PRESS RELEASE **TSXV: HEO**
For immediate release **Alternext: MNEMO: ALHEO**
OTCQX : HEOFF

H_2O Innovation reports fiscal year 2017 third quarter results: Continues to build growth

Key highlights

- Continuous revenue growth of 49.9% to reach $21.3 M, compared to $14.2 M for the same period of the previous fiscal year;
- 81.4% of the revenues recorded in this third quarter are coming from O&M and SP&S activities, which are recurring in nature;
- Consolidated backlog reached new high of $117.1 M as at March 31, 2017, boosted by new projects bookings and renewal of O&M contract;
- Adjusted EBITDA[1] stood at $411,737, compared to $1,245,324 for the same quarter last year, impacted by lower revenues coming from Projects, and investment in selling expenses and product development;
- Net (loss) earnings amounted to ($1,345,695), compared to $646,422 for the same period of the previous fiscal year, impacted by acquisition-related costs and integration costs of Utility Partners;
- Operating activities used ($1,135,127) in cash, compared with ($318,078) of cash used during the same quarter of the previous fiscal year.

All amounts in Canadian dollars unless otherwise stated.

Quebec City, May 15, 2017 – (TSXV: HEO) – H_2O Innovation Inc. ("H_2O Innovation" or the "Corporation") announces its results for the third quarter of fiscal year 2017 ended March 31, 2017. During this quarter, the Corporation's revenues increased by 49.9% to $21.3 M, up from $14.2 M for the same quarter of fiscal year 2016. This increase is largely attributable to the acquisition of Utility Partners, effective July 1, 2016, which added significant revenues coming from Operation & Maintenance ("O&M") activities.

"On this third quarter, the integration of Utility Partners reached a new level. We can now consider this entity fully merged into H_2O Innovation. We recently captured our first bookings from cross selling generated by Utility Partners. The Corporation, through Utility Partners, has been able to renew or extend all of its O&M contracts coming up for renewal and has secured a new one, using the support of the Projects and SP&S resources. The strategy to grow O&M and SP&S business pillars is proven to be efficient since it minimizes the impact of revenue volatility associated with water treatment projects and thus increase predictability in our business model. With three strong business pillars, the Corporation is very well balanced and not dependent on a single source of revenues", **stated Frédéric Dugré, President and Chief Executive Officer of H_2O Innovation.**

For this third quarter, 40.9% of the revenues came from O&M activities, 40.5% of the revenues came from the SP&S and 18.6% came from water treatment projects. "As our project backlog enters into manufacturing phase, we expect to see our revenues coming from this pillar in the neighborhood to 25% to 30%", **added Mr. Dugré**. The consolidated backlog as of March 31, 2017 stood at $117.1 M, with $56.7 M coming from our projects business pillar and $60.4 M from the O&M activities.

Revenues from water treatment projects have declined momentarily to $4.0 M compared to $4.8 M in the corresponding period of the previous fiscal year, representing a 17.0% decrease. This is not unusual since revenues from water treatment projects vary from quarter to quarter and depends on the different milestones

[1] The definition of adjusted earnings before interest, tax depreciation and amortization (adjusted EBITDA) does not take into account the Corporation's finance costs – net, stock-based compensation costs, gain on purchase price adjustment, unrealized exchange (gains) / losses and acquisition and integration costs. See reconciliation of this non-IFRS measure below. The definition of adjusted EBITDA used by the Corporation may differ from those used by other companies.

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reached for revenue recognition. Over the last twelve months, revenues for projects reached $17.9 M, which represent a decrease of 27.8% decrease compared to the previous twelve months, where revenues were at $24.8 M. This decrease is explained by the fact that the nature of projects has changed. The actual water treatment projects backlog consists of municipal projects that have a more extensive engineering phase, which phase generates less revenue under the revenue recognition accounting method and this phase tends to spread out over longer periods than what we were used to with our past projects. Once projects are entering into the manufacturing phase, it allows recognition of significantly more revenues as fabrication and assembly moves forward. Also, project execution is sometimes postponed due to situations outside of the control of the Corporation, and therefore impacts revenue recognition.

Even though revenues are slower and lumpy, the water treatment projects are still a growth vehicle of the Corporation. The water treatment projects order backlog stood at $56.7 M as at March 31, 2017, compared to $42.1 M a year ago, representing a 34.7% increase over the last twelve months. The increase of bookings is not converting into revenue growth at the same pace, due to the longer period of execution per contract. “Since July 1st 2016, we secured $20.9 M in bookings, with a current pipeline of water treatment projects rich in opportunities, which should allow the Corporation to continue to increase its project order backlog and support its revenue growth. We maintain strong bidding activities and business development mainly in Canada and in United States”, **added Mr. Dugré.**

Revenues from SP&S reached $8.6 M compared to $9.4 M in the comparable quarter of the previous fiscal year. Even though it is a decrease of 8.5% compared to the same quarter last year, it is the second best quarterly result of the Corporation’s history for the SP&S pillar. Over the last twelve months, revenues reached $28.1 M, which represents an increase of 6.3% compared to the previous twelve months where revenues were at $26.6 M. This increase in SP&S revenues is the direct result of investments made during the last few years in our operating and selling functions to support the growth of this business line.

Revenues coming from O&M amounted to $8.7 M. These revenues are recurring sales and came mainly from the recently acquired Utility Partners. The backlog related to these O&M contracts stood at $60.4 M as at March 31, 2017 and consists of long-term contracts, mainly with municipalities, which contain multi-year renewal options. The backlog increased by $5.5 M in this quarter, from $54.9 M as at December 31, 2016 to $60.4 M as at March 31, 2017.

In this third quarter of fiscal year 2017, the Corporation generated a 23.8% gross profit before depreciation and amortization, a lower level than the 31.8% gross profit before depreciation and amortization generated in the third quarter of fiscal year 2016. The revenue mix has been modified with the acquisition of Utility Partners which operates in a different model than our previous core activities. Indeed, O&M activities generally generates lower gross margin. Therefore, the integration of Utility Partners into H_2O Innovation, which in this quarter represents 40.9% of the total revenues, puts pressure on the overall gross margin of the Corporation, although increasing the predictability and stability of the financial results, and ultimately profitability.

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CONSOLIDATED RESULTS **Selected financial data**	**Three-month periods ended on March 31, (Unaudited)**		**Nine-month periods ended on March 31, (Unaudited)**	
	2017	2016	**2017**	2016
	$	$	**$**	$
Revenues	**21,284,643**	14,199,860	**61,111,336**	39,624,778
Gross profit before depreciation and amortization	**5,060,641**	4,522,640	**14,358,617**	11,853,728
Gross profit before depreciation and amortization	**23.8%**	31.8%	**23.5%**	29.9%
Operating expenses	**523,721**	356,160	**1,448,128**	1,009,026
Selling expenses	**1,975,348**	1,679,681	**5,186,872**	4,648,798
Administrative expenses	**2,307,189**	1,289,659	**6,300,002**	3,521,379
Research and development expenses – net	**16,075**	24,126	**131,319**	144,300
Net (loss) earnings	**(1,345,695)**	646,422	**(3,521,051)**	872,972
Basic and diluted (loss) earnings per share	**(0.034)**	0.031	**(0.104)**	0.042
Adjusted EBITDA	**411,737**	1,245,324	**1,850,377**	2,717,600
Adjusted EBITDA over revenues (%)	**1.9%**	8.8%	**3.0%**	6.9%

The Corporation's ratio of selling, operating and administrative expenses ("SG&A") as a whole over revenues amounted to 22.6% for this quarter, down from 23.4% for the corresponding quarter of the previous fiscal year. This decrease is mostly attributable to the acquisition of Utility Partners in July 2016 which increased the overall revenues without impacting proportionally the selling and operating expenses.

Adjusted EBITDA for the quarter was recorded at $411,737, compared with $1,245,324 for the same period ended March 31, 2016. The adjusted EBITDA over revenues represents 1.9%, compared to 8.8% for the same quarter in fiscal year 2016. The decrease in the adjusted EBITDA over revenues ratio is essentially due to the lower volume coming from revenues of water treatment projects. Moreover, the shift in product mix and the addition of Utility Partners results impacted negatively the overall gross margin, decreasing the adjusted EBITDA. Once the volume of revenues will increase, the Corporation expects this percentage to increase accordingly since all the fixed charges are already covered.

The net loss amounted to ($1,345,695) or ($0.034) per share for the third quarter of fiscal year 2017 compared with net earnings of $646,422 or $0.031 per share for the third quarter of fiscal year 2016. The net loss is largely due to the acquisition of Utility Partners and the related acquisition and integration costs and to a higher level of SG&A expenses, aimed to support the constant growth of the Corporation.

Operating activities used ($1,135,127) in cash for the three-month period ended March 31, 2017, compared with ($318,078) of cash used during the corresponding period ended March 31, 2016. The increase is mostly due to the net loss before income taxes generated during this quarter, to the addition of Utility Partners, and the increase in non-cash items.

Reconciliation of adjusted EBITDA to net (loss) earnings

Even though adjusted EBITDA is a non-IFRS measure, 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 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,	
	2017	2016	**2017**	2016
	$	$	**$**	$
Net (loss) earnings for the period	**(1,345,695)**	646,422	**(3,521,051)**	872,972
Finance costs – net	**328,485**	233,260	**984,780**	597,514
Income taxes	**(189,262)**	205,077	**(580,855)**	417,930
Depreciation of property, plant and equipment	**191,850**	175,192	**548,314**	447,178
Amortization of intangible assets	**1,272,620**	276,852	**2,774,142**	744,957
Gain on purchase price adjustment	**-**	-	**-**	(375,977)
Unrealized exchange loss	**(59,586)**	(292,260)	**118,282**	(35,173)
Acquisition and integration costs	**45,867**	781	**1,066,696**	48,199
Stock-based compensation costs	**167,458**	-	**460,069**	-
Adjusted EBITDA	**411,737**	1,245,324	**1,850,377**	2,717,600

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 financial results for 2017 third quarter in further details at 10:00 a.m. (EDT) on Monday, May 15, 2017.

To access the call, please call (877) 223-4471 or (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 and 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 concern analysis and other information based on forecast future results, performance and achievements and the estimate of amounts that cannot yet be determined. Forward-looking statements include the use of words such as "anticipate", "if", "believe", "continue", "could", "estimate", "expect", "intend", "may", "plan", "potential", "predict", "project", "should" or "will", and other similar expressions, as well as those usually used in the future and the conditional, notably regarding certain assumptions as to the success of a venture. Those forward-looking statements, based on the current expectations of management, involve a number of risks and uncertainties, known and unknown, which may result in actual and future results, performance and achievements of the Corporation to be materially different than those indicated. Information about the risk factors to which the Corporation is exposed is provided in the Annual Information Form dated September 26, 2016 available on SEDAR (www.sedar.com). 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 pillars which are i) water and wastewater projects; ii) specialty products and services, including a complete line of specialty chemicals, consumables, specialized products for the water treatment industry as well as control and monitoring systems; and iii) operation and maintenance services for water and wastewater treatment systems For more information, visit www.h2oinnovation.com.

Neither TSX Venture Exchange nor its Regulation Services Provider (as that term is defined in the policies of the TSX Venture Exchange) nor the Alternext Exchange accepts responsibility for the adequacy or accuracy of this release.

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