



LIQTECH INTERNATIONAL, INC.
(NASDAQ: LIQT)

LIQTECH

**THIRD QUARTER FISCAL YEAR 2020
FINANCIAL RESULTS CONFERENCE CALL**

Monday, November 9, 2020
9:00 a.m. Eastern

CORPORATE PARTICIPANTS

Sune Mathiesen - Chief Executive Officer, LiqTech International, Inc.
Robert Blum - Managing Partner, Lytham Partners, LLC

PRESENTATION

Operator

Good day and welcome to the LiqTech International Third Quarter Fiscal Year 2020 Financial Results Conference Call. All participants will be in listen-only mode. Should you need assistance, please signal a conference specialist by pressing the "*" key followed by "0." After today's presentation, there will be an opportunity to ask questions. To ask a question, you may press "*" then "1" on a touch-tone phone. To withdraw your question, please press "*" then "2." Please note, today's event is being recorded.

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

Robert Blum

Thank you, Rocco. And good morning, everyone, and thank you all for joining us today to discuss LiqTech International's third quarter 2020 financial results. I'm Robert Blum of Lytham Partners. I will be your moderator for today's call. Joining us on the call from the company is Sune Mathiesen, the company's Chief Executive Officer.

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.

Before I 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 the risks or uncertainties materialize or if the underlying assumptions prove incorrect, 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, Chief Executive Officer of LiqTech International. Sune, please proceed.

Sune Mathiesen

Thank you, Robert. And good morning to all of you and thank you for joining us today. I've been looking very much forward to speaking with you today, despite a soft third quarter. I've been looking forward to the opportunity to expand on a number of the very exciting announcements we made this morning, which all have the ability to be rather transformative for the business, going forward.

From a financial standpoint, the third quarter financial results came in line with our internal expectations, given the global impact from COVID-19 on the marine scrubber market. The slowdown that started in March is improving over the last quarter, and we are seeing increased market activity.

I'll expand more on the marine scrubber market in a moment but wanted to first discuss the black carbon and NOx reduction product from marine we talked about in the press release this morning. This is a very exciting opportunity with the market potential being much, much bigger than any market we've ever worked in. And let's take a step back and help you understand how this opportunity came to be, which is significantly ahead of our internal planning and expectations.

First, for many years LiqTech has been a leader in diesel particulate filters, or DPFs, which are designed to remove diesel particulate matter from the exhaust gas of a diesel engine. For 20 years, we have applied our DPF products into trucks, buses, and off-road vehicles, first in Europe and later in North and South America. And for the past few years, the market has mainly been in Asia. And to be clear, our market has always been retrofits of existing vehicles.

In 2019, we had approximately \$5.7 million in sales from our DPF business. The increase in global regulation of diesel engine exhaust particles is expected to drive growth in the DPF market as more and more jurisdictions are expected to begin requiring DPF filters. Emissions from diesel engines have been linked to a variety of health problems in humans, and therefore reducing these emissions will have many health as well as social benefits.



In response to these health impacts, governments have been implementing legislation to regulate emissions from diesel engines. Due to the economic growth shown in Asian countries, pollution in major cities has reached high particulate matter levels. As a result, governments have instituted additional regulations for vehicles to meet new emission standards.

After this tightening legislation for on-road vehicles, we now see that governments, particularly in China, have turned their focus to reduction of black carbon and NOx in the marine industry. We have known for some time that it would happen, but the opportunity came much faster than we, and many others, previously anticipated.

This move by the Chinese government, coupled with potential mandates by other organizations such as the IMO, to, in essence, implement an IMO 2020-type mandate for black carbon and NOx reduction led us down the path to leverage our expertise in DPF filters, along with our new operating history in the marine scrubber market to develop a black carbon and NOx reduction product. We communicated our intent with you during our Investor Day in 2019, and I am extremely pleased to announce that we have now completed our engineering work and have entered commercial negotiations with numerous customers.

One of the entities we entered negotiations with is our largest customer in the marine scrubber market. And this company, based in China, saw an opportunity for us to work together to leverage their relationships in the region with our leading DPF capabilities. Over the past couple of months, end market conversations have significantly picked up steam, and we are now in advanced negotiations with customers to deliver our systems.

Further, having worked with our partner in China for a number of years now in the marine industry, we have confidence that we are in an ideal position to become one of the market leaders in this emerging industry, leveraging our 20-year experience from the DPF industry and the recent success in the marine scrubber market.

And let me just be clear about something I said at the beginning. The market potential for black carbon and NOx reduction is much, much bigger than any market we have ever worked in. The opportunity has come much quicker than we originally expected, and I look forward to being able to share more exciting news on this front in the new year.

While we are extremely excited about this new opportunity in China, we are likewise excited about the continued progress we are making in the oil and gas market in the Middle East. The oil and gas joint venture we announced last quarter to supply water treatment solutions where this is local water scarcity is currently in negotiations on multiple projects. Again, these systems will be built based on LiqTech's proprietary silicon carbide technology and operated by the joint venture on the long-term water supply agreements with oil and gas producers.

As I mentioned last quarter, the execution of the joint venture occurred following the successful completion of several pilot projects in the oil and gas industry over more than 24 months, utilizing our filtration technology with end users, for which the joint venture is currently negotiating long-term water supply agreements.



What makes LiqTech Solution unique in this market is our ability to treat difficult water and reuse it in the process. In our tests with some of the largest oil and gas companies in the world, we have proven that our technology offers a much better solution in terms of both quality and costs compared to existing alternatives in the market.

While the black carbon and NOx reduction opportunity has advanced rather quickly, it remains my expectation that oil and gas markets will be a very important contributor of revenue in 2021, and I'm optimistic that we'll be able to announce something very soon for you on this front. And if things couldn't get any busier for us than they already are, we are also launching our next generation membrane later this month to address the \$5.5 billion ceramic membrane market.

As compared to our current membranes, which are specifically designed to be about 200 nanometers, this new membrane has a pore size of 60 nanometers, which will allow us to enter some very large markets, including industrial and municipal wastewater market, food and beverage market, pharmaceutical market, as well as the drinking water market. Longer term, this will enable LiqTech to be both a system provider as well as a component supplier, working with OEMs, that can quickly accelerate adoption of the technology.

While we'll be competing against well-established players in this industry, we believe that the unique advantages of our silicon carbide technology and the lower manufacturing costs due to our recently upgraded manufacturing equipment will enable us to be competitive and win market shares. Our expectation is that we'll be expecting initial orders in 2021 with revenue beginning to ramp up in 2022.

We laid out our plans for this during our Analyst Day at the beginning of the year in Denmark. I couldn't be more pleased to once again be able to deliver on the goals we set forth to bring this product to market. The research and engineering team at LiqTech really has done a phenomenal job in advancing the development of this opportunity.

So, with all the exciting news today on these three additional market opportunities, I don't want to take away from the marine scrubber market. As I mentioned, the near-term market for marine scrubbers continues to be affected by the global impacts of COVID-19, including a decrease in fuel spreads as a result of decreased global transportation. However, the market activity has picked up from the lows of Q2 and Q3.

It's important to understand that we continue to benefit from a macro transition by vessels away from open loop scrubbers and towards closed loop scrubbers, which are enabled by the company's filtration technology. This transition to closed loop systems may accelerate with the potential of a global ban on open looped systems that is currently being discussed.

For those that have not yet seen it, a majority of the European Parliament's environmental committee recently voted to out-phase and ban open loop scrubbers. We believe that this will further drive the transition towards closed loop scrubbers and ultimately provide an opportunity to convert some 4,000 already installed open loop scrubbers.

This is a \$1.5 billion to \$2 billion opportunity in itself, and we estimate that we currently have a 50 percent market share in the closed loop scrubber filtration market. So, while the marine scrubber



industry is still hit by the economic consequences of the pandemic, we feel confident that this still represents a great potential for the company in the years to come.

To wrap things up, the team has done an incredible job of utilizing the slowdown to advance a number of key new product development initiatives that--each of them have the potential to become transformative revenue drivers for the business beginning in 2021.

Normally, I would be excited about any one of the four main areas I discussed, whether it be our entry into the black carbon and NOx reduction market in the marine industry, the continued progress in the oil and gas market in the Middle East, the launch of our next generation 60 nanometer membrane allowing us to enter markets with \$5.5 billion, our historical marine scrubber market, which we believe is poised for growth, again, as COVID-19 hopefully subsides, and a continuous transition towards closed loop systems.

As I was saying, normally I'd be excited about the progress we're making on any one of these. To have them all sort of hitting simultaneously takes the excitement to a completely different level. Needless to say, I think the company is in great shape. We have a strong cash balance, and the new manufacturing equipment we installed this year has increased our capacity significantly and also enabled us to lower our costs and manufacture new and better products.

We have completed the development of several new products and increased environmental focus around the world and new mandates is opening up new opportunities for us. I believe that we are extremely well-positioned to take a sizeable leap forward in 2021.

Just one final note, I'll be participating in a couple of upcoming conferences, including the Craig-Hallum and Stephens conferences in November and the Lytham Partners conference in December. I look forward to talking with many of you during these events.

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

QUESTION AND ANSWER SESSION

Operator

Thank you. We will now begin the question-and-answer session. To ask a question, you may press "*" then "1" on your touch-tone phone. If you are using a speakerphone, we ask that you please pick up your handset before pressing the keys. To withdraw your question, please press "*" then "2."

Today's first question comes from Eric Stine with Craig-Hallum. Please go ahead.

Eric Stine

Good morning, Sune.

Sune Mathiesen

Good morning, Eric.



Eric Stine

Hey. So maybe just starting on the black carbon and NOx reduction--I may have missed this--you reference that you think it's substantially larger than the other end markets that you've been participating in now. I mean, I would love to hear your--I know it's big--but at least your estimate of how much larger. And then also, obviously you expect this to be a contributor to 2021. I mean, what should we look for, or the cadence of developments in advance of that over the next couple of months?

Sune Mathiesen

We referenced to it at our Investor Day back in January, and we have been expecting black carbon reduction and NOx reduction in the marine industry to be an important end market for us for some time now. I think what has surprised us a little bit is how quickly this has come to fruition. When we talked about it nearly a year ago, it was in anticipation of new mandates, both in China but also worldwide.

In general, I think we can say that the shipping industry is moving towards a zero emissions industry, and we think that this will be the next big global mandate. What we're seeing now is local mandates, especially for inland vessels, for transportation in many European countries and also in China now. And we are also seeing mandates for ocean-going vessels that are operating in coastal areas.

And longer term, we think that we'll see that global mandate. What we're specifically seeing right now is mandates in China for inland vessels and ocean-going vessels and to size the opportunity, well, there is approximately 180,000 inland vessels in China. And all of them will be hit by this new mandate. We think ASP for one of these systems will be around \$130,000 to \$140,000, so it's a really, really, really sizable opportunity.

Eric Stine

Got it. And maybe just, I guess, a second one, or to follow up on that, I mean, when you look at these regulations, how they are now developing relative to what you saw on the marine scrubber side with IMO 2020--I mean, what are--it sounds like you clearly expect this to move faster than that. I mean, what are some of the things--whether it's the options available to meet these standards? Or what makes you think and gives you the confidence that it will move faster than on the scrubber side?

Sune Mathiesen

I think what gives us the confidence is the global increased environmental focus. So, there was a big push for sustainability in shipping, and there were new mandates. And this is one of the first of them.

What we see in China now is not--is really something we expected. They have been focusing on on-road transportation for the last three or four years. They have operated commercial vehicles to meet new emission standards. And now, they are taking the next big step, which is the inland vessels. What is unique about China is that an incredible amount of the country's transportation is on the rivers.

So, they have an enormous amount of inland vessels, which is why the opportunity is as big as it is. So, what provides us with confidence here is a track record in China for the last three or four years, where they have operated on-road vehicles, which really provides us with confidence that now they have a new mandate for inland vessels that will actually also come to fruition .

Another thing that provides us with great confidence is that we are teaming up with our largest customer in the marine scrubber business, a customer that we've known for three or four years now as



well, who has proven very trustworthy and with whom we have done a lot of marine scrub installations. So, all of that really provides us with great confidence that this is a real opportunity and something that is happening.

Eric Stine

Got it. Maybe last one for me, just turning to oil and gas, I know in the past you had said that you thought that in 2021 that might be bigger than your scrubber business. And I know that you've got a lot of moving parts there, given COVID and what--the impact that has been. But, I mean, is that still the way you view it? I know you've got some things that are still in negotiation, and you're waiting on some things. I mean, is that still a fair statement?

Sune Mathiesen

Absolutely. We still think that oil and gas will be a very significant revenue opportunity for us in 2021. We think that it will be bigger than marine scrubbers. So, the new developments in China with black carbon and NOx reduction doesn't take anything away from the developments in oil and gas. That is kind of happening simultaneously.

Eric Stine

Got it. Thank you very much.

Operator

And our next question today comes from Rob Brown at Lake Street Capital Markets. Please go ahead.

Rob Brown

Good morning, Sune.

Sune Mathiesen

Good morning, Rob.

Rob Brown

Just staying with the black carbon market, are you--will you be providing a full up system for that market, or is this a component supply that goes into a bigger system?

Sune Mathiesen

We are looking to supply DPFs, including coating and canning, for ocean-going vessels and a complete system for inland vessels.

Rob Brown

Great. And then maybe switching to the oil and gas market, I think you said there were a number of projects you're quoting on. Could you characterize kind of the size range of those at this point and sort of the--is it all through the JV, or are there other systems outside of the JV that you've got?

Sune Mathiesen

Yeah, we are quoting for a large number of projects right now in the Middle East. And that process is going extremely well. We are in competition for some projects. Other projects we are actually alone because the specifications specifically mention our proprietary technology.



It's progressing well. We're doing all of the projects together with our joint venture partner right now. We're not ruling out doing projects on our own for different regions. But right now, all of them are together with joint venture partners. It's all progressing according to plan. We think that we'll see first orders in the near future, and I dare say in terms of the size of the potential orders, they are all quite transformative for the company.

Rob Brown

Thank you. And then, the last question is really on the scrubber market. I think you talked about some signs that that's coming back. Is that just--what's driving that? Is that the greater sort of trend toward closed loop scrubbers? Or are you seeing kind of order activity picking up more recently? Or maybe just how you kind of sense that and when--how dependent on COVID is that recovery--and starting to recover at this point?

Sune Mathiesen

So there's no doubt that the scrubber industry as a whole has been hit by COVID-19. Global transportation--and that means both on-road and marine transportation--has come down significantly due to COVID-19, which has caused an overcapacity in the refineries to manufacture clean diesel.

That, again, has caused low-sulfur diesel prices to come down, and the price break between low-sulfur and tanker fuel has been on a very low level and probably not just justifying a scrubber installation. That coupled with people not working due to COVID-19, shipyards being shut down, has caused a significant slowdown in the industry.

We have seen the people are now back. There has been a second wave of COVID-19 in Europe, which has always been--also been challenging. But in general, we see that people are back now. We have seen activity in the market take off in terms of inquiries, in terms of ship owners announcing that they are moving forward with scrubber installation plans. And we are also winning orders. But the industry as a whole is still affected by COVID-19.

We see a lot of light at the end of the tunnel, though. Again, activity has picked up. We had the vote in the European Parliament to out-phase and ban marine scrubbers, which is a great positive. And it really proves to us that a global ban of open loop scrubbers eventually is very likely. We still think there will be a lot of scrubber installations in the next years. We think that with a ban of open loop scrubbers, it opens up the opportunity to convert the 4,000 already installed open loop scrubbers.

And then finally, we think that the scrubber installation will again also be an attractive business case, once things get back to normal. But as long as COVID-19 is around--and let's hope it's not for long--we had exciting news from Pfizer this morning regarding a vaccine--but as long as it's around, the scrubber market will be affected by COVID-19. But there should be light at the end of the tunnel and definitely a huge potential for open loop conversions, which we are focused on right now.

Rob Brown

Thank you. I'll turn it over.

Operator

Ladies and gentlemen, as a reminder, to ask a question, please press "*" then "1." Our next question today comes from Tommy Moll with Stephens. Please go ahead.



Tommy Moll

Good morning, and thanks for taking my questions.

Sune Mathiesen

Good morning, Tommy.

Tommy Moll

Understanding the crystal ball may be a bit hazy as we get into year-end here and have some potentially significant impacts from COVID, etc.--but would you be able to hazard a guess just for 4Q top-line to get us calibrated appropriately? Do you think flat, up, or down revenue versus 3Q? And then on the margin side, is there a pathway back to the black into Q4, or does that look more like a 2021 event when some of these new markets start to light up for you?

Sune Mathiesen

Yeah. So, if you focus on Q4 first, so based in current orders and deliveries that we already made, it looks like Q4 will be up sequentially from the third quarter, which is positive. So hopefully, third quarter was a low point. And as we move into 2021, we have a lot more things moving. We have oil and gas, we have black carbon and NOx reduction, and we have the marine scrubber market as revenue drivers. So, it certainly looks like we're set for growth in 2021 as well.

Tommy Moll

Good to hear on both fronts. And then shifting to capital allocation, for a lot of the new opportunities you've talked about so far on the call and in the release, as you look forward to next year, do you feel pretty well set in terms of capacity, and so we should think about 2021 as more of a maintenance CapEx year? Or are there some other dynamics that we should consider as we start to think about 2021?

Sune Mathiesen

Yeah. What we have been successful in doing in 2020 is to build a \$150 million to \$250 million capacity. We have brand-new furnaces and definitely capacity to grow our business as we go into 2021. The size of the opportunities in both black carbon reduction and oil and gas could mean that we have to expand that capacity even further. But our focus right now is obviously to fill the advanced capacity we have, which would be substantial growth from where we are today.

And that's our first focus, and then we'll start focusing on what to do after that. I think the positive thing here is also that we have been able to expand our capacity, and at the same time, we have a very strong cash position. And so, we feel in great shape for growth, heading into 2021.

Tommy Moll

Good to hear. Thank you. And I'll turn it back.

Sune Mathiesen

Thanks, Tommy.

Operator

And our next question today comes from Liam Burke with B. Riley, FBR. Please go ahead.



Liam Burke

Thank you. Hi, Sune. How are you doing today?

Sune Mathiesen

I'm good. How are you, Liam?

Liam Burke

I'm fine, thank you. Just quickly on your investment in plant would drive manufacturing efficiencies, but your gross margins took a turn for the worse sequentially. What was the contribution during the quarter of the sequentially down gross margins?

Sune Mathiesen

We continue to see improvements in our contribution margins for marine scrubber units, and we actually see improvements in our DPF contribution margins due to the new manufacturing equipment. The reason why it's not really affected in the gross margins in the quarter is mainly due to the volume--the low volume--and it's also due to us shutting down the manufacturing in North America. And we had some costs that is reflected also in the gross margin. So, overall improvements in contribution margins is continuing, and it will reflect as we return to growth and normal levels of business.

Liam Burke

Great. And the CDP contribution for the quarter, can you give us a sense of that?

Sune Mathiesen

Yeah, I'd like to get back to you on that, so we give you some exact numbers.

Liam Burke

OK. And then I guess finally, this NOx carbon emission filtration for the marine market would be pretty significant, since there's tremendous debate out there right now as to what a solution would be, looking into the 2030 time frame. Have you had any discussions with IMO about what this can do for the industry?

Sune Mathiesen

Yeah. So, the idea of black carbon and NOx reduction in marine is definitely not new. It's known technology that it can be done. It's basically what we've done in passenger cars, trucks, and buses on-road for many, many years. There has been--in this debate how the future shipping industry looks like, there has been a big push on LNG. And many have said that it will be the next big phase. And there's also been an uptick in orders for new builds based on LNG. What we note is that the European Parliament last week voted to out-phase open loop scrubbers and ban open loop scrubbers.

And they also expressed skepticism to LNG because the overall footprint--environmental footprint for LNG--is not good either. So, we think that closed loop scrubbers represents probably the best solution to sulfur reduction in international shipping, and coupled with black carbon and NOx reduction, we think that diesel still has quite a future in shipping.

Liam Burke

Great. Thank you, Sune.



Sune Mathiesen

Thanks, Liam.

Operator

And our next question today comes from Roger Liddell of Clear Harbor Asset Management. Please go ahead.

Roger Liddell

Yeah, good morning, Sune.

Sune Mathiesen

Good morning, Roger.

Roger Liddell

You have not said anything about coal-fired power plant water treatment scrubber--water treatment. Is there anything cooking there?

Sune Mathiesen

Yes, it continues to be a focus. We actually recently won a couple of orders in power plants, so it's definitely still something that we think will be--will grow in the future. A lot of investment in power plants has been postponed due to COVID-19, and they continue to be so. As I said, we recently won a couple of orders. It is still a focus for us.

In terms of the market potential, it's interesting but not the billion-dollar industry that we have talked about today with oil and gas and black carbon and NOx reduction. But we have definitely not forgotten about it, and we are continuing our efforts to sell systems.

Roger Liddell

And it would be premature now, but with the other things ramping up that you've been discussing--but the issue of coal-fired power plant ash lagoons is a big deal in the eastern, particularly southeastern, part of the U.S. with multi-hundred million dollar judgments against utility companies. Do you foresee that ultimately becoming a relevant item--and related, but separately, the success you had in mine discharge cleanup and whether tightening environmental standards are putting that market into sharper relief?

Sune Mathiesen

I think it will, personally. And when I listen to experts in the market, I think that the general expectation, when the world has recovered from COVID-19, is that a lot of investments will be focused on sustainability. And I personally think that we'll see tightening legislation in this area. And as we do that, it will open up opportunities for us. So, yes, my personal expectation is that this will be an issue for the future.

Roger Liddell

Potable water--there is increasing concern, at least in the U.S., of contamination with PFOS and PFAS. The EPA guidance--not a mandate but a guidance only--is 70 parts per trillion, and a number of stockholder-owned companies--water distribution companies--have decided to meet the lowest of the state mandates at around 12 or 13 parts per trillion. And I noted in the November issue of Consumer

Reports magazine a lengthy and very interesting, very provocative article on, well water quality generally but PFOS, PFAS.

They argue, along with major environmental groups in the U.S., that one part per trillion is the maximum that should be tolerated. And there's an argument for zero discharge on forever chemicals, as they're called. So, apparently it is not a dramatic increase in the cost of delivered water to strip out PFOS, PFAS compounds down to the one part per trillion area. Is this a market that you see opening up to silicon carbide and your technology?

Sune Mathiesen

I think that we'll see a lot of changes in the drinking water market, going forward. There is no doubt that there is more and more local water scarcity around the world and also that we see more and more drinking water polluted by different substances. We have been focused on drinking water for some time.

And one of the other things we discussed today is our 60-nanometer new membrane product, which is really targeted for, amongst others, this industry. So yes, I think we'll see tightening legislation on drinking water. We'll see more and more water scarcity. And I think with our newly developed membrane, we will be one of the players in this industry.

Roger Liddell

Thank you.

Operator

And ladies and gentlemen, this concludes the question-and-answer session. I'd like to turn the call back over to the management team for final remarks.

CONCLUSION**Sune Mathiesen**

Thank you very much, Operator, and thanks for everyone joining us today on the call. I look forward to speaking with many of you again next--during our virtual presentation and one-on-one and hope that we can all visit face-to-face again in the near future. Have a good day and stay safe.

Operator

Thank you. This concludes today's conference call. We thank you all for attending today's presentation. You may now disconnect your lines and have a wonderful day.