

August 4, 2011

Investment Analysis for Intelligent Investors

IWG Technologies Inc. (TSX-V: IWG) - Acquires Complimentary Product Line; Raising Revenue/EPS Estimates

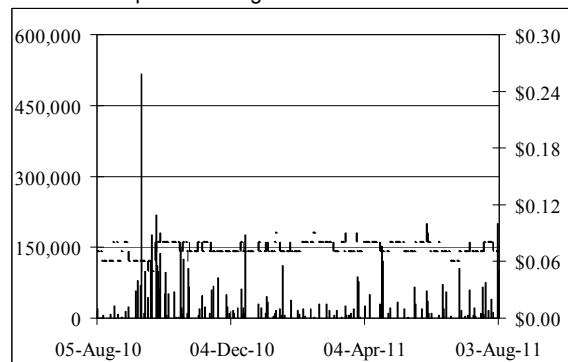
Sector/Industry: Aerospace Products and Services

www.iwgtech.com

Market Data (as of August 4, 2011)

Current Price	C\$0.07
Fair Value	C\$0.30 (↑)
Rating*	BUY
Risk*	3 (Average)
52 Week Range	C\$0.05 –C\$0.10
Shares O/S	37.87 mm
Market Cap	C\$2.65 mm
P/S (forward)	0.6x
P/E (forward)	9.2x
P/B	0.9x
YoY Return	0.0%
YoY TSX-V	36.4%

*see back of report for rating and risk definitions



Highlights

- On July 8, 2011, the company completed the acquisition of the aviation water heater product line of Keltech, Inc. for US\$0.70 million (US\$0.35 million was paid upfront; the balance will be paid over the next four years).
- IWG's water treatment units and Keltech's water heaters are complimentary products and have similar target markets. IWG can now market the water heaters to IWG's customers as well as market their water treatment units to Keltech's customers.
- Keltech was generating about \$0.50 million per year from this product line.
- On July 20, 2011, within two weeks of the acquisition, IWG announced it received its first order for the water heaters.
- Q3-2011 revenues were up 4% from \$1.06 million to \$1.10 million. Q3-2011 earnings were \$1,196 (EPS: \$0.00), up from a loss of \$0.12 million (EPS: -\$0.00) in Q3-2010.
- We have raised our revenue and EPS forecasts for FY2011 and FY2012.
- Despite the upfront cash payment of US\$0.35 million for the acquisition, we expect the company to continue to maintain a strong balance sheet.

Financial Summary (YE Sept 30)

(C\$)	2008	2009	2010	2011E	2012E
Revenue	4,156,469	4,952,911	4,381,894	4,536,705	5,297,992
Gross Margin	53.75%	63.11%	54.35%	54.75%	55.00%
Net Income	(97,044)	312,016	135,423	288,990	370,218
EPS (basic)	(0.00)	0.01	0.00	0.01	0.01
Cash	940,302	1,362,363	1,122,172	922,972	1,148,508
Assets	2,941,421	3,249,308	3,350,627	3,575,134	4,059,352
Debt to Capital	3.44%	1.57%	1.05%	0.37%	0.22%
ROE	-4.41%	12.09%	4.78%	9.53%	11.01%
ROIC	-6.11%	20.87%	8.32%	14.24%	15.84%

International Water-Guard Industries Inc. ("IWG"), based in Burnaby, BC, Canada, focuses on the design, manufacture, sale, and service of aircraft potable water treatment equipment and systems. IWG has been selling its products to corporate, VIP and military transport manufacturers/operators around the world since 1982. The company is now seeking to break into the largest market of the aircraft industry, the commercial airline sector.

Acquires Aviation Water Heater Products

On July 8, 2011, the company completed the acquisition of the aviation water heater product line of Michigan based Keltech, Inc. for US\$0.70 million (US\$0.35 million was paid upfront; the balance will be paid over the next four years).

Keltech, a private company founded in 1987, produces tankless water heating solutions. Tankless water heaters are typically energy efficient as they only draw energy when required - a feature that makes it an ideal solution for consumers/businesses that do not require hot water continuously. The company started with products targeting residential applications, and gradually expanded to industrial and commercial applications. Keltech currently has 80+ products, including four patents. The following chart shows a list of their products targeting various segments.

	Large Industrial	Light Industrial	Commercial	Light Commercial / Residential	Safety Shower	Emergency Eyewash	Aircraft
Product Line Name	CN Series	C1N Series C2N Series	L and HL Series	Standard Series	SN Series	CLE Series	E87 Series
Display							
ASME Certified	ASME HLW and National Board BPV Certified Options Available	N/A	N/A	N/A	ASME HLW and National Board BPV Certified Options Available	N/A	N/A

Source: Keltech

IWG acquired the aircraft water heater product line (extreme right on the above image). These water heaters will be typically used in aircraft showers and galleys. The following table shows the product's specifications:

Specifications	
Dimensions	Height 15.25" Width: 14" Depth: 4.25"
kW Range	5-18 KW
Flow Range	0.5 - 2.5 GPM
Set Point Temperature	100F-140F - Digital

Source: Keltech

The main advantage for IWG is that both IWG and Keltech's products are

complementary and have similar target markets. IWG can now market the water heaters to their customers as well as market their water treatment units to Keltech's customers.

Keltech had annual revenues of about \$0.50 million from this product line. Therefore, the acquisition price of US\$0.70 million reflects a P/S ratio of 1.4x. Recent acquisitions in the Aerospace and Defence Industry suggest that the acquisition price is reasonable. P/S ratios of few recent transactions include: Astrium's acquisition of Vizada - 1.5x, Airbus's acquisition of Satair (CPSE:SAT) - 1.3x, ILFC's acquisition of AeroTurbine - 0.9x.

Receives first order - IWG announced on July 20, 2011, that they received their first order for their new IWG-ES7 On-Demand Aircraft Water Heater. According to management, the company has already started to see *"a very positive response"* from their existing customer base. **We believe it is highly encouraging that the company was able to get its first order in less than two week of the acquisition.**

According to the company, they should have **authorization to ship units as aeronautical products with a Transport Canada Form One in the next few months.** IWG's AS9100 quality status and engineering and certification expertise specific to the aviation market would be highly beneficial in this process.

According to management, existing product patents on the water heater have expired. We believe that the aerospace qualifications (which IWG expects to receive shortly) and Keltech's long track record will be the primary competitive advantages.

Q3-2011 Performance

Q3-2011 revenues were up 4% YOY from \$1.06 million to \$1.10 million. We were very pleased to see that revenues were in line with our expectations because - a) revenues in the first six months of FY2011 were down 1%YOY, and b) the US\$ (versus the C\$) was 9% weaker YOY in Q3-2011. We estimate that the growth primarily came from increased sales of water treatment units.

Stronger sales and a significant drop in selling expenses (due to reductions in promotional activities) resulted in stronger margins in Q3-2011 as show in the table below:

Margins	2010-Q3	2010-Q3
Gross	52.59%	54.85%
EBITDA	-6.29%	9.92%
EBIT	-7.64%	8.78%
EBT	-8.15%	8.48%
Net Margin	-10.81%	0.11%

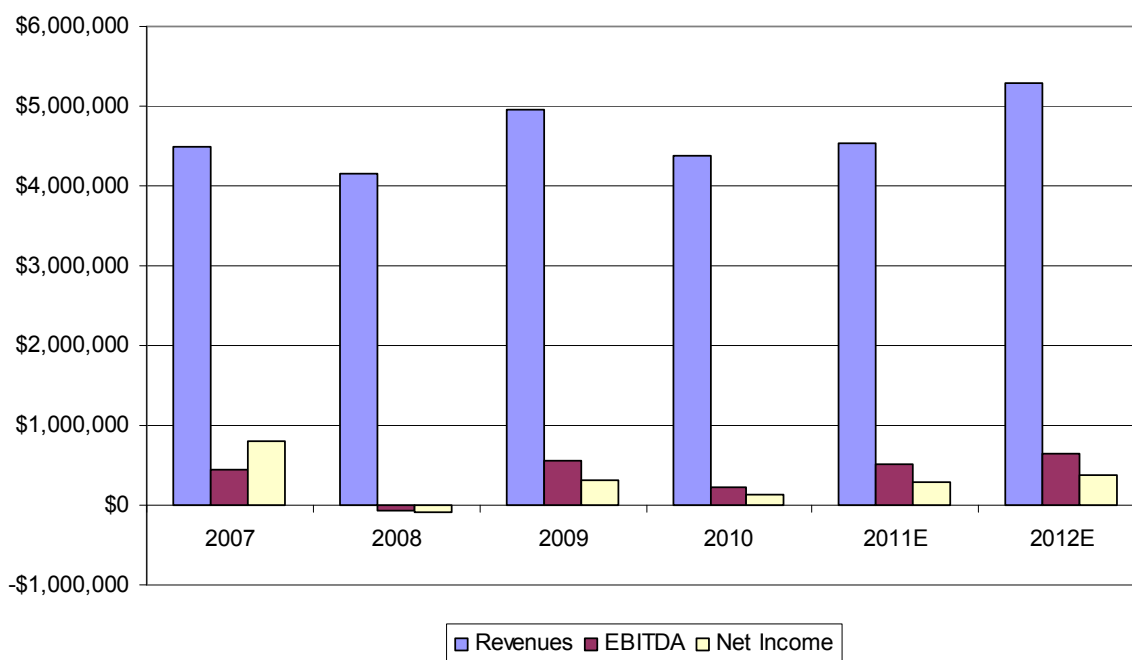
Q3-2011 earnings were \$1,196 (EPS: \$0.00), up from a loss of \$0.12 million (EPS: -\$0.00) in Q3-2010. In the first nine months, the company reported net income of \$0.12 million (EPS: \$0.00) versus a net loss of \$0.02 million (EPS: -\$0.00) in the comparable period in the previous year.

Revenue growth and the improvement in margins resulted in strong growth in cash flow from operations from a negative \$0.08 million in Q3-2010, to a positive \$0.11 million in Q3-

2011. The company had cash of \$1.15 million at the end of Q3, up from \$1.11 million at the end of Q2.

Revenue and EPS Forecasts

We have raised our revenue and EPS forecasts for FY2011, and FY2012, (primarily as a result of the acquisition). Our revised revenue forecasts are \$4.54 million (up from \$4.41 million) and \$5.30 million (up from \$4.80 million). Our net income forecasts are \$0.29 million (EPS: \$0.01) and \$0.37 million (EPS: \$0.01). Our previous forecasts were \$0.19 million (EPS: \$0.01) and \$0.20 million (EPS: \$0.01), respectively.



Cash Position Despite the US\$0.35 million payment in July, we expect the company to maintain its strong balance sheet, as shown in the following table.

Liquidity Analysis	2008	2009	2010	2011E
Working Capital	\$1,722,974	\$2,266,003	\$2,289,382	\$2,053,793
Current Ratio	4.52	5.77	6.34	5.94
Debt / Capital	3.4%	1.6%	1.05%	0.4%
EBIT Interest Coverage Ratio	(11.6)	30.2	8.2	29.5

Stock Options and Warrants

We estimate the company currently has 2.46 million stock options outstanding (weighted average exercise price of \$0.13) and 5 million warrants outstanding exercisable at \$0.17 (expiry date - August 2011).

Valuation and Rating

Our revised DCF valuation is \$0.30 per share (previous estimate: \$0.25 per share) as we raised our revenue/EPS forecasts.

DCF Valuation Model								
	Q4-2011	2012E	2013E	2014E	2015E	2016E	2017E	2018E
FFO	\$215,577	\$505,888	\$741,697	\$917,097	\$1,123,381	\$1,259,414	\$1,406,490	\$1,439,593
Investment in WC	(\$51,221)	(\$8,996)	(\$143,912)	(\$182,638)	\$277,129	(\$112,309)	(\$123,540)	(\$67,947)
CFO	\$164,356	\$496,892	\$597,785	\$734,459	\$1,400,510	\$1,147,105	\$1,282,950	\$1,371,646
CAPEX	(\$405,171)	(\$267,500)	(\$30,000)	(\$30,000)	(\$30,000)	(\$30,000)	(\$30,000)	(\$30,000)
FCF	(\$240,815)	\$229,392	\$567,785	\$704,459	\$1,370,510	\$1,117,105	\$1,252,950	\$1,341,646
PV	(\$234,088)	\$199,093	\$439,991	\$487,413	\$846,653	\$616,168	\$617,051	\$7,341,466
Discount Rate	12%							
Terminal Growth Rate	3%							
Total PV	\$10,313,747							
Cash - Debt	\$1,133,448							
Equity Value	\$11,447,195							
Shares O/S (dil)	37,871,694							
Value per share	\$0.30							

We reiterate our BUY rating and raise our fair value estimate from \$0.25 per share to \$0.30 per share.

Risk

The following risks, though not exhaustive, will cause our estimates to differ from actual results:

- Growth of the company is highly dependent on the overall health of the aerospace industry
- IWG's revenues are dependent on aircraft delivery rates and are subject to industry cycles and customer adoption of its products.
- A significant portion of revenues is non-recurring.
- The company has yet to break into the commercial aircraft sector, the largest market in the aerospace industry.
- Foreign exchange fluctuation risks: Most of IWG's sales are in US dollars.

We have maintained our risk rating at 3 (Average).

Appendix

STATEMENTS OF OPERATIONS (in C\$)	2008	2009	2010	2011E	2012E
Sales	4,156,469	4,952,911	4,381,894	4,536,705	5,297,992
COGS	1,922,205	1,827,070	2,000,349	2,052,859	2,384,096
Gross Profit	2,234,264	3,125,841	2,381,545	2,483,846	2,913,896
Expenses					
Selling Expenses	328,773	427,924	449,708	419,645	503,309
Research&Development	772,194	875,219	421,517	432,783	443,603
General & Administration	1,186,442	1,230,689	1,264,151	1,207,845	1,262,416
Stock Option Compensation	18,408	35,396	27,364	32,422	52,980
Foreign exchange loss(gain)				(120,000)	
EBITDA	(71,553)	556,613	218,805	511,151	651,588
Amortization	64,758	60,389	56,969	57,091	82,691
EBIT	(136,311)	496,224	161,836	454,060	568,897
Interest & Bank Charges	11,733	16,454	19,715	15,399	6,940
	-				
Earnings from operations, before undernoted	(148,044)	479,770	142,121	438,662	561,957
Government Assistance					
Gains on settlement of notes and accounts payable	-	-	-	-	-
Gain on sale of commercial division assets	-	-	-	-	-
Foreign Exchange		(54,754)	47,202		
Write-down of assets and costs	-	-	-	-	-
Extraordinary					
EBT	(148,044)	425,016	189,323	438,662	561,957
Taxes/(Income Tax Recovery)	(51,000)	113,000	53,900	149,671	191,740
Net Earnings for the period	(97,044)	312,016	135,423	288,990	370,218

BALANCE SHEETS (in C\$)	2008	2009	2010	2011E	2012E
Assets					
Cash	940,302	1,362,363	1,122,172	922,972	1,148,508
Accounts receivable	710,770	672,010	880,150	873,552	850,116
Inventory	496,335	577,993	569,976	557,901	647,920
Prepaid Expenses	65,407	42,807	75,696	45,168	52,456
Future Income Tax		86,000	70,000	70,000	70,000
Current Assets	2,212,814	2,741,173	2,717,994	2,469,592	2,769,001
Equipment & Furniture	250,607	229,135	213,363	536,272	571,081
Deferred Dev Costs and foreign exchange loss			178,170	328,170	478,170
Future income tax assets	478,000	279,000	241,100	241,100	241,100
Total Assets	2,941,421	3,249,308	3,350,627	3,575,134	4,059,352
Liabilities & Shareholders' Equity					
Accounts Payables & Accrued Liabilities	449,247	449,413	409,381	411,943	476,819
Demand / Factoring Loan	-	-	-	-	-
Customer Deposits, Bank and Shareholder's loan					
Current portion of capital lease obligations and loan	40,593	25,757	19,231	3,855	-
Current portion of notes payable					
Current Liabilities	489,840	475,170	428,612	415,799	476,819
Convertible Debentures					
Obligations under capital lease and other loan	45,206	18,101	11,566	7,711	7,711
Notes and Loans payable					
Shareholder's Equity					
Share Capital	8,108,202	8,111,487	8,103,112	8,022,876	8,022,876
Contributed surplus	165,803	200,164	227,528	259,950	312,930
Deficit	(5,867,630)	(5,555,614)	(5,420,191)	(5,131,201)	(4,760,983)
Total Liabilities & Shareholders' Equity	2,941,421	3,249,308	3,350,627	3,575,134	4,059,352

STATEMENTS OF CASH FLOWS

(in C\$)	2008	2009	2010	2011E	2012E
Operating Activities					
Net earnings for the period	(97,044)	312,016	135,423	288,990	370,218
Items not involving cash					
Income tax recovery	(51,000)	113,000	53,900		
Gain on liabilities and sale of commercial division					
Unrealized foreign exchange and other gains	(6,500)	(47,688)	24,024		
Compensation related to stock option plan	18,408	35,396	27,364	32,422	52,980
Write-downs					
Interest accrued (on NP, on shareholder loan)					
Amortization and equipment write-down	64,758	60,388	56,969	57,091	82,691
	(71,378)	473,112	297,680	378,503	505,888
Changes in non-cash operating working capital					
Accounts receivable	17,008	86,448	(232,164)	6,598	23,436
Inventory	145,897	(81,658)	8,017	12,075	(90,020)
Prepaid expenses	(27,438)	22,600	(32,889)	30,528	(7,288)
Accounts payable and accrued liabilities	24,175	166	(40,032)	2,562	64,876
Customer Deposits	-	-	-	-	-
	159,642	27,556	(297,068)	51,764	(8,996)
Cash from from (used in) operations	88,264	500,668	612	430,267	496,892
Investing activities					
Purchase of furniture and equipment	(47,173)	(38,916)	(25,074)	(30,000)	(30,000)
Product development costs incurred			(178,170)	(150,000)	(150,000)
Acquisition Costs				(350,000)	(87,500)
Proceeds on sale of commercial division					
Deferred Development Costs					
Purchase of equipment and leaseholds	(47,173)	(38,916)	(203,244)	(530,000)	(267,500)
Financing activities					
Proceeds (repayments) of demand loans					
Proceeds (repayments) of payables and leases	(33,801)	(41,941)	(29,184)	(19,231)	(3,855)
Convertible debenture issued					
Issue of common share for cash	494,080	2,250		-	
Purchase of capital stock			(8,375)	(80,236)	
	460,279	(39,691)	(37,559)	(99,467)	(3,855)
Increase (decrease) in cash	501,370	422,061	(240,191)	(199,200)	225,537
Cash beginning of period	438,932	940,302	1,362,363	1,122,172	922,972
Cash end of period	940,302	1,362,363	1,122,172	922,972	1,148,508

Buy – Annual expected rate of return exceeds 12% or the expected return is commensurate with risk

Hold – Annual expected rate of return is between 5% and 12%

Sell – Annual expected rate of return is below 5% or the expected return is not commensurate with risk

Suspended or Rating N/A— Coverage and ratings suspended until more information can be obtained from the company regarding recent events.

Fundamental Research Corp. Risk Rating Scale:

1 (Low Risk) - The company operates in an industry where it has a strong position (for example a monopoly, high market share etc.) or operates in a regulated industry. The future outlook is stable or positive for the industry. The company generates positive free cash flow and has a history of profitability. The capital structure is conservative with little or no debt.

2 (Below Average Risk) - The company operates in an industry where the fundamentals and outlook are positive. The industry and company are relatively less sensitive to systematic risk than companies with a Risk Rating of 3. The company has a history of profitability and has demonstrated its ability to generate positive free cash flows (though current free cash flow may be negative due to capital investment). The company's capital structure is conservative with little to modest use of debt.

3 (Average Risk) - The company operates in an industry that has average sensitivity to systematic risk. The industry may be cyclical. Profits and cash flow are sensitive to economic factors although the company has demonstrated its ability to generate positive earnings and cash flow. Debt use is in line with industry averages, and coverage ratios are sufficient.

4 (Speculative) - The company has little or no history of generating earnings or cash flow. Debt use is higher. These companies may be in start-up mode or in a turnaround situation. These companies should be considered speculative.

5 (Highly Speculative) - The company has no history of generating earnings or cash flow. They may operate in a new industry with new, and unproven products. Products may be at the development stage, testing, or seeking regulatory approval. These companies may run into liquidity issues, and may rely on external funding. These stocks are considered highly speculative.

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The distribution of FRC's ratings are as follows: BUY (68%), HOLD (7%), SELL (4%), SUSPEND (21%).

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