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Green hydrogen not only bypasses grids, it also allows for the storage of intermittent renewable supply – supply that can fuel planes, trains and automobiles and replace fossil fuels in steel and ammonia.

Planned projects our recommendations are involved in include powering all manner of transport applications on hydrogen, using it as a replacement for natural gas in both our gas networks, domestic boilers and power plants, and as a way of storing excess electricity produced by renewables such as wind and solar on particularly sunny and windy days.

But there's a gaping hole in our hydrogen recommendations, a part of the equation that all the other components wholly rely upon.

Indeed, this application is a critical enabler of the hydrogen economy, a vital part of the value chain in which hydrogen plays a decisive role in the development of a fossil-free future.

The application involves the storage and distribution of the hydrogen itself.

Storage is the critical part of the hydrogen value chain

After all, hydrogen storage is an important issue to solve in order to bring the various elements of the hydrogen economy together.

So this is something I want to put right today..

The firm I am recommending is a manufacturer of hydrogen storage tanks.

But, having been in business for nearly 20 years, it's not just any old manufacturer.

It is now the world's largest manufacturer of hydrogen tanks, a market that itself is expected to rise from less than €100 million today to €8 billion in just ten years – a factor 80 increase.

Much of the company's work has been done with research and development projects throughout the world. In the past five years, it has been really ramping up its efforts in the hydrogen field.

Before I introduce the company, let me explain why exactly hydrogen storage is so important.

Hydrogen storage – a vital part of the value chain

Early in 2020, Deloitte released a hydrogen report. It was called “Fuelling the Future of Mobility: Hydrogen and fuel cell solutions for transportation”.

The report provides a thorough and detailed look at where hydrogen fuel cells are in disrupting transportation and where they might get to. It uses a model of “total cost of ownership” (TCO) which includes purchase price, operating costs and fuel costs in its predictions.

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It included some stark predictions, such as that FCEVs would become TCO-competitive with internal combustion engine vehicles (ICEVs) by 2026, and with battery electric vehicles by 2027. That's globally.

In Europe, the disruption will happen even faster, with FCEVs breaking even on a TCO basis with BEVs by 2023 and ICEVs by 2024.

This will be achieved through cost improvements in components, fuel and infrastructure.

In the US, for example, purchase cost is expected to fall by around 30% by 2024, while operation costs should fall by over 50% in that same timeframe. These are seriously rapid cost declines.

The lifecycle of a fuel cell in a vehicle is also expected to grow from 25,000 hours to 30,000 hours, both lengthening their life and lowering part replacement costs.

But one key factor holding this transition back at the moment, according to the report, is the cost of storage infrastructure, both for refuelling stations and in the vehicles themselves – the fuel tanks.

Together with fuel costs, these made up over 50% of operational costs in 2019.

One of the reasons for this is the low density of hydrogen gas, which makes it difficult to store and transport cheaply or efficiently.

So one key development will need to be technological advancements in storage capabilities.

After all, successful commercialisation of FCEVs, for example, will depend upon the creation of a hydrogen delivery infrastructure that provides the same level of safety, ease and functionality as the existing gasoline and diesel delivery infrastructure.

This is where our latest *Exponential Energy Fortunes* recommendation – a company by the name of Hexagon Composites – comes in.

Hexagon has developed large composite tanks and optimised hauling systems for the efficient and cost-effective storage and transportation of energy gasses, including compressed hydrogen gas.

Hexagon Composites (HEX.OL) – delivering infrastructure for the hydrogen economy

Hexagon is another Norwegian company, just like another of our hydrogen stocks, Nel. Hexagon has technological leadership globally in the storage space, and is also busily acquiring subsidiaries to broaden its exposure to all aspects of the burgeoning hydrogen industry.

Broadly speaking, the firm is a global leader in the supply of clean energy technology, specifically for gas storage, distribution, and fuel systems. It's collaborating with leading gas distributors, vehicle manufacturers, and system and component suppliers to deliver projects all along the hydrogen industry's value chain.

But its original speciality is in storage and transmission – specifically, in what it calls type-4 cylinders and systems. Type 4 is just a designation – each “type” of gas storage cylinder has different characteristics and benefits. Type 4 cylinders are metal-free, plastic bodies wrapped in a strong fibre material.

Their key advantages include weight – Hexagon’s type 4 cylinders are 70% lighter than their steel-equivalents. They are also corrosion and fatigue resistant relative to metal containers, and have improved economics for transport because of their lighter weight, as well as better operational efficiency through lower maintenance and lower fuel consumption.

These containers are not hydrogen-specific. In fact, Hexagon is active in the storage and distribution of compressed natural gas (CNG) storage, a fuel that can also be used in place of gasoline, diesel fuel and liquefied petroleum gas (LPG). CNG combustion produces fewer undesirable gases than these aforementioned fuels.

So while hydrogen is certainly the next big thing, Hexagon is already generating revenues and profits, with healthy margins to show that the business model is profitable. I’ll get to that in more detail later on.

A solid defensive moat

Hexagon’s experience goes longer than a decade, which is important as handling flammable gases comes with a fierce regulatory regime, naturally. This gives Hexagon something of a defensive moat – it won’t be easy for other companies to just step in and decide to encroach on their business once hydrogen takes off.

An established relationship with the regulator, well-rehearsed safety procedures and technical expertise are all vital in this line of work. So as hydrogen demand rises, Hexagon’s business will be better protected than most.

Hexagon mass-produces these type 4 cylinders and is the global market leader in gas storage cylinders. This covers all gases, including non-green CNG amongst others.

As it’s not totally focused on hydrogen at the moment, Hexagon is a slightly broader play on the decarbonisation theme. But with targets being set all over the world (EU – 40% cut in CO2 emissions before 2030), the market for low-carbon fuels will have a contribution to make, just as zero-carbon solutions will. And as the hydrogen momentum picks up, both the company and I expect it to move more and more in the latter direction.

Hexagon has the luxury of existing revenues streams from other gases, so it’s not reliant on hydrogen taking off this month or this year. Rather, as the economics become more favourable, it can increase its exposure.

Hydrogen is Hexagon’s future

Saying all this, Hexagon is shifting strongly towards hydrogen. Over 50% of its business now comes from the hydrogen economy. For example, the company has been busily acquiring companies to broaden its offering to the coming wave of hydrogen applications.

Indeed, Hexagon is investing NOK 660 million in the production of hydrogen storage tanks, a venture the firm describes as a potential “game changer”.

But its hydrogen strategy is multi-faceted. It’s not just a global leader and specialist in the crucial field of safe storage and transmission. It is now a direct play on the rapidly expanding FCEV market.

Fuel cells emerged late last year as one of the most exciting investment stories right now, but the market hasn’t yet picked up on Hexagon’s potential.

We’ve seen that investors are greedily chasing hydrogen fuel cell stock prices higher (including our recommendation AFC Energy). But because Hexagon is a storage specialist, first and foremost, we are still ahead of the rush.

To cement the idea that its hydrogen business is really starting to pick up steam, Hexagon announced in 2018 that it had received an order worth NOK 1.8 billion (circa £150 million) for two hydrogen storage tanks for FCEVs. This was the largest hydrogen tank order ever for the automotive industry.

So many things were confirmed by this order, including that:

- FCEVs are now receiving huge investment
- Storage is viewed as critical
- Hexagon is seen as a trusted partner by the fuel cell industry
- The money involved is becoming really serious
- We’re seeing a rapid acceleration in the hydrogen economy, all along the industry value chain.

All things considered, the order was a really positive sign for the company and the industry as a whole.

In another example, 2019 saw the major German carmaker Audi pick Hexagon to supply high-pressure tanks for a multi-year hydrogen tank development and production project.

Audi has already stated it will increase investment in bringing hydrogen fuel cell technology to market – which can only be good news for Hexagon.

Daimler is a customer, too. In fact, Hexagon now has four contracts to supply hydrogen storage tanks to original equipment manufacturers (OEMs) for FCEVs. Many of these tanks will be manufactured at Hexagon’s plants in Ohio and Germany, with production beginning in 2020 and the contract lasting five years thereafter.

It’s already signing deals and the party hasn’t even started

Remember, this is just for cars, and the real party hasn’t even started yet.

The firm is also moving into the maritime industry, providing tanks for the first hydrogen vessel in the US.

Not just that, Hexagon is also part of a hydrogen-focused joint venture with Nel and PowerCell called Hyon which utilises each partner's respective technologies and competencies to develop hydrogen projects. As part of this it has at least four exciting hydrogen fuel cell maritime projects on the go.

More broadly, Hexagon has delivered on hydrogen contracts in the distribution, refuelling station, rail, marine, passenger vehicle, and heavy-duty vehicle sectors. This shows what a truly remarkable market it can access, which makes its potential growth enormous in the coming years.

The company itself offers its most conservative estimate for its own market opportunity as NOK 28 billion, and that's just from the passenger car market. Adding in the other hydrogen segments takes it to NOK 81 billion. And I repeat – this is its most conservative estimate, using an incredibly modest 1.9% annual adoption growth rate for hydrogen vehicles between now and 2028.

That would take FCEVs to a 1% share in the global market from below 0.1% today. Given the targets provided by different countries and companies over the last few years, I think it could be much higher than that.

Remember, supplying hydrogen tanks means huge scope for Hexagon to transport green hydrogen from wind and solar plants once the electrolysis process is centralised.

But it's not just its core business' strong performance that is turning Hexagon into a hydrogen superstar...

Entering the hydrogen vehicle market directly

You see, as well as playing a key role in supplying hydrogen to consumers, it is also entering into the hydrogen vehicle market directly.

Last year it completed the acquisition of a company called Agility, which has an offering of fuel solutions for medium- and heavy-duty vehicles. It was a buy-out acquisition, in which Hexagon bought the 50% that it didn't already own, and consolidated it fully into the company. Agility's hydro revenues now account for almost half of the total group revenues.

What Agility adds to Hexagon's current specialism is a direct application to the vehicle and transportation industry.

Agility's specialism is in integrating energy storage, delivery and conversion systems into commercial vehicles, making it the perfect addition to Hexagon's storage expertise.

FCEVs are set for explosive growth, whoever you ask. The acquisition, for me, shows that the company understands where some of the best growth is in the hydrogen industry

(FCEVs), and it also shows that the company is commercially minded and well prepared for the coming S-curved growth in hydrogen cars, buses and trucks.

The company itself had a strong 2018, with deals made with hydrogen bus companies in Italy, Portugal, India and more.

The consolidation of Agility's accounts with Hexagon's has given the revenue and profit figures an enormous boost. We will see a smoothening out over the next year and beyond.

Setting itself up for the future

Slightly less of an immediate impact will be felt from last year's acquisition of a company called Digital Wave to Hexagon's portfolio.

Digital Wave is a smaller, more niche technology company whose capabilities are in the unique testing and requalification of high pressure gas cylinders.

That makes it more of a supporting act to Hexagon's existing storage and transmission business, rather than a distinct addition in its own right.

Digital Wave's technology will allow for cheaper and better maintenance of Hexagon's storage and transmission products by allowing for "smart censoring" – ie, self-maintenance by the products themselves.

So in Hexagon we've got a company that's a specialist and a global leader in a growing field with high barriers to entry, relatively low competition, and an extraordinarily strong and urgent tailwind. With a proven business model and smart, timely acquisitions, I'm very excited about the future of Hexagon.

Now, as ever, let's see how the company is looking from a financial perspective, before making sure we're clear on some of the risks involved as well.

Financials

Hexagon is in good shape financially.

It's not the perfect picture, but for a company in such a young and developing sector of the energy market, it's doing very well indeed.

That's because its products are already utilised by natural and compressed gas markets, so it has existing revenue streams from those markets, as well as growing sales from the hydrogen industry.

Revenue fell a few years ago, from NOK 1,651 million to NOK 1,221 million between 2014 and 2016, but it has since risen back up to NOK 1,487 million in 2018 and a huge NOK 3,416.2 million in 2019.

Net profit fluctuated rather erratically in the same period, having four excellent years in 2014, 2016, and 2018 and 2019 (NOK 256 million, NOK 299 million, and NOK 142 million

and NOK 108 million respectively), with profit under 100 million for the years between 2015 and 2017.

So far in 20, the growth trends into 2018 have continued.

Revenue in Q3 2019 grew 178% quarter on quarter, to NOK 770 million (from NOK 276 million). The nine-month revenue for the first three quarters of the year also grew rapidly – 133%– from NOK 1,059 million to NOK 2,474 million. The financials in general paint quite an erratic picture, so there isn't so much value extrapolating these Q3 figures out into the next few years, especially as they will have been distorted by the acquisitions mentioned above.

The financials, then, are more helpful as an indication of where the money is being made. A few years ago, we would've seen a company more focused on the natural and compressed gas markets. Whereas now, we are seeing a much higher proportion of revenues coming from its hydrogen solutions, and the business' organic growth being driven by that side of things.

It's also reasonably well capitalised, having raised NOK 493 million last year via a private placement of new shares. It's getting ready.

Risks

As always, I want to make you aware of some of the risks involved in this investment. Today, they fall into two very specific categories: systematic risks and specific ones.

Systematic risks are what they call market risks. The idea is that the risks are to the market, but affect the company.

In Hexagon's case, the market risks are two-fold. Firstly, that the rollout of the hydrogen economy, which is currently accelerating at an incredible pace, stumbles slightly in real terms – ie, battery electric vehicles get a technological boost somehow, making FCEVs less competitive. Or an incident such as an explosion at a hydrogen facility freaks out the market and deal-making slows.

The other market risk lies in the stockmarket. You will have noticed (via our other very profitable hydrogen plays) that investors are loving the hydrogen sector right now. There are companies going vertical.

One reason I like Hexagon so much is that it hasn't done that yet. I feel that investors have underrated its potential relative to its peers.

However, in such market conditions, volatility and fragility do increase. Prices are swinging more wildly than normal, even for the renewables sector as a whole.

A loss of the widespread bullish sentiment on the sector as a whole could hurt Hexagon's share price, regardless of the positive trajectory of the company.

If that did occur, it would be a short-term loss as I am enormously confident that with a five-year or ten-year time horizon, the only way is up for Hexagon and the hydrogen sector as a whole.

So those are the systemic risks – market risks out of the company’s control. There are also some specific risks to Hexagon that are directly related to its business model and operations.

The first one relates to its product – type 4 gas container tanks. These are currently an excellent solution to the gas industry’s storage and distribution needs, but they are not the only one.

The cheapest form of long-distance gas transportation will be to build pipelines. Currently, as the hydrogen economy is only in its very early stages, there is little appetite or money from government to build such pipelines, but once hydrogen has become

the global gas of choice as we expect it to, infrastructure spending should catch up and pipelines will be built – which will be competition for Hexagon.

Pipelines can’t do everything, mind, and won’t replace what Hexagon offers by any stretch, but their addition to the hydrogen economy will be a limiting factor on Hexagon’s potential market.

Also, and I alluded to this above, safety is a key concern with hydrogen.

As hydrogen gains traction globally, the risk increases that safety isn’t adequately handled in places with underdeveloped infrastructure or policies.

So as ever, this investment is not without risk. And it certainly is a volatile time in the hydrogen stockmarket right now, so this is a risky pick, but in the short-, medium- and long-term I remain confident that Hexagon will be our next hydrogen winner in the *Exponential Energy Fortunes* portfolio as Hexagon becomes a real superpower in the industry.

A hydrogen play primed for “double growth”

Remember, Hexagon is solving one of the hardest problems in hydrogen: storage.

It supplies critical technology for not one but two fast growing sectors of the hydrogen market.

First, it plays a key role in supplying and storing hydrogen to, and at, commercial sites. Think of it like an oil pipeline business – but for hydrogen. It gets the fuel to the places that need it, quickly and efficiently.

That alone is going to be a key market in the future.

But this business has also signed a series of deals to deploy hydrogen-powered vehicles on the road.

It's already teamed up with Audi and Daimler amongst others.

And I think we can expect more big deals to be signed in the future.

The bottom line: this unknown firm is quietly becoming a key player in the hydrogen markets. I doubt it'll stay under the radar for long.

I recommend you BUY Hexagon Composites ASA

Action to take: buy Hexagon Composites ASA

Ticker: HEX.OL

Price as of 28.04.20: NOK 27.92

Market cap: NOK 5.13 billion

52-week high/low: NOK 44.95/ 19.48

Buy up to: NOK 31

