



## **Fuel Tech's growth is good, but investors want more**

*by Molly Seltzer*

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Fuel Tech Inc., a Batavia-based technology company that helps coal-driven power plants run cleaner and more efficiently, is taking on the biggest market in the power industry – China.

In January Fuel Tech began demonstrating its signature efficiency-increasing technology, Fuel Chem, at coal plants in China and India. It announced new orders worth \$6.7 million, including one from China, in early March.

Fuel Tech, with fewer than 200 employees and a market capitalization of \$393 million, last year earned \$7.2 million, or 29 cents per diluted share, up 6 percent from \$6.8 million or 28 cents per diluted share the year earlier. Revenues were a record \$80.3 million, up 7 percent from \$75.1 million.

The company recorded notable fourth-quarter growth, posting a record net income of \$5.2 million, or 21 cents per diluted share, up 259 percent from \$1.5 million, or 6 cents per diluted share, in the year-earlier period. But is that enough to satisfy Wall Street?

“For this company the expectations are so high and the growth potential is so huge... they’ve really got to ratchet this growth up...10 to 16 percent top line growth is good for a lot of companies, but a company this young with this much growth potential, it’s not going to cut it for investors,” said John Kearney, an equity analyst at Morningstar Inc.

Fuel Tech’s stock trades around \$17, for a lofty price-to-earnings ratio of 65, far above that of the Standard & Poor’s 500 Index stocks, 19.

Fuel Tech’s revenues have increased on a yearly basis since Norris took the helm two years ago. Earnings have fluctuated quarter by quarter, but overall growth has been steady.

However, after Fuel Tech announced lower-than-expected 2008 growth estimates, many analysts think the company has its work cut out. Dan Mannes, vice president and senior research analyst at Avondale Partners LLC agreed, “They’re in all the right places, they definitely have a nice growth ramp, but the ability to meet investor expectations might be a little bit more difficult.”

Despite increasing earnings, Fuel Tech’s shares have dropped about 30 percent compared with one year ago. The slump is mostly attributed to a December report issued by Merriman Curhan Ford & Co., which said Fuel Tech did not have an advantage over its competitors and the market for its Fuel Chem technology was already tapped. The report cited most of its information from “an independent study involving a panel of industry experts.” The study was performed by a subsidiary of MCF Corp., and after its publication, several panelists said they felt misled as to the purpose of the study.

Fuel Tech released a statement debunking the report in January. The combination of what President and CEO John Norris called “a dedicated short attack” and the company’s low 2008 expectations continued the stock’s hemorrhaging.

Bloomberg LP lists eight analysts with buy ratings, four with hold ratings and two with sell ratings. One of the two sell analysts is Jesse Herrick, who published the Merriman Curhan Ford report. He declined to comment on Fuel Tech or the report.

GE BETZ, a unit of General Electric Co., and Environmental Energy Services Inc. are widely considered Fuel Tech’s biggest competitors. However, they spray chemicals onto the burning coal instead of injecting it above and below the actual flame, which Fuel Tech believes is the secret to success. “There are some

companies that do something similar, but there's a question of whether it's as effective or not," Kearney said.

Richard Hoss, an equity analyst at Roth Capital Partners LLC, agreed. "They're the most competitive of the companies in the fuel additive field right now."

Jimmy Blakley is the maintenance superintendent at Western Farmers Electric Cooperative's Hugo plant in Oklahoma. The plant burns about 6,500 tons of coal per day and has used Fuel Chem since 2003.

"I've got 30 years of experience, and I've seen everything in the world... urea put on it to control sulfur, we've dumped stuff in, we've ground stuff in, we've done everything in the world and nothing ever helped," he said. He added, "there's stuff out there, but the plants that are using it aren't seeing the results that the plants that are using Fuel Tech are seeing."

There are about 4,000 coal plants in China, compared to about 1,500 in the U.S. Development and renovation are continuing at such rapid rates that some experts estimate China opens two new plants a week.

Norris agreed, "China is the mother lode of the market... by 2010 they'll probably be burning three times the coal we burn."

Coal provides about 50 percent of America's energy. Fuel Chem is currently used at 33 U.S. plants and operates in about 30 countries.

As coal burns, its impurities melt and settle, hardening into slag, which clogs up the boiler. The boilers have to be stopped as workers climb in the sometimes eight-story-high structures and break off the slag. Pieces of it have been known to reach the size of Volkswagens.

The Fuel Chem program uses computerized models to inject chemicals into the boiler of a coal plant as the coal burns. The chemical's main purpose is to reduce slag. Less slag means fewer boiler outages which means more efficiency, less coal used and more money saved. The company also claims Fuel Chem reduces toxic emissions.

Blakley said that after using Fuel Chem, workers needed only six hours to de-slag the boiler, instead of the 96 hours it usually took. He claimed it saved the company about \$2 million.

"We were kind of amazingly surprised," he said.

Before he worked there, Norris was skeptical about Fuel Tech's tech.

"Fuel Tech approached me in 2005 about being an executive consultant for them, and I actually said no at first. 'I don't do injection stuff.' I always considered that to be snake oil," he said.

The turning point came when Norris visited a client using the technology. "The plant manager was euphoric. I was amazed because that had not been my experience with such kinds of things," he said.

Much of Fuel Tech's recent success can be attributed to Norris, who has headed the company for two years. The 58-year-old is a former football player for North Carolina State University, has a B.S. in nuclear engineering and was a fighter pilot for 10 years.

Norris said the chemical they inject into the boilers isn't snake oil. It's magnesium hydroxide – also known as milk of magnesia.

"The chemical is non-hazardous, other than you don't want to take more than a spoonful," he joked.

Fuel Tech's use of computerized models is where it distinguishes itself from its competitors. The company pitches the model technology to power plants. If they accept, it stages demonstrations, where each plant's individual boilers are reconstructed on computers and a trial process begins – on Fuel Tech's nickel. After a two or three month period, the plants decide if the product is worth installing full-scale.

Norris said Fuel Tech has completed over 90 demonstrations worldwide and never been turned down after the trial period.