

LIQTECH INTERNATIONAL, INC.
(NYSE American: LIQT)



Fourth Quarter and Fiscal Year 2018
Financial Results

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CORPORATE PARTICIPANTS

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

PRESENTATION

Operator

Hello. And welcome to LiqTech International Reports Fourth Quarter and Fiscal Year 2018 Financial Results Conference 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. After today's presentation, there will be an opportunity to ask questions. To ask a question, you may press star then one on your telephone keypad. To withdraw your question, please press star then two. Please note this event is being recorded.

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

Robert Blum

Thank you, Keith. Good morning, everyone, and thank you for joining us today as LiqTech International discusses its fourth quarter 2018 financial results and provides an update on its first quarter. I am Robert Blum of Lytham Partners. I will be your moderator for today's call. Joining us on today's call from the company is Sune Mathiesen, CEO of LiqTech International.

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 the live call, and that a transcript of the call will be available on the Investor Relations section of the company's website shortly thereafter as well.

Before we begin with prepared remarks, we submit for the record the following statements. 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 our business, financial condition and sales of operations and cash flows. If one or more of these risks or uncertainties materialize or if the underlying assumption is proven correct, the company's actual results may vary materially from those expected or projected.

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 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 Mathiesen, CEO of LiqTech International. Sune, please proceed.

Sune Mathiesen

Thank you very much, Robert. Good morning to all of you and thank you for joining us today. I'm excited to be speaking with you today. Today we are reporting our 2018 year-end results, and the fourth quarter of 2018 was in line with our expectations. And as we already took the excitement out of it by pre-announcing it last year, I want to spend my time today speaking with you about the other announcement we made this morning, the record first quarter 2019 and the uplist of our shares to the Nasdaq.

The first quarter of 2019 is a significant turning point in the history of LiqTech. We are set to report record revenues of approximately \$7 million, and equally important to return the company to solid profitability. We are also continuing to significantly grow our order backlog. These positive results for the first quarter should continue to accelerate as we move throughout the rest of the year.

On a sequential basis, we expect second quarter revenue and profitability to both surpass that of the first quarter of 2019, driven by the continued ramp in shipments from the current order backlog.

I would like to remind everyone that it's still early stages in the marine scrubber industry, but the interest for our standardized water treatment systems continues to be strong and even getting stronger, as regulation seems to be moving in our favor. I'm pleased with the progress being made. We are executing on a high level as we work to take full advantage of this important opportunity.

Now bear with me as I take a step back and talk about what we see is taking place in the marine market following the IMO 2020 mandate. As many of you know, IMO 2020 mandates the reduction of sulphur emissions from marine vessels, and it leaves the ship owners with two options to comply with the new regulations.

One is to switch to a lower sulphur fuel that is significantly more expensive than the bunker fuel they're using today. The second option is to install a scrubber system. A scrubber is a device that will spray water containing a solution of reagents over the emissions from the diesel engine. By doing so, it will capture harmful substances in the emissions and contain them in the water.





There are two basic types of scrubbers, an open loop system and a closed loop system. An open loop scrubber will take in seawater and return it to the sea after the scrubber process without being cleaned, so also including the before-mentioned harmful substances.

In a closed loop scrubber, there will be a water treatment system, such as the one that LiqTech provides. It will separate the harmful particles from the water, and it will 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 do have a water treatment system installed. These scrubbers are called hybrid scrubbers.

Over the last number of months, some of the largest ports, including China and Singapore, have banned the discharge of water from open loop scrubbers. Many in the industry expect that this banning of open loop scrubbers will continue throughout the world. When you think about it, at the core an open loop scrubber is simply moving the contaminants from the air to the water, and this is not what the IMO was looking to accomplish.

As countries such as China and Singapore ban the discharge of water from open loop scrubbers, we are now starting to see three types of orders. The first is retrofit of closed loop scrubbers on the existing fleet, which is the majority of what we have been doing so far.

The second is new builds, so orders where we are specced into the design of the new ship, and it looks like the adoption of scrubbers and new builds is higher than it is for retrofits. It implies that it will be a more significant part of our business moving forward.

The third one is conversion of already installed open loop scrubbers into closed loop systems. This is a new market opportunity opening up for us following the before-mentioned bans.

In addition to our ability to help ship owners meet the sulphur emission standards set by IMO 2020, we also have the ability to remove heavy metals and other harmful substances from the water. This removal of heavy metals is currently not regulated, but many in the industry believe that it will be in the future. Forward-looking ship owners, and especially the world's largest ship owners, are now positioning themselves to address this potential change.

As mentioned earlier, we continue to see a ramp in our backlog of confirmed orders. And while we are very pleased with our progress so far, I would like to emphasize that we are still in the early stages in the adoption of marine scrubber technology and we do expect to see a continued ramp in this industry in the years to come.

We believe that our market share in the marine scrubber market is very strong due to our enhanced capabilities. We have been building our product for more than five years now, and we have strong relationships with both the leading scrubber manufacturers and ship owners. We believe that our well proven system offers a very attractive solution in terms of both capex and opex, and that our first mover advantage should allow us to stay ahead of the competition.

As we discussed on the January call, we continue to be very busy. We're experiencing a significant ramp in our business and we're focused on expanding staff and manufacturing capacity. We remain on track to meet all scheduled deliveries in the upcoming quarters.

As previously announced, we're taking steps to increase our membrane [ph] manufacturing capacity. We remain on schedule to increase capacity in the second half of 2019, and we have taken steps to further increase capacity in the coming years.

We have also taken steps to increase our systems manufacturing capacity. We will more than double our manufacturing and office space, and we will be improving our testing and laboratory facilities. This expansion will be done without any capex spending.

I'm very pleased with the progress we have made so far. For the past more than two years we have been focusing most of our efforts into the marine scrubber industry, and we're excited to see that the growing order book is now turning into revenue and profitability.

As earlier mentioned, we expect that the marine scrubber market will continue to ramp for the next couple of years and remain on high level until 2025. We are, however, also preparing for future production beyond this and we are in the process of developing a couple of new exciting products.

One is a NOx reduction product for the marine industry. We continue to see tightening legislation, and we know from our discussions with ship owners that there is a great demand for such a product. The product is based on silicon carbide diesel particulate filters, a product that we have been manufacturing for nearly 20 years. We believe that our long-term experience in the manufacturing of DPFs and our current success in the marine industry puts us in a unique position to take advantage of this new opportunity.

As we grow our business, we are taking steps to continue reshaping the company going forward. Over the last year, we have brought on new individuals in key management positions, including Claus Toftegaard as our new CFO.

We have also looked to update and strengthen our board, and I was very pleased to have recently announced the appointment of Peter Leifland as a new board member. Peter recently retired as Executive Vice President and Member of Group Management of the Alfa Laval Group from 1999 to 2019. In particular, Peter served as President of the Alfa Laval Marine Division since 2011, and he was responsible for Global Operations from 1999 to 2011.

As we continue to gain significant market traction in the marine scrubber market, and other new markets and applications for the company's silicon carbide membrane systems and filters, I am confident that Peter will bring meaningful and relevant experience to LiqTech as we further build our business.

We believe that our company is growing into a more established company, and as we grow our business, we continue to see a greater level of interest from institutional investors. As announced today, we have taken steps to uplist our shares from the NYSE American to the Nasdaq. We expect to begin trading on the Nasdaq on April 16.

I'm excited to announce this transition, and we believe it will allow for added investor participation, especially from funds who have restrictions against owning stocks on the NYSE American.



Overall, 2019 is set to be an exciting year for LiqTech. We're set to report record revenues for the first quarter of 2019 and turn the company profitable. Our order book and delivery schedule further indicates a new quarterly revenue record in the second quarter with continued profitability.

The dynamics surrounding IMO 2020 continue to favorably benefit LiqTech and our unique silicon carbide water filtration technology. Again, we expect the continued ramp in our backlog and shipments in the coming quarters.

We are also positioning the company to take advantage of new market opportunities that should begin to come online in the coming year, including a NOx reduction product that our customers are eagerly awaiting. We appreciate the continued support of our investors, and we're working hard every day to meet the opportunity that we believe is available for LiqTech to be an industry leader going forward.

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

QUESTIONS AND ANSWERS

Operator

Yes. Thank you. We will now begin the question and answer session. To ask a question, you may press star then one on your telephone keypad. If you are using a speakerphone, please pick up the handset before pressing the keys. To withdraw your question, please press star then two. At this time we will pause momentarily to assemble the roster.

And the first question comes from Eric Stine with Craig-Hallum.

Eric Stine

Good morning.

Sune Mathiesen

Hi, Eric.

Eric Stine

A couple questions, but just on the market mix in the breakdown between retrofit, new and then the conversion open loop to closed, maybe just thoughts on specific percentages, or narrow that down a little bit. And then could you also just talk about what the economics look like for LiqTech, is this something that will look the same whether it's for retrofit or new, or is a conversion a lower ASP?

Sune Mathiesen

Yes. Let's take the first thing first. Up until this point, most of the business we have been doing has been retrofits. We have seen some new builds, but not a lot up until this point. What we are starting to see now is that we are spec'd in to some new builds, and that is something we think will accelerate in the future. There is a long process from when they spec a new build to when it's actually completed, and we are beginning to see the first signs that we are spec'd into some new builds, but that will be more moving forward.

The third, let's say, type of orders that we are starting to see and type of inquiries really is conversion of existing open loop scrubbers into closed loop. And this is really something that has come up since



the bans in China and Singapore especially, bans that we think we will continue to see in other parts of the world, and we think that will accelerate that part of the business.

In terms of ASP, it's very similar. If anything, I would say we're probably able to ask a little bit more for new builds because we're already spec'ed in, but it's very similar to the retrofits.

Eric Stine

Got it. Okay. That is helpful. And then just turning to the order book, you mentioned that it's well above the update you gave in mid-January. I'm just wondering if you're able to give a specific number. And then as you think about that, how that breaks down between the two framework agreements or work you've started there, the third and then the other customers that you are shipping to or servicing?

Sune Mathiesen

Yes. Let's take the two framework agreements we signed in the spring of 2018. They are both performing very well. One of the customers is getting very close to already having fulfilled the expectation for 2018 and 2019, that's really a positive. The other one is really on track to meet the expectations, that's also positive.

That leaves us with the third framework agreement that we signed in October last year. We are not seeing revenue come out of that yet, which we didn't expect either. The expectation is still to see meaningful revenue from that in the third quarter and onwards, and real revenue streams in 2020.

In regards to the backlog, we are solidly above where we were in January, and the reason why we have not disclosed at this time is because we think the company is getting a little bit more mature. The reason why we are disclosing the backlog last year and in January was the fact that we were booking a lot of orders but not yet turning it into revenue. With the record first quarter that we have announced today, we're now starting to turn some of that into revenue and we think that is a much better measurement for the performance of the company.

Eric Stine

Okay. Got it. Maybe last one for me, just on the other marine opportunities, and you mentioned DPF filters for ships. Is that something that you're able to do in your current DPF footprint or would that involve new capacity and some investment on your end?

Sune Mathiesen

We are in the process of adding capacity into our factory. We'll see the first furnaces being installed in the third quarter this year and we will get several deliveries after that. It's the same type of furnaces that we need for DPF and for membranes, we can control how we allocate that total capacity that we'll have. It's something we can't do in the existing factory, but let's hope that we have to buy even more furnaces. That will be a good problem to have, right?

Eric Stine

Okay. Thanks, Sune.

Operator

Thank you. And the next question comes from Rob Brown with Lake Street Markets.

Rob Brown

Hi. Thanks for taking my call.

Sune Mathiesen

Good morning.

Rob Brown

Just in terms of market share in the scrubber market, how do you see that developing for your product and the water treatment system at this point, and where do you see it going?

Sune Mathiesen

We actually had a very healthy market share in 2018 for our system, we had a big proportion of the closed loop systems that were installed. And we have been saying for some time that we thought our market share would come down, and a little bit to our surprise it seems it's not. It actually seems we are at least at the same level, and I would even say maybe we are gaining a little bit market share. That's a huge positive.

Rob Brown

Okay. Great. Specifically, to Q4, did you ship any marine units in the quarter and how many, if so?

Sune Mathiesen

We have not disclosed how many. But, yes, we shipped the marine systems in Q4 as well, but obviously had a significant ramp in the first quarter, going from \$3 million of revenue in the fourth quarter to \$7 million of revenue in the first quarter.

Rob Brown

Okay. Good. And then the capacity addition, I think, you mentioned taking steps to increase capacity beyond the furnaces, you're expecting this year. Could you clarify that? Are you looking to capacity increases beyond the furnaces you've already ordered?

Sune Mathiesen

We are making sure that we can get more furnaces. It means that we have put in orders not yet confirmed, but we have reserved the capacity from the furnace manufacturer to have additional deliveries in 2020, just trying to stay prepared. We have not committed to any capex spending, but we made sure that they would have capacity to service.

Rob Brown

Okay. Good. And then on the order book, I know you're not giving units, but how much visibility does that give you for 2019 and into 2020, and how far ahead are customers ordering units?

Sune Mathiesen

We're getting better and better visibility. I think we're never going to get two years visibility, that we have experienced that we have X amount of months of visibility. Our order book is growing right now and that just corresponds to the growth on a quarter-to-quarter basis, more than it corresponds to an increased visibility.



**Rob Brown**

Okay. Got it. Thank you. I'll turn it over.

Operator

Thank you. Once again, please press star and then one if you would like to ask a question. The next question comes from Liam Burke with B. Riley FBR.

Liam Burke

Thank you. Good morning, Sune. How are you?

Sune Mathiesen

Doing very well. Good morning.

Liam Burke

Sune, on the conversion of the hybrid ready or open loop scrubbers, do you need the actual ban to occur to the open seas in addition to the individual countries like China and Singapore, or do you think that as countries come on board, you'll see the conversion rate increase?

Sune Mathiesen

Our personal opinion is that we will see a complete ban again towards discharge from open loop scrubbers, and we think that will be worldwide, even in international seas. Right now it's not. We think that the steps that China and Singapore have taken is they're the first and we have seen others follow. We think that more countries and ports will follow, and we think eventually it will be completely banned all over the world.

Liam Burke

But do you need the open seas ban or do you think that you will see the conversion anyway?

Sune Mathiesen

We think that we'll see the conversion anyway, because there is an attractive economic model to install a closed loop scrubber and be able to burn the high sulphur fuel. Of course, it will be nice, not least for the environment, to see it completely banned also in international waters, but it's not something we need for adoption. We think the local bans are sufficient for that.

Liam Burke

Got you. And just a comment on the legacy business, DPF business, it seems to be flattish to down. How do you see that shaking out going forward?

Sune Mathiesen

We have not been focusing that much into the legacy business. As I talked about a little earlier, we see an upcoming opportunity for our DPF product in the marine industry, which we think is much more interesting than the automotive industry, where we have traditionally been. That will be our focus going forward, to take the 20 years of experience that we have and apply it into the marine industry that will have a much more attractive revenue opportunity and also more attractive margins.

Liam Burke

Great. Thank you, Sune.

Sune Mathiesen

Thanks.

Operator

Thank you. And the next question comes from John Werner with JCP.

John Werner

Hi, guys. Thanks for taking my call.

Sune Mathiesen

Good morning.

John Werner

My question is if you can give any visibility as far as the estimates for Q2 and Q3. You have spoken about \$6.4 million in revenues, and I know you're saying that you expect to be up sequentially, if I understood correctly from \$7 million in Q1, that would answer the question on Q2. What about Q3? Do you have visibility that far out, where your estimates are about \$8 million at this point in time?

Sune Mathiesen

The current order book gives us good visibility. As we said before, we know that the same quarter will be sequentially up on the first quarter and we have no reason to believe why that should not be the case for the third quarter as well.

John Werner

Thank you for taking my question.

Sune Mathiesen

Thank you very much.

Operator

Thank you. And the next question comes from John Henderson with KTG.

John Henderson

Hi, guys. Congrats on the progress. One quick question also on Q2. Sune, in your opening comments you actually referenced how Q2 will be up, I think, you said well above Q1, or something along those lines. Can you try to give us a little more granularity? You guys grew 125% sequentially from Q4 to Q1, clearly none of us were expecting any type of massive ramp in Q2, but a little bit more granularity I think would be helpful for a lot of investors, if you could.

Sune Mathiesen

Absolutely. The first quarter was great growth from the fourth quarter last year. And you are absolutely right, percentage-wise we're not going to see the same growth into the second quarter, but we will see substantial growth in both revenues and profitability. We are very pleased with the progress.

John Henderson

And in terms of the first couple framework agreements, it's logical to assume that at least one or two of these guys is most likely a very big player in the open loop area. I'm assuming it would be logical to expect orders from these guys to filter through as well as part of the third vertical, right?

Sune Mathiesen

Absolutely. We think all the players in the industry will be met with this challenge. The existing open loop systems will have to be converted into closed loop systems, and it opens up this new attractive opportunity for us. It's still early stages, I think China implemented the ban in January, Singapore did it in November last year, it's early stages. But we see a tremendous amount of interest for open loop conversions, and I'm sure it will be a big part of our business in, let's say, the second half of 2019 and 2020.

John Henderson

And maybe a final question, maybe one for Claus. At scale, I think three quarters ago you guys mentioned that the incremental margins on the new Mark 6 product were around 70%. Are you guys still feeling good a couple quarters out as you iron out the kinks with the ramp that the incremental flow through will be along those levels that you mentioned three quarters ago?

Sune Mathiesen

Claus is not on, I'll try and answer that, John. Yes, we feel very positive that we'll see margin improvements as we move forward. As you know, we have a lot of the depreciation in the margins that we are reporting today and as we grow our businesses, and as we grow revenue we're seeing margin improvements alone, for that reason. But also because the more you build the better you get, the lower prices you get from your suppliers, and you will be able to improve your margins that way. That is a continued focus from our side and something we are working on every day.

John Henderson

Great. Congrats on the progress. Thanks.

Sune Mathiesen

Thank you so much.

Operator

Thank you. And the next question comes from Roger Liddell with Clear Harbor Asset Management.

Roger Liddell

Hello, Sune.

Sune Mathiesen

Good morning, Roger.

Roger Liddell

Hi. I realize I don't fully understand the propulsion system, the different propulsion system installations out there, and just help me understand that there are boilers and diesels, and I don't know the mix that you're selling into and they are obviously in different aspects with each. Can you just ballpark what your markets are out there between boilers and diesels?



**Sune Mathiesen**

Yes. Basically, we are selling into everything diesel, and the only alternative to that is LNG. I would say that probably 95% to 96% of the fleet is diesel currently. We are seeing more and more LNG. We think that maybe the 3% to 4% of the market it is today will grow to about 6% to 7%. But long-term we are addressing 93% to 94% of all vessels.

Roger Liddell

There is an interesting aspect to low sulphur diesel fuel, and perhaps this has been addressed and resolved by the industry, my knowledge may be a little stale. But there have been meaningful questions about the lubricity of diesel fuel when you get into the low sulphur or ultra-low sulphur area, a loss of some of the lubrication quality of the fuel. I don't think it's productive to go any further with that point other than the noted and that could be if the issues aren't resolved, an incentive to go with the higher sulphur fuel and use LiqTech for addressing the other issues. On NOx control I take it that urea or some compound like that is added to what would have been sprayed inside the scrubber and that's what captures the NOx. Is that basically correct?

Sune Mathiesen

Yes. Let me give a little comment on your first comment regarding the low sulphur of fuel. You are absolutely correct, if you change into low sulphur fuel, you will also need to install other lubricants for the engine. And there are not so many lubricants in the low sulphur fuel and that could hurt your engine if you don't do something about it, that's an added cost for the ship owner.

From an environmental perspective, what makes the best sense is really to continue to use the high sulphur fuel and install a scrubber with water treatment, because also the engine efficiency is lower with low sulphur fuel, it has a higher environmental impact actually. You are absolutely correct.

On to the NOx product, what we do today with scrubbers is SOx reduction and a NOx reduction is what we know from passenger diesel cars, trucks and buses, a completely different issue that needs to be addressed. There is significant NOx pollution from shipping industry and we think it will be heavily mandated in the future.

From discussions with our customers, we know that they are looking for good NOx reduction products, and with the experience we have from the automotive industry and the experience we now have with the marine industry, we think we could be quite successful in this market.

Roger Liddell

Finally, is there any other pollutant screens from shipping that your installation can address, as it were, a freebie capability to address other issues?

Sune Mathiesen

Absolutely. The shipping industry is one of the most polluting industries in the world, and we know that it is moving towards a zero emissions industry. There is a lot of focus on it and we think we will see a lot of mandates in the future in this industry.

The other areas that we're looking into NOx reduction, another area we are looking into and we actually just sold the first systems is treatment of gray and black water from ships, and we are also looking into bilgewater treatment systems, which is also a big problem, where you discharge oily water into the sea.



We think all of this will be further mandated in the future, and we think we are ideally positioned to deal with some of these problems.

Roger Liddell

Okay. Thank you.

Sune Mathiesen

Thanks a lot.

Operator

Thank you. Once again, please press star and then one if you would like to ask a question. And the next question comes from Andy Preikschat with Edgebrook Partners. Please go ahead, sir. Your line is open.

Andy Preikschat

This is Andy Preikschat with Edgebrook Partners. Good morning, Sune.

Sune Mathiesen

Good morning.

Andy Preikschat

How are you able to convince the marine scrubber makers to go with your silicon carbide filter versus a high speed centrifuge? I think the cost is about the same. Can you explain technically why it's so much better?

Sune Mathiesen

Yes, the cost is about the same, you are absolutely correct. We offer significant advantages over the centrifuge technology. One, we are less footprint. Two, we have a fully automated system, which means that it has less maintenance. But the most important difference between the two technologies is that we offer a guaranteed output from the systems, a discharge that is guaranteed to be within the discharge limits, and you're not able to get that same guarantee with a centrifuge.

To give you an example, the framework agreement we signed in October last year is with one of the big scrubber manufacturers in the world. They also happen to be one of the largest manufacturers of high speed centrifuges. They have now taken the decision no longer to use the centrifuges but to include filtration in their offering just for this, because they know that they're not able to stay within the discharge limits. I think that proves our point that we have a different technology offering this guaranteed output and security for the ship owner.

Andy Preikschat

Okay. Great. And how many companies are selling centrifuges versus how many companies other than yours are selling the silicon carbide filters?

Sune Mathiesen

If we go back to 2018, we thought we had about 45% market share of the closed loop systems, we think that market share is growing. More and more scrubber manufacturers are seeing the benefits from this, more and more ship owners are seeing the benefits, and my guess is that we are more than 50% market share today.

Andy Preikschat

Are there other companies that offer the silicon carbide filters this year?

Sune Mathiesen

We are still seeing the competition as being high speed centrifuges. That's really what we are competing against in the market.

Andy Preikschat

Okay. Great. In other words, you haven't really seen anyone with a competitive offering in the silicon carbide filter?

Sune Mathiesen

We have seen some small companies try to break in. There will always be somebody who tries to copy what you're doing, but so far we have not seen it very successfully.

Andy Preikschat

Okay. Great. Thank you very much.

Sune Mathiesen

Thank you.

CONCLUSION**Operator**

Thank you. And as there are no more questions at the present time, I would like to turn the floor over to Sune Mathiesen for any closing comments.

Sune Mathiesen

Thank you very much, operator, and thank you, everyone, for joining us today on the call. We look forward to speaking with you again soon, and that will likely be on a conference call in May. Thank you very much. Have a good day.

Operator

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