H2O Innovation Reports Q3 2021 Results With Strong Profitability and Strong Cash Flow Generation

May 13, 2021 (Source) – **Key Financial Highlights**

- Acquisition of the remaining 76.0 % of the issued and outstanding shares of Genesys Membrane Products, S.L. ("GMP") to expand the specialty chemical products and laboratory services to the large international distributor network and to increase the commercial presence in Latin America, notably within the mining industry;
- Revenue growth of 8.6 % over the same period of the previous fiscal year, reaching $39.2 M for the third quarter of fiscal year 2021;
- Adjusted EBITDA[1] reached $4.5 M, or 11.5 % of revenues, for the third quarter of fiscal year 2021 compared to $3.8 M, or 10.5 % of revenues, for the comparable quarter of previous fiscal year;
- Net earnings amounted to $2.1 M for the third quarter of fiscal year 2021, compared to a net loss of ($3.1 M) for the comparable quarter of previous fiscal year;
- Strong financial position with a net debt[1] of $3.3 M at the end of the quarter, compared to a net debt of $10.5 M as at June 30, 2020; and
- Cash flows from operating activities generated $10.2 M for the third quarter of fiscal year 2021, compared to $0.9 M for the comparable quarter of previous fiscal year.

All amounts in Canadian dollars unless otherwise stated.

(TSXV: HEO) – H_2O Innovation Inc. (“H_2O Innovation” or the “Corporation”) announces its financial results for the third quarter of fiscal year 2021 ended March 31, 2021.

“Once again we are extremely proud to present a strong financial performance for our Q3 results. The sustained free cash generated from our operations combined with constant margin improvement testifies to the work of the last months, even years. As we continue to build our platform of complementary water treatment technologies and services through acquisitions and innovations, we multiply the synergies between these technologies and services which simultaneously fosters an exceptional business culture full of diverse talents. The multiple synergies become our competitive advantage as they generate value for our customers and help the Corporation preserve long term business relationships, thus causing high recuring revenues. With a strong financial position showing a net debt-to-adjusted EBITDA ratio of 0.20, we have room to invest in organic growth opportunities and to realize strategic acquisitions, and therefore achieve our 3-year Plan. Despite the lasting COVID-19 pandemic, our business model combined with the essential nature of the products and services offered is providing financial robustness and resiliency”, **stated Frédéric Dugré, President and Chief Executive Officer of H_2O Innovation.**

(In thousands of Canadian dollars)	**Three-month periods ended March 31,**						**Nine-month periods ended March 31,**					
	2021		2020				**2021**		2020			
	$	**%** [a]	$		% [a]		**$**	**%** [a]	$		% [a]	
Revenues per business pillar												
WTS	**10,095**	**25.7**	6,726		18.7		**23,281**	**21.3**	22,316		22.9	
Specialty products	**11,810**	**30.2**	12,893		35.8		**33,586**	**30.8**	28,459		29.1	

O&M	**17,250**	**44.1**	16,442		45.5		**52,253**	**47.9**	46,843		48.0	
Total revenues	**39,155**	**100.0**	36,061		100.0		**109,120**	**100.0**	97,618		100.0	
Gross profit margin before depreciation and amortization	**11,081**	**28.3**	10,336		28.7		**29,943**	**27.4**	25,310		25.9	
SG&A expenses[(b)]	**6,497**	**16.6**	6,777		18.8		**18,546**	**17.0**	17,732		18.2	
Net earnings (loss) for the period	**2,062**	**5.3**	(3,097	)	(8.6	)	**3,314**	**3.0**	(5,040	)	(5.2	)
EBITDA[1]	**5,347**	**13.7**	3,890		10.8		**11,279**	**10.3**	6,044		6.2	
Adjusted EBITDA[1]	**4,513**	**11.5**	3,775		10.5		**11,557**	**10.6**	7,692		7.9	
Adjusted net earnings[1]	**2,181**	**5.6**	2,310		6.4		**6,014**	**5.5**	3,254		3.3	
Recurring revenues[1]	**32,339**	**82.6**	31,796		88.2		**95,070**	**87.1**	83,731		85.8	

a. % of revenues.
b. Selling, general and administrative expenses (“SG&A”).

Third Quarter Results

Despite the significant negative CAD-USD foreign exchange rate impact, consolidated revenues from the Corporation’s three business pillars for the three-month period ended on March 31, 2021, increased by $3.1 M, or 8.6 %, to reach $39.2 M compared to $36.1 M for the comparable quarter of previous fiscal year. Assuming a constant USD exchange rate during this quarter, the consolidated percentage increase would have been 12.1 %, or $4.3 M. This overall increase is fueled by the strong performance of our WTS business pillar, the acquisition of GUS on July 1, 2020, which contributed $1.3 M in revenues, and the acquisition of GMP on February 1, 2021, which contributed $1.5 M in revenues during this quarter.

Revenues coming from the WTS business pillar increased by $3.4 M compared to the same quarter of fiscal year 2020. The increase was primarily due to the recent wave of projects captured as well as the resumption of work following the delays caused by the COVID-19 pandemic. With $3.2 M of new industrial and municipal projects secured at the end of the second quarter and early January 2021, revenues from the WTS business pillar are gaining positive momentum. It is in line with the Corporation’s business plan to prioritize WTS’ projects with higher gross profit margins, or projects that can fuel opportunities for other business pillars. The O&M business pillar was positively impacted by the acquisition of GUS and showed organic growth of $0.5 M this quarter, offset by an unfavorable USD exchange rate impact of $1.0 M. Revenues coming from the Specialty Products business pillar decreased compared to the same quarter of last fiscal year, explained by the business mix and the timing of certain deliveries. During the third quarter of fiscal year 2020, Piedmont business line had exceptional deliveries which generated record revenues, while during the third quarter of this fiscal year, the number of deliveries for Piedmont business line was not at the same level. Nevertheless, revenues coming from the Specialty Products business pillar for the last twelve months increased by 28.0 % compared to the previous twelve-month period, largely coming from acquisitions.

The Corporation’s gross profit margin[2] stood at $11.1 M, or 28.3 %, during the third quarter of fiscal year 2021, compared to $10.3 M, or 28.7 % for the previous fiscal year, representing an increase of $0.8 M, or 7.2 %. The decrease of gross profit margin (%) before depreciation and amortization is explained by the business mix, with more sales coming from the WTS business pillar and less sales coming from the Specialty Products business pillar this quarter. The WTS business pillar showed an improvement of gross profit margin (%) before depreciation and amortization, in line with the Corporation’s strategy to focus on projects with a higher margin profile. O&M business pillar’s focus is to improve efficiency through the business combination of Utility Partners, Hays Utility South Corporation and Gulf Utility Services announced on December 1, 2020 and effective on January 1, 2021. The merger of these companies will enhance the vertical integration of our product and service offering to our customers. By operating under a single brand, the Corporation believes it should also facilitate the generation of cross-selling synergies between the Corporation’s different business lines. Moreover, this single brand identity will contribute to elevate H_2O Innovation profile and awareness within the different geographies where H_2O Innovation is established in North America. From a financial and commercial perspectives, it will allow the Corporation to generate additional savings, to streamline the business processes and to solidify the O&M platform for future acquisitions and organic growth opportunities. This initiative shall continue to improve the gross profit margin.

The Corporation’s SG&A reached $6.5 M during the third quarter of fiscal year 2021, compared to $6.8 M for the same period of the previous fiscal year, representing a decrease of $0.3 M, or 4.1 %, while the revenues of the Corporation increased by 8.6 %. The decrease is driven in part by lower travel expenses due to the COVID-19 pandemic and the decrease in the USD exchange rate compared to the same quarter of last fiscal year. Moreover, the Corporation had full impact of the 2020 restructuring plan related to the WTS business pillar, which reduced the S&GA this quarter, partly offset by the acquisition of GUS on July 1, 2020 and the acquisition of GMP on February 1, 2021, which contributed $0.1 M and $0.2 M respectively in SG&A expenses. On a sequential basis, when compared to the second quarter of fiscal year 2021, the Corporation’s SG&A increased by $0.7 M to $6.5 M, from $5.8 M, partly due to the acquisition of GMP and higher employee compensation costs compared to the previous quarter.

Net earnings amounted to $2.1 M, or $0.026 per share, for the third quarter of fiscal year 2021 compared to a net loss of ($3.1 M), or ($0.040) per share, for the comparable quarter of fiscal year 2020. The variation was impacted by the increase in the Corporation's consolidated revenues, lower impairment costs and the fair value gain on step acquisition that were compensated by higher other losses, higher income taxes expenses, higher finance costs and higher acquisition and integration costs. Moreover, the SG&A ratio decreased from 18.8 % to 16.6 %. The Corporation recognized a gain of $2.3 M as a result of measuring at fair value its 24.0 % equity interest in GMP held before the business combination. Adjusted net earnings amounted to $2.2 M, or $0.027 per share, for the third quarter of fiscal year 2021 compared to adjusted net earnings of $2.3 M, or $0.030 per share, for the comparable quarter of fiscal year 2020. The variation of the adjusted net earnings is explained by the same factors mentioned above, and by an impairment taken during the third quarter of fiscal year 2020.

The Corporation's adjusted EBITDA increased by $0.7 M, or 19.5 %, to reach $4.5 M during the third quarter of fiscal year 2021, from $3.8 M for the comparable period of fiscal year 2020. The adjusted EBITDA % improved and reached 11.5 % for the third quarter of fiscal year 2021, compared to 10.5 % for the same quarter of last fiscal year. Improvement of the adjusted EBITDA was driven by the increase in the Corporation's consolidated revenues and the decrease of SG&A ratio, partly offset by a gross profit margin in % reduction associated with product mix.

Cash flows from operating activities generated $10.2 M for the quarter ended March 31, 2021, compared to $0.9 M of cash flows generated from operating activities during the same period of previous fiscal year. The cash flows for the three-month ended March 31, 2021 resulted primarily from the net earnings of $2.1 M, plus $1.6 M of non-cash adjustments to the net earnings consisting primarily of depreciation and amortization, stock-based compensation costs, changes in fair value of contingent considerations, finance costs – net, income taxes, partially offset by the share of profit of an associate and the fair value gain on step acquisition, and $6.5 M in favorable changes in working capital items. In comparison, the cash flows for the three-month ended March 31, 2020 resulted primarily from the net loss of $3.1 M, plus $7.1 M of non-cash adjustments to the net loss consisting primarily of depreciation and amortization, impairment of intangible assets and goodwill, stock-based compensation costs, changes in fair value of contingent considerations, finance costs – net, partially offset by deferred taxes, and $3.1 M in unfavorable changes in working capital items.

Nine-months results

Revenues stood at $109.1 M, compared to $97.6 M last year; gross margin was $29.9 M, or 27.4 %, compared to $25.3 M, or 25.9 % last year; adjusted EBITDA was $11.6 M, or 10.6 %, compared to $7.7 M, or 7.9 % last year; and net earnings was $3.3 M, or $0.042 per share, compared to a net loss of ($5.0 M), or ($0.079) per share last year, essentially for the same reasons mentioned for the third quarter.

Reconciliation of net earnings (loss) to EBITDA and to adjusted EBITDA

The definition of adjusted earnings before interest, income taxes, depreciation and amortization ("adjusted EBITDA") does not take into account the Corporation's finance costs – net, stock-based compensation costs, unrealized exchange (gains) / losses, change in fair value of contingent consideration, acquisition and integration costs, impairment of intangible assets and goodwill, the faire value gain on step acquisition and litigation provision. The reader can establish the link between adjusted EBITDA and net earnings (loss) by looking at the reconciliation presented below. The definition of adjusted EBITDA used by the Corporation may differ from those used by other companies. Even though EBITDA and adjusted EBITDA are non-IFRS measures, it is used by management to make operational and strategic decisions. Providing this information to the stakeholders, in addition to the GAAP measures, allows them to see the Corporation’s results through the eyes of the management, and to better understand the financial performance, notwithstanding the impact of GAAP measures.

	Three-month periods ended March 31,				**Nine-month periods ended March 31,**			
(In thousands of Canadian dollars)	**2021**		2020		**2021**		2020	
	$		$		**$**		$	
Net earnings (loss) for the period	**2,062**		(3,097	)	**3,314**		(5,040	)
Finance costs – net	**862**		469		**1,975**		1,508	
Income taxes	**590**		(631	)	**529**		(937	)
Depreciation of property, plant and equipment and right-of-use assets	**789**		702		**2,367**		2,082	
Amortization of intangible assets	**1,044**		1,139		**3,094**		3,123	
Impairment of intangible assets and goodwill	**–**		5,308		**–**		5,308	
EBITDA	**5,347**		3,890		**11,279**		6,044	
Unrealized exchange (gain) loss	**(3**	**)**	(273	)	**639**		(616	)
Stock-based compensation costs	**39**		55		**121**		169	

Changes in fair value of the contingent consideration	**615**		57		**719**		268	
Acquisition and integration costs	**212**		46		**496**		1,827	
Fair value gain on step acquisition	**(2,347**	**)**	—		**(2,347**	**)**	—	
Litigation provision	**650**		—		**650**		—	
Adjusted EBITDA	**4,513**		3,775		**11,557**		7,692	

Adjusted net earnings

The definition of adjusted net earnings excludes acquisition and integration costs, amortization of intangibles assets from acquisition, unrealized exchange (gain) loss, change in fair value of the contingent considerations, stock-based compensation costs, impairment of intangible assets and goodwill, fair value gain on step acquisition, litigation provision and realized net loss on swap termination. The reader can establish the link between net earnings (loss) and adjusted net earnings with the reconciliation items presented in this report. The definition of adjusted net earnings used by the Corporation may differ from those used by other companies. Adjusted net earnings is a non-IFRS measure and it is used by management to monitor financial performance and to make strategic decision.

Reconciliation of net earnings (loss) to adjusted net earnings

	Three-month periods ended March 31,				**Nine-month periods ended March 31,**			
(In thousands of Canadian dollars)	**2021**		2020		**2021**		2020	
	$		$		**$**		$	

Net earnings (loss) for the period	**2,062**		(3,097	)	**3,314**		(5,040	)
Acquisition and integration costs	**212**		46		**496**		1,827	
Amortization of intangible assets related to business combinations	**931**		1,018		**2,853**		2,544	
Unrealized exchange (gain) loss	**(3**	**)**	(273	)	**639**		(616	)
Changes in fair value of the contingent considerations	**615**		57		**719**		268	
Stock-based compensation costs	**39**		55		**121**		169	
Impairment of intangible assets and goodwill	**–**		5,308		**–**		5,308	
Fair value gain on step acquisition	**(2,347**	**)**	–		**(2,347**	**)**	–	
Litigation provision	**650**		–		**650**		–	
Realized net loss on swap termination	**237**		–		**237**		–	
Income taxes related to above items	**(215**	**)**	(804	)	**(668**	**)**	(1,206	)
Adjusted net earnings	**2,181**		2,310		**6,014**		3,254	

Recurring Revenues

Recurring revenue by nature is a non-IFRS measure and is defined by management as the portion of the Corporation’s revenue coming from customers with whom the Corporation has established a long-term relationship and/or coming from a business with a recurring customer sales pattern. However, there is no guarantee that recurring revenues will last indefinitely. The Corporation’s recurring revenues are coming from the Specialty Products and O&M business pillars as well as the service activities of the WTS business pillar. This non-IFRS measure is used by management to evaluate the stability of revenues from one year to the other.

Net Debt

The definition of net debt consists of bank loans and long-term debt less cash. The definition of net debt used by the Corporation may differ from those used by other companies. Net debt-to-adjusted EBITDA ratio is a non-IFRS measure without a standardized definition within IFRS. The Corporation uses this ratio as a measure of financial leverage and it is calculated using our trailing twelve month adjusted EBITDA.

(In thousands of Canadian dollars)	**March 31, 2021**		June 30, 2020	
	$		$	
Bank loans	**–**		3,415	
Current portion of long-term debt	**2,971**		2,782	
Long-term debt	**13,647**		13,766	
Less: Cash	**(13,308**	**)**	(9,417	)
Net debt	**3,310**		10,546	

H_2O Innovation Conference Call

Frédéric Dugré, President and Chief Executive Officer and Marc Blanchet, Chief Financial Officer, will hold an investor conference call to discuss the third quarter financial results in further details at 10:00 a.m. Eastern Time on Thursday, May 13, 2021.

To access the call, please call 1 (877) 223-4471 or 1 (647) 788-4922, five to ten minutes prior to the start time. Presentation slides for the conference call will be made available on the Corporate Presentations page of the Investors section of the Corporation’s website.

The third quarter financial report is available on www.h2oinnovation.com. Additional information on the Corporation is also available on SEDAR (www.sedar.com).

Prospective Disclosures

Certain statements set forth in this press release regarding the operations and the activities of H_2O Innovation as well as other communications by the Corporation to the public that describe more generally management objectives, projections, estimates, expectations or forecasts may constitute forward-looking statements within the meaning of securities legislation. Forward-looking statements include the use of the words such as “anticipate”, “if”, “believe”, “continue”, “could”, “estimate”, “expect”, “intend”, “may”, “plan”, “potential”, “predict”, “project”, “should” or “will” and other similar terms as well as those usually used in the future and the conditional. Forward-looking statements concern analysis and other information based on forecast future results and the estimate of amounts that cannot yet be determined and are based on the estimates and opinions of management on the date the statements are made.

In this press release, such forward-looking statements include, but are not limited to, statements regarding the Corporation’s ability to grow its business and to reach specific financial objectives and targets and involve several risks and uncertainties. Those risks and uncertainties include, without limitations, the Corporation’s ability to maintain its financial position and its business improvements and to complete, deliver and execute new WTS and O&M projects, in due time and as expected by the customers, despite the challenges the world is facing with the current COVID-19 pandemic. Information about the risk factors to which the Corporation is exposed is provided in the Annual Information Form dated September 23, 2020 available on SEDAR (www.sedar.com).

Should one or more of these risks or uncertainties materialize, or should the assumptions underlying those forward-looking statements prove incorrect, actual results may vary materially from those described herein. Unless required to do so pursuant to applicable securities legislation, H_2O Innovation assumes no obligation to update or revise forward-looking statements contained in this press release or in other communications as a result of new information, future events, and other changes.

About H_2O Innovation

H_2O Innovation designs and provides state-of-the-art, custom-built and integrated water treatment solutions based on membrane filtration technology for municipal, industrial, energy and natural resources end-users. The Corporation's activities rely on three main pillars. The first one is ***Water Technologies and Services*** and includes all types of projects as well as digital solutions (Intelogx™ and Clearlogx®) to monitor and optimize water treatment plants. H_2O Innovation's second pillar, ***Specialty Products***, includes a complete line of maple equipment and products, specialty chemicals, consumables and specialized products for the water industry, through H_2O Innovation Maple, PWT, Genesys and Piedmont. The Corporation is now exporting his specialty products in more than 75 countries. Finally, H_2O Innovation operates, maintains, and repairs water and wastewater treatment systems, distribution equipment and associated assets for all of its clients and ensures that water quality meets regulatory requirements, through the third pillar – ***Operation and Maintenance***. Together, they employ nearly 470 employees for the operation of more than 275 utilities in two Canadian provinces and twelve US states, mainly on the US Gulf coast, Southeast, Northeast (New England) and the West Coast. For more information, visit www.h2oinnovation.com.

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[1] These non-IFRS measures are presented as additional information and should be used in conjunction with the IFRS financial measurements presented in this press release. Definition of all non-IFRS measures and additional IFRS measures are provided at the end of this press release to give the reader a better understanding of the indicators used by management.

[2] Gross profit margin presented before depreciation and amortization.