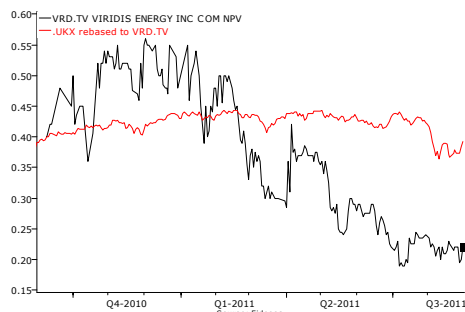


**Viridis Energy Inc.**  
Equity Capital Raising

**22c.**

5 September 2011



**12m High:** 55c

**12m Low:** 19c

**Market Cap:** CAN\$9m

**Shares in Issue:** 41.28m ordinary shares  
17.63m convertible units  
~26.40m out-of-the-money warrants  
Total fully diluted capital 85.31m shares

**NAV/Share:** 17c/share inc intangibles.

3c/share excluding intangibles

**Gearing:** After capital raising, 12% categorising subordinated convertible as equity

**Interest Cover:** n.a.

**EPIC Code:** TSX: VRD.V / VRD.TV

**Sector:** Forest Products

**Market:** Toronto TSX Venture Exchange (move to Main Board planned). Also OTC QX. A European market quote is likely shortly.

**Broker:** To be Announced

**IR Agent:** Grannus Financial Advisors, 001 212 681 4108

**PR:** -

**Website:** www.viridisenergy.ca

**Description:** Manufacturer and distributor of carbon neutral wood pellets for domestic heating and commercial power generation.

**Analysts:** Roger Hardman/Yingheng Chen

**Tel:** +44 (0)207 929 3399

Canadian wood pellet specialist Viridis Energy has reported Q2 results that ought to be the nadir of its fortunes. Since the period end it has closed a \$5.3 equity capital raising in a mixture of shares and subordinated convertible unsecured loan stock bringing the total raised in this round to \$7m. The financing transforms the prospects here, and lays the way open for the company to treble capacity in order to fulfil orders already in hand from Europe (via a Canadian wholesaler) and Asia.

This could enable Viridis to produce its first profit in early 2012.

Key items for investors are:

- The market capitalisation of the company at present is \$9m, rising to \$18m on full conversion of the Convertible Unsecured Loan Stock and all warrants and options.
- The warrants issued to sweeten the financing are well out of the money.
- The money raised reduces gearing to 12%, categorising the CULS as equity.
- The news follows closely on the announcement a of 5 year wood pellet contract from Abellon CleanEnergy Ltd of Ahmedabad India as part of a broader worldwide tie-in with Abellon that includes Abellon subscribing to 10% of the Viridis equity.
- The acquisition of Confluence Energy in Colorado will double group wood pellet capacity. A new plant at the Monte Lake facility will be completed within twelve months. Improvements at the Okanagan site will also be undertaken. By end 2012 Viridis Energy should have increased its capacity from 60,000 tpa to 225,000 tonnes a year, suggesting annualised revenue of \$23m compared to last year's \$7.8m.
- Additional revenue from the Palm Kernel Shell supply contract, is likely to add over \$10m a year to the top line, at lower margins. This is totally separate from the pellet producing capacity. The first shipment is currently at port waiting to be picked up. This is about three weeks behind schedule, which we think perfectly acceptable for a new operation.

Y/E	Sale	Declared Pre-tax Profit	Adjusted Pre-tax Profit	Undiluted EPS*	P/E	Divi	Yield
Dec	CAN\$ m	CAN\$m	CAN\$m	c.	X	c.	%
<b>2009A</b>	0					-	-
<b>2010E</b>	7.81	-0.1	-2.9	-14.1	-	-	-
<b>2011E</b>	17.9	-2.9	-3.1	-8.8	-	-	-
<b>2012E</b>	46.1	0.7	0.7	1.4	12.2	-	-

\* Assumes conversion of CULS

## Q2 Results

Q2 results show a modest improvement over those of Q1.

\$m	Q1/11A	Q2/11A
Group Sales Revenue	2.67	2.87
Group Gross Profit	0.02	0.37
Gross Margin %	0.8%	12.8%
Expenses	-1.09	-1.18
Operating Profit/Loss	-1.06	-0.81
Operating Margin %	-39.7%	-28.3%
Finance Costs	-0.09	-0.16
Loss on Asset Disposal	0.00	-0.03
Pre-tax Profit/Loss	-1.15	-1.00
Tax Charge %	0%	0%
Tax Charge \$m	0.00	0.00
For Ordinary Holders	-1.15	-1.00
No. Shares, Undiluted, m.	30.3	30.3
No. Shares, Diluted, m.	44.2	44.2
EPS Undiluted c/share	-3.79	-3.29
EPS Fully Diluted c/share	-2.46	-2.12

Q2 sales up on Q1

GM still low, but improved

Key points are:

- Sales increased by 7% over Q1, in spite of Q2 being seasonally the weakest of the four quarters of the financial year.
- Gross margin improved, although it is still inadequate. New contracts are now being negotiated with better margins, as industry capacity is becoming tighter.
- The loss was slightly reduced.

The Q2 figures incorporate an important change of accounting policy, and the Q1 comparatives have been prepared on the same basis. Previously, Viridis Energy included the transport costs of raw material from supplier's sawmill to its own factory gate in cost of sales, and those transport costs from its factory gate to the customer's place of business in General and Administrative costs. The new policy is for all categories of transport costs to be included in Cost of Sales, and therefore to come out of gross margin. Furthermore, some of the transport costs are being capitalised in as cost of inventory.

It is interesting to note that so far in 2011 however, cash used in operations is running at half the rate of the declared comprehensive loss. For the first two quarters combined, the comprehensive loss has been \$2.2m. Yet net cash used in operations has been only \$1.1m.

Cash burn less than losses declared

The largest single operating cost is raw material. Net of freight, this soaked up 47% of sales revenue in Q2, compared to 43% in Q1. This is obviously a matter of concern, and we are glad to note that Viridis has renegotiated some supply contracts and will be operating with a considerably lower cost of raw material from Q3 onwards. Increasingly, Viridis Energy is operating its own road haulage rather than using contractors. Now that it has predictable volumes, this is a major cost saving.

In other areas, also, costs are being brought down. The payroll has been reduced, as have director and management fees. The two combined have been cut by 13%, and we expect a further reduction in Q3. There appears to be particular scope for reduction in General and Administrative employee benefits, which account for 37% of the total, in what is a very production-focussed business at present.

Some of the surplus inventory on site after the poor Q1 has now been shifted, and the Q2 results benefit from this to some extent. We believe there is further inventory to go during Q3, especially as the bulk customers that Viridis now has under contract are hungry for

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pellets and have greater demand than the current production capacity.

**Current Funding Position**

The providers of the new capital will own 50% of the company, assuming full conversion of the CULS but ignoring the warrants. This is a heavy price for existing holders to pay. On the other hand, the company is in a different league to the one investors were faced with at the turn of the year, which was over-borrowed in short term loans due for imminent maturity, without the capital to close acquisitions, and lacking the critical mass to obtain economies of scale.

We understand that Cornwall Investments llc of New Jersey, the holders of the CULS, intends to convert at the earliest opportunity. The financing was structured this way because approval of the Toronto Stock Exchange is needed before any single investor buys over the 20% ownership threshold. This has been applied for.

New capital puts Viridis in a different league

**Capital Spending Programme**

We view the likely future capital spending programme as follows:

Financial completion of Monte Lake and Confluence Energy purchases (deals previously announced but not yet concluded)	\$2.8m maximum – purchase costs currently being negotiated downwards with vendors
Monte Lake – build out of 70,000 tonnes/yr plant to use beetle kill timber, project financed	\$8.0m proposed joint ownership with Abellon. 80% debt financing for the JV already arranged, the remaining 20% to be funded by equity investment from each partner.
Okanagan, second wood pellet production line, using new “tower” space saving technology, 40,000 tonnes/yr, project financed	Possible second press to increase capacity by a further 15,000 tonnes. \$0.5m?
Working capital needed for palm kernel pressings Asian contract	\$0.5m
Other working capital	\$0.5m
<b>TOTAL</b>	<b>\$12.3m</b>

As can be seen from this, by end-2012 Viridis Energy will once again have built itself up to the position of having significant debt, The nature of the debt will be very different, however, and the JV debt for Monte Lake may even be non-recourse. Until this latest share issue wiped out the group’s indebtedness, all debt was held centrally, some of it on onerous terms.

Viridis Energy after its capital raisings has shareholders’ equity of \$7m, and this will be slightly eroded by operating losses in Q3. In our opinion this is compatible with a possible \$12.3m capital expenditure programme.

This rate of expansion would be sufficient for most companies. However, if it wishes to expand faster, Viridis Energy would have several possible courses of action. They would include:

- Joint venturing some of the capital projects, as already proposed at Monte Lake
- Leasing plants or their equipment
- Leaving the plants in the ownership of its blue chip customers and running them on a “design build operate” contract. This may be logical, because the projects are capital intensive and the customers will have a lower cost of capital than Viridis Energy.
- A further equity capital raising exercise in H1 2012.

## Key Contracts

We believe the current state of play on the key contracts announced by the company during 2011 to be as follows:

- In April, Viridis Energy announced a contract with “a major BC wood pellet producer” to supply it 22,000 tonnes of pellets in 2011, rising to 48,000 tonnes/yr in 2012-2014. Shipments have to date run below the planned level, at c. 2,000 tonnes/month against the hoped for 4,000 tonne/month, because the customer has had difficulty sourcing enough rail wagons. This logistical problem is currently being overcome. Much of this output is destined for power stations in the UK.
- Abellon CleanEnergy. This Indian company has signed a 30,000 tonne/yr contract, rising to 40,000 tonne/yr, and has subscribed to a 10% interest in Viridis equity. The agreement was announced on August 3. It will become a joint owner with Viridis Energy of the Monte Lake property and will be intimately involved with the choice of plant design there. The first shipment was made on August 30.
- Italian contract. This has never been officially announced, but is turning into a major factor, and may take 2,000 tonne/month for the remainder of 2011.
- Palm Kernel Shell contract. This was announced in April. Heracles International has contracted to take 40,000 tonne/month of palm kernel pressings supplied by Viridis for sale into the mainland Chinese market. First deliveries have been made to the port and are awaiting shipment. When fully operational this contract will be worth \$2.8m/month. At the time, Viridis issued a public announcement stating it expected 10-15% margins on this sourcing contract.

Key contracts starting to perform

## Plant Output

Viridis Energy at present only has one operational wood pellet plant. This is at Okanagan in BC. When we visited this plant a year ago, its theoretical maximum output was 4,000 tonne/month, but this was rarely being achieved in practice. A combination of operational improvements and the greater predictability of customer demand because of the new bulk contracts mean that Viridis Energy has been able to increase the output of this unit without any further capital spend. In June 2011, we understand, it produced 6,500 tonnes of pellets. We expect output in future to be in the 5,500 – 6,000 tonne/month range. The installation of a second press, to raise output by an additional 15,000 tonne/yr, is under consideration.

Output being increased

## Forward Projections

We expect the cost of production to fall over the coming quarters, as the renegotiated raw material supply contracts at lower prices come into force, further internal economies are made and economies of scale take effect. Running the Okanagan plant, and then the other new factories, consistently at full capacity will further reduce unit costs. Transport costs will fall, as an increasing proportion of output is taken on FOB contracts, where the pellets are priced for sale at the factory gate and the customer is responsible for freight. This should more than compensate for the lower prices seen on the bulk contracts. We expect the wood pellet operations to be operating at breakeven by the end of the current year, and to be returning a profit to shareholders in 2012.

Production costs to fall

If the Monte Lake build-out is undertaken on a JV basis, of course a proportion of earnings from this plant will go to the partner, possibly as a minority interest. For the sake of simplicity, we have included Monte Lake at 50% of its output for the final two quarters of 2012 in which it is likely to be operating.

Our projections, in terms of tonnage output, pricing, revenue, profit and eps currently as follows:

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Viridis Energy

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Tonnage Throughput Quarterly	Q1/11A	Q2/11E	Q3/11E	Q4/11E	Q1/12W	Q2/12E	Q3/12E	Q4/12E
Okanagan Pellet	12,000	14,000	14,000	14,000	14,000	17,000	17,000	17,000
Inventory clearance		6,000	6,000					
Other High Value Product	1,000	1,000	1,000	1,000	1,000	1,000	1,000	1,000
Okanagan 2nd Plant								
Confluence				10,000	10,000	10,000	10,000	10,000
Monte Lake JV at 50% of Likely Output							5,000	7,500
<b>Total Tonnage</b>	<b>13,000</b>	<b>21,000</b>	<b>21,000</b>	<b>25,000</b>	<b>25,000</b>	<b>28,000</b>	<b>33,000</b>	<b>35,500</b>
Average Price \$/tonne	205	140	145	120	120	120	110	110
Wood Pellet Revenue	2.7	2.9	3.0	3.0	3.0	3.4	3.6	3.9
Cost of Sales per tonne	146	110	90	80	80	80	75	70
Gross Margin per tonne	59	30	55	40	40	40	35	40
Gross Wood Pellet Profit	0.8	0.6	1.2	1.0	1.0	1.1	1.2	1.4

Tonnage should nearly treble by end-2012

Palm Kernel Pressings	Q1/11A	Q2/11A	Q3/11E	Q4/11E	Q1/12W	Q2/12E	Q3/12E	Q4/12E
Tonnage			10,000	80,000	100,000	120,000	120,000	120,000
Average Price \$/tonne			70	70	70	70	70	70
Revenue \$m			0.7	5.6	7	8.4	8.4	8.4
Cost of Sales per tonne \$			63	63	63	63	63	63
Gross Margin per tonne \$			7	7	7	7	7	7
Gross Profit PKP Pressings \$m			0.07	0.56	0.7	0.84	0.84	0.84

Palm kernel revenue to contribute

	\$m	Q1/11A	Q2/11A	Q3/11E	Q4/11E	Q1/12W	Q2/12E	Q3/12E	Q4/12E
Group Sales Revenue		2.67	2.87	3.75	8.60	10.00	11.76	12.03	12.31
Group Gross Profit		0.02	0.37	1.23	1.56	1.70	1.96	2.00	2.26
Gross Margin %		0.8%	12.8%	32.7%	18.1%	17.0%	16.7%	16.6%	18.4%
Expenses		-1.09	-1.18	-1.60	-1.60	-1.60	-1.70	-1.70	-1.70
Operating Profit/Loss		-1.06	-0.81	-0.38	-0.04	0.10	0.26	0.30	0.56
Operating Margin %		-39.7%	-28.3%	-10.0%	-0.5%	1.0%	2.2%	2.5%	4.6%
Finance Costs		-0.09	-0.16	-0.20	-0.10	-0.10	-0.10	-0.14	-0.16
Loss on Asset Disposal		0.00	-0.03	0.00	0.00	0.00	0.00	0.00	0.00
<b>Pre-tax Profit/Loss</b>		<b>-1.15</b>	<b>-1.00</b>	<b>-0.58</b>	<b>-0.14</b>	<b>0.00</b>	<b>0.16</b>	<b>0.16</b>	<b>0.40</b>
Tax Charge %		0%	0%	0%	0%	0%	0%	0%	0%
Tax Charge \$m		0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
For Ordinary Holders		-1.15	-1.00	-0.58	-0.14	0.00	0.16	0.16	0.40
No. Shares, Undiluted, m.		30.3	30.3	36.5	42.6	42.6	42.6	42.6	42.6
No. Shares after CULS conversion		30.3	30.3	36.5	60.2	60.2	60.2	60.2	60.2
No. Shares, Fully Diluted, m.		44.2	44.2	64.0	85.3	85.3	85.3	85.3	85.3
EPS Undiluted c/share		-3.79	-3.29	-1.58	-0.33	0.00	0.38	0.36	0.94
<b>EPS if CULS Converted c/share</b>		<b>-3.79</b>	<b>-3.29</b>	<b>-1.58</b>	<b>-0.17</b>	<b>0.07</b>	<b>0.33</b>	<b>0.32</b>	<b>0.73</b>
EPS Fully Diluted c/share		-2.46	-2.12	-0.80	0.06	0.22	0.41	0.40	0.69

Profits in 2012

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Management	Major Shareholders								
<p><b>Chairman: John Campbell.</b> He is also CEO of Stealth Energy.</p> <p><b>Chief Executive Officer:</b> Chris Robertson, founder of Cypress Pacific Marketing, the largest subsidiary of Viridis Energy. Previously an executive with Forest City, a NYSE listed company.</p> <p><b>Chief Financial Officer:</b> Michele Rebiere. 18 years senior management experience. Studied finance at Wharton.</p> <p><b>Vice President Sales and Marketing:</b> Geordie Munro, part of the Cypress Pacific management team for five years.</p> <p><b>Export Manager:</b> Bob Wood, part of Cypress Pacific management team.</p> <p><b>Non-Executive Directors:</b></p> <p><b>John Heimbecker,</b> Vice President of Parrish &amp; Heimbecker, an agricultural company with \$1.7bn of sales. Also chairman of Canada Ports Clearing Association.</p> <p><b>Alphonse Plaktis,</b> Principal of Soho Ventures Inc.</p>	<table border="0"> <tr> <td><b>Cornwall Investments Ilc of New Jersey</b></td> <td>18%</td> </tr> <tr> <td><b>Abellon CleanEnergy</b></td> <td>10%</td> </tr> <tr> <td><b>NextView Capital of Chicago</b></td> <td>6%</td> </tr> <tr> <td><b>Insider Shareholdings:</b></td> <td>17%</td> </tr> </table>	<b>Cornwall Investments Ilc of New Jersey</b>	18%	<b>Abellon CleanEnergy</b>	10%	<b>NextView Capital of Chicago</b>	6%	<b>Insider Shareholdings:</b>	17%
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Key Dates	Key Milestones								
<p><b>November:</b> Q3 Results Announcement</p> <p><b>March 2012:</b> Full Year Results Announcement</p>	<p><b>June 2009:</b> Sale of Grid Sense Systems, its previous business leaving a clean shell. Change of name to Viridis Energy.</p> <p><b>March 8 2010:</b> Acquisition of Cypress Pacific Marketing, a wood pellet distribution company.</p> <p><b>April 30, 2010:</b> Acquisition of Okanagan Pellet Company (known at the time as Westwood Fibre Products), a wood pellet producer in BC.</p> <p><b>February 2011:</b> Strategic switch of emphasis from seasonal domestic business to international commercial and residential contracts.</p> <p><b>April 2011:</b> Letter of Intent signed with Heracles International to supply oil palm biomass from Malaysia to China and other Asian countries.</p> <p><b>August 2011:</b> Closure of equity fundraising, doubling share capital and almost eliminating debt.</p>								

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