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H_2O Innovation's 2019 Second Quarter Results - Hays' Acquisition in Texas Integrated to our Business Model Strives for Additional Recurring Revenues and Synergies

Key highlights

- Sustained revenue growth of $3.6 M, or 13.8% over the same period of the previous fiscal year, reaching $29.4 M for the second quarter of fiscal year 2019;
- Recurring revenues from Aftermarket, Specialty Products and Operation & Maintenance ("O&M"), representing 70.8% of total revenues;
- Selling, operating and administrative expenses ("SG&A") decrease to 16.7% for the second quarter of fiscal year 2019, from 18.8% for the same quarter of the previous fiscal year;
- Consolidated backlog, combining Projects and O&M business pillars, stood at $147.7 M as of December 31, 2018, compared to $116.1 M for the period ended December 31, 2017;
- Adjusted EBITDA[1] of $1.4 M, or 4.7% over revenues, during the second quarter of fiscal year 2019;
- Net loss decreased by $0.1 M to reach ($1.2 M) for the second quarter of fiscal year 2019, from a net loss of ($1.3 M) for the same quarter of the previous fiscal year;
- Adjusted net loss[2] stood at ($0.3 M) for the second quarter of this fiscal year, compared to an adjusted net loss of ($0.8 M) for the same quarter of the previous fiscal year.

All amounts in Canadian dollars unless otherwise stated.

Quebec City, February 13, 2019 – (TSXV: HEO) – H_2O Innovation Inc. ("H_2O Innovation" or the "Corporation") announces its results for the second quarter of fiscal year 2019 ended December 31, 2018. Revenues for the second quarter of fiscal year 2019 amounted to $29.4 M, representing a $3.6 M, or 13.8% increase, as compared with revenues of $25.8 M recorded for the second quarter of the previous fiscal year. This increase is partially fueled by the acquisition of Hays Utility South Corporation ("Hays"), as well as the organic growth from the Projects & Aftermarket and O&M business pillars. The Projects & Aftermarket business pillar is showing a revenue increase of $2.2 M, or 21.9%, while having a healthier backlog with better projects' diversification. The Corporation will focus on improving its gross profit margin before depreciation and amortization in this business pillar prior to focusing on growing the volume of revenues. Therefore, to reach that goal, H_2O Innovation is executing more industrial and wastewater projects previously secured in the backlog and is observing positive upside in the gross profit margins being recorded. Specialty Products business pillar is showing a momentary decrease of $1.6 M, or 21.4% of revenues, for the second quarter of fiscal year 2019 compared to the same quarter of the previous fiscal year. This decrease is partially explained by delays beyond Corporation's control in delivering significant orders of couplings for recurring customers. Specialty Products business pillar's revenue was also impacted by a general slowdown in the maple syrup industry due to adverse weather conditions

[1] The definition of adjusted earnings before interest, taxes, depreciation and amortization (adjusted EBITDA) does not take into account the Corporation's finance costs – net, stock-based compensation costs, net loss on bank fraud, unrealized exchange (gains) / losses and acquisition and integration costs. The reader can establish the link between adjusted EBITDA and net earnings. The definition of adjusted EBITDA used by the Corporation may differ from those used by other companies.

[2] The definition of adjusted net earnings (loss) excludes acquisition-related costs and integration costs. The definition of adjusted net earnings (loss) used by the Corporation may differ from those used by other companies.

during the last maple syrup season. As a result, maple syrup producers have experienced a challenging year resulting in a lower production, thus lowering the investments they can spend in new capital equipment purchase. As for PWT, our specialty chemicals product line, the Corporation increased its in-house manufacturing capacity of liquid cleaners. This manufacturing improvement, along with the addition of new distributors in strategic territories, enabled the increase of the Corporation's gross profit margin before depreciation and amortization. Regarding Piedmont's operations, the bookings of new couplings and filter housings orders have reached a new high at the end of the second quarter, as explained in the press release of January 31, 2019. However, most of the revenues from these large orders have not been recognized in this current quarter. The O&M business pillar is showing a constant growth, with a revenue increase of $3.0 M, or 35.2%, during the second quarter of fiscal year 2019, compared to the same quarter of the previous fiscal year. This significant revenue growth is explained by a sustained organic growth mostly driven by scope of work increases on existing projects, and the acquisition of Hays, adding $1.5 M of revenues to this business pillar for the second quarter of fiscal year 2019.

"We are already seeing upsides from the acquisition of Hays in Texas completed on December 1, 2018. Indeed, additional revenues are impacting positively this quarter's results and cross-selling synergies have been targeted for the coming quarters. Our $147.7 M combined backlog is not only providing visibility on revenues but is an unbelievable source of additional sales synergies generated by our multiple product lines. With proper business mix, combining Projects & Aftermarket, Speciality Products and O&M, I am confident to see an improvement in our gross profit margin and thus our EBITDA's performance", **stated Frédéric Dugré, President and Chief Executive Officer of H_2O Innovation.**

(in thousands of Canadian dollars, except per share data)	**Three-month periods ended December 31, 2018**	2017	**Six-month periods ended December 31, 2018**	2017
	$	$	**$**	$
Revenues	**29,378**	25,819	**53,749**	48,437
Gross profit margin before depreciation and amortization	**6,244**	6,213	**11,750**	10,667
Gross profit margin before depreciation and amortization (%)	**21.3%**	24.1%	**21.9%**	22.0%
Operating expenses	**1,246**	1,009	**2,574**	1,886
Selling expenses	**1,990**	2,218	**3,637**	3,856
Administrative expenses	**1,671**	1,625	**3,072**	3,112
Total SG&A	**4,907**	4,852	**9,283**	8,854
% SG&A over revenues	**16.7%**	18.8%	**17.3%**	18.3%
Net loss	**(1,212)**	(1,341)	**(1,535)**	(2,431)
Basic and diluted net loss per share	**(0.027)**	(0.033)	**(0.036)**	(0.061)
Adjusted net loss [(a)]	**(343)**	(783)	**(14)**	(842)
Basic and diluted adjusted net loss per share	**(0.008)**	(0.020)	**(0.000)**	(0.023)
EBITDA [(a)]	**910**	1,227	**2,005**	1,349
Adjusted EBITDA[(a)]	**1,377**	1,358	**2,643**	1,946
Adjusted EBITDA over revenues (%)	**4.7%**	5.3%	**4.9%**	4.0%

(a) Non-IFRS financial measurement reconciled below.

Revenues from Projects & Aftermarket stood at $11.9 M compared to $9.7 M in the corresponding period of the previous fiscal year, representing a 21.9% increase. The Corporation developed a more diversified backlog portfolio between water and wastewater projects, with 32.7% of the projects being in the field of wastewater as of December 31, 2018, compared to 34.0% as of December 31, 2017. Diversification is also seen between industrial and municipal projects, with 38.8% of the projects for industrial customers as of December 31, 2018, compared to 23.0% as of December 31, 2017. Both wastewater and industrial projects are characterized by better gross profit margins. The current Projects' pipeline remains very rich in opportunities and, as of December 31, 2018, the backlog stood at $52.5 M, compared to $51.9 M for the comparable quarter of fiscal year 2018.

On the Specialty Products side, recurring revenues stood at $5.9 M, compared to $7.5 M in the comparable quarter of the previous fiscal year, representing a $1.6 M, or 21.4% decrease. The decrease in revenue for this business pillar is attributable to timing of significant orders related to Piedmont, which were delayed by the customers. It was also impacted by a general slowdown in the maple syrup industry, due to adverse weather conditions during the last maple season. Specialty Products business pillar expanded its products offering by adding new products and new distributors, broadening its existing offering and positioning the Corporation strategically in the market. The Corporation continues to improve its gross profit margin before depreciation and amortization by manufacturing some products in-house, while the manufacturing of these products was fully outsourced during the comparable quarter of the previous fiscal year.

The recurring revenues coming from O&M business pillar stood at $11.6 M for the second quarter of fiscal year 2019, compared to $8.6 M for the comparable period of fiscal year 2018, representing an increase of $3.0 M or 35.2%. Of this increase, $1.5 M is attributable to the acquisition of Hays and represents revenues for the one-month period following the acquisition's effective date. The growth of the O&M business pillar during this quarter is also explained by the renewal of projects and scope expansions, as well as annual consumer price index ("CPI") adjustments. The backlog coming from O&M contracts stood at $95.2 M as at December 31, 2018, representing an increase of 48.3% compare to the $64.2 M backlog as at December 31, 2017, and consists of long-term contracts, mainly with municipalities, comprising multi-year renewal options.

In this second quarter of fiscal year 2019, the Corporation generated a 21.3% gross profit margin before depreciation and amortization compared to 24.1% for the second quarter of fiscal year 2018. The gross profit margin before depreciation and amortization was fairly stable at $6.2 M, while revenues increased by 13.8%. This decrease of gross profit margin before depreciation and amortization in % is explained by the business mix, with an increase of the sales coming from the O&M business pillar characterized by lower margins but steadier revenues and profits. Lower revenues coming from the Specialty Products business pillar also impacted negatively the gross profit margin before depreciation and amortization in % since this business pillar is characterized by a higher gross profit margin before depreciation and amortization.

The Corporation's selling, operating and administrative expenses ("SG&A") in dollar remained stable at $4.9 M this quarter and for the comparable quarter of the previous fiscal year. The SG&A over revenues in % decreased to 16.7%, compared to 18.8% for the second quarter of the previous fiscal year. This decrease is explained by a stable level of SG&A expenses, while revenues grew by 13.8% over the same period.

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The Corporation's adjusted EBITDA was stable at $1.4 M for the second quarter of fiscal year 2019 and for the comparable period of fiscal year 2018. The Corporation's adjusted EBITDA over revenues decreased to 4.7% for the three-month period ended December 31, 2018, compared to 5.3% for the same quarter of last fiscal year. The decrease of the adjusted EBITDA in % is due to a decrease of the gross profit margin before depreciation and amortization, associated to a lower level of revenues having higher gross profit margins and coming mainly from the Specialty Products business pillar.

The net loss amounted to ($1.2 M), or ($0.027) per share, for the second quarter of fiscal year 2019 compared with a loss of ($1.3 M), or ($0.033) per share, for the comparable quarter of fiscal year 2018. The net loss of the comparable quarter of the previous fiscal year was significantly impacted by the Tax Cuts and Jobs Act, a tax legislation reducing the federal tax rate enacted by the U.S. government and leading to an additional deferred tax expense of $1.1 M for that quarter. Without the $1.1 M impact from the new U.S. tax legislation, net loss for the second quarter of fiscal year 2018 would have been ($0.2 M). This quarter, the net loss is mostly due to an increase of non-recurring costs associated with the acquisition of Hays and the related financing, amounting to $0.4 M and $0.3 M respectively. Furthermore, the decrease of the gross profit margin before depreciation and amortization also contributed to the net loss.

The definition of adjusted net earnings (loss) excludes of acquisition-related costs and integration costs. The reader can establish the link between net loss and adjusted net earnings (loss) with the following reconciliation items. The definition of adjusted net earnings (loss) used by the Corporation may differ from those used by other companies.

	Three-month periods ended December 31,		**Six-month periods ended December 31,**	
(in thousands of Canadian dollars)	**2018**	2017	**2018**	2017
	$	$	**$**	$
Net loss	**(1,212)**	(1,341)	**(1,535)**	(2,431)
Acquisition-related costs, integration costs and other costs USA (net of tax 23.71%)	**307**	-	**333**	-
Net loss on bank fraud Canada (net of tax 0%)[3]	**-**	-	**-**	363
Amortization of intangible assets from acquisition Canada (net of tax 0%)[3]	**39**	39	**79**	79
Amortization of intangible assets from acquisition USA (net of tax 23.71%)	**448**	413	**951**	821
Stock based compensation expenses Canada (net of tax 0%)[3]	**75**	106	**158**	226
Adjusted net loss	**(343)**	(783)	**(14)**	(942)

Operating activities generated $2.1 M in cash for the quarter ended December 31, 2018, compared to $0.6 M of cash generated during the same period of previous fiscal year. The cash flow increase generated by operating activities is a reflection of the change in the working capital items. This change is mostly due to the advancement of major projects, for which significant invoicing milestones have been reached during the quarter.

[3] For Canada the tax rate is 0% since the Corporation does not recognise the deferred tax asset.

Reconciliation of net loss to adjusted EBITDA

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 the management, and to better understand the financial performance, notwithstanding the impact of GAAP measures.

	Three-month periods ended December 31,		Six-month periods ended December 31,	
	2018	2017	**2018**	2017
	$	$	**$**	$
Net loss for the period	**(1,212)**	(1,341)	**(1,535)**	(2,431)
Finance costs – net	**969**	473	**1,500**	824
Income taxes	**72**	1,177	**(19)**	1,039
Depreciation of property, plant and equipment	**288**	243	**567**	550
Amortization of intangible assets	**793**	675	**1,492**	1,366
EBITDA	**910**	1,227	**2,005**	1,348
Unrealized exchange (gains) losses	**(11)**	25	**44**	(73)
Stock-based compensation costs	**75**	106	**158**	226
Net loss on bank fraud	**-**	-	**-**	363
Acquisition-related costs, integration costs and other costs	**403**	-	**436**	81
Adjusted EBITDA	**1,377**	1,358	**2,643**	1,945

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 2019 second quarter in further details at 10:00 a.m. Eastern Time on Wednesday, February 13, 2019.

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 second 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 concern analysis and other information based on forecast future results and the estimate of amounts that cannot yet be determined. 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. Those forward-looking statements involve a number of risks and uncertainties, which may result in actual and future results 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 25, 2018 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 and services; ii) specialty products, which include a complete line of maple equipment and products, specialty chemicals, consumables and specialized products for the water treatment industry; and iii) operation and maintenance services for water and wastewater treatment systems and utilities. For more information, visit www.h2oinnovation.com.

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