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Fundamental Research Corp.

Investment Analysis for Intelligent Investors

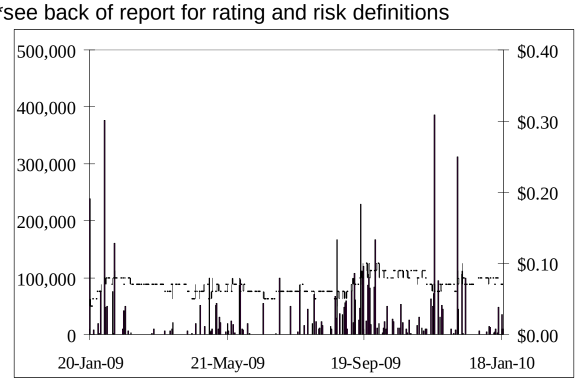
International Water-Guard Industries Inc. (TSX-V: IWG) – Revenues hit all-time high in FY2009; Working capital alone accounts for $0.055 per share

Sector/Industry: Aerospace Products and Services **www.water.aero**

Market Data (as of January 20, 2010)

Current Price	**C$0.07**
Fair Value	**C$0.30**
Rating*	**BUY**
Risk*	**3 (Average)**
52 Week Range	C$0.04 –C$0.10
Shares O/S	39,340,694
Market Cap	C$2.75 mm
Current Yield	N/A
P/E	8.83
P/B	1.00
YoY Return	75.0%
YoY TSX-V	84.8%

*see back of report for rating and risk definitions



Q4-2009 Highlights

- Q4 revenues well exceeded our expectations as the company reported $1.21 million in revenues, versus our forecast of $0.98 million.
- The company reported revenues of $4.90 million in FY09 (an all-time record), versus $4.16 million in FY08, an increase of 18% YOY.
- Although we have raised our revenue forecast for FY2010 (from $4.29 million, to $4.49 million), we expect FY2010 revenues to stay soft primarily because of the weak US$, and the drop in net orders for business jets in 2009.
- In December 2009, the company announced it has retained Haywood Securities to advise on corporate development, and potential M&A opportunities.
- In December 2009, the company announced the delivery of its 2,000th aircraft water treatment unit - a significant milestone for the company.
- At current prices, IWG's Enterprise Value (EV)/Revenues, and EV/EBITDA, are just 0.1, and 1.2, versus the industry (Aerospace and Defense) average ratios of 0.9, and 8.9, respectively. The company's working capital alone accounts for $0.055 per share; which implies the market values the company's business at just $0.59 million, or $0.015 per share.
- Although we expect business jet deliveries to fall YOY in 2010, we believe the global economic recovery will drive demand for business jets, and, as a result, we expect demand to bounce back in 2011.

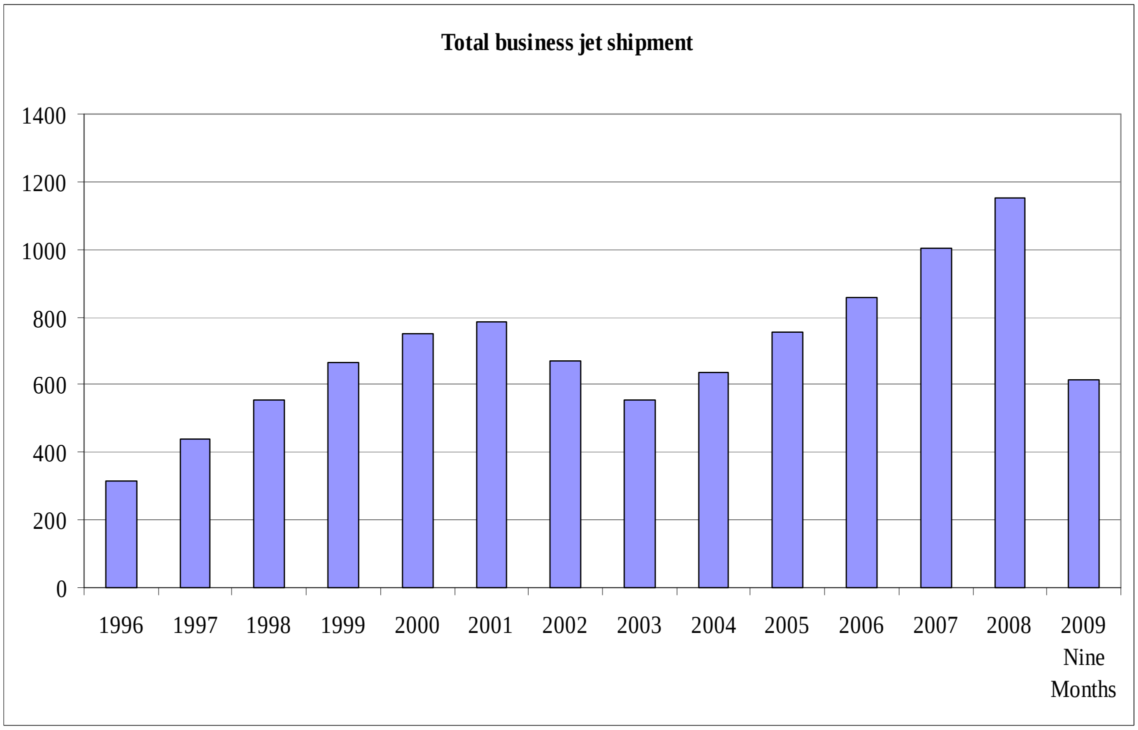
Financial Summary (YE Sept 30)

(C$)	**2006**	**2007**	**2008**	**2009**	**2010E**	**2011E**
Revenue	3,662,460	4,484,903	4,156,469	4,898,157	4,493,126	4,913,126
Gross Margin	59.92%	54.91%	53.75%	62.70%	58.00%	60.00%
Net Income	404,545	808,147	(97,044)	312,016	96,062	271,902
EPS (basic)	0.01	0.02	(0.00)	0.01	0.00	0.01
Cash	133,529	438,932	940,302	1,362,363	1,545,099	1,769,325
Assets	1,505,304	2,486,701	2,941,421	3,249,308	3,313,292	3,615,764
Debt to Capital	9.21%	3.43%	3.44%	1.57%	2.19%	1.64%
ROE	49.62%	53.24%	-4.41%	12.09%	3.44%	9.13%
ROIC	49.05%	61.22%	-6.11%	20.87%	6.90%	19.73%

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.

Demand for business jets expected to bounce back in 2011

The global economic recession, credit crunch, and declining corporate profits resulted in a significant drop in the demand for business jets in 2009. According to the General Aviation Manufacturers Association (GAMA), global shipments of business jets in the first nine months of 2009, were 615, compared to 988 during the same time period in the previous year, a decrease of 38%YOY.



Source: GAMA

<u>On a positive note, small business jets experienced a steeper fall in deliveries than larger-business jets; which is encouraging for IWG because most of its customers are in the large business jet sector.</u>

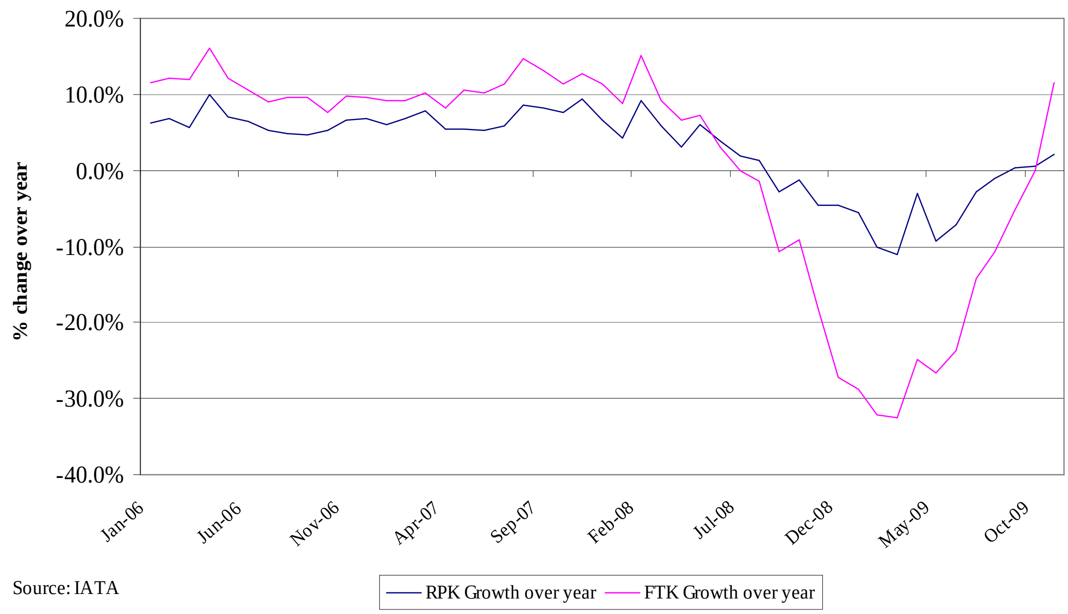
Most of the major business jet manufacturers experienced a decline in their backlogs in the 12 month period ended October 2009. The following are some examples:

a) Bombardier (TSX: BBD-A) had a backlog of US$18.5 billion for its aerospace segment in October 2009, compared to US$26 billion in October 2008.
b) General Dynamics (NYSE: GD) had a aerospace backlog of US$19 billion in October 2009, compared to US$22 billion in October 2008.
c) Hawker’s backlog was US$6.6 billion in October 2009, compared to US$7.9 billion as of October 2008.
d) Cessna’s backlog was US$6.9 billion at October 2009, compared to US$15.6 billion same period last year.

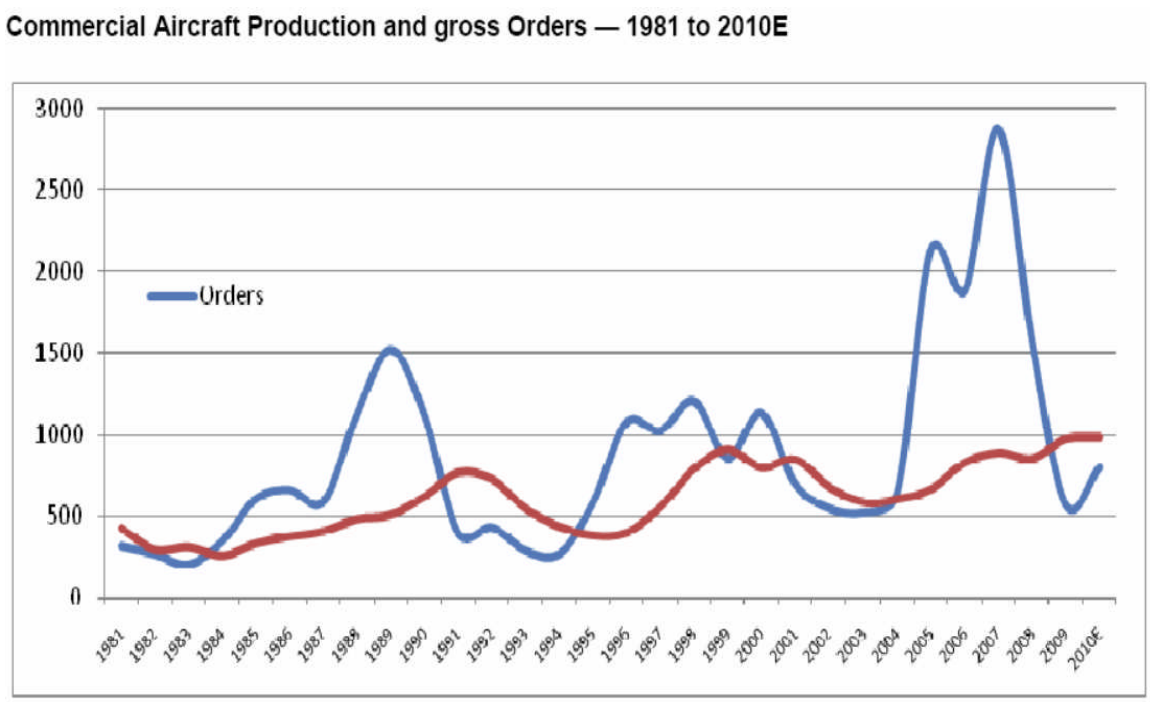
Although we expect business jet deliveries to fall YOY in 2010, we believe the global economic recovery will drive demand for business jets, and, as a result, we expect demand to bounce back in 2011.

The following charts, which indicate increasing international passenger and freight growth, increasing commercial aircraft orders in the U.S., and declining net loss projections in 2010 and 2011, show that the commercial airline industry is on its path to recovery. We believe these are leading indicators for a rebound in the business jet market.

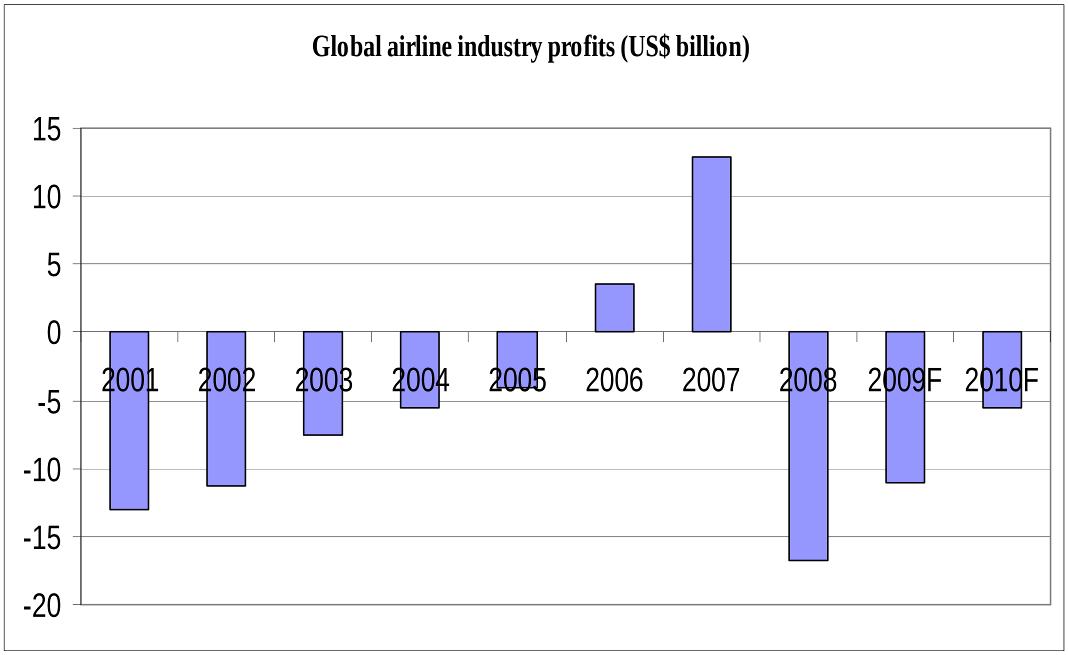
International Passenger and Freight Growth



Source: IATA



Source: Deloitte



Source: IATA

Recent Developments

- In October 2009, **the Environmental Protection Agency (EPA) published the Aircraft Drinking Water Rule (ADWR)** to ensure that safe and reliable drinking water is provided to aircraft passengers and crew. The rule basically provides additional protection to the passengers/crew from disease-causing organisms sometimes found in aircraft drinking water. The ADWR primarily focuses on the inspection of all components associated with an aircraft's potable water storage and distribution system, and coliform (bacterial indicator) sampling. Although the ADWR only addresses aircraft within U.S. jurisdiction, the EPA supports the World Health Organization's (WHO) efforts to develop international guidelines for aircraft drinking water.

  These regulations, which will take effect in October 2011, are very positive for IWG, especially because:

  a) We believe these rules will prompt more aircraft owners/operators/manufacturers to install efficient water equipment units/systems, in order to stay in compliance.

  b) Regulators' increasing focus on aircraft water quality is highly beneficial for IWG's long-term prospects.

- In October 2009, IWG announced that they are **developing an In-Flight Drain System (IFDS™)** as a retrofit package with Supplemental Type Certificate (STC) for the Boeing (NYSE: BA) Business Jet. This system basically addresses the operational concerns associated with the Boeing 737 BBJ's inability to drain the aircraft water system. Typically, crews must stay with the aircraft until it is completely drained in order to avoid a system freeze during cold weather. IWG's IFDS™ solves this problem by draining during an aircraft's descent. The company expects to release a cost-effective system by Q3-2010.

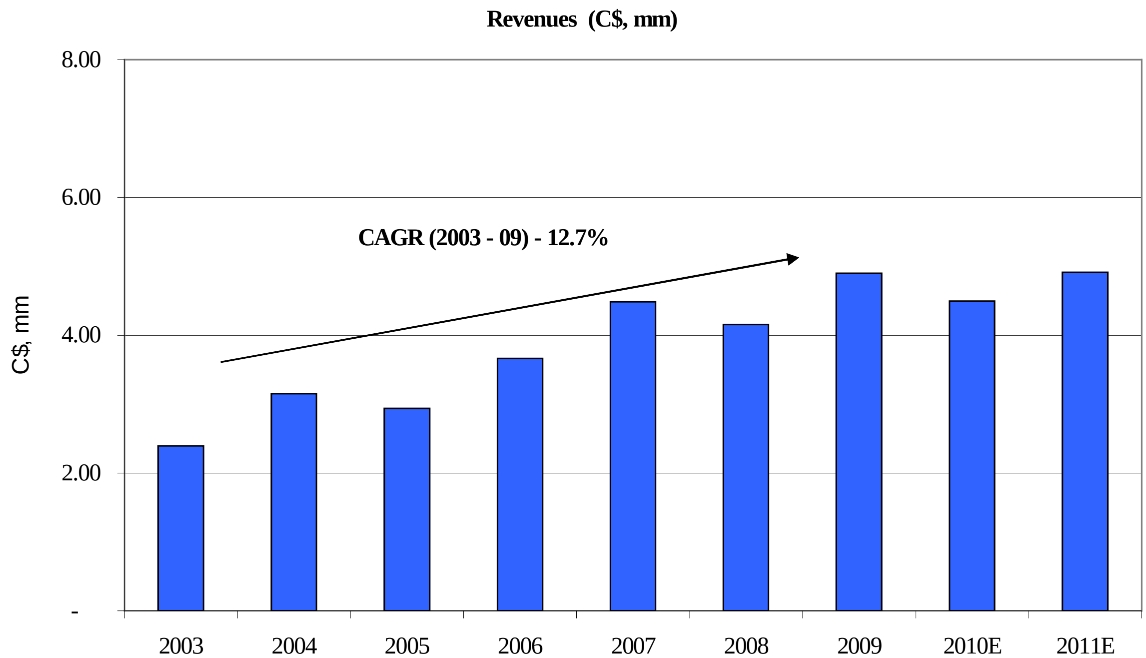
- In December 2009, the company announced it has retained Haywood Securities to advise on corporate development, and potential M&A opportunities. The company has yet to disclose any details on this matter. We believe the company's financial position is sound enough to pursue acquisitions. At the end of FY2009, the company had $1.36 million in cash. Debt to capital at the end of FY2009 was only 1.6%, versus the industry (Aerospace and Defence) average ratio of 40.2%.

Review of Q4-2009 results

Q4 revenues well exceeded our expectations as the company reported $1.21 million in revenues, versus our forecast of $0.98 million. Q4 revenues were up 5% YOY. We were pleased to see the YOY revenue growth in Q4, especially because Q3-2009 revenues were down 11% YOY.

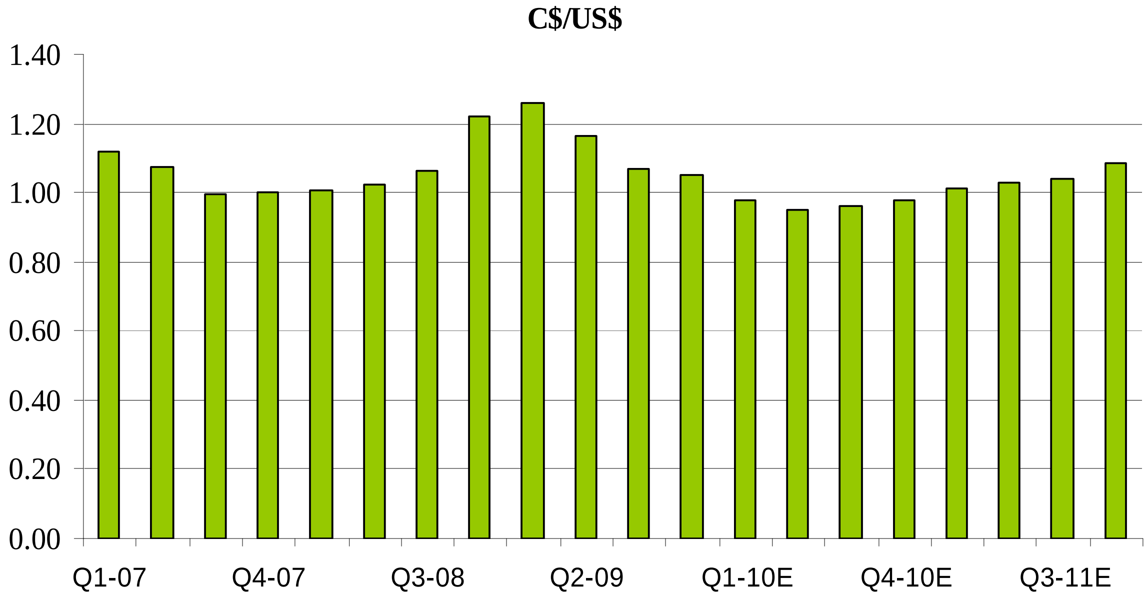
The company reported revenues of $4.90 million in FY2009 (an all-time record), versus $4.16 million in FY2008, an increase of 18% YOY. Note that revenues in FY2009 are not directly comparable to FY2008, as revenues in the first half of FY2008 were unusually low due to delays in orders from a major customer.

The following chart shows IWG's revenue growth since FY2003.



Note: Revenues in FY2003-05 are only from aviation sales; IWG sold its industrial division in 2005.

During FY2003-09, revenues grew at a compounded annual growth rate of 12.7%. **Revenue growth during FY2005-09 was 11.8% - well above the industry (Aerospace and Defense) average growth rate of 6.1% during the same period.** Revenue growth in FY2009 came primarily from a stronger US$ (see chart below), and increased sales of service and replacement parts, and water system components, offset by a 5% drop in unit sales.



Source: TD Economics

Although we have raised our revenue forecast for FY2010 (from $4.29 million, to $4.49 million), we expect FY2010 revenues to stay soft primarily because of the weak US$, and the drop in net orders for business jets in 2009. Our forecast for FY2010 is $4.91 million.

Margins improve YOY

The strong US$ also had a very positive impact on gross margins in FY2009. Gross margins in FY2009 were 62.7%; well above our forecast of 60%, and the best in recent years.

Margins	**2006**	**2007**	**2008**	**2009**
Gross	59.92%	54.91%	53.8%	62.7%
EBITDA	13.68%	9.86%	-1.72%	10.25%
EBIT	12.61%	8.70%	-3.28%	9.01%
EBT	11.05%	8.50%	-3.56%	8.68%
Net Margin	11.05%	18.02%	-2.33%	6.37%
Expenses / Sales	**2006**	**2007**	**2008**	**2009**
Selling Expenses	10.20%	8.23%	7.91%	8.74%
R&D	11.61%	11.16%	18.58%	17.87%
G & A	23.61%	23.85%	28.54%	25.35%
Stock Option Compensation	0.81%	1.80%	0.44%	0.50%
Total	**46.24%**	**45.05%**	**55.48%**	**52.45%**

Strong gross margins, and a drop in operating expenses (which includes selling, research and development, and general and administrative expenses) as a percentage of revenues, resulted in a significant improvement in EBITDA margins, from -1.72% in FY2008, to 10.25% in FY2009.

EPS Forecasts

IWG posted net profits of $0.31 million (EPS: $0.01), versus a net loss of $0.01 million (EPS: -$0.00) in FY2008. Our forecast for net profit was $0.11 million (EPS: $0.00).

Our revised EPS forecast for FY2010 is net profit of $0.10 million (EPS: $0.00), versus our previous forecast of $0.11 million (EPS: $0.00). Our forecast for FY2011 is net profit of $0.27 million (EPS: $0.01).

Cash Flows and Liquidity

IWG generated $0.50 million from operations in FY2009 ($0.09 million in FY2008), and spent $0.04 million on capital expenditures ($0.05 million in FY2008); reflecting free cash flows of $0.46 million ($0.04 million in FY2008).

Positive free cash flows resulted in an improved balance sheet at the end of FY2009. At the end of FY2009, the company had $1.36 million in cash ($0.03 per share). Working capital was $2.27 million, or $0.06 per share.

Liquidity Analysis	**2006**	**2007**	**2008**	**2009**
Working Capital	$909,496	$1,387,326	$1,722,974	$2,266,003
Current Ratio	3.33	4.06	4.52	5.77
Debt / Capital	9.2%	3.4%	3.4%	1.6%
Interest Coverage Ratio	8.0	44.1	(11.6)	26.8

Profitability Analysis	**2006**	**2007**	**2008**	**2009**
Return on Avg Assets	29.8%	40.5%	-3.6%	10.1%
Return on Avg Equity	49.6%	53.2%	-4.4%	12.1%
Return on Average Invested Capital	49.1%	61.2%	-6.1%	20.9%

Activity Analysis	**2006**	**2007**	**2008**	**2009**
Days Inventory Outstanding	84	93	108	107
Days Accouts Receivable	63	60	63	52
Days Accouts Payable	72	70	83	90
Cash Conversion Cycle	**74**	**83**	**88**	**69**

In FY2009, the company generated ROA and ROE of 10.1% (industry average - 4.3%), and 12.1% (industry average - 12.1%). The company continues to maintain a strong balance sheet and we do not foresee any need for external financings in the near future.

Stock Options and Warrants

At the end of FY2009, the company had 2.58 million stock options outstanding (all of them are currently ‘out-of the-money’), with exercise prices ranging between $0.09 and $0.21, and a weighted average time to maturity of 31 months. The company also had 5 million warrants (exercise price of $0.17 per share) outstanding.

Valuation and Rating

Our Discounted Cash Flow valuation is maintained at $0.27 per share.

DCF Valuation Model							
	2010E	**2011E**	**2012E**	**2013E**	**2014E**	**2015E**	**Terminal**
FFO	$183,178	$359,910	$674,117	$842,198	$1,060,086	$1,343,435	$1,711,859
Investment in WC	$85,315	($64,413)	($16,842)	($214,754)	($279,180)	($362,934)	($471,814)
CFO	$268,493	$295,497	$657,275	$627,444	$780,906	$980,501	$1,240,045
CAPEX	($60,000)	($60,000)	($60,000)	($60,000)	($60,000)	($60,000)	($60,000)
FCF	$208,493	$235,497	$597,275	$567,444	$720,906	$920,501	$1,180,045
PV	$202,669	$204,391	$462,843	$392,613	$445,350	$507,726	$7,232,051
Discount Rate	12%						
Terminal Growth Rate	3%						
Total PV	$9,447,643						
Cash - Debt	1,318,505						
Equity Value	**$10,766,148**						
Shares O/S (dil)	39,340,694						
Value per share	**$0.27**						

At current prices, IWG's Enterprise Value (EV)/Revenues, and EV/EBITDA, are just 0.1, and 1.2, versus the industry (Aerospace and Defense) average ratios of 0.9, and 8.9, respectively. The company's working capital alone accounts for $0.055 per share; which implies the market values the company's business at just $0.59 million, or $0.015 per share!

Based on our review of the company's progress since our previous update, we reiterate our BUY rating, and maintain our fair value estimate at $0.30 per share.

Risks

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$)	2006	2007	2008	2009	2010E	2011E
Sales	**3,662,460**	**4,484,903**	**4,156,469**	**4,898,157**	**4,493,126**	**4,913,126**
COGS	1,467,763	2,022,031	1,922,205	1,827,070	1,887,113	1,965,250
Gross Profit	**2,194,697**	**2,462,872**	**2,234,264**	**3,071,087**	**2,606,013**	**2,947,876**
Expenses						
Selling Expenses	373,683	369,189	328,773	427,924	381,916	448,937
Research&Development	425,338	500,718	772,194	875,219	707,667	687,838
General & Administration	864,836	1,069,852	1,186,442	1,241,740	1,272,784	1,304,603
Stock Option Compensation	29,745	80,709	18,408	24,345	22,332	24,419
EBITDA	**501,095**	**442,404**	**(71,553)**	**501,859**	**221,315**	**482,079**
Amortization	39,078	52,414	64,758	60,389	64,784	63,588
EBIT	**462,017**	**389,990**	**(136,311)**	**441,470**	**156,531**	**418,491**
Interest & Bank Charges	57,472	8,843	11,733	16,454	10,717	5,767
			-			
Earnings from operations, before undernoted	**404,545**	**381,147**	**(148,044)**	**425,016**	**145,814**	**412,724**
Government Assistance						
Gains on settlement of notes and accounts payable	-	-	-	-	-	-
Gain on sale of commerical division assets	-	-	-	-	-	-
Wite-down of assets and costs	-	-	-	-	-	-
EBT	**404,545**	**381,147**	**(148,044)**	**425,016**	**145,814**	**412,724**
Taxes/(Income Tax Recovery)	-	(427,000)	(51,000)	113,000	49,752	140,821
Net Earnings for the eperiod	**404,545**	**808,147**	**(97,044)**	**312,016**	**96,062**	**271,902**
EPS	0.01	0.02	(0.00)	0.01	0.00	0.01

BALANCE SHEETS (in C$)	**2006**	**2007**	**2008**	**2009**	**2010E**	**2011E**
Assets						
Cash	133,529	438,932	940,302	1,362,363	1,545,099	1,769,325
Accounts receivable	755,321	721,278	710,770	672,010	634,219	693,503
Inventory	388,844	642,232	496,335	577,993	508,083	529,121
Prepaid Expenses	21,664	37,969	65,407	42,807	36,539	38,052
Future Income Tax				86,000	86,000	86,000
Current Assets	**1,299,358**	**1,840,411**	**2,212,814**	**2,741,173**	**2,809,941**	**3,116,001**
Equipment & Furniture	205,946	219,290	250,607	229,135	224,351	220,763
Deferred Dev Costs and foreign exchange loss						
Future income tax assets		427,000	478,000	279,000	279,000	279,000
Total Assets	**1,505,304**	**2,486,701**	**2,941,421**	**3,249,308**	**3,313,292**	**3,615,764**
Liabilities & Shareholders' Equity						
Accounts Payables & Accrued Liabilities	354,383	425,072	449,247	449,413	420,759	438,181
Demand / Factoring Loan	-	-	-	-	-	-
Customer Deposits, Bank and Shareholder's loan						
Current portion of capital lease obligations and loan	35,479	28,013	40,593	25,757	11,271	17,345
Current portion of notes payable						
Current Liabilities	**389,862**	**453,085**	**489,840**	**475,170**	**432,030**	**455,527**
Convertible Debentures						
Obligations under capital lease and other loan	70,567	42,685	45,206	18,101	52,036	34,691
Notes and Loans payable						
Shareholder's Equity						
Share Capital	7,533,289	7,607,553	8,108,202	8,111,487	8,111,487	8,111,487
Contributed surplus	90,319	153,964	165,803	200,164	177,290	201,709
Deficit	(6,578,733)	(5,770,586)	(5,867,630)	(5,555,614)	(5,459,552)	(5,187,649)
Total Liabilities & Shareholders' Equity	**1,505,304**	**2,486,701**	**2,941,421**	**3,249,308**	**3,313,292**	**3,615,764**

STATEMENTS OF CASH FLOWS

(in C$)	2006	2007	2008	2009	2010E	2011E
Operating Activities						
Net earnings for the period	404,545	808,147	(97,044)	312,016	96,062	271,902
Items not involving cash						
Income tax recovery		(427,000)	(51,000)	113,000		
Gain on liabilities and sale of commerical division						
Unreallized foreign exchange and other gains			(6,500)	(47,688)		
Compensation related to stock option plan	29,745	80,709	18,408	35,396	22,332	24,419
Write-downs						
Interest accrued(on NP, on shareholer loan)						
Amortization and equipment write-down	39,078	52,414	64,758	60,388	64,784	63,588
	473,368	**514,270**	**(71,378)**	**473,112**	**183,178**	**359,910**
Changes in non-cash operating working capital						
Accounts receivable	(246,545)	34,043	17,008	86,448	37,791	(59,284)
Inventory	(105,922)	(253,388)	145,897	(81,658)	69,910	(21,038)
Prepaid expenses	10,264	(16,305)	(27,438)	22,600	6,268	(1,513)
Accounts payable and accrued liabilities	128,363	70,689	24,175	166	(28,654)	17,422
Customer Deposits		-	-	-	-	-
	(213,840)	**(164,961)**	**159,642**	**27,556**	**85,315**	**(64,413)**
Cash from from (used in) operations	**259,528**	**349,309**	**88,264**	**500,668**	**268,493**	**295,497**
Investing activities						
Purchase of furniture and equipment	(107,791)	(65,758)	(47,173)	(38,916)	(60,000)	(60,000)
Proceeds on sale of commerical division						
Deferred Development Costs						
Purchase of equipment and leaseholds	**(107,791)**	**(65,758)**	**(47,173)**	**(38,916)**	**(60,000)**	**(60,000)**
Financing activities						
Proceeds(repayments) of demand loans	(367,900)	(4,146)				
Proceeds (repayments) of payables and leases	(29,862)	(31,202)	(33,801)	(41,941)	(25,757)	(11,271)
Convertible debenture issued						
Issue of common share for cash	24,750	57,200	494,080	2,250		-
	(373,012)	**21,852**	**460,279**	**(39,691)**	**(25,757)**	**(11,271)**
Increase (decrease) in cash	(221,275)	305,403	501,370	422,061	182,736	224,226
Cash beginning of period	354,804	133,529	438,932	940,302	1,362,363	1,545,099
Cash end of period	**133,529**	**438,932**	**940,302**	**1,362,363**	**1,545,099**	**1,769,325**

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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