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Investment Thesis: Consolidated Water Company (CWCO)

Summary

Desalinated water provider CWCO is down over 40% from 2020 highs due to several shocks to its businesses and uncertainties in its negotiations with regulators. I believe the market is currently pricing its water production business at 10-12x its 2021E reported earnings, normalized for COVID-19 effects and that earnings for its water production segment are already being underrecognized by the market due to the company's accounting decisions. Thus I believe CWCO is conservatively worth 20% more than current market price, and that it can easily justify 30+% premiums given that utility peers often trade at P/E multiples of 20x+, electric utilities in the same territories trade at 16x, and that the company has virtually no debt load with ample liquidity. I believe the higher valuation can be realized when long-term supply agreements are finalized and when impairment losses of a project cancellation (which has no associated debts and has been priced in) stop impacting the income statement. This will allow investors to realize the true profitability of the water-production business and assign a more appropriate multiple.

Company Background

Consolidated Water Company (CWCO) is a utility company that specializes in seawater desalination projects in the Cayman Islands, Bahamas, and United States. CWCO has operated in the Cayman Islands since 1979, and its water is sold both directly to customers and in bulk to government-owned utilities. CWCO has the following main business segments (See Appendix 1):

1. Retail Water Operations (38% of 2019 revenue) in which CWCO provides water directly to customers in the Seven Mile Beach and West Bay areas of the Cayman Islands. This operation was previously part of an exclusive retail license issued by the Cayman Islands government which first expired in 2010 but has been extended multiple times. The license once again expired in 2018 and has not yet been renewed, and the government has stated intentions to lower prices in future agreements. CWCO has been supplying water under the terms of the previous agreement on a good faith basis for the past 2+ years.
2. Bulk Water Operations (39% of 2019 revenue) in which CWCO is contracted to operate desalination plants and provide water to government-owned utilities in the Bahamas and Cayman Islands.
3. Manufacturing Operations (20% of 2019 Revenues) in which CWCO manufactures specialized and custom products related to desalination and water utilities. Production is headquartered in Florida and substantially all customers are American.
4. Services Operations (3% or 2019 Revenues) in which CWCO and its subsidiaries provide operations and management services of water and wastewater plants in the United States, British Virgin Islands, and Mexico. The services segment includes a (now cancelled) plan to build and service a 100 million gallon per day desalination plant in Baja California, Mexico.

Company Headwinds

CWCO's market price has fallen by 40+% from 2020 highs due to project cancellations, uncertainty regarding retail operations, and recent price cuts in the bulk water operations. First in June 2020, the Baja California government cancelled the Rosarito desalination plant project to the surprise of investors and the company, which had already invested at least $20 million in land alone into the project (See Appendix 2). There is uncertainty concerning the future of the project as the CWCO's affiliates planned to sue to recover costs, yet there have also been talks of resuming the project on a smaller scale as Baja California governor Jaime Bonilla had always been a public proponent of the project.

In addition, the retail water operations include more risks than average utilities due to the lack of an active service agreement with the Cayman Islands government regulator. The previous exclusive license for the Seven Mile Beach and West Bay areas of the Grand Caymans expired in 2018 and has not been renewed. For the previous 2 years, CWCO has been supplying water on a good faith basis under the previous terms of the license as the terms could not be reached with the government. Instead government regulators have denied requests for CWCO to raise prices in 2017 and stated that they intend to amend future agreements to include price cuts.

Lastly in its Bulk Water Operations, CWCO manages three desalination plants for the state-owned utility in the Cayman Islands and the service contracts for these plants all expired in 2019. CWCO managed to renew all three contracts but at approximate reductions in price per gallon of freshwater of 25%, 25% and 29% from 2018 prices for the three plants.

Valuation by Parts

Water Production Plant Management

Rather than making detailed attribution decisions or attributing general SG&A expenses based on revenue contribution, **CWCO attributes all "non-direct" SG&A expenses to its retail segment**, making it more difficult to value each segment separately. Based on the low P/E multiples for which CWCO acquired other segments of its businesses (which will be addressed below), I believe this accounting method understates retail water earnings, while overstating that of other segments. The company has allocated SG&A in a similar manner since at least 2007, and this decision may have the coincidental effect of lowering retail segment net incomes as part of the bargaining for a long-term supply contract with the government.

Nonetheless I will consider the retail and bulk water production segments together since the business geographies and operations are largely the same; CWCO manages desalination plants to produce water which is eventually delivered to end consumers. In addition, these two segments have the same drivers of supply and demand; mainly alternative supplies of water are affected by rainwater and demand is driven by tourist arrivals and populations of the Cayman Islands and Bahamas. I make the following assumptions:

1. 2019 is an indicative base year for these operations as 2019 did not have any tourism effects of COVID-19. Because the bulk water operation agreements between CWCO and the Cayman Islands government utility were signed in February 2020 for two water plants and in June 2020 for one, the 2019 revenues are mostly reflective of future cash flows in this segment (Financial statements all in Appendix 7).

2. Water demand is projected to be negatively impacted due to COVID-19 in 2020 as supported by quarterly results, but I will assume that 2021 will be a “normal year” with no changes from 2019 in terms of real water demand.
3. I will project 1% increases in SG&A in 2020 and 2021.
4. Given the lack of an effective supply contract in the retail segment, I will project that in 2021 an agreement is reached in which retail prices are cut by 10%. This is reflected by decreasing 2021/2019 revenues by 10% and keeping COGS constant. The resulting gross margin is 51.23% from 56.11% in 2019. In actuality, such price cuts may not materialize in 2021 since CWCO has not operated with a long-term license since 2010.
5. I will not reallocate non-direct SG&A away from this segment in order to be coservative.

Projection Inputs							
2020 Retail Revenue Change (Constant Margins)	-10%	-3.27%	Actual 2020 1H YOY Change				
2020 Bulk Revenue Change	-15%	-12.42%	Actual 2020 1H YOY Change				
2021/2019 Retail Revenue Change (Constant COGS	-10%						
	2018		**2019**		**2020E**	2021/2019	**2021**
Retail Revenues	25,621,048	3.26%	26,456,022	-10.00%	23,810,420	-10%	23,810,420
Retail COGS	11,011,456	5.45%	11,611,165	-10.00%	10,450,049	0.00%	11,611,165
Retail Gross Profit	14,609,592	1.61%	14,844,857	-10.00%	13,360,371	-8.69%	12,199,255
Retail Gross Profit Margin	57.02%	-1.60%	56.11%	0.00%	56.11%	-8.69%	51.23%
Retail SGA (Total CWCO SGA)	12,029,646	11.58%	13,422,821	1.00%	13,557,049	1.00%	13,692,620
(Gain) From Sale of Assets	0		398,041		-		-
Retail Net Recurring Income	2,579,946	-44.88%	1,422,036		(196,678)		(1,493,365)
Bulk Water Revenues	31,031,287	-13.04%	26,986,108	-15.00%	22,938,192	0.00%	26,986,108
Bulk Water COGS	21,551,383	-13.66%	18,606,805	-15.00%	15,815,784	0.00%	18,606,805
Bulk Water Gross Profit	9,479,904	-11.61%	8,379,303	-15.00%	7,122,408	0.00%	8,379,303
Bulk Water Gross Margin	30.55%	1.64%	31.05%	0.00%	31.05%	0.00%	31.05%
Bulk Water SGA	1,301,042	-4.82%	1,238,296	1.00%	1,250,679	1.00%	1,263,186
Bulk Water Net Recurring Income	8,178,862	-12.69%	7,141,007	-17.77%	5,871,729	-0.35%	7,116,117
							-
Water Production Net Recurring Income	**10,758,808**	**-20.41%**	**8,563,043**	**-33.73%**	**5,675,051**	**-34.34%**	**5,622,752**

The result is that future net incomes are expected to decrease about $3 million per year to approximately $5.6 million per year. I apply the below multiples valuation on 2021 expected earnings.

Water Production 2021 Expected Earnings	5,622,752								
Water Production P/E 2021E	12	13	14	15	16	17	18	19	20
Water Production Segment Valuation	67,473,028	73,095,781	78,718,533	84,341,285	89,964,038	95,586,790	101,209,542	106,832,295	112,455,047

I obtained a valuation of the water production business ranging from **$67 million to $112 million** based on PE multiples ranging from 12-20. I believe a multiple in the mid-teens to be reasonable, if not conservative. First the valuations are also lower than the carrying values of these segments’ assets below which CWCO owns outright. Thus if in the worst case no agreement is reached with regulators regarding its retail business, the government would have to make significant investments to purchase these plant assets to operate these segments - resources and expertise it likely lacks since it contracts CWCO to operate its own desalination plants. This fact also explains why CWCO has been able to operate its retail business for so long without an official long-term license, CWCO is established on the island, there are no private competitors that can operate without significant investment, and lastly the government lacks leverage in forcing CWCO to accept any price cuts.

	Retail	Bulk
Accounts receivable, net	$ 2,872,089	$ 20,126,330
Inventory, current and non-current	$ 2,758,051	$ 4,138,547
Property, plant and equipment, net	$ 28,701,759	$ 29,253,459
Construction in progress	$ 225,663	$ 31,737
Intangibles, net	$ —	$ —
Goodwill	$ 1,170,511	$ 1,948,875
Land and rights of way	$ —	$ —
Total segment assets	$ 52,401,338	$ 72,695,342

Source: CWCO 2020 Q2 quarterly report

Second, the U.S. average gross margins in the water utility industry is approximately 56%, in line with current CWCO figures. CWCO can therefore be understood to be charging customers fair fees that reflect the increased costs of desalination in island environments. Though I modelled a 10% future price reduction in water, reductions may be smaller in scale or may not materialize for some time.

In addition, water is not even the most expensive utility in the Cayman Islands for average customers, electricity is. Electricity is provided by Cayman Utilities Company (CUC) which is an actual monopoly that supplies the entire island's electricity and is more likely to be a target of regulatory attention in the future. CUC trades on the Toronto Stock Exchange at a market capitalization of $478 million or 16.69x 2019 earnings as of 9/24/20 (Appendix 3). CUC also lists $295 million of long-term debt as of 2Q 2020 (Appendix 4) whereas CWCO has $11 million of total liabilities across all its segments. Thus I consider valuing CWCO's water projects at only 12-20x 2021 expected reported earnings to be extremely conservative.

In addition, I projected no increase in demand for water from 2019 to 2021. However assuming COVID-19 related effects are resolved, tourism may be a long-term growth driver. The 351-room Grand Hyatt Grand Cayman Hotel and Residences is expected to open in 2021 at Seven Mile Beach, within CWCO's current retail service area which currently includes approximately 6,300 residential and commercial customers. In addition, the 80-room CURIO Collection by Hilton Hotel is also expected to open on the island in 2021. The below tourist arrivals numbers also show the general increase over the past 5 years.

Tourist Arrivals to the Cayman Islands

(for the years ended December 31)

	2019	2018	2017	2016	2015
By Air	502,739	463,001	418,403	385,451	385,379
By Sea	1,831,011	1,921,057	1,728,444	1,711,849	1,716,812
Total	2,333,750	2,384,058	2,146,847	2,097,300	2,102,191

Source: Carribean Utilities Company 2019 Annual Report

Thus for our base case, I will use CUC's PE ratio of 16 to obtain a valuation of **$89 million** for this main segment.

Services Segment
The main operations within the services segment was the planned 100 million gallon per day desalination plant in Baja California which has been in planning since 2012. Under the terms of the previous agreement, CWCO's subsidiary company has invested \$20.6 million in land involved with the project. CWCO was to then sell 65-75% of the equity in its subsidiary to partners that would help fund and construct the project, and CWCO's affiliate company would enter into an agreement to operate the desalination plant while also retaining 23-35% of the equity interest of the plant. The plant would then be transferred to the Mexican government after 37 years of operation. However the plan was cancelled due to negative macroeconomic factors (exchange rates and interest rates), and it is unclear how much CWCO has invested in the project and how much it can recover. In addition, there have been discussions of reviving the project on a smaller scale, but nothing definitive has been made public. Thus valuing this part of the services segment at \$21.6 million, the carrying value of associated lands and right of use assets after impairment may be reasonable.

In addition, as of December 2019, CWCO has an investment of \$1.9 million in OC-BVI which also provides water desalination services in the British Virgin Islands. Likewise, in October 2019, CWCO purchased 51% of PERC, a water treatment service provider in the United States for \$3.1 million, and in August of 2020 CWCO purchased another 10% for \$900,000 and thus valuing PERC at \$9 million and its 61% stake at \$5.4 million.

By summing the recent valuations of PERC and OC-BVI and the amount likely to be recovered in Baja California, we get a segment value of **approximately \$28 million.**

Manufacturing Segment
In January 2020, CWCO acquired all outstanding interests in its manufacturing affiliate Aerex (49%) for \$8.5 million, implying a **value of \$17 million** for the entire company which makes up the entirety of the manufacturing segment. I will use this value for the segment as it seems reasonable given the recent acquisition date. However given 2019 reported earnings for this segment was \$2,558,313 (Appendix 1) and H1 2020 earnings were \$2,114,166 (Appendix 6), this implies a P/E of less than 7x 2019 earnings and less than 5x 2020 earnings (provided H2 2020 matches H1 2020). These low multiples suggest the importance of the non-direct SG&A allocations which CWCO allocates entirely to the retail segment.

If we choose to allocate some of the non-direct SG&A to manufacturing, we can do so either by estimating a P/E ratio for the manufacturing segment or by allocating costs on the basis of revenue contribution. In the P/E ratio method, if we assume reasonable P/E ratios for the Aerex acquisition, we can therefore calculate "implied earnings" and then deduce the non-direct SG&A for the manufacturing segment that was attributed to the retail segment. This method differs from the simplistic method of attributing non-direct SG&A based only on revenue contribution.

The below calculations first show the extra SG&A costs attributed to retail using the different methods.

Manufacturing Segment Value	17,000,000	17,000,000	17,000,000	17,000,000	17,000,000	17,000,000	17,000,000	17,000,000	17,000,000	17,000,000	17,000,000
Assumed P/E	15	16	17	18	19	20	21	22	23	24	25
2019 Implied Earnings	1,133,333	1,062,500	1,000,000	944,444	894,737	850,000	809,524	772,727	739,130	708,333	680,000
2019 Reported Earnings	2,558,313	2,558,313	2,558,313	2,558,313	2,558,313	2,558,313	2,558,313	2,558,313	2,558,313	2,558,313	2,558,313
2019 Manufacturing Nondirect SGA from PE	1,424,980	1,495,813	1,558,313	1,613,869	1,663,576	1,708,313	1,748,789	1,785,586	1,819,183	1,849,980	1,878,313
2019 Firmwide nondirect SGA	12,029,646	12,029,646	12,029,646	12,029,646	12,029,646	12,029,646	12,029,646	12,029,646	12,029,646	12,029,646	12,029,646
Manufacturing as % of total revenues	20%	20%	20%	20%	20%	20%	20%	20%	20%	20%	20%
2019 Manufacturing nondirect SGA from Revenues	2,405,929	2,405,929	2,405,929	2,405,929	2,405,929	2,405,929	2,405,929	2,405,929	2,405,929	2,405,929	2,405,929

The P/E method allocates less SG&A costs to manufacturing, and I believe it is more fundamentally sound as it supports the acquisition price of the manufacturing segment. In either case, we can see that retail segment SG&A is overstated by about $1.5 million. I will therefore use this method and an assumed P/E ratio for the retail water segment to calculate the marginal additional value of the retail water segment if we reallocate SG&A costs.

	Retail Marginal Additional Value With Manufacturing Assumed PE Ratio (X) vs. Retail PE Ratio (Y)										
14,714,243	15	16	17	18	19	20	21	22	23	24	25
15	14,714,243	13,651,743	12,714,243	11,880,910	11,135,296	10,464,243	9,857,100	9,305,152	8,801,200	8,339,243	7,914,243
16	15,695,193	14,561,859	13,561,859	12,672,970	11,877,649	11,161,859	10,514,240	9,925,496	9,387,946	8,895,193	8,441,859
17	16,676,142	15,471,975	14,409,475	13,465,031	12,620,002	11,859,475	11,171,380	10,545,839	9,974,693	9,451,142	8,969,475
18	17,657,092	16,382,092	15,257,092	14,257,092	13,362,355	12,557,092	11,828,520	11,166,183	10,561,439	10,007,092	9,497,092
19	18,638,041	17,292,208	16,104,708	15,049,152	14,104,708	13,254,708	12,485,660	11,786,526	11,148,186	10,563,041	10,024,708
20	19,618,991	18,202,324	16,952,324	15,841,213	14,847,061	13,952,324	13,142,800	12,406,869	11,734,933	11,118,991	10,552,324
21	20,599,940	19,112,440	17,799,940	16,633,274	15,589,414	14,649,940	13,799,940	13,027,213	12,321,679	11,674,940	11,079,940
22	21,580,890	20,022,556	18,647,556	17,425,334	16,331,767	15,347,556	14,457,080	13,647,556	12,908,426	12,230,890	11,607,556
23	22,561,839	20,932,673	19,495,173	18,217,395	17,074,120	16,045,173	15,114,220	14,267,900	13,495,173	12,786,839	12,135,173
24	23,542,789	21,842,789	20,342,789	19,009,455	17,816,473	16,742,789	15,771,360	14,888,243	14,081,919	13,342,789	12,662,789
25	24,523,738	22,752,905	21,190,405	19,801,516	18,558,826	17,440,405	16,428,500	15,508,587	14,668,666	13,898,738	13,190,405

In conclusion, **$17 million** is a good estimation of this segment value since the acquisition of the segment was so recent. However analyzing the financial statements deeper we see that properly reallocating SG&A costs to this segment would not affect manufacturing's valuation but would increase the valuation of the water production segment by over $10 million.

Balance Sheet Assets

As of June 30, 2020, the total value of cash, accounts receivables and inventories net of total liabilities was $55.6 million. The accounts receivables includes $19.9 million from WSC, a Bahamian government agency. The company believes that all receivables from WSC will be paid in full based on previous payment histories. Thus I will value these net assets at the full **$55.6 million** value since (aside from the receivables) the cash and inventory are very liquid and cash flow from operations are positive and enough to meet investment needs.

Equity Value and Revaluation Opportunities

Water Production 2021 Expected Earnings	5,622,752										
Water Production P/E 2021E	12	13	14	15	16	17	18	19	20	21	22
Water Production Segment Valuation	67,473,028	73,095,781	78,718,533	84,341,285	89,964,038	95,586,790	101,209,542	106,832,295	112,455,047	118,077,799	123,700,552
Services Valuation	28,000,000	28,000,000	28,000,000	28,000,000	28,000,000	28,000,000	28,000,000	28,000,000	28,000,000	28,000,000	28,000,000
Manufacturing Valuation	17,000,000	17,000,000	17,000,000	17,000,000	17,000,000	17,000,000	17,000,000	17,000,000	17,000,000	17,000,000	17,000,000
Value of Liquid Assets	55,600,000	55,600,000	55,600,000	55,600,000	55,600,000	55,600,000	55,600,000	55,600,000	55,600,000	55,600,000	55,600,000
Total Valuation	168,073,028	173,695,781	179,318,533	184,941,285	190,564,038	196,186,790	201,809,542	207,432,295	213,055,047	218,677,799	224,300,552
Upside to Current Market Price	5.71%	9.24%	12.78%	16.32%	19.85%	23.39%	26.92%	30.46%	34.00%	37.53%	41.07%
Additional Value From Reallocation of SG&A	~10,000,000	~10,000,001	~10,000,002	~10,000,003	~10,000,004	~10,000,005	~10,000,006	~10,000,007	~10,000,008	~10,000,009	~10,000,010

Summing the previous parts, I obtain a conservative equity value of $190 million or a 20% premium to current market price of $159 million in our base case in which CWCO's retail prices are cut by 10% in 2021 and water production is valued at a 16x P/E ratio of future earnings. It is important to understand that actual earnings may be higher if SG&A costs are allocated differently. Thus this valuation would be based on a low P/E multiple on a low base when in reality the base may be much higher.

Even if SG&A costs are all appropriately allocated, I believe this valuation may be conservative as 16x P/E is the ratio of CUC with significantly more debt, I did not predict future demand growth, and I valued other segments of the business largely at book value without any potential synergies. I also view the possibility of developing new desalination projects in Baja Mexico or elsewhere to be nonzero, and at CWCO's current market prices, we can be purchasing a free call option on these future cash flows.

I believe CWCO can obtain a revaluation to $190 million once there is additional clarity concerning COVID-19, its retail license, and compensation from the Baja California plant. A new long-term agreement with the Cayman Islands regulator should also allow the P/E ratio to rise even if there are substantial price cuts since the segments are again still profitable and this would eliminate substantial uncertainty. I believe this will also allow CWCO to more accurately allocate its SG&A costs and help the market realize the current underpricing. Lastly, I believe the market has overreacted to the Baja California plant cancellation, and once related impairment losses stop impacting the income statement, the market will be able to more accurately value the other segments.

Appendix

1. 2019 Segment Income Breakdown

	Year Ended December 31, 2019				
	Retail	Bulk	Services	Manufacturing	Total
Revenue	$ 26,456,022	$ 26,986,108	$ 1,759,446	$ 13,592,075	$ 68,793,651
Cost of revenue	11,611,165	18,606,805	1,215,193	9,086,140	40,519,303
Gross profit	14,844,857	8,379,303	544,253	4,505,935	28,274,348
General and administrative expenses	13,422,821	1,238,296	2,740,219	1,947,622	19,348,958
Gain on asset dispositions and impairments, net	398,041	47,000	-	-	445,041
Income (loss) from operations	$ 1,820,077	$ 7,188,007	$ (2,195,966)	$ 2,558,313	9,370,431
Other income, net					801,091
Income before income taxes					10,171,522
Provision for income taxes					66,621
Net income from continuing operations					10,104,901
Income from continuing operations attributable to non-controlling interests					1,549,978
Net income from continuing operations attributable to Consolidated Water Co. Ltd. stockholders					8,554,923
Net income from discontinued operations					3,621,170
Net income attributable to Consolidated Water Co. Ltd. stockholders					$ 12,176,093

2. Baja California Land Investment

5. NSC and AdR project development

In May 2010, the Company acquired, through its wholly owned Netherlands subsidiary, CW-Cooperatief, a 50% interest in NSC, a development stage Mexican company. CW-Cooperatief subsequently purchased, through the conversion of a loan it made to NSC, additional shares that increased its ownership interest in NSC to 99.99%. NSC was formed to pursue a project (the "Project") that originally encompassed the construction, operation and minority ownership of a 100 million gallon per day seawater reverse osmosis desalination plant to be located in northern Baja California, Mexico and accompanying pipelines to deliver water to the Mexican public water system. As discussed in paragraphs that follow, during 2015 the scope of the Project was defined by the State of Baja California (the "State") to consist of a first phase consisting of a 50 million gallons per day plant and an aqueduct that connects to the Mexican public water infrastructure and a second phase consisting of an additional 50 million gallons per day of production capacity.

Through a series of transactions that began in 2012, NSC purchased 20.1 hectares of land for approximately $21.1 million on which the proposed Project's plant would be constructed.

3. CUC Valuation

CUC Valuation (Trades in USD despite Canadian listing)		
Shares Outstanding	33,843,624	
Price Per Share USD	14.35	as of 9/24/20
Market Cap USD	485,656,004.40	
2019 Earnings USD	29,100,000	
PE	16.68920977	

4. CUC Balance Sheet

Caribbean Utilities Company, Ltd.

Condensed Consolidated Interim Balance Sheets

(expressed in thousands of United States Dollars)

Unaudited	Note	As at June 30, 2020	As at December 31, 2019
Assets			
Current Assets			
Cash		**24,927**	23,662
Accounts Receivable (Net of Allowance for Credit Losses of $1,555 and $1,335)	6	**12,681**	9,121
Related Party Receivables	12	**6**	5
Regulatory Assets	7	**13,730**	18,144
Inventories		**2,369**	4,530
Prepayments		**1,323**	2,980
Total Current Assets		**55,036**	58,442
Property, Plant and Equipment, net		**545,638**	537,986
Intangible Assets, net		**3,630**	3,598
Other Assets		**410**	391
Total Assets		**604,714**	600,417
Liabilities and Shareholders' Equity			
Current Liabilities			
Accounts Payable and Accrued Expenses		**17,972**	25,377
Related Party Payables	12	**23**	-
Regulatory Liabilities	7	**1,816**	1,298
Short-Term Debt		**25,000**	-
Current Portion of Long-Term Debt	9	**14,857**	14,857
Current Portion of Lease Liability		**78**	76
Consumers' Deposits and Advances for Construction		**10,681**	10,520
Total Current Liabilities		**70,427**	52,128
Defined Benefit Pension Liability		**1,798**	1,827
Long-Term Debt	9	**295,382**	307,193
Other Long-Term Liabilities		**1,034**	1,327
Total Liabilities		**368,641**	362,475
Commitments and Contingency	13, 14		
Shareholders' Equity			
Share Capital[1]		**2,250**	2,243
Share Premium		**131,996**	130,283
Retained Earnings		**103,660**	107,281
Accumulated Other Comprehensive Loss		**(1,833)**	(1,865)
Total Shareholders' Equity		**236,073**	237,942
Total Liabilities and Shareholders' Equity		**604,714**	600,417

5. PERC Revenue and Margins

PERC, our principal services segment subsidiary, generates most of its revenue from contracts ("O&M contracts") to operate and maintain water treatment and reuse facilities owned by third parties. For the three and six months ended June 30, 2020, we generated revenue of approximately $2.5 million and $4.1 million, respectively, under these O&M contracts. PERC's O&M contracts have terms ranging from one to five years, with varying renewal options exercisable

Services segment revenue increased to $6,590,813 for 2020 from $191,369 for 2019 due to the addition of $6,374,502 in revenue from PERC as a result of our acquisition of 51% of this company in late October 2019.

Gross profit for the services segment improved to $1,685,780 (26% of services revenue) in 2020 as a result of the addition of PERC. The services segment generated a gross profit of $24,356 (13% of services revenue) for 2019.

6. H1 2020 Segment Income Breakdown

	Six Months Ended June 30, 2020				
	Retail	Bulk	Services	Manufacturing	Total
Revenue	$ 13,223,728	$ 12,306,681	$ 6,590,813	$ 7,691,746	$ 39,812,968
Cost of revenue	5,756,117	8,505,889	4,905,033	4,902,465	24,069,504
Gross profit	7,467,611	3,800,792	1,685,780	2,789,281	15,743,464
General and administrative expenses	6,640,621	553,146	2,145,903	675,115	10,014,785
Gain (loss) on asset dispositions and impairments, net	—	200	(3,030,840)	—	(3,030,640)
Income (loss) from operations	$ 826,990	$ 3,247,846	$ (3,490,963)	$ 2,114,166	2,698,039
Other income, net					14,229
Income before income taxes					2,712,268
Provision for income taxes					410,351
Net income					2,301,917
Income attributable to non-controlling interests					541,152
Net income attributable to Consolidated Water Co. Ltd. stockholders					$ 1,760,765

7. CWCO Financial Statements

CONSOLIDATED WATER CO. LTD.
CONDENSED CONSOLIDATED BALANCE SHEETS

	June 30, 2020 (Unaudited)	December 31, 2019
ASSETS		
Current assets		
Cash and cash equivalents	$ 34,956,328	$ 42,902,669
Accounts receivable, net	26,858,584	23,229,689
Inventory	5,067,873	3,287,555
Prepaid expenses and other current assets	1,738,472	2,346,918
Costs and estimated earnings in excess of billings	2,202,524	1,675,781
Total current assets	70,823,781	73,442,612
Property, plant and equipment, net	59,808,325	61,248,979
Construction in progress	399,463	1,335,597
Inventory, noncurrent	4,738,617	4,404,378
Investment in OC-BVI	1,987,878	1,903,602
Goodwill	13,325,013	13,325,013
Land and rights of way	21,126,898	24,162,523
Intangible assets, net	4,573,333	5,040,000
Operating lease right-of-use assets	1,250,157	4,439,212
Other assets	2,791,458	2,990,228
Total assets	$ 180,824,923	$ 192,292,144
LIABILITIES AND EQUITY		
Current liabilities		
Accounts payable, accrued expenses and other current liabilities	$ 3,613,387	$ 3,672,142
Accrued compensation	1,519,911	1,821,395
Dividends payable	1,298,321	1,292,187
Current maturities of operating leases	628,161	755,751
Current portion of long-term debt	42,211	17,753
Billings in excess of costs and estimated earnings	899,942	614,386
Total current liabilities	8,001,933	8,173,614
Long-term debt, noncurrent	145,822	61,146
Deferred tax liabilities	1,384,268	1,529,035
Noncurrent operating leases	930,072	3,836,475
Net liability arising from put/call options	745,000	664,000
Other liabilities	75,000	75,000
Total liabilities	11,282,095	14,339,270
Commitments and contingencies		
Equity		
Consolidated Water Co. Ltd. stockholders' equity		
Redeemable preferred stock, $0.60 par value. Authorized 200,000 shares; issued and outstanding 40,237 and 33,751 shares, respectively	24,142	20,251
Class A common stock, $0.60 par value. Authorized 24,655,000 shares; issued and outstanding 15,114,506 and 15,049,608 shares, respectively	9,068,704	9,029,765
Class B common stock, $0.60 par value. Authorized 145,000 shares; none issued	—	—
Additional paid-in capital	86,234,521	88,356,509
Retained earnings	65,536,646	66,352,733
Total Consolidated Water Co. Ltd. stockholders' equity	160,864,013	163,759,258
Non-controlling interests	8,678,815	14,193,616
Total equity	169,542,828	177,952,874
Total liabilities and equity	$ 180,824,923	$ 192,292,144

CONSOLIDATED WATER CO. LTD.
CONDENSED CONSOLIDATED STATEMENTS OF INCOME (LOSS)
(UNAUDITED)

	Three Months Ended June 30, 2020	Three Months Ended June 30, 2019	Six Months Ended June 30, 2020	Six Months Ended June 30, 2019
Total revenue	$ 19,087,247	$ 18,305,260	$ 39,812,968	$ 35,293,784
Total cost of revenue	11,784,104	10,752,511	24,069,504	20,778,732
Gross profit	7,303,143	7,552,749	15,743,464	14,515,052
General and administrative expenses	4,861,028	4,994,992	10,014,785	9,373,026
Gain (loss) on asset dispositions and impairments, net	(3,030,420)	397,301	(3,030,640)	441,070
Income (loss) from operations	(588,305)	2,955,058	2,698,039	5,583,096
Other income (expense):				
Interest income	109,819	140,467	246,259	290,652
Interest expense	(2,818)	(1,482)	(5,344)	(1,482)
Profit-sharing income from OC-BVI	14,175	2,025	24,300	8,100
Equity in the earnings (losses) of OC-BVI	34,093	(24,949)	59,976	(11,488)
Net unrealized gain (loss) on put/call options	80,000	—	(81,000)	(24,000)
Other	(390,384)	(65,728)	(229,962)	48,641
Other income (expense), net	(155,115)	50,333	14,229	310,423
Income (loss) before income taxes	(743,420)	3,005,391	2,712,268	5,893,519
Provision for income taxes	204,268	64,233	410,351	113,192
Net income (loss) from continuing operations	(947,688)	2,941,158	2,301,917	5,780,327
Income from continuing operations attributable to non-controlling interests	180,154	464,896	541,152	738,804
Net income (loss) from continuing operations attributable to Consolidated Water Co. Ltd. stockholders	(1,127,842)	2,476,262	1,760,765	5,041,523
Gain on sale of discontinued operations	—	—	—	3,621,170
Total income from discontinued operations	—	—	—	3,621,170
Net income (loss) attributable to Consolidated Water Co. Ltd. stockholders	$ (1,127,842)	$ 2,476,262	$ 1,760,765	$ 8,662,693
Basic earnings (loss) per common share attributable to Consolidated Water Co. Ltd. common stockholders				
Continuing operations	$ (0.07)	$ 0.16	$ 0.12	$ 0.34
Discontinued operations	—	—	—	0.24
Basic earnings (loss) per share	$ (0.07)	$ 0.16	$ 0.12	$ 0.58
Diluted earnings (loss) per common share attributable to Consolidated Water Co. Ltd. common stockholders				
Continuing operations	$ (0.07)	$ 0.16	$ 0.12	$ 0.33
Discontinued operations	—	—	—	0.24
Diluted earnings (loss) per share	$ (0.07)	$ 0.16	$ 0.12	$ 0.57
Dividends declared per common and redeemable preferred shares	$ 0.085	$ 0.085	$ 0.17	$ 0.17
Weighted average number of common shares used in the determination of:				
Basic earnings per share	15,114,506	15,020,344	15,114,506	15,020,344
Diluted earnings per share	15,114,506	15,185,812	15,269,175	15,185,463

CONSOLIDATED WATER CO. LTD.

CONSOLIDATED STATEMENTS OF INCOME

	Year Ended December 31, 2019	Year Ended December 31, 2018
Total revenue	$ 68,793,651	$ 65,719,857
Total cost of revenue	40,519,303	38,977,570
Gross profit	28,274,348	26,742,287
General and administrative expenses	19,348,958	18,709,419
Gain (loss) on asset dispositions and impairments, net	445,041	(56,774)
Income from operations	9,370,431	7,976,094
Other income (expense):		
Interest income	588,509	663,197
Interest expense	(2,814)	(8,427)
Profit-sharing income from OC-BVI	16,200	654,075
Equity in the earnings of OC-BVI	44,765	1,798,280
Net unrealized gain (loss) on put/call options	56,000	(256,000)
Other	98,431	(111,061)
Other income, net	801,091	2,740,064
Income before income taxes	10,171,522	10,716,158
Provision for (benefit from) income taxes	66,621	(157,291)
Net income from continuing operations	10,104,901	10,873,449
Income from continuing operations attributable to non-controlling interests	1,549,978	695,787
Net income from continuing operations attributable to Consolidated Water Co. Ltd. stockholders	8,554,923	10,177,662
Gain on sale of discontinued operations	3,621,170	-
Net income from discontinued operations	-	1,115,825
Total income from discontinued operations	3,621,170	1,115,825
Net income attributable to Consolidated Water Co. Ltd. stockholders	$ 12,176,093	$ 11,293,487
Basic earnings per common share attributable to Consolidated Water Co. Ltd. common stockholders		
Continuing operations	$ 0.57	$ 0.68
Discontinued operations	0.24	0.07
Basic earnings per share	$ 0.81	$ 0.75
Diluted earnings per common share attributable to Consolidated Water Co. Ltd. common stockholders		
Continuing operations	$ 0.56	$ 0.68
Discontinued operations	0.24	0.07
Diluted earnings per share	$ 0.80	$ 0.75
Dividends declared per common and redeemable preferred shares	$ 0.34	$ 0.34
Weighted average number of common shares used in the determination of:		
Basic earnings per share	15,025,639	14,962,760
Diluted earnings per share	15,137,076	15,074,147