

LIQTECH INTERNATIONAL, INC.
NYSE American: LIQT



Investor Update Conference Call

Monday, January 14, 2019
9:00 a.m. Eastern

CORPORATE PARTICIPANTS

Sune Mathiesen – Chief Executive Officer, LiqTech International
Robert Blum – Managing Partner, Lytham Partners

PRESENTATION

Operator

Good morning and welcome to the LiqTech International Investor Update Call. All participants will be in listen-only mode. Should you need assistance, please signal a conference specialist by pressing the star (*) key followed by zero (0). After today's presentation there will be an opportunity to ask questions. To ask a question, you may press star (*) then one (1) on your telephone keypad. To withdraw your question, please press star (*) then two (2). Please note this event is being recorded.

I would now like to turn the conference over to Robert Blum. Please go ahead.

Robert Blum

Thanks so much, Brandon. Good morning everyone and thank you for joining us today as LiqTech International provides an update to investors. As the operator indicated, I am Robert Blum with Lytham Partners, and I will be your moderator for today's call. Joining us on today's call from the Company is CEO Sune Mathiesen. Before I turn the call over to Sune, let me remind listeners that following the conference call there will be an open Q&A session. You should also note that a replay of this call will be available shortly following the conclusion of this live call and that a transcript of the call will be made available on the Investor Relations section of the Company's website.

Before we begin with prepared remarks, we submit for the record the following statement. This conference call may contain forward-looking statements. Although the forward-looking statements reflect the good faith and judgment of management, forward-looking statements are inherently subject to known and unknown risks and uncertainties that may cause actual results to be materially different from those discussed during the conference call. The Company, therefore, urges all listeners to carefully review and consider the various disclosures made in the reports filed with the Securities and Exchange Commission, including risk factors that attempt to advise interested parties of the risks that may affect the Company's business, financial condition, and sales of operations and cash flows. If one or more of these risks or uncertainties materialize or if the underlying assumptions prove incorrect, the Company's actual results may vary materially from those projected or expected. The Company, therefore, urges all listeners not to place undue reliance on these forward-looking statements, which speak only as of this



date and the date of the press release and conference call. The Company assumes no obligation to update any forward-looking statements in order to reflect any events or circumstances that may arise after the date of this release and conference call.

Now, I'd like to turn the call over to Sune, CEO of LiqTech International. Sune, please proceed.

Sune Mathiesen

Thank you very much, Robert, and good day to all of you. Thank you very much for joining us today on this investment update call. It has now been two months since we had our last conference call, and I'm very pleased to have this opportunity today to discuss our progress and the near- and longer-term outlook for our business.

As you can see from the press release this morning, we made tremendous progress during the quarter. It is still early stages in the marine scrubber industry, but the interest for our standardized water treatment systems continues to increase. Our sales pipeline continues to grow day by day, and we're continuing to form new relationships with scrubber manufacturers and ship owners. More importantly, we're building a very healthy backlog, and I'm pleased to report that we now have confirmed orders for more than 110 systems. This is a significant increase from the more than 50 systems backlogged we reported in mid-November 2018. We are very pleased with the progress we have made so far, and the current activity in the market leads us to believe that we'll continue to see a strong order intake in the coming quarters.

In addition to the current backlog, we also expect to deliver a significant number of systems in 2019 under the framework agreement we signed in October 2018. Based on fulfillment of orders from our current backlog, we'll still expect the first quarter to be a record for the Company. We also still expect to be solidly profitable in the first quarter and onwards. Based on our backlog and visibility we have, we believe that the second quarter is likely to surpass the first quarter of 2019 and set another record for the Company.

Overall, we are very pleased with our progress so far. I would like to emphasize that this is still early stages in the marine scrubber industry and that we are continuing to see a ramp in this industry. We believe that this ramp will continue in the years to come. We have been building a strong market position for more than four years now, and we have strong relationships with leading scrubber manufacturers, and we believe that our world-proven system offers a very attractive solution in terms of both Capex and Opex. We believe that we have been increasing our market share in this industry, and we will continue to use our first mover advantage to stay ahead of any competition.

I get a lot of questions about the difference between an open-loop scrubber and a closed-loop scrubber, and I would like to take a few moments to explain this difference. A scrubber is a device that will spray water containing a solution of reagents over the emissions from diesel engines. By that, it will capture harmful substances and contain them in the water. In open-loop scrubbers, the water will be dumped into the sea, including the harmful substances.

In a closed-loop scrubber, there will be a water treatment system which will separate the harmful particles from the water and allow the now clean water to be discharged into the sea or reused in the process. Some scrubber systems are capable of operating in both open loop and closed loop, which means that they have a water treatment system. These scrubbers are called hybrid scrubbers.

FINAL TRANSCRIPT

Transcript Provided by Chorus Call Teleconferencing

Up until this point, the vast majority of scrubbers ordered and installed have been open-loop or hybrid ready. This has always been bad news for the environment, and the industry has been expecting a ban against open-loop scrubbers to be implemented at some point. Last week, China banned the use of open-loop scrubbers following the ban that Singapore implemented late last year. To date, most of our orders came from some of the largest ship owners in the world who knew that this would happen at some point. We believe that actions from China and Singapore will lead others to follow and drive and further rise the demand for water treatment systems for closed-loop and hybrid scrubbers. Recent customer activity leads us to believe that this is already happening.

I'm sure you can all imagine that we are keeping very busy these days. We're experiencing great ramp in our business and we are busy ramping up staff and manufacturing capacity. First of all, let me assure you that we are on track to meet all scheduled deliveries in the first and second quarters. Most of the systems manufacturing has been outsourced, and we have operated our testing facilities to meet the increase in demand. As previously discussed, we have taken steps to increase our membrane manufacturing capacity. I'm happy to report that we are on schedule to more than double this capacity by the end of the third quarter 2019. This will be the first step in the larger plan to increase and improve our membrane manufacturing facility.

We have also taken steps to increase our systems manufacturing capacity. We will more than double our manufacturing and office space and will be improving our testing and laboratory facilities. This expansion will be done without any Capex spending. Our working capital position remains a strong focus for us. We have positioned ourselves as efficiently as possible from a working capital perspective. The systems manufacturing has now been completely outsourced, and we have been successful in negotiating better terms with our key suppliers. This provides us with a good cash flow profile in our system orders.

Even though our headcount has increased due to the ramp in our business, and even though we have been busy manufacturing systems for delivery in the first quarter, I'm pleased to report that our cash balance at the end of December 2018 was \$3.8 million. This is largely unchanged since the end of June 2018. We believe that this is a great accomplishment.

As earlier mentioned, we expect to be solidly profitable in the first quarter and onwards, and we will continue our work to manage cash flow and optimize terms with our customers and suppliers. We plan to continue to provide investors with an update on the traction we are achieving sometime between our quarterly conference calls. We will not issue a press release on every new order we receive but will instead look to provide a bit of a recap sometime throughout the quarter. Our next conference call is likely to be in March when we announce our 2018 results.

2019 is starting off to be a great year for LiqTech. We have a great sales pipeline, a great backlog of orders, great employees and suppliers, and importantly, great and loyal customers. The interest for our product continues to build day by day, and recent developments in the industry gives us reason to believe that we are carving a path for continued growth and profitability in 2019 and the years to come. I want to thank every one of you for your continued support of LiqTech.

Having said that, let me now turn the call over to any questions you might have. Operator, please.



QUESTIONS AND ANSWERS

Operator

Thank you. We will now begin the question-and-answer session. To ask a question you may press star (*) then one (1) on your telephone keypad. If you are using a speakerphone, please pick up your handset before pressing the keys. To withdraw your question, please press star (*) then two (2). At this time, we will pause momentarily to assemble our roster. Our first question comes from Eric Stine with Craig-Hallum. Please go ahead.

Eric Stine

Hi Sune. Thanks for taking the questions.

Sune Mathiesen

Good morning, Eric.

Eric Stine

Good morning. So, maybe just starting with the 110+ orders that you've got in hand right now, I'm just curious. Are you able to break those down between the two, the initial framework customers and some of the other OEMs that you are working with?

Sune Mathiesen

Yes, we can do that. So, we signed two framework agreements in the spring of 2018, and I would say approximately half of what we have in the backlog right now comes from those two framework agreements. The other half comes from customers outside the framework agreements and in addition to all of this, we have the framework agreement we signed in October last year from which we also expect to see a significant number of systems in 2019.

Eric Stine

Got it. And the, I mean, is it fair, I know that the framework agreements, they were targeting delivery of a greater number than what you've got in hand right now by the end of 2019. Is it fair to think about these 110+ that a good portion of those are for 2019 delivery?

Sune Mathiesen

That would be a fair assumption, yes.

Eric Stine

Okay, good. And then maybe just on the third framework agreement that you mentioned and just to confirm, those are still the smaller systems. I think last time you had sized that at, you know, potentially 80 to 100 systems a year. Is that still the way that we should think about that opportunity and just any thoughts on when, I know you're not going to announce them when you get them, but when you might start to see the initial orders for that opportunity?

Sune Mathiesen

We think we'll see meaningful revenue come out of that agreement from the third quarter this year, and we think we are on track to book the orders that we are anticipating. Revenue wise, some of that might fall into 2020, though. But again, meaningful revenue should start to come out that agreement by the third quarter of this year.

Eric Stine

Okay. Got it. Then maybe just talk about the representative order size. It would seem, given the trajectory you're on, you're certainly beyond the ones and twos and maybe at the fives to tens, but maybe is that what you see now and when do you think that you start to see the industry or the orders you're getting taking that next step?

Sune Mathiesen

We think that we have already gone to that next step. You're absolutely right, we're away from the one and twos. We are now seeing bulk orders, and what the ship owners typically do is that they take a certain class ships that they own. So, they might own 10, 15 identical ships and they would order scrubbers for all of these ships at the same time. And, that's starting to happen now. I would, however, like to remind everyone that this is just the beginning. This is, this market is just forming. It's early stages. We have seen a significant amount of orders being placed and a few of them have yet installed. We have this new development with closed-loop versus open-loop scrubbers. We have seen a ban in China and Singapore. We think that others will follow. And, it actually means that some of the open-loop scrubbers that have already been ordered are likely to be upgraded to closed-loop scrubbers even before they are commissioned. So, early stages still, but we're definitely away from the one and twos.

Eric Stine

Got it. Thank you very much.

Sune Mathiesen

Thanks, Eric.

Operator

As a reminder, if you would like to ask a question, please press star (*) then one (1).

Our next question comes from Rob Brown with Lake Street Capital Markets. Please go ahead.

Rob Brown

Good morning, Sune.

Sune Mathiesen

Good morning, Rob.

Rob Brown

In terms of the 110 units, could you give us a sense of the cadence on how that's delivered? Is that erratically throughout the year or is there some frontend loading or backend loading to that?

Sune Mathiesen

Ah, yes. The vast majority of it is for delivery in 2019 and it looks like this could be a continuous ramp throughout the year. What we know at this stage is that we're looking into a record first quarter. It looks like the second quarter will be another record for the Company, but we're trying to just take it quarter by quarter and reach the first goal lines, which is really a successful first quarter, a record quarter, a profitable quarter, and then we'll start looking into the coming quarters. But our backlog is filling up and we think we could book more orders for 2019 but it does look to be [unintelligible].



**Rob Brown**

Okay, great. And, then in terms of capacity, what's your current capacity and then maybe some further color on the new furnaces being ordered. When do they get delivered and how does that play out?

Sune Mathiesen

Yeah, so we have this current capacity of about between 230 to 250 sequence. We are ramping-up capacity. We are on track to increase capacity by end of the third quarter this year. We are more than doubling our capacity by then and this is kind of the first step in a larger plan to further increase our capacity over the coming years and also do some upgrades in the way that are manufacturing the membranes to ensure that we have an even better and more consistent quality. So, it's a lot of things going on in our membrane manufacturing facility, and they will be significantly changed a year from now.

Rob Brown

Okay, good. And, then last question. You mentioned a little bit about China banning open-loop scrubbers. What's the dynamics in the market? Do people look at that and say, when you get enough countries banning it then no one buys open loop at that point, or, what's the dynamics that have changed in terms of the order rates of water treatment systems?

Sune Mathiesen

Yeah, so the orders we have booked so far, they have come from some of the world's largest ship owners. And the reason for that is they have always expected such a ban to come in place and they would much rather, you know, be first movers and make sure they get the right equipment installed the first time and not have to go in and retrofit water treatment to convert the scrubber into a closed-loop scrubber. So, they have been first movers for closed-loop.

Where again some of the smaller ship owners, they have taken the short cuts. Maybe they knew that there would be a ban at some point of open-loop scrubbers but for now they just wanted to be compliant and get a scrubber installed.

For us and for the environment, it's great news to see that China and Singapore have moved ahead and implemented this ban against open-loop marine scrubbers and we think that other countries will follow and we actually believe that in the longer time open-loop scrubbers will be entirely banned. So, a great step for the environment and obviously a great step for LiqTech. Right now, we have more than enough to deal with the orders we have from the large ship owners, and I'm sure that we'll see a further ramp in closed-loop scrubbers following these bans.

Rob Brown

Okay, great. Thank you. I'll turn it over.

Sune Mathiesen

Thanks, Rob.

Operator

Again, if you have a question please press star (*) then one (1).

Our next question comes from Andrew Lester with Harla Capital. Please go ahead.

Andrew Lester

Hi. Thank you for your update and congratulations on the continued strong build in your book. What I'd like to understand in following things is I know there's a certain amount of capital required as you grow your pipeline and I just wondered in light of the cash balance, which does remain the same but sort of relatively modest compared to the build you have, whether there's going to be or an expected need for additional capital, a capital raise or line of credit in light of the growth of your business? Thank you.

Sune Mathiesen

Yeah, thank you for that question. So, what we report now is that our cash balance at end December last year was about \$3.8 million, which is by the way largely unchanged since June 2018. So, we have been more or less cash flow neutral for six months. We also know by now that the first quarter will be solidly profitable, which we expect to be a trend for the future. So, we will be adding to that cash position.

What we have been doing and that's really a continuous, what we have done over the past 12 to 24 months is to negotiate better terms with our suppliers so we had quite good, great terms with our suppliers. We are quite strict on collecting upfront payments from our customers as well, and progress payments. So, it actually means that each and single one of these projects are at a very nice cash flow profile. It also allows us to grow our business quite substantially on the cash balance that we have today. So, we do not have the expectation to raise capital in 2019.

Andrew Lester

Thank you very much.

Sune Mathiesen

Thank you.

Operator

Our next question comes from James Gerson, an investor. Please go ahead.

James Gerson

Well, congratulations and thank you for the update. My question is are you starting to see any competitive filters available in the marketplace and any other alternatives?

Sune Mathiesen

Yes, good morning, James. There was, as we have discussed in the past that we have seen some, let's say smaller filtration companies trying to break into this industry. We think that we have been building market share over the past six months. We see that we have been successful in outperforming high-speed sensor futures, in some cases, so we are not too concerned at this point. We have certainly been first movers in this industry. We've been building solid relationships to a number of ship owners, to a number of scrubber manufacturers, and so far, it looks like we have a very, very healthy market share and we anticipate adding to that.

James Gerson

Thanks.



**Sune Mathiesen**

Thank you.

Operator

Again, if you have a question please press star (*) then one (1). Our next question comes from Keith Schaefer with Oil and Gas Investments Bulletin. Please go ahead.

Keith Schaefer

Thank you. Sune, I'm just curious, is there much of a sales cycle difference between the ship owners and the scrubber manufacturers? And, is there any incentive difference there amongst the various customers that would be notable for your sales cycle?

Sune Mathiesen

Yes, good morning, Keith. What we think is that it is very attractive to install the scrubber. A lot of initiatives around the world to help ship owners to make the decision to install the scrubber are we have seen financing programs put in place by several banks and countries. So, yes, there are initiatives in place that would motivate ship owners to invest in scrubbers.

Keith Schaefer

So, okay, so what I'm hearing you not say is that there really isn't that much difference in either incentive or sales cycle between any of the different customers that you've got, whether it's direct to shippers or the scrubbers or anybody else.

Sune Mathiesen

No, there is not. The same cycle is pretty similar.

Keith Schaefer

Okay. Thank you so much. That's it.

Sune Mathiesen

Thanks, Keith.

Operator

Our next question comes from Andy Preikschat with Edgebrook Partners. Please go ahead.

Andy Preikschat

Yes, congrats on the recent progress. Just to clarify, the 110 confirmed orders, that's for the main product lines, not for the new products, smaller product that was under the October 1 framework agreement.

Sune Mathiesen

No, that is confirmed. So, the October framework agreement comes in addition to that number.

Andy Preikschat

Okay, great. I've seen companies that ramp-up their manufacturing sometimes have quality problems, so I was wondering what quality initiatives that you're putting in place like ISO 9000 to make sure that you have the proper quality in your manufacturing.

Sune Mathiesen

Yeah, so we have been in business for nearly 20 years now, which is really an advantage for us in ramping our business now. We have been ISO 9000 certified for a very long time, so we have systems in place for quality control, supplier relations, stuff like that. So, being in business for so long gives us some tools that other companies would not have in this situation.

Andy Preikschat

Okay, great. Thank you.

Sune Mathiesen

Thank you, Andy.

Operator

This concludes our question-and-answer session. I would like to turn the conference back over to Sune Mathiesen for any closing remarks.

CONCLUSION**Sune Mathiesen**

Thank you very much, Brandon, and thank you for everyone joining us today on the call. We look forward to speaking with you again on our next conference call that is likely to be in March. Thank you very much and have a good day.

Operator

The conference has now concluded. Thank you for attending today's presentation. You may now disconnect.

