

# ESG Investor Spotlight on Climate Change and Water

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As world leaders gather in Glasgow for the United Nations Climate Change Conference (also known as COP26) one has to be aware that as the world continues to suffer from more severe weather, some of the things we take for granted may become more costly and/or scarce. The impact of extreme heat and droughts could potentially affect the supply and availability of clean water for drinking, as well as for irrigation and our supply of fresh food. Albeit COP26 is primarily focused on mitigating greenhouse gas emissions, we need to look past that to what the consequences of a changing environment could have on humanity. For years, if not decades, clean water has been portrayed as a critical commodity whose time will come. Perhaps now that weather patterns appear to be getting more volatile, we may finally be seeing the start of this.

Today we are updating an InvestorIntel favorite – [H2O Innovation Inc.](#) (TSXV: HEO | OTCQX: HEOFF) which designs, manufactures and commissions customized membrane water treatment systems, provides operation and maintenance services for that equipment, and designs, manufactures and sells a complete line of OEM specialty products such as chemicals, consumables, couplings, fittings, cartridge filters and other components for multiple markets in the water treatment industry. For the last 20 years the company has designed and fabricated state-of-the-art, integrated water treatment solutions for municipal, energy production, and natural resource end users, specializing in applications for drinking water, water reuse, wastewater treatment and industrial process water. Developed in-house, the company's solutions are custom designed, adapted and built for

all types of applications.

The Company breaks down its activities into three operating segments: Water Technologies & Services (WTS), which designs and builds custom water, wastewater and water reuse systems; Specialty Products (SP), utilizing a global network of more than 100 distribution partners to manufacture and deliver specialty chemicals, components, and consumables to end-users, with a particular focus on membrane applications; and Operations and Maintenance (O&M), for contract operations for water, wastewater, water reuse treatment, collection, distribution systems, pumping stations, and associated assets for customers throughout North America.

At the end of September, the Company released its [results for its fiscal year](#) ended June 30, 2021, reporting record fiscal year 2021, revenues and profitability. Highlights included annual revenues reaching \$144.3 million, representing a \$10.7 million growth or 8.0 % year over year; net earnings of \$3.1 million, or \$0.039 per share, compared to a net loss of \$4.2 million, or \$0.061 per share, for the previous fiscal year; and a strong financial position with a net debt of \$0.5 million at year end, compared to a net debt of \$10.5 million as of June 30, 2020. On the M&A side, H2O Innovation completed two acquisitions complementing its [O&M services in Texas](#), and expanded its reach in Spain and Latin America with the [acquisition of Genesys Membrane Products, S.L.](#), a specialty products marketing and sales network.

The Company fell a little short of market expectations, however, despite the positive results, and the stock lost 10% upon the announcement of its fiscal 2021 numbers. However, redemption may be right around the corner when [Q1 results](#) for the current fiscal year come out on Wednesday, November 10<sup>th</sup>. If we ask why an investor should be optimistic, the answer is that since June

30<sup>th</sup> H2O Innovations has announced an [O&M contract](#) for the City of Laurel, MS with a total value of \$10.4 million over 4 years; it has also been awarded [six new capital equipment projects](#) in its WTS business line, and reached completion on six others, with the new contracts valued at \$4.8 million; its Piedmont business line [secured new orders](#) for fiber reinforced polyester cartridge filter housings and duplex stainless couplings totaling \$4.0 million along with the signing of five new distribution agreements in Latin America; and its SP business line has been [selected to provide antiscalant](#) to the world's largest seawater reverse osmosis desalination plant. This is important because one of primary focuses of H2O Innovations is building recurring revenues across its three business segments, and it has realized an 87% threshold. That suggests that all the above announcements should be additive to the upcoming Q1 results.

Thankfully the planet earth hasn't descended into the harsh, inhospitable environment of the desert planet, [Arrakis](#), the setting of the latest version of the movie "[Dune](#)" based on the must-read [book\(s\) by Frank Herbert](#). But as the reliability of fresh water becomes more of a concern, it's good to know that companies like H2O Innovations have our back. Perhaps we are finally starting to see the commoditization of water that could make the stewards of clean water, like H2O Innovations, which was [Water Company of the Year at the 2020 Global Water Awards](#), very important and valuable. In the meantime, this Company with its recurring revenues, clean balance sheet and a market cap of just over \$200 million.

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# Frédéric Dugré on why H2O Innovation's Q3 2021 Financial Results were "the best quarter ever announced"

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In a recent InvestorIntel interview, Tracy Weslosky speaks with Frédéric Dugré, President and CEO of [H2O Innovation Inc.](#) (TSXV: HE0 | OTCQX: HE0FF) about how H2O's [Q3 2021 financial results](#) provided "...the best quarter ever announced" and why "...water is the right space to invest in".

In this InvestorIntel interview, which may also be viewed on YouTube ([click here to subscribe to the InvestorIntel Channel](#)), Frédéric also discusses the significance of H2O winning two [new projects](#) and four contract renewals in North America and how they are positioned to potentially benefit from President Biden's US\$111B [water infrastructure plan](#). Further to his Q3 2021 update, Frédéric provides an update on how H2O has increased efforts in the North American water reuse market and is continuing to expand in Latin America. With 7 financial analysts following H2O, Frédéric shares more on how the ESG investment community benefits from investing in clean water.

To watch the full interview, [click here](#)

## About H2O Innovation Inc.

H2O 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 (Intellogx™ and Clearlogx®) to monitor and optimize water treatment plants. H<sub>2</sub>O 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<sub>2</sub>O Innovation Maple, PWT, Genesys and Piedmont. The Corporation is now exporting his specialty products in more than 75 countries. Finally, H<sub>2</sub>O 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.

To learn more about H2O Innovation Inc., [click here](#)

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If you have any questions surrounding the content of this interview, please email [info@investorintel.com](mailto:info@investorintel.com).

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**H2O Innovation looks set to potentially benefit from President Biden's US\$111B water infrastructure spending**

# plan

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Did you know that globally [1 in 3 people](#) do not have access to safe drinking water? And yes, mostly in the third world; however, there are also problems in the first world. As part of U.S President Biden's American Jobs & Infrastructure Plan, he intends to allocate [US\\$111 billion](#) for water infrastructure. The Biden plan seeks to modernize aging drinking water, stormwater, and wastewater systems in the USA.

The White House Fact Sheet [states](#):

"Across the country, pipes and treatment plants are aging and polluted drinking water is endangering public health...An estimated six to ten million homes still receive drinking water through lead pipes and service lines...President Biden's plan will eliminate all lead pipes and service lines in our drinking water systems, improving the health of our country's children and communities of color."

Water treatment company [H2O Innovation Inc.](#) (TSXV: HE0 | OTCQX: HE0FF) looks to be in the right place at the right time. H2O Innovation has been in the water treatment industry for over 20 years but the future has never looked so good.

H2O Innovation designs and provides state-of-the-art, custom-built and integrated water treatment solutions based on membrane filtration technology. They provide multiple water solutions in the areas of drinking water, wastewater, water reuse & recycling, desalination, and water solutions. H2O Innovation's customers include those from municipal, energy, and natural resource end users.

**A summary of H2O Innovation's business**



Source: [Company presentation](#)

## **H2O Innovation to grow their water reuse business**

H2O Innovation is capitalizing on the momentum from the U.S plan to improve water infrastructure by developing a new digital marketing strategy that focuses on its globally recognized expertise in water reuse. The Company [recently hired Alejandro Sturniolo](#) to fulfill the role of Global Head of Water Reuse and Strategic Partnerships. Alejandro has been involved in the water industry for the past 22 years and he currently serves as Vice-President and board member for the International Desalination Association (“IDA”) and Latin American Association of Desalination and Water Reuse (“ALADYR”).

## **H2O Innovation continues to win new contracts and renew existing ones**

On May 12 they [announced](#): “H2O Innovation wins two new projects and renews four operation and maintenance contracts in North America. These contracts, with a total value of \$3.3 million, bring the O&M backlog to \$77.3 million.” The backlog refers to H2O Innovation’s backlog of orders for their business and highlights the strength of demand for their services.

Chief Strategy Officer of H2O Innovation, Gregory Madden, [stated](#): “The contract renewals show a commitment to the H2O Innovation Playbook concept that we win by creating value and delighting our customers. We have great relationship with our customers which is shown in our industry leading contract renewal rates. In Western Canada, we started with our first O&M contract in the region only three years ago, and we are now operating more than 15 facilities.”



## **H2O Innovation is expanding in Latin America**

In news released on May 3, 2021, H2O Innovation [announced](#) that in addition to their acquisition of Genesys Membrane Products, which added an office for the Corporation in Santiago, Chile; H2O Innovation plans to strengthen existing and generate new relationships with original equipment manufacturers in Latin America, a high growth potential market. Their subsidiary, Piedmont, has recently signed Pavax as a new distributor in Brazil, and now has over 20 distributors in Latin America.

## **Growing revenues, margins, and profits**

H2O Innovation's combined strategy of acquisition and organic growth has resulted in a steady increase in revenues over the past years, to the point where they are forecast to be profitable in 2021. Net profits are forecast to reach [C\\$4 million in 2021](#) (on C\$147 million revenue, 3.03% net margin), C\$5 million in 2022 (on C\$156 million revenue, 3.42% net margin), and C\$7 million in 2023 (on C\$167 million revenue, 4.47% net margin). This equates to a forecast 2021 PE of 43.5 and a 2022 PE of 35.1.

Looking at [the latest financial results](#) from Q3 in the 2021 financial year, where net earnings amounted to C\$2.1 million (up from a net loss of C\$3.1 million YoY), H2O Innovation looks to be on track to exceed the above forecasts. Another nice bonus was that net debt fell to C\$3.3 million at the end of the quarter, compared to a net debt of C\$10.5 million as at June 30, 2020.

H2O Innovation President & CEO Frédéric Dugré [stated](#): "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.”

## **Closing remarks**

H2O Innovation has been successfully growing their business to the point where the company reached profitability last quarter and has also dramatically reduced their debt. Additionally, the company has a huge order backlog of business and rising recurring revenues. A great achievement. Not surprisingly the stock price is up [147%](#) over the past year.

Looking ahead the outlook continues to brighten, notably more so if the Congress passes President Biden’s American Jobs & Infrastructure Plan (containing the water infrastructure US\$111 billion plan). H2O Innovation’s expansion into Latin America should potentially be another winner.

H2O Innovation trades on a market cap of C\$192 million. A great company and having a great year.

## **Appendix**

**President Biden’s plan to ensure clean water and to upgrade wastewater and support clean water infrastructure**



Source: [White House Fact Sheet](#)

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# **Innovation in the water**

# treatment business is in their name.

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As the name states, [H2O Innovation Inc.](#) (TSXV: HEO | OTCQX: HE0FF) is an innovator in the water treatment business focused on membrane technology. For the last 20 years the company has designed and fabricated state-of-the-art, integrated water treatment solutions for municipal, energy and natural resource end users, specializing in applications for drinking water, water reuse, wastewater treatment and industrial process water. Developed in-house, their solutions are custom built to adapt to all types of applications.

The company further breaks down their activities into three operating segments: Water Technologies & Services (WTS) which designs and builds custom water, wastewater and water reuse systems, supporting the customer with both site and remote services, as well as digital solutions, to optimize performance and maximize life of the equipment; Specialty Products (SP) utilizes a global network of more than 100 distribution partners to manufacture and delivers specialty chemicals, components, and consumables to end-users with a focus on membrane applications; and Operations and Maintenance (O&M) for contract operations of water, wastewater, and water reuse treatment, collection, and distribution systems, pumping stations, and associated assets for customers throughout North America.

H2O Innovations certainly has positive momentum for itself as a company but also being in a business segment that is becoming a greater focus for the world in general but also the [ESG investing](#) community. In their most recent [quarterly and year-end results](#), they posted their fourth consecutive year of revenue

and adjusted EBITDA growth. Additionally, the company has reported positive earnings for the last 3 quarters, which is very impressive for a growing company.



When it comes to growth, one of H2O Innovation's Key Strategic Objectives is M&A. Most recently the company announced on February 1, 2021, that it had acquired [Genesys Membrane Products, S.L.](#) located in Madrid, Spain to boost its membrane chemicals capabilities. It positions the company to better access the Latin American membrane chemical market, in particular the mining industry. H2O Innovation has averaged just under one acquisition a year since 2013. There are over 1,200 privately owned businesses active in the water industry with revenues in excess of \$50M, but only one larger than \$10B. So there is a lot of opportunities to grow the business this way and so far H2O Innovation has had success finding the right fit and successfully integrating these acquisitions.

As for organic growth, the company is focusing on improving gross margins through increased sales, improved operational excellence and via product innovation. Another key is further reduction in SG&A likely to come from acquisition synergies.

By 2023, the stated goal is to increase revenue from \$134M (Actual FY 2020) to between \$175-250M including 2-4 strategic acquisitions. With only 78M shares outstanding (90M fully diluted) and a paltry \$14.1M in debt there is some good upside for shareholders if the company can execute on its goals. Globally there is no shortage of potential acquisitions available to H2O Innovations and a clean balance sheet gives the company the option to fund these with debt or equity, whichever is more accretive.