

# Energy Recovery Reports Fiscal Year End 2018 Financial Results

SAN LEANDRO, Calif., March 7, 2019 /PRNewswire/ --Energy Recovery, Inc. (NASDAQ: ERII) ("Energy Recovery" or the "Company"), the leader in pressure energy technology for industrial fluid flows, today announced its financial results for the fiscal year and fourth quarter ended on December 31, 2018.



## Full Year Summary

- Total revenue of \$74.5 million, an increase of 8% year-over-year
- Product gross margin of 70.7%
- Total gross margin<sup>(1)</sup> of 76.0%
- Net income of \$22.1 million, or \$0.40 per diluted share

## Fourth Quarter Summary

- Total revenue of \$17.7 million
- Product gross margin of 74.5%
- Total gross margin<sup>(1)</sup> of 79.9%
- Net income of \$2.4 million, or \$0.04 per diluted share

Energy Recovery's President and CEO Chris Gannon commented, "2018 was a record year for the Company, setting all-time highs in full year revenue, as well as product and total gross margins<sup>(1)</sup>. At the start of 2018, Energy Recovery had solid fundamentals with a healthy balance sheet and cash position, commanding market share in seawater reverse osmosis (SWRO) desalination energy recovery solutions, and a product concept that has the potential to transform fracing operations. Throughout the year, we built upon this foundation and invested to strengthen our infrastructure and position resources for long-term growth across our Water and Oil & Gas businesses."

Mr. Gannon continued, "As it relates to our Water segment, we believe the current expansion phase in the desalination business cycle is far from over, as we currently have the strongest project backlog and pipeline in the Company's history. While the timing of this revenue varies from quarter to quarter, growth shows every sign of continuing in 2019 and beyond. Governments and private enterprises worldwide are investing in SWRO desalination to counter the impacts of fresh water scarcity."

Mr. Gannon concluded, "In our Oil & Gas segment, throughout 2018 and early 2019 we materially advanced the VorTeq™ system-level enhancements. We also have taken firm

control of our technology development process by acquiring the field resources and equipment necessary to accelerate commercialization of the VorTeq system. Construction is underway on our Commercial Development Center outside of Houston, TX, which will enable us to test and validate our oil & gas solutions at scales representative of real-world conditions as often as necessary. These investments underscore our confidence in the VorTeq system, and we are collaborating closely with our partners as we move into the next phase of development towards commercialization."

## Revenues

For the fiscal year ended December 31, 2018, the Company generated total revenue of \$74.5 million. Total revenue for the fiscal year ended December 31, 2018 increased by \$5.4 million, or 8%, from \$69.1 million in the fiscal year ended December 31, 2017. The \$5.4 million increase in total revenue was chiefly attributable to higher Water segment revenue.

The Water segment generated total product revenue of \$60.5 million for the fiscal year ended December 31, 2018, compared to \$54.3 million for the fiscal year ended December 31, 2017. The \$6.2 million, or 11%, increase in product revenue was due to higher Mega-Project ("MPD") and Aftermarket ("AM") shipments in 2018.

The Oil & Gas segment generated total revenue of \$14.0 million for the fiscal year ended December 31, 2018, compared to \$14.8 million for fiscal year ended December 31, 2017. The \$0.8 million, or 6%, decrease in revenue was due to lower cost-to-total cost (previously known as percentage of completion) revenue in 2018 associated with the sale of multiple IsoBoost® systems, offset by an increase in license and development revenue of \$2.4 million during this period.

For the fourth quarter ended December 31, 2018, the Company generated total revenue of \$17.7 million. Total revenue decreased by \$6.0 million, or 25%, from \$23.7 million in the fourth quarter ended December 31, 2017. Of the \$6.0 million decrease in total revenue, \$6.7 million was attributed to a decrease in Water segment revenue due to MPD product shipments shifting into the third quarter from the fourth quarter, offset by a \$0.7M increase in Oil & Gas segment revenue due to higher license and development revenue.

## Gross Margin

For the fiscal year ended December 31, 2018, product gross margin was 70.7%. Product gross margin increased by 360 basis points from 67.1% in the fiscal year ended December 31, 2017. This increase was largely driven by favorable price and product mix, manufacturing efficiencies, and higher production levels in the Water segment. Including license and development revenue, total gross margin<sup>(1)</sup> was 76.0% for fiscal year ended December 31, 2018. Total gross margin<sup>(1)</sup> increased 360 basis points from 72.4% in the fiscal year ended December 31, 2017.

The Water segment generated product gross margin of 71.6% for the fiscal year ended December 31, 2018. Water segment product gross margin increased by 110 basis points, compared to 70.5% in the fiscal year ended December 31, 2017. This increase was largely driven by favorable price and product mix, manufacturing efficiencies, and higher production levels in 2018.

The Oil & Gas segment generated product gross margin of (29.0%) for the fiscal year ended December 31, 2018. This decrease was attributable to higher project costs and revenue adjustments associated with our IsoBoost revenue. Including license and development revenue, the Oil & Gas segment total gross margin<sup>(1)</sup> for the fiscal year ended December 31, 2018 was 95.3%.

For the fourth quarter ended December 31, 2018, product gross margin was 74.5%. Product gross margin increased by 620 basis points from 68.4% in the fourth quarter ended December 31, 2017. This increase was largely driven by favorable price and product mix and manufacturing efficiencies in the Water segment. Including license and development revenue, total gross margin<sup>(1)</sup> was 79.9% for the fourth quarter ended December 31, 2018. Total gross margin<sup>(1)</sup> increased 800 basis points from 71.9% in the fourth quarter ended December 31, 2017.

### Operating Expenses

For the fiscal year ended December 31, 2018, operating expenses were \$46.7 million, an increase of \$5.9 million from \$40.8 million for the fiscal year ended December 31, 2017. The increase in operating expenses was due to increases in our Water, Oil & Gas, and Corporate segments.

The Water segment operating expenses for the fiscal year ended December 31, 2018 were \$10.2 million, an increase of \$1.3 million from \$8.9 million for the fiscal year ended December 31, 2017. This increase was driven by higher sales incentive expenses associated with increased Water segment sales and higher research and development investment in Water organic growth strategy.

The Oil & Gas segment operating expenses for the fiscal year ended December 31, 2018 were \$18.3 million, an increase of \$2.3 million from \$16.0 million for the fiscal year ended December 31, 2017. This increase was driven by the Company's continued investment in Oil & Gas research and development activities.

The Corporate segment operating expenses of \$18.1 million for fiscal year ended December 31, 2018 were \$2.2 million higher than the fiscal year ended December 31, 2017. This increase was driven by non-recurring CEO transition expenses, higher tax planning, and employee expenses.

For the fourth quarter ended December 31, 2018, operating expenses were \$12.7 million, in line with the fourth quarter ended December 31, 2017.

### Bottom Line Summary

To summarize our financial performance, on a full year basis, the Company reported a net income of \$22.1 million, or \$0.40 per diluted share, compared to a net income of \$18.4 million, or \$0.33 per diluted share in the fiscal year ended December 31, 2017. This increase was driven by a one-time tax benefit of \$12.3 million, which is related to simplifying the Company's international tax structure in Ireland considering the 2017 U.S. Tax Cuts and Jobs Act. On an adjusted basis, the Company reported an adjusted net income<sup>(1)</sup> of \$10.9 million or \$0.20 per diluted share for the fiscal year ended December 31, 2018. Net income of \$18.4 million, or \$0.33 per diluted share in the fiscal year ended December 31, 2017 was

driven by a tax benefit of \$8.4 million, which included a net release of tax valuation allowance, a one-time tax expense related to the 2017 Tax Cuts and Jobs Act, and other tax adjustments. Excluding the tax benefit, net income for the fiscal year ended December 31, 2017 was \$0.18 per diluted share.

On a quarterly basis, the Company reported a net income of \$2.4 million, or \$0.04 per diluted share for the fourth quarter ended December 31, 2018, compared to a net income of \$13.5 million, or \$0.24 per diluted share for the fourth quarter ended December 31, 2017. Net income for the fourth quarter ended December 31, 2018 includes a non-recurring tax benefit of \$0.6 million related to simplifying the Company's international tax structure in Ireland considering the 2017 U.S. Tax Cuts and Jobs Act. On an adjusted basis, the Company reported an adjusted net income<sup>(1)</sup> of \$0.03 per diluted share for the fourth quarter ended December 31, 2018. Net income of \$13.5 million, or \$0.24 per diluted share in the fourth quarter ended December 31, 2017, was driven by a tax benefit of \$8.4 million, which included a net release of tax valuation allowance, a one-time tax expense related to the 2017 Tax Cuts and Jobs Act, and other tax adjustments. Excluding the tax benefit, net income for the fourth quarter ended December 31, 2017 was \$0.09 per diluted share.

### Cash Flow Highlights

The Company finished the fiscal year ended December 31, 2018 with cash and cash equivalents of \$21.9 million, restricted cash of \$0.2 million, and short-term & long-term investments of \$74.6 million, all of which represent a combined total of \$96.7 million. As of December 31, 2018, 1,193,102 shares of the Company's common stock were repurchased for \$10.0 million under the stock repurchase program authorized by the Company's Board of Directors on March 7, 2018.

### **Forward-Looking Statements**

Certain matters discussed in this press release and on the conference call are "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, including the Company's belief that the Company's Water business will continue to grow in the future, the Company's belief that the current expansion phase in the desalination business cycle will continue in 2019 and beyond, the Company's belief that our product concept has the potential to transform fracing operations, and the Company's belief that the Company is well positioned for success in 2019 across all of our business units. These forward-looking statements are based on information currently available to us and on management's beliefs, assumptions, estimates, or projections and are not guarantees of future events or results. Potential risks and uncertainties include the Company's ability to achieve the milestones under the VorTeq license agreement, any other factors that may have been discussed herein regarding the risks and uncertainties of the Company's business, and the risks discussed under "Risk Factors" in the Company's Form 10-K filed with the U.S. Securities and Exchange Commission ("SEC") for the year ended December 31, 2018 as well as other reports filed by the Company with the SEC from time to time. Because such forward-looking statements involve risks and uncertainties, the Company's actual results may differ materially from the predictions in these forward-looking statements. All forward-looking statements are made as of today, and the Company assumes no obligation to update such statements.

## **Use of Non-GAAP Financial Measures**

This press release includes certain non-GAAP financial measures, including total gross margin. Generally, a non-GAAP financial measure is a numerical measure of a company's performance, financial position, or cash flows that either exclude or include amounts that are not normally excluded or included in the most directly comparable measure calculated and presented in accordance with generally accepted accounting principles in the United States of America, or GAAP. These non-GAAP financial measures do not reflect a comprehensive system of accounting, differ from GAAP measures with the same captions, and may differ from non-GAAP financial measures with the same or similar captions that are used by other companies. As such, these non-GAAP measures should be considered as a supplement to, and not as a substitute for, or superior to, financial measures calculated in accordance with GAAP. The Company uses these non-GAAP financial measures to analyze its operating performance and future prospects, develop internal budgets and financial goals, and to facilitate period-to-period comparisons. The Company believes these non-GAAP financial measures reflect an additional way of viewing aspects of its operations that, when viewed with its GAAP results, provide a more complete understanding of factors and trends affecting its business.

(1) "Total gross margin" and "Adjusted net income" are non-GAAP financial measures. Please refer to the discussion under headings "Use of Non-GAAP Financial Measures" and "Reconciliations of Non-GAAP Financial Measures."

## **Conference Call to Discuss Fourth Quarter and Fiscal Year 2018 Financial Results**

### LIVE CONFERENCE CALL:

Thursday, March 7, 2019, 2:00 PM PDT / 5:00 PM EDT  
Listen-only, US / Canada Toll-free: (+1) 877-709-8150  
Listen-only, Local / International Toll: (+1) 201-689-8354  
Access code: 13687375

### CONFERENCE CALL REPLAY:

Expiration: Thursday, April 4, 2019  
US / Canada Toll-free: (+1) 877-660-6853  
Local / International Toll: (+1) 201-612-7415  
Access code: 13687375

Investors may also access the live call or the replay over the internet at [ir.energyrecovery.com](http://ir.energyrecovery.com). The replay will be available approximately three hours after the live call concludes.

## **Disclosure Information**

Energy Recovery uses the investor relations section on its website as means of complying with its disclosure obligations under Regulation FD. Accordingly, investors should monitor Energy Recovery's investor relations website in addition to following Energy Recovery's press releases, SEC filings, and public conference calls and webcasts.

## **About Energy Recovery, Inc.**

Energy Recovery, Inc. (ERII) is an energy solutions provider to industrial fluid flow markets worldwide. Energy Recovery solutions recycle and convert wasted pressure energy into a usable asset and preserve pumps that are subject to hostile processing environments. With award-winning technology, Energy Recovery simplifies complex industrial systems while

improving productivity, profitability, and efficiency within the oil & gas, chemical processing, and water industries. Energy Recovery products save clients \$1.9 billion (USD) annually. Headquartered in the Bay Area, Energy Recovery has offices in Dubai, Houston, Madrid and Shanghai. For more information about the Company, please visit [www.energyrecovery.com](http://www.energyrecovery.com).

## Contact

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**ENERGY RECOVERY, INC.**  
**CONSOLIDATED BALANCE SHEETS**  
*(In thousands, except share data and par value)*

|   | December 31, |            |
|---|--------------|------------|
|   | 2018         | 2017*      |
| <b>ASSETS</b>   |              |            |
| Current assets:   |              |            |
| Cash and cash equivalents   | \$ 21,955    | \$ 27,780  |
| Restricted cash   | 97           | 2,664      |
| Short-term investments  | 73,338       | 70,020     |
| Accounts receivable, net of allowance for doubtful accounts of \$396 and \$103 at December 31, 2018 and 2017, respectively  | 10,212       | 12,465     |
| Contract Assets   | 4,083        | 6,278      |
| Cost and estimated earnings in excess of billings   |              |            |
| Inventories   | 7,138        | 5,514      |
| Prepaid expenses and other current assets   | 2,810        | 1,342      |
| Total current assets  | 119,648      | 126,063    |
| Restricted cash, non-current  | 86           | 182        |
| Deferred tax assets, non-current  | 18,318       | 7,933      |
| Property and equipment, net   | 14,619       | 13,393     |
| Goodwill  | 12,790       | 12,790     |
| Other intangible assets, net  | 640          | 1,269      |
| Other assets, non-current   | 282          | 12         |
| Total assets  | \$ 179,841   | \$ 164,485 |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>   |              |            |
| Current liabilities:  |              |            |
| Accounts payable  | \$ 1,439     | \$ 4,091   |
| Accrued expenses and other current liabilities  | 8,019        | 7,948      |
| Income taxes payable  | —            | 432        |
| Accrued warranty reserve  | 478          | 366        |
| Contract liabilities  | 16,270       | 15,909     |
|   | —            | 11         |
| Current portion of long-term debt   |              |            |
| Total current liabilities   | 27,132       | 30,360     |
| Long-term debt, less current portion  | —            | 16         |
| Deferred tax liabilities, non-current   | —            | —          |
| Contract liabilities, non-current   | 26,539       | 40,517     |
| Other non-current liabilities   | 236          | —          |
| Total liabilities   | 66,463       | 72,591     |
| Commitments and Contingencies (Note 9)  |              |            |
| Stockholders' equity:   |              |            |
| Preferred stock, \$0.001 par value; 10,000,000 shares authorized; no shares issued or outstanding at December 31, 2018 and 2017   | —            | —          |
| Common stock, \$0.001 par value; 200,000,000 shares authorized; 59,396,020 shares issued and 53,940,085 shares outstanding at December 31, 2018 and 58,168,433 shares issued and 53,905,600 shares outstanding at December 31, 2017 | 59           | 58         |
| Additional paid-in capital  | 158,404      | 149,006    |
| Accumulated comprehensive loss  | (133)        | (125)      |
| Treasury stock, at cost, 5,455,935 shares repurchased at December 31, 2018 and 4,262,833 shares repurchased at December 31, 2017  | (30,486)     | (20,486)   |
| Accumulated deficit   | (14,466)     | (36,559)   |
| Total stockholders' equity  | 113,378      | 91,894     |
| Total liabilities and stockholders' equity  | \$ 179,841   | \$ 164,485 |

\*Prior-period information has been retrospectively adjusted due to our adoption of ASU 2014-09, *Revenue from Contracts with Customers (Topic 606)* and ASU No. 2016-02, *Leases (Topic 842)* on January 1, 2018.

**ENERGY RECOVERY, INC.**  
**CONSOLIDATED STATEMENTS OF OPERATIONS**  
*(In thousands, except per share data)*

|  | Years Ended December 31, |           |           |
|--|--------------------------|-----------|-----------|
|  | 2018                     | 2017*     | 2016*     |
| Product revenue                                  | \$ 61,025                | \$ 58,023 | \$ 49,715 |
| Product cost of revenue                          | 17,873                   | 19,061    | 17,849    |
| Product gross profit                             | 43,152                   | 38,962    | 31,866    |
| License and development revenue                  | 13,490                   | 11,106    | 8,069     |
| Operating expenses:                              |                          |           |           |
| General and administrative                       | 21,476                   | 17,354    | 16,626    |
| Sales and marketing                              | 7,546                    | 9,391     | 9,116     |
| Research and development                         | 17,012                   | 13,443    | 10,136    |
| Amortization of intangible assets                | 630                      | 631       | 631       |
| Total operating expenses                         | 46,664                   | 40,819    | 36,509    |
| Income from operations                           | 9,978                    | 9,249     | 3,426     |
| Other income (expense):                          |                          |           |           |
| Interest income                                  | 1,543                    | 870       | 309       |
| Interest expense                                 | (1)                      | (2)       | (3)       |
| Other non-operating expense, net                 | (80)                     | (188)     | (19)      |
| Total other income, net                          | 1,462                    | 680       | 287       |
| Income before income taxes                       | 11,440                   | 9,929     | 3,713     |
| Benefit from income taxes                        | (10,653)                 | (8,425)   | (6)       |
| Net income                                       | \$ 22,093                | \$ 18,354 | \$ 3,719  |
| Income per share:                                |                          |           |           |
| Basic  | \$ 0.41                  | \$ 0.34   | \$ 0.07   |
| Diluted  | \$ 0.40                  | \$ 0.33   | \$ 0.07   |
| Number of shares used in per share calculations: |                          |           |           |
| Basic  | 53,764                   | 53,701    | 52,341    |
| Diluted  | 55,338                   | 55,612    | 55,451    |

\*Prior-period information has been retrospectively adjusted due to our adoption of ASU 2014-09, *Revenue from Contracts with Customers (Topic 606)* on January 1, 2018.

**ENERGY RECOVERY, INC.**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(In thousands)

|   | Years Ended December 31, |                  |                  |
|---|--------------------------|------------------|------------------|
|   | 2018                     | 2017*            | 2016*            |
| Cash Flows From Operating Activities:   |                          |                  |                  |
| Net income  | \$ 22,093                | \$ 18,354        | \$ 3,719         |
| Adjustments to reconcile net income to net cash provided by operating activities: |                          |                  |                  |
| Stock-based compensation  | 5,240                    | 4,087            | 3,263            |
| Depreciation and amortization   | 3,869                    | 3,666            | 3,680            |
| Amortization of premiums on investments   | 362                      | 460              | 174              |
| Provision for warranty claims   | 326                      | 246              | 208              |
| Reversal of accruals related to expired warranties                                | (180)                    | (200)            | (236)            |
| Unrealized (gain) loss on foreign currency translation                            | (10)                     | 144              | 13               |
| Provision for doubtful accounts   | 336                      | 55               | 76               |
| Adjustments for excess or obsolete inventory                                      | 197                      | 201              | (361)            |
| Deferred income taxes   | (10,385)                 | (8,865)          | (459)            |
| Other non-cash adjustments  | —                        | (196)            | (131)            |
| Changes in operating assets and liabilities:                                      |                          |                  |                  |
| Accounts receivable   | 1,917                    | (761)            | (244)            |
| Contract assets   | 2,196                    | (4,263)          | (130)            |
| Costs and estimated earnings in excess of billings                                |                          |                  |                  |
| Inventories   | (1,872)                  | (1,250)          | 2,287            |
| Prepaid and other assets  | (682)                    | (39)             | (402)            |
| Accounts payable  | (2,274)                  | 2,118            | (360)            |
| Accrued expenses and other liabilities  | 87                       | 611              | (262)            |
| Income taxes payable  | (447)                    | 385              | 398              |
| Litigation settlement   | —                        | —                | —                |
| Contract Liabilities  | (13,616)                 | (11,858)         | (6,268)          |
| Deferred revenue, license and development   |                          |                  |                  |
| Net cash provided by operating activities   | <u>7,565</u>             | <u>2,895</u>     | <u>4,965</u>     |
| Cash Flows From Investing Activities:   |                          |                  |                  |
| Restricted cash   |                          | —                |                  |
| Maturities of marketable securities   | 81,268                   | 49,106           | 7,535            |
| Purchases of marketable securities  | (86,192)                 | (80,641)         | (46,552)         |
| Capital expenditures  | (5,235)                  | (7,376)          | (1,112)          |
| Net cash used in investing activities   | <u>(10,159)</u>          | <u>(38,911)</u>  | <u>(40,129)</u>  |
| Cash Flows From Financing Activities:   |                          |                  |                  |
| Net proceeds from issuance of common stock  | 4,291                    | 5,508            | 6,600            |
| Tax payment for employee shares withheld  | (150)                    | (270)            | —                |
| Proceeds from long-term debt  | —                        | —                | —                |
| Repayment of long-term debt   | (27)                     | (11)             | (10)             |
| Repurchase of common stock  | (10,000)                 | (4,276)          | (9,375)          |
| Net cash (used in) provided by financing activities                               | <u>(5,886)</u>           | <u>951</u>       | <u>(2,785)</u>   |
| Effect of exchange rate differences on cash and cash equivalents                  | <u>(8)</u>               | <u>(57)</u>      | <u>(41)</u>      |
| Net change in cash and cash equivalents and restricted cash                       | <u>(8,488)</u>           | <u>(35,122)</u>  | <u>(37,990)</u>  |
| Cash and cash equivalents and restricted cash, beginning of year                  | 30,626                   | 65,748           | 103,738          |
| Cash and cash equivalents and restricted cash, end of year                        | <u>\$ 22,138</u>         | <u>\$ 30,626</u> | <u>\$ 65,748</u> |

\*Prior-period information has been retrospectively adjusted due to our adoption of ASU 2014-09, *Revenue from Contracts with Customers (Topic 606)* and ASU No. 2016-18, *Statement of Cash Flows, Restricted Cash (Topic 230)* on January 1, 2018.



**ENERGY RECOVERY, INC.**  
**FINANCIAL INFORMATION BY SEGMENT**  
*(Unaudited)*

|                                    | Three Months Ended December 31, 2018 |                   |                 | Three Months Ended December 31, 2017 * |                   |                 |
|------------------------------------|--------------------------------------|-------------------|-----------------|--|-------------------|-----------------|
|                                    | Water                                | Oil & Gas         | Total           | Water                                  | Oil & Gas         | Total           |
|                                    | <i>(In thousands)</i>                |                   |                 |  |                   |                 |
| Product revenue                    | \$ 13,884                            | \$ 99             | \$ 13,983       | \$ 20,594                              | \$ 460            | \$ 21,054       |
| Product cost of revenue            | 3,497                                | 64                | 3,561           | 6,029                                  | 631               | 6,660           |
| Product gross profit               | <u>10,387</u>                        | <u>35</u>         | <u>10,422</u>   | <u>14,565</u>                          | <u>(171)</u>      | <u>14,394</u>   |
| License and development revenue    | —                                    | 3,723             | 3,723           | —                                      | 2,611             | 2,611           |
| Operating expenses:                |                                      |                   |                 |  |                   |                 |
| General and administrative         | 636                                  | 377               | 1,013           | 436                                    | 480               | 916             |
| Sales and marketing                | 1,538                                | 266               | 1,804           | 1,748                                  | 593               | 2,341           |
| Research and development           | 692                                  | 4,526             | 5,218           | 254                                    | 4,483             | 4,737           |
| Amortization of intangibles        | 156                                  | —                 | 156             | 158                                    | —                 | 158             |
| Operating expenses                 | <u>3,022</u>                         | <u>5,169</u>      | <u>8,191</u>    | <u>2,596</u>                           | <u>5,556</u>      | <u>8,152</u>    |
| Operating income (loss)            | <u>\$ 7,365</u>                      | <u>\$ (1,412)</u> | 5,953           | <u>\$ 11,969</u>                       | <u>\$ (3,116)</u> | 8,853           |
| Less: Corporate operating expenses |                                      |                   | <u>(4,533)</u>  |  |                   | <u>4,513</u>    |
| Consolidated operating income      |                                      |                   | 1,420           |  |                   | 4,340           |
| Non-operating income               |                                      |                   | 486             |  |                   | 220             |
| Income before income taxes         |                                      |                   | <u>\$ 1,906</u> |  |                   | <u>\$ 4,560</u> |

**Year Ended December 31, 2018**

|                                    | <b>Water</b> | <b>Oil &amp; Gas</b>  | <b>Total</b> |
|------------------------------------|--------------|-----------------------|--------------|
|                                    |              | <i>(In thousands)</i> |              |
| Product revenue                    | \$ 60,512    | \$ 513                | \$ 61,025    |
| Product cost of revenue            | 17,211       | 662                   | 17,873       |
| Product gross profit               | 43,301       | (149)                 | 43,152       |
| License and development revenue    | —            | 13,490                | 13,490       |
| Operating expenses:                |              |                       |              |
| General and administrative         | 2,078        | 1,771                 | 3,849        |
| Sales and marketing                | 5,783        | 1,264                 | 7,047        |
| Research and development           | 1,711        | 15,276                | 16,987       |
| Amortization of intangibles        | 629          | —                     | 629          |
| Operating expenses                 | 10,201       | 18,311                | 28,512       |
| Operating income (loss)            | \$ 33,100    | \$ (4,970)            | 28,130       |
| Less: Corporate operating expenses |              |                       | 18,152       |
| Consolidated operating income      |              |                       | 9,978        |
| Non-operating income               |              |                       | 1,462        |
| Income before income taxes         |              |                       | \$ 11,440    |

**Year Ended December 31, 2017\***

|                                    | <b>Water</b> | <b>Oil &amp; Gas</b>  | <b>Total</b> |
|------------------------------------|--------------|-----------------------|--------------|
|                                    |              | <i>(In thousands)</i> |              |
| Product revenue                    | \$ 54,301    | \$ 3,722              | \$ 58,023    |
| Product cost of revenue            | 16,032       | 3,029                 | 19,061       |
| Product gross profit               | 38,269       | 693                   | 38,962       |
| License and development revenue    | —            | 11,106                | 11,106       |
| Operating expenses:                |              |                       |              |
| General and administrative         | 1,401        | 1,565                 | 2,966        |
| Sales and marketing                | 5,787        | 2,228                 | 8,015        |
| Research and development           | 1,064        | 12,217                | 13,281       |
| Amortization of intangibles        | 631          | —                     | 631          |
| Operating expenses                 | 8,883        | 16,010                | 24,893       |
| Operating income (loss)            | \$ 29,386    | \$ (4,211)            | 25,175       |
| Less: Corporate operating expenses |              |                       | 15,926       |
| Consolidated operating income      |              |                       | 9,249        |
| Non-operating income               |              |                       | 680          |
| Income before income taxes         |              |                       | \$ 9,929     |

**Year Ended December 31, 2016\***

|                                    | <b>Water</b> | <b>Oil &amp; Gas</b> | <b>Total</b> |
|------------------------------------|--------------|----------------------|--------------|
|                                    |              | <i>(In thousand)</i> |              |
| Product revenue                    | \$ 47,545    | \$ 2,170             | \$ 49,715    |
| Product cost of revenue            | 16,353       | 1,496                | 17,849       |
| Product gross profit               | 31,192       | 674                  | 31,866       |
| License and development revenue    | —            | 8,069                | 8,069        |
| Operating expenses:                |              |                      |              |
| General and administrative         | 1,081        | 1,000                | 2,081        |
| Sales and marketing                | 5,076        | 2,985                | 8,061        |
| Research and development           | 1,331        | 8,705                | 10,036       |
| Amortization of intangibles        | 631          | —                    | 631          |
| Operating expenses                 | 8,119        | 12,690               | 20,809       |
| Operating income (loss)            | \$ 23,073    | \$ (3,947)           | 19,126       |
| Less: Corporate operating expenses |              |                      | 15,700       |
| Consolidated operating income      |              |                      | 3,426        |
| Non-operating income               |              |                      | 287          |
| Income before income taxes         |              |                      | \$ 3,713     |

\*Prior-period information has been retrospectively adjusted due to our adoption of ASU 2014-09, *Revenue from Contracts with Customers (Topic 606)* and ASU No. 2016-18, *Statement of Cash Flows, Restricted Cash (Topic 230)* on January 1, 2018.

## ENERGY RECOVERY, INC. RECONCILIATION OF NON-GAAP FINANCIAL MEASURES

*(In thousands, except per share data)*

*(Unaudited)*

This press release includes non-GAAP financial information because we plan and manage our business using such information. Our non-GAAP Total Gross Margin is determined by adding back the license and development revenue associated with the amortization of the VorTeq exclusivity fee. Our non-GAAP Adjusted Net Income or Loss is determined by adding back non-recurring operating expenses and tax expenses/(benefits)

|   | Three Months Ended<br>December 31, |                  | Years Ended<br>December 31, |                  |
|---|------------------------------------|------------------|-----------------------------|------------------|
|   | 2018                               | 2017*            | 2018                        | 2017*            |
| Product revenue   | \$ 13,983                          | \$ 21,054        | \$ 61,025                   | \$ 58,023        |
| License and development revenue                         | 3,723                              | 2,611            | 13,490                      | 11,106           |
| Total revenue   | <u>\$ 17,706</u>                   | <u>\$ 23,665</u> | <u>\$ 74,515</u>            | <u>\$ 69,129</u> |
| Product gross profit                                    | \$ 10,422                          | \$ 14,394        | \$ 43,152                   | \$ 38,962        |
| License and development revenue                         | 3,723                              | 2,611            | 13,490                      | 11,106           |
| Total gross profit (non-GAAP)                           | <u>\$ 14,145</u>                   | <u>\$ 17,005</u> | <u>\$ 56,642</u>            | <u>\$ 50,068</u> |
| Product gross margin                                    | 74.5 %                             | 68.4 %           | 70.7 %                      | 67.1 %           |
| Total gross margin (non-GAAP)                           | 79.9 %                             | 71.9 %           | 76.0 %                      | 72.4 %           |
| Net income (loss)                                       | \$ 2,418                           | \$ 13,531        | \$ 22,093                   | \$ 18,354        |
| Reversal of non-recurring expense (benefit) (non-GAAP)  | (649)                              | (8,348)          | (11,159)                    | (8,394)          |
| Adjusted net income (loss) (non-GAAP)                   | <u>\$ 1,769</u>                    | <u>\$ 5,183</u>  | <u>\$ 10,934</u>            | <u>\$ 9,960</u>  |
| Income (loss) per share:                                |                                    |                  |                             |                  |
| Diluted   | \$ 0.04                            | \$ 0.24          | \$ 0.40                     | \$ 0.33          |
| Diluted (non-GAAP)                                      | \$ 0.03                            | \$ 0.09          | \$ 0.20                     | \$ 0.18          |
| Number of diluted shares used in per share calculations | <u>55,217</u>                      | <u>55,715</u>    | <u>55,338</u>               | <u>55,612</u>    |

\*Prior-period information has been retrospectively adjusted due to our adoption of ASU 2014-09, *Revenue from Contracts with Customers (Topic 606)* and ASU No. 2016-18, *Statement of Cash Flows, Restricted Cash (Topic 230)* on January 1, 2018.

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