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Pure Technologies Limited

Second Quarter 2017 Results Conference Call & Webcast Transcript

Date: **Friday, August 4th, 2017**

Time: **8:30 am MT / 10:30 am ET / 7:30 am PT**

Speakers:

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OPERATOR:

Thank you for standing by. This is the Conference Operator. Welcome to the Pure Technologies Limited Second Quarter 2017 Results Conference Call. As a reminder, all participants are in listen-only mode and the conference is being recorded. After the presentation, there will be an opportunity to ask questions. To join the question queue, you may press star, then one on your telephone keypad. Should you need assistance during the conference call, you may signal an Operator by pressing star, and zero.

I would now like to turn the conference over to Paul Moon, Investor Relations. Please go ahead.

PAUL MOON:

Thank you, Operator, and thanks to all for joining today's conference call and webcast. With me today to discuss our Q2 results are Jack Elliott, President and CEO, and Geoff Krause, Chief Financial Officer. Also, joining us for the Q&A is Mark Holley, Executive Vice President and COO.

Certain statements made during this call, as well as other information provided periodically by the Company, may contain forward-looking statements. Information that could cause actual results to differ materially from these statements are detailed in the earnings press release and in other publicly filed documents, including Pure's annual and interim reports.

Also, certain measures we use are not recognized under IFRS, such as Adjusted EBITDA, adjusted net income, gross margin, cash from operations, and working capital. We recommend that listeners review the discussion of these measures in the Company's financial disclosure documents.

As a reminder, this call will be archived and a replay will be accessible approximately two hours after these proceedings. Slides accompanying this event can be accessed on our Investor website under the Events heading. I understand that there's been a slight delay in the publishing of these slides so we apologize for that. Those slides are on our website now. For this call, however, the slides are for quick reference material only and may not be specifically addressed.

With that, I'd like to hand over the call to Jack Elliott. Jack?

JACK ELLIOTT:

Thank you, Paul. As shown in the consolidated results, I am pleased to report strong revenue, Adjusted EBITDA and net income growth for the three and six-month period. In the second quarter, on a consolidated basis, revenue increased by 16% to $33.7 million, while Adjusted EBITDA increased by 34% to $6.1 million. For the six months, revenue also increased by 16% to $62.9 million, while Adjusted EBITDA increased by 94% to $11 million. Net income showed similar trends improving by 36% to $1.3 million in the second quarter. For the first six months, net income was $1.6 million compared to a loss of $1.5 million last year. It is important to remember that net income for the second quarter and year-to-date period in 2016 included $1.1 million of receipts from the Libyan accounts receivable.

When I combine these results with what is shaking out to be a busy second half, I'm upbeat about our prospects for 2017 and beyond. A number of factors contribute to this performance to date and our positive outlook. In our Water business, our investment in sales personnel in 2015 and increased focus on operational excellence and cost control are driving both sales growth and increased profitability within our segments.

In the Americas region, increased activity in Canada and Eastern U.S. were the primary drivers behind this segment's 12% revenue growth in the second quarter. The commencement of new programs, the scheduling of work with new clients in subsequent periods, and the potential for AFO equipment sales support our expectation of a busy second half of the year for this region.

For Wachs Water Services, the combination of increased activity through a renewed sales force and a focus on productivity resulted in a 32% increase in revenue and Adjusted EBITDA growth from $0.1 million to $1.3 million in the quarter. This is the fourth consecutive quarter with improved revenue and profitability.

For our International business, the nature, size and timing of projects makes quarter-over-quarter comparisons difficult. While revenues were down 14% in the second quarter, on a year-to-date basis, revenue was up 35% reflecting a very strong first quarter. Expected activity in the second half of 2017 includes a large PipeDiver project in the U.K. and Pure's first conditioned assessment project in South-East Asia, along with the continuation of Leak detection projects in Qatar, South Africa and Brazil. We also continue to develop our partnership with Xylem, Inc., as discussed in the first quarter, with meaningful benefits expected in 2018.

At PureHM, our Oil and Gas Division, second quarter revenues was the highest on record for the division with EBITDA margins consistent with our expectations. Much of the focus in the first half of the year has been on integrating the E-MAC business, which we acquired at the end of 2016. With integration, essentially complete in a traditionally busier second half for E-MAC, activity levels are expected to remain high for the remainder of the year. We will continue investing in our people to ensure that we can deliver the work we see ahead. In addition, to support the continued growth of our remote pig tracking business in 2018, we expect to invest an additional $1.5 million in tracking equipment this year.

From a corporate perspective, our cost control initiatives have become part of the Company's culture, with a third consecutive quarter of flat general and administrative cost, all while increasing our focus and investment in our HSE and training programs that are integral to our continued success. Given the scalability of the corporate foundation that has been built over the last two years, we expect that this will result in EBITDA margin expansion as revenues grow.

I'd now like to turn the call over to Geoff, who will provide more details on our business and financial results. Geoff.

GEOFFREY KRAUSE:
Thanks, Jack. Let me start by breaking down our second quarter and year-to-date results by segment. Our Americas segment revenues increased 12% in the second quarter, driven by inspection and consulting activity in the Eastern U.S. and Canada, with the latter largely from projects that were previously delayed, as we explained in the fourth quarter of 2016. The segment's gross margin decreased to 82% in the second quarter from 93% last year, primarily due to project mix and higher sub contractor use during the period. Despite this lower gross

margin, Q2 Adjusted EBITDA improved by 20% to $4 million due to lower operating cost and increased revenues. As a percentage of revenue, America's Adjusted EBITDA increased to 25% from 23% last year.

Looking at the first six months, America's revenue increased by 6%, while Adjusted EBITDA increased 12% over the same period of last year. As the first quarter's typically the slowest, with this year being no exception, these increases were driven by higher second quarter activity. Looking forward to the remainder of the year, the second half of 2017 is expected to be the segment's busiest period on current scheduling, which includes work with several new clients. The new scheduled work is a direct result of our investment in sales personnel which began in the second half of 2015 to drive future top line growth.

Revenue from the International Water segment decreased by 14% in the second quarter as a result of lower inspection activity in Europe and South America as compared to last year. Year-to-date revenue, however, increased 35% due to the completion of a major PipeDiver inspection for a repeat customer in Europe and higher inspection and consulting activity in Australia and South America in the first quarter. As Jack said, the size and nature of international projects often results in significant inter-quarter variability.

Adjusted EBITDA for the segment was down 6% in the second quarter due to the slower activity, but up 137% year-to-date as a result of the PipeDiver project, previously mentioned, and our efforts to control cost in the region.

At Wachs Water Services, we had our fourth consecutive quarter with improved revenue and profitability. Second quarter and year-to-date revenue improved 32% and 27%, respectively. Adjusted EBITDA improved 1,021% in the quarter, with year-to-date Adjusted EBITDA improving by $2.4 million from a negative position last year. These results reflect a refocusing of Management, including new sales personnel and cost controls, giving further confidence in future performance.

PureHM's revenue for the three-month period grew 30%, which includes $1.4 million of revenues from E-MAC and 6% organic growth. Overall, revenue growth in Canada was tempered by lower than expected activity in the U.S. On a year-to-date basis, revenues increased 22%, which includes $2.1 million of E-MAC revenues and 3% organic growth. As disclosed previously, the first quarter experienced slow growth due primarily to weather delays and the transition period to integrate E-MAC's operations.

Q2's Adjusted EBITDA was consistent with last year, in line with our expectations as increased revenues were offset by a higher cost base due largely to the addition of E-MAC. Sales productivity was lower when compared to the same period of 2016 due to lower than expected activity in the U.S. and an overall decline in higher margin SmartBall activity. Historically, the second half of the year is more active for E-MAC and related productivity is expected to improve. Year-to-date, PureHM's Adjusted EBITDA declined 13% due to the reasons mentioned previously, combined with the impacts of E-MAC integration activities in the first quarter.

Market acceptance of PureHM's technologies and services does continue to grow and our R&D efforts continue to reach new milestones. In the first half of this year, we installed our first permanent pig tracking equipment on a major operator pipeline. This pilot project not only demonstrates the efficacy and value of the product and service but opens for the commercial launch of the system expected by the fourth quarter of 2017.

As anticipated, G&A expenses in the second quarter of 2017, down 3% compared to last year, were consistent with the first quarter and fourth quarter of 2017, a direct result of our successful ERP implementation, shared service consolidation and process redesign work completed in the third quarter of 2016. For the remainder of 2017, I expect G&A expenses will remain consistent with the current levels, subject to changes in bonus provisions which are adjusted for corporate performance. In short, we set a plan in place here and we're sticking to it.

R&D expenses increased $0.4 million and $0.1 million for the three and six month periods over last year. The increase reflects a lower proportion of capitalized development cost in the quarter compared to 2016, which is variable based on project mix and time spent on operations during busier periods. We've capitalized $900,000 and $2.2 million of development expenditures for the three and six month periods, respectively.

Capitalized expenditures are primarily associated with ongoing development of Pure's existing technologies and platforms, including the permanent pig tracking equipment mentioned earlier. We continue to focus on increasing the capabilities of our technologies in all end markets.

Moving on to the balance sheet, the collection's speed of receivables continues to be highlighted with DSO at the end of the first quarter at 108 days which is consistent with year-end 2016. At June 30, we had $5.8 million in cash on hand compared to $5.4 million at year-end, no debts with undrawn credit facilities. We continue to enjoy a strong financial position with net cash sufficient to meet all operating capital and financial obligations.

As Jack stated earlier, we are supporting the growth in PureHM's remote tracking business. As a result, subsequent to the end of the second quarter, we increased our field equipment capital budget by $2 million to allow for this incremental investment in tracking equipment as well as some other miscellaneous items. We also increased our development budget by $0.5 million to reflect the timing of anticipated spending on certain of our R&D projects.

Accordingly, we expect total capital spending of approximately $7 million for field and office equipment, and $4 million for intangibles. We further anticipate that cash flow from operations in 2017 will be more than sufficient to fund capital spending and quarterly dividends. Our credit facilities remain undrawn at this time, and subject to continued collection speed or any unforeseen major expenditures, I expect that we will be building our cash balances through the remainder of the year.

With that, I would ask the Operator to open up the call for questions. Operator?

OPERATOR:
Thank you. We will now begin the question-and-answer session. To join the question queue, you may press star, then one on your telephone keypad. You will hear a tone acknowledging your request. If you're using a speakerphone, please pick up your handset before pressing any keys. To withdraw your question, please press star, then two. We will pause for a moment as callers join the queue.

The first question is from Amr Ezzat of Echelon Partners. Please go ahead.

AMR EZZAT:
Good morning gents. Congrats on a strong quarter.

JACK ELLIOTT:
Hey Amr.

GEOFFREY KRAUSE:
Hey Amr.

JACK ELLIOTT:
Thank you.

AMR EZZAT:
On the Oil and Gas side, I've got two questions for you, one on the top line and the other on the margin front. Indeed, it's a record quarter but organic growth is a little lower than last year's levels. I'm just trying to get a sense of your view for the rest of the year, excluding E-MAC. Are we going to the 20% organic growth rate again over the next couple of quarters or do you expect a more tamed growth rate? Then the second question there on the margin front, above 30% despite the E-MAC acquisition. That's impressive. My question is, is that level sustainable with the expected strong second half of the year for E-MAC which is lower margin?

JACK ELLIOTT:
Amr, I'll address the top line question and Geoff can talk about the EBITDA question. On the top line, I would say that first of all we had a very strong quarter in Canada. Organic growth in Canada was 30% or so for PureHM. In the U.S., last year we had a large contract so we had kind of a tough comp there which hasn't recurred. We have a much stronger infrastructure in Canada to deliver the business and to procure the business so we do need to build up that capability in the U.S. We will be doing that over the next year.

In relation to the balance of the year, it's going to be more difficult now to separate E-MAC from PureHM as the XLI inspection operations are fully integrated. I would say that we expect a continuing strong rate of activity for both the third and fourth quarters along the run rates we're seeing we saw in the second quarter. We're quite optimistic that they will have combined a very strong year and as I said it would be difficult to sort out what's organic and not by the end of the year here.

I hope that addresses the 6% question. We do expect to invest in building up our U.S. business so that we can deliver our technologies and solutions on a relationship basis down there that we are currently doing in Canada. Over to Geoff for the EBITDA question.

GEOFFREY KRAUSE:
Sure, Amr. If you remember during our year-end call, we had noted that we'd expected the combined margins to be around 32%. We think that's going to continue for the remainder of the year. The increase in the E-MAC activity is in their larger margin areas which would be in their engineering and consulting side as well, some of their XLI activity and we haven't taken into account the impact of the lower product sales. We think those margins are going to still stay strong and in fact as the last part gets busier that further supports that because there's a bit of leverage into that number.

AMR EZZAT:

Okay, that's great to hear. Then, switching gears on Wachs Water. Very impressive numbers there. It seems like you might reach your pre-acquisition levels before your target date of 2019. My questions on the margin front again. Big jump from last year, obviously, but sequentially as well very healthy jump. Just wondering if there was anything specific during the quarter that drove that or do we continue to see improvements from these levels?

JACK ELLIOTT:
Amr, I would say that the improvement in EBITDA, the contribution came from increased efficiency and better management of our resources and more efficient execution of the work. We expect that to continue as this current pace. I think they're a very well run operation right now, very pleased with the improvements they've made. They have a really good handle on control on their business and Wachs adds to the productivity of the business. We're very happy with that.

In relation to the top line, we are looking at expanding their range of activities. Perhaps, Mark, you can talk a little bit about some of the things we're looking at there.

MARK HOLLEY:
Sure. Hi, Amr. Yes, so there's a few things that we're looking at trying to take advantage of some of the technologies developed actually in our Oil and Gas business and moving them into our Wachs Water platform to help them develop some other solutions for our clients that they can bring to market. In addition to that, there's a keen focus on our large diameter valve program. We've just hired management for that role and Wachs is feeling pretty upbeat about the opportunity of building that solution into their portfolio.

With those combined opportunities and a few others we're working on, we're encouraged with what next year will bring.

AMR EZZAT:
Great. Then in your prepared remarks you touched on a few upcoming projects on the International Water fronts, including that large PipeDiver in the U.K. Just trying to get a sense of size. Would it be of comparable size to the PipeDiver project you had in Q1? Then perhaps you could comment on what sort of margins to expect there? I mean, in Q1 I think it was very high margin. You delivered 60% on the International Water fronts.

JACK ELLIOTT:
Amr, no, it won't be the size of the one we did in Q1 but it's a sizable enough (inaudible 19:40). This is part of a three-year program, actually, for this particular client in the U.K. We completed a smaller run in Q2 which went very well and we're hoping that this will continue beyond this year as they rollout the program.

In terms of margins, as you know we don't disclose margins on individual business lines, but I can tell you that with our current cost structure internationally, it is delivering–the International business delivers really strong EBITDA margin and we're very pleased with the current configuration of that part of our business. We obviously exited some areas to reduce costs, and nevertheless we are pursuing some of these projects that we've identified and we do have the resources to pursue them and secure them.

I'm upbeat about the International business. We are working with Xylem right now, for example. They're putting together their business development team to promote their smart water initiatives including Pure services and we're working with them to pursue some opportunities that we're currently actively pursuing in addition to helping them understand the value proposition that we offer.

AMR EZZAT:
Then maybe one last one for me on the Americas Water MWD   Are you still expecting this for 2018? Any updates on project scope and potential size?

JACK ELLIOTT:
In short, no. They are still–we do work for MWD on a continuing basis, but they haven't, as far as I'm aware, Mark, nailed down exactly how they want to pursue with this big program, but we have been talking to them about it. Is that correct?

MARK HOLLEY:
(Inaudible 21:33)

JACK ELLIOTT:
But I would say on the Americas Water business, we are very excited about the level of activity right now. We have over $160 million in backlog in our overall Water business which I think is a record for us. If you look at our combined opportunity funnel and our backlog it's over $0.5 billion. We're very excited about the potential in the Water space and I would say the level of project activity that we're currently scheduling in the second and– sorry, the third and fourth quarters is significant. Mark, would you say so?

MARK HOLLEY:
Exactly. Currently scheduling over 200 projects for the second half of the year.

JACK ELLIOTT:
We're delighted with that, actually. We're seeing increasing momentum. There are also regulatory factors that we think will continue to drive the business. For example, Ontario is introducing a requirement for water agencies to have an asset management plan that will, I believe, help drive our business in the future. New Jersey is another state in the U.S. that's recently introduced regulations through a new act that's been passed that again will cause not only the private water operators down there but the public utilities to pay more attention to their underground assets. These initiatives are starting to, I think, take hold and governments are paying more attention to this issue of infrastructure sustainability.

AMR EZZAT:
Great. Thank you very much and good luck.

JACK ELLIOTT:
Thanks.

OPERATOR:
The next question is from Mona Nazir of Laurentian Bank. Please go ahead.

MONA NAZIR:
Good morning and thank you for taking my questions.

JACK ELLIOTT:

Hi Mona.

GEOFFREY KRAUSE:
Hey Mona.

MONA NAZIR:
Hi. Firstly, great progress on the Wachs front. We saw that they had very strong margins, 23% in the quarter. When you first purchased it, and going over the transaction and highlights, I believe the margins were lower than your legacy 20%. I believe they were in and around 16%. Can you delve a little bit into the variance, particularly in this quarter? Were there any one-time items? What's a kind of good run rate to use now? Then I know in your commentary you'd said continuing to work through the Wachs, some of the legacy issues. What's a good future rate, so 2018/2019? Thank you.

JACK ELLIOTT:
Mona, thanks, that's a good question. First of all, I want to sort of rewind a little bit.

MONA NAZIR:
Yes.

JACK ELLIOTT:
If we look at the Wachs transaction, (phon 24:14) transaction, we made a decision to exit their gravity sewer business which generated about US$2. million, US$2.5 million in revenue because it was–the margins were not to our satisfaction there. That really had a top line impact and what we're doing now is focusing on higher margin work

The main driver for their EBITDA increase has been operational efficiency and more robust management of field crews. That is going to continue. We are looking, as Mark pointed out, to adding higher value services to their portfolio which we would expect to be equal or higher margin than the current activities. We're focusing on moving them up the margin ladder, I guess, and to not pursue low margin work because we believe that even at the expense of growing the top line we can generate stronger EBITDA performance by doing that.

GEOFFREY KRAUSE:
There were no, it's Geoff here Mona, there were no one-time items that drove that margin which I think is important. We also did take some G&A cost out of the business, and as a result should service consolidation and those sorts of things. Looking forward we would expect to be north of that 20% level.

MONA NAZIR:
Okay. Okay. Then secondly for me, just turning to Xylem and sometime has now passed since you first announced the partnership. Is there any idea of the magnitude of revenues that we could see coming from this venture as we head into 2018 or is it challenging to quantify? I'm just trying to get a sense that if it could be a material contribution or is it mainly strategic at this point in time and you saw it as an avenue to increase International revenue along with gaining a strong partner.

JACK ELLIOTT:
Yes, you're correct in your assumption. We don't have any significant revenue expectations, certainly for this year, and next year we haven't quantified that yet.

MONA NAZIR:
Mm-hmm.

JACK ELLIOTT:
We continue to engage with them to develop a budget to our expectation for next year. But you are absolutely correct in your comment that we entered into this arrangement, number one to, as we said at the time, to help us reduce our cost of operating in these markets, and number one to leverage their branding and their corporate presence and infrastructure in these markets. They have a very similar perspective on infrastructure sustainability to us. As a result, it's going to be, I think, a very interesting relationship in the future and we're looking forward to it evolving.

MONA NAZIR:
Okay, perfect. Then lastly for me. Last call, I believe it was you had pointed on the PureHM side to a $30 million, plus $35 million run rate and looking out this quarter we're surpassing that. You already touched on the growth profile continuing on with PureHM in the previous questioning line. It seems as if things are just going so, so, so smoothly there. Are there any headwinds or potential bottlenecks? Any challenges that you could envision coming up or growth could temper materially?

JACK ELLIOTT:
Well, Mona, it's a little bit like a duck. Everything that's smooth on the surface but they're peddling like hell underwater. They're going through–so the business has grown and they are dealing with operational challenges, I think, but I believe they have a handle on it and they're working hard to put the infrastructure and the people in place to manage the growth but I'm pleased with the way they're addressing it. We have some experience of that on the Water side and we think that our experience in that area will help to accelerate the evolution of the PureHM business so that they can continue to grow in a controlled manner.

We're very pleased with it. They have great people. We're delighted with the E-MAC people, they fit in very well and they're a significant contributor to the progress we're making there.

MONA NAZIR:
Okay, very helpful. Thank you.

OPERATOR:
The next question is from Raveel Afzaal of Canaccord Genuity. Please go ahead.

RAVEEL AFZAAL:
Yes, thank you. Thank you for taking my questions. First of all, on your backlog, you have such a terrific, healthy backlog at the moment. I'm wondering on the Water side, what sort of–I mean when you look at the utilization rate for your infrastructure, your resources in terms of looking at the data itself, how much revenues can you generate on an annual basis on the Water side?

JACK ELLIOTT:
On the Water side, well, let me put it this way. If I look at the overall consolidated delivery capacity, I think we're in the hundred-delivery capacity. I think we're probably in the $137 million, $138 million range in terms of capacity. Whether or not we fit that all in remains to be seen, but at the same time on the Water side we are building up our operations and project

management. We have, I think actually we're hiring aggressively on the operations side and the project management side. Mark, would you say?

MARK HOLLEY:
Correct.

JACK ELLIOTT:
We'll continue to add capacity to service the opportunities we see in front of us.

RAVEEL AFZAAL:
Great. Thank you. What are your expectations for total capital requirements for 2017 and 2018?

GEOFFREY KRAUSE:
Raveel, it's Geoff here. We haven't disclosed anything for '18, but for '17, as we said, our total capital will be $7 million field equipment and $4 million of intangibles. Looking into '18, intangibles should go down as we finish off one of our major development projects, and on the capital side, a large chunk of our increase has been the additional tracking units, about $1.5 million that we talked to in our prepared numbers, and that's really to support increased growth in that tracking unit. I think that side has grown a little faster than we thought it was going to so we're going to put some more money into it.

RAVEEL AFZAAL:
Awesome. Great. Just one final question for me. I was thinking about the leak detection business with this condition assessment business. Have you guys quantified in the past how much is the leak detection business with this condition assessment on the Water side? What are the different macro tailwinds for these two businesses?

JACK ELLIOTT:
Raveel, I would say we look at leak detection as the first stage of condition assessment. But having said that, if you look at Pure leak detection generated from SmartBall and Sahara on the Water side, it's probably about 15% of our Water business. I think the condition assessment business is in the high 30%s, 40% and the engineering work and then the valve management Wachs component. We actually have quite a diverse range of products and services now, so that gives us some comfort in terms of risk or any one of them being negatively impacted, and when we look at the overall business it's a very diverse mix through all of our business units. But around the 15% would be a good number, I think.

RAVEEL AFZAAL:
Very good. That's all for me. Thank you so much for taking my questions.

OPERATOR:
As a reminder, it is star, one to ask a question.

The next question is from Jason Zandberg of PI Financial. Please go ahead.

JASON ZANDBERG:
Hi guys and congratulations on a good quarter. I'd like to also point out that I'm impressed on the improvement on the Wachs Water this last three or four quarters. Congratulations on that.

JACK ELLIOTT:
Thank you Jason.

JASON ZANDBERG:
I wanted to ask, you'd mentioned that the second half, I believe that you'd mentioned there are up to 200 projects that are either active or starting in the second half. Are there any timing issues, any timing risks on say some of the, let's say, the top five or the more large projects coming up here in the second half?

JACK ELLIOTT:
Well as a general comment I would say there are always timing risks in our business. We're dealing with utilities and they're not used to putting things in their pipe and sometimes they're not ready or something happens that causes them to postpone or delay the work. I would say, Mark, that we have some cushion built in there in terms of risking. Do you want to talk a little bit about how we'd do that?

MARK HOLLEY:
Yes. Hi Jason. As Jack alluded to last year, we took–sort of moved or pivoted from more of a binary approach to our project scheduling, either it's in or it's not, to a weighted approach. So within that those 200-odd projects they have been risked and weighted and that should–it gives us a little bit more of a cushion to manage the variability in the scheduling around our clients, weather and other such things. To the point where if push comes to shove we can actually feel more comfortable this year in moving some of these into Q1 if we need to. The combined operational focus, the improved weighting and risking on the projects and working more closely with our clients at a project management level, is allowing us to kind of get a better handle on that, but as Jack alluded to, there's always risk associated with these in situ in line inspections. But we feel like we've got a much better handle than previous years.

JACK ELLIOTT:
Jason, I just want to add that overall I'm really pleased with the progress our regional teams have made in this type of approach to our business. I think what I see now is a lot more confidence in their business and the business execution and it gives me a lot of confidence that we can deliver what we see in front of us. We've also improved our technical delivery. Far fewer incidents of rework or remodelization or poorly executed projects, and that's all part of our systems improvement that we've been implementing over the last 18 months or so. We see continued opportunities for improvement and for efficiencies. Geoff, I think it's fair to say that our gross margin has improved significantly as a result of the focus on project execution and third party cost management.

GEOFFREY KRAUSE:
If you look at our gross margin in our Water business from 2014 to where we are today, it's up about 6%, which is a direct result of the improvement in our project management processes, as well as Jack has alluded to, the operational execution, the increased planning, increased working with our customers to make sure that we do it once and we do it right. All in all, really good progress over the last two years.

JASON ZANDBERG:
Okay, great. Sounds like you've given it quite a bit of thought and resources, so that gives me a lot of comfort. Just on your EBITDA margin, I think if my numbers are correct, you had four consecutive quarters here of an improvement on that EBITDA margin. In this last quarter being

18% you're close to your historical 20% EBITDA margin. In order to get to 20% on a company level, is that–do you see that as a situation of lowering cost or will that getting to 20% just be a function of increasing that top line? Because it looks like all your individual divisions are above 20% but I would imagine that the corporate cost or the reason that you're not quite at that level on a company-wide basis. Are we looking at cost reduction or revenue growth to get to 20%?

JACK ELLIOTT:
You're absolutely correct. It's leverage in the business and what we're seeing is increasing leverage as our top line goes. What you will see as, and I think we've seen it over the last few quarters, is increasing EBITDA margin growth as our revenues grow. The 20% overall margins is not that far away, I would say, on a consolidated basis, and I'm reasonably confident we'll get there by the end of the year here.

Overall, we continue focusing on cost efficiencies on the one hand; on the other hand, building up the business and driving top line growth to increase our EBITDA margin.

JASON ZANDBERG:
All right, perfect. Thanks very much.

JACK ELLIOTT:
Yes, thank you.

OPERATOR:
The next question is from Ryan Wong of National Bank. Please go ahead.

RYAN WONG:
Good morning everyone. This is Ryan filling in for Rupert.

GEOFFREY KRAUSE:
Hey Ryan.

RYAN WONG:
I just have a question. I'm just wondering if you guys are still exploring other partnership agreements? If you are, how do you think about it to get to an agreement and what's the process surrounding that?

JACK ELLIOTT:
Ryan, I think the first thing is we have to like the company and look at their corporate governance and their ethics and their business mix to see if it's a good fit for us. We're very cautious about it. Having said that, we do have partnerships that we currently have with WRC in the U.K., for example, which we're very pleased with, and the Xylem partnership is another one that we have, we're happy with the people and all of the people we've met in the organization. We do have another very, I would say successful, a smaller partnership in South Africa with an engineering company there that's been ongoing for several years. We don't like to get into partnerships on a short-term basis, so we want to make sure we have the right partners.

In terms of new partners, I'd say the most likely place where we will look at that right now is in China through a joint venture, a company there, and we're actively looking at partnership opportunities over there because we see significant opportunity in the non-revenue water area and also in the condition assessment, pre-stress pipe condition assessment business in China. That will probably be the next place where we would look at a partnership.

RYAN WONG:
Okay, great. That's some good color. Can you remind me how much of your revenue is recurring in nature?

JACK ELLIOTT:
That's a really good question because we have two sources of recurring revenue, I would say. The first is from our monitoring and licensing revenue. Geoff, do you know the number?

GEOFFREY KRAUSE:
It's about $11 million a year.

JACK ELLIOTT:
About $11 million a year. But I think a more interesting number are the programs we have with some of our long-term clients. They're usually three-year programs, two, three-year programs, generally renewed. If you add that to the mix, that's another probably $40 million in revenue a year that we would–you could consider to be recurring. That's a key focus for us is building these relationships to develop that recurring revenue stream. All told, you could say that our recurring revenue is probably in the $50 million to $60 million range.

RYAN WONG:
Okay, great. That's perfect. One last question for me. What is the M&A market kind of look like right now? Is Pure considering anything there or is it just focused on organic growth at this point?

JACK ELLIOTT:
For this year, we're focusing on organic growth, for sure. We are looking at some potential opportunities in the oil and gas sector. We want to make sure that E-MAC has its operational efficiencies and its organization, the PureHM business, sorry, have that under control. But having said that, we are looking at expanding our business in the U.S. and it's possible that that could be through acquisition.

On the Water side, we plan to grow organically. We think we have a terrific suite of technologies and solutions, industry-leading and we plan to grow that organically.

RYAN WONG:
Okay, great. That's it for me. Thanks.

GEOFFREY KRAUSE:
Thanks Ryan.

OPERATOR:
This concludes the question-and-answer session. I'd like to turn it back over to Jack Elliott for any closing remarks.

JACK ELLIOTT:
Thank you. I just want to close by saying we're excited about the second half on the Water Division. We're seeing a high level of activity from new client activity and from current project

scheduling in the Americas. We are investing in sales personnel in the Americas and we believe that will help impact the year ahead. We have ongoing and new work internationally, and as you know, we are working with Xylem to help grow our business in those markets. We're pleased with Wachs. I think they've done very well and with the addition of some new business lines; I think they can continue to grow profitability. On the Oil and Gas side, the first half was consistent with our expectations. We recovered from the slow first quarter and we expect to have a very active second half of the year. E-MAC is pretty well fully integrated now and as I said it's going to be more difficult to separate out what's organic and not from that business, so we'll see how that evolves.

We are adding more CapEx to generate additional business opportunities for the PureHM business, and again, we believe that there's a growing addressable market for our solutions. We want to become a technology–or continue to be a technology innovator in the Oil and Gas side. We think that's the key to success for us in the future.

With that, I'll conclude the meeting and thank you all.

OPERATOR:
This concludes today's conference call. You may disconnect your lines. Thank you for participating and have a pleasant day.