14 September 2011

Modern Water plc ("Modern Water", "the Company" or "the Group")

Modern Water (AIM:MWG), the owner of world-leading technologies for the production of fresh water and monitoring of water quality, announces Interim Results for the six-month period ended 30 June 2011

Highlights

Operational

- Winning a £500,000 contract for the world's first commercial desalination plant to use forward osmosis
- Successful acquisition and integration of Cogent monitoring business
- Accelerating revenues from sales of water monitoring systems
- Strong sales in China – Shanghai based Non-executive Chairman of MW China appointed

Financial

- Gross revenue £430,000 (H110 £1,000)
- Gross profit margin of 33%
- Strong balance sheet – debt free with £16.7m cash

Commenting on the results, Neil McDougall, Executive Chairman of Modern Water, said:

"Modern Water made excellent progress in the first half of 2011. We won the world's first commercial contract to build a desalination plant using forward osmosis. This is a major breakthrough for the Company as we bring our lower energy, cost-saving technology to a multi-billion dollar marketplace.

"Accelerating sales in China of our water monitoring systems helped us to achieve our first significant revenues and gross profit. I am delighted to announce today the appointment of Simon MacKinnon as Non-executive Chairman of Modern Water's operations in China. I am sure he will be of great help to the Company as we drive forward sales and pursue new opportunities for our desalination technology.

"Modern Water has excellent technology, a strong and growing market presence and a sound balance sheet, with £16.7m cash in hand. The second half of 2011 has started well and we look forward to reporting further strong progress at the end of the year."

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Report to shareholders

The first half of 2011 saw two milestone developments for Modern Water. First, and most importantly, we won the contract for the world's first commercial desalination plant using forward osmosis. Secondly, and also of considerable importance to the future growth of the company, we started to achieve volume sales of our water monitoring systems (£430k gross revenue compared to £27k for the whole of 2010).

Modern Water owns a fully patented desalination technology using forward osmosis which is not only substantially cheaper to run than traditional methods but is also able to produce higher quality water and is far more robust in demanding seawater conditions. This was fully recognised by the award, in June 2011, by the Public Authority for Electricity and Water (PAEW) in Oman of a contract to build the world's first fully commercial desalination plant using forward osmosis technology. Detailed planning is underway and we expect installation to start later this year.

The major increase in sales of our water monitoring systems follows our acquisition in February 2011 of Cogent Environmental. Cogent has been successfully assimilated into our Monitoring division resulting in a reduction in unit costs and an increase in cross-selling opportunities. We are now seeing good sales growth of our Cymtox Continuous Toxicity Monitor alongside the Cogent real-time trace metal analyser, particularly in China. We are continuing to expand our portfolio with distribution routes in over 20 countries and have an excellent platform for cross-selling our other monitoring and treatment systems. Having established a firm presence in this fast growing sector, we aim to develop the business organically and, where appropriate, through acquisition.

Outside of the reporting period in July we signed a distribution agreement with Crown Bio Technology Limited. This low cost field instrument, which uses bioluminescence for the rapid detection of soil contamination, fits well with our existing range of monitoring equipment. Also in July, we acquired the remaining shares of AguaCure which develops water treatment systems using electro-coagulation.

In the light of our strong and growing presence in China, we are announcing separately today the appointment of the first Non-executive Chairman of our China division. Simon MacKinnon is a long-term resident of Shanghai with 25 years of China business leadership, Board and corporate governance experience. We are confident that Simon will be instrumental in our strategy for introducing our desalination technology to the Chinese market as well as further strengthening sales of our water monitoring and treatment systems.

2011 is proving to be a significant year for Modern Water. The contract award in Oman recognises the commercial advantages of our forward osmosis technology. We are working closely with the Omani authorities on their future desalination requirements as well as establishing ourselves in other markets. The precise timing of future contract awards is difficult to predict but, as pressure increases for more efficient, less energy intensive means of producing our most important natural resource, we are confident of a strong commercial future for our technology. The second half of 2011 has started well with a continuing acceleration of sales from our water monitoring and treatment systems. Backed by a robust balance sheet, with £16.7m cash in hand, we look forward to reporting further strong progress at the end of the year.

None of our success could have been achieved without the dedication of our team at Modern Water. On behalf of the Board I would like to extend my appreciation to our staff and reiterate our commitment to deliver long term value to our shareholders.

Neil McDougall
Executive Chairman
14 September 2011

Group statement of comprehensive income (unaudited)

Six month period ended 30 June 2011

	Note	**6 months ended 30 June 2011 £'000**	6 months ended 30 June 2010 £'000	Year ended 31 December 2010 £'000
Revenue	4	**430**	1	27
Cost of sales		**(289)**	(1)	(2)
Gross profit		**141**	—	25
Administrative expenses	6	**(2,446)**	(2,241)	(4,489)
Operating loss		**(2,305)**	(2,241)	(4,464)
Finance income		**196**	286	490
Share of loss of joint venture	10	**(20)**	(93)	(131)
Loss on ordinary activities before taxation		**(2,129)**	(2,048)	(4,105)
Taxation	8	**29**	14	40
Loss and total comprehensive loss for the half year		**(2,100)**	(2,034)	(4,065)
Loss is attributable to:				
Owners of the Company		**(2,100)**	(2,026)	(4,051)
Non-controlling interests		—	(8)	(14)
		(2,100)	(2,034)	(4,065)
Loss per share attributable to the equity holders of the Company				
Basic loss per share	9	**3.54p**	3.44p	6.88p
Diluted loss per share	9	**3.54p**	3.44p	6.88p

The notes form an integral part of this condensed consolidated interim financial information.
Items in the statement above are all derived from continuing operations.

Group statement of financial position (unaudited)

As at 30 June 2011

	Note	**30 June 2011 £'000**	30 June 2010 £'000	31 December 2010 £'000
Assets				
Non-current assets				
Property, plant and equipment	10	**886**	**1,068**	942
Intangible assets	10	**15,339**	**14,391**	14,366
Investments	10	**195**	**253**	215
		16,420	**15,712**	15,523
Current assets				
Inventories		**173**	—	20
Trade and other receivables		**841**	**457**	568
Cash and cash equivalents		**16,702**	**21,225**	19,252
		17,716	**21,682**	19,840
Total assets		**34,136**	**37,394**	35,363
Equity and liabilities				
Equity				
Ordinary shares		**149**	**147**	147
Share premium account		**30,532**	**30,532**	30,532
Merger reserve		**13,180**	**12,782**	12,782
Retained earnings		**(11,107)**	**(7,260)**	(9,133)
		32,754	**36,201**	34,328
Non-controlling interests		—	**6**	—
Total equity		**32,754**	**36,207**	34,328
Liabilities				
Non-current liabilities				
Deferred tax liability	8	**407**	**376**	350
Current liabilities				
Trade and other payables		**975**	**811**	685
Total liabilities		**1,382**	**1,187**	1,035
Total equity and liabilities		**34,136**	**37,394**	35,363

The notes form an integral part of this condensed consolidated interim financial information.

Group statement of changes in equity (unaudited)

Six month period ended 30 June 2011

	Note	Called up share capital £'000	Share premium account £'000	Merger reserve £'000	Retained earnings £'000	Total £'000	Non-controlling interests £'000	Total equity £'000
Six month period ended 30 June 2010								
Balance as at 1 January 2010		**147**	**30,532**	**12,782**	**(5,394)**	**38,067**	**14**	**38,081**
Comprehensive loss								
Loss and total comprehensive loss for the period ended 30 June 2010		—	—	—	(2,026)	(2,026)	(8)	(2,034)
Total comprehensive loss		—	—	—	(2,026)	(2,026)	(8)	(2,034)
Transactions with owners								
Share-based payments	7	—	—	—	160	160	—	160
Total transactions with owners		—	—	—	160	160	—	160
Balance as at 30 June 2010		**147**	**30,532**	**12,782**	**(7,260)**	**36,201**	**6**	**36,207**
Six month period ended 30 June 2011								
Balance as at 1 January 2011		**147**	**30,532**	**12,782**	**(9,133)**	**34,328**	**—**	**34,328**
Comprehensive loss								
Loss and total comprehensive loss for the period ended 30 June 2011		—	—	—	(2,100)	(2,100)	—	(2,100)
Total comprehensive loss		—	—	—	(2,100)	(2,100)	—	(2,100)
Transactions with owners								
Issues of shares	5	2	—	398	—	400	—	400
Share-based payments	7	—	—	—	126	126	—	126
Total transactions with owners		2	—	398	126	526	—	526
Balance as at 30 June 2011		**149**	**30,532**	**13,180**	**(11,107)**	**32,754**	**—**	**32,754**

The notes form an integral part of this condensed consolidated interim financial information.

Group statement of cash flows (unaudited)

Six month period ended 30 June 2011

	Note	**6 months ended 30 June 2011 £'000**	6 months ended 30 June 2010 £'000	Year ended 31 December 2010 £'000
Cash flows from operating activities				
Cash used in operations	11	**(2,131)**	(2,075)	(4,185)
Net cash flows used in operating activities		**(2,131)**	(2,075)	(4,185)
Cash flows from investing activities				
Purchase of property, plant and equipment	10	**(106)**	(65)	(122)
Proceeds from sale of property, plant and equipment		**23**	—	—
Purchase of patents and development costs	10	**(70)**	(65)	(134)
Acquisition of subsidiaries, net of cash acquired	5	**(411)**	—	—
Acquisition of joint venture	5	**—**	(100)	(100)
Interest received		**144**	395	669
Net cash flows (used in)/generated from investing activities		**(420)**	165	313
Cash flows from financing activities				
Cash-settled share-based payments		—	—	(4)
Net cash flows used in financing activities		—	—	(4)
Net decrease in cash and cash equivalents		**(2,551)**	(1,910)	(3,876)
Cash and cash equivalents at start of period		**19,252**	23,123	23,123
Exchange gains on bank balances		**1**	12	5
Cash and cash equivalents at end of period		**16,702**	21,225	19,252

The notes form an integral part of this condensed consolidated interim financial information.

Notes (unaudited)

Six month period ended 30 June 2011

1 GENERAL INFORMATION

Modern Water plc ('the Company'), its subsidiaries and joint venture (together, 'the Group') invests in, develops and deploys new water technology.

The Company is a public limited company incorporated and domiciled in England and Wales, whose shares are publically traded on the Alternative Investment Market (AIM), a market operated by the London Stock Exchange. The registered office and principal place of business is Bramley House, The Guildway, Old Portsmouth Road, Guildford, Surrey GU3 1LR.

This condensed consolidated interim financial information was approved for issue by the Board of Directors on 14 September 2011.

These interim financial results are unaudited and do not comprise statutory accounts within the meaning of section 438 of the Companies Act 2006.

Statutory accounts for the year ended 31 December 2010 were approved by the board of directors on 9 March 2011 and delivered to the Registrar of Companies. The report of the auditors on those accounts was unqualified, did not contain an emphasis of matter paragraph and did not contain any statement under section 498 of the Companies Act 2006.

2 BASIS OF PREPARATION

The principal accounting policies have been applied consistently throughout the period in the preparation of these financial statements.

This condensed consolidated interim financial information for the six months ended 30 June 2011 has been prepared in accordance with the AIM Rules for Companies of the London Stock Exchange plc and with IAS 34, 'Interim financial reporting' as adopted by the European Union.

The condensed consolidated interim financial information should be read in conjunction with the annual financial statements for the year ended 31 December 2010, which have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union.

3 ACCOUNTING POLICIES

3.1 Accounting policy and disclosure changes

The accounting policies applied are consistent with those of the annual financial statements for the year ended 31 December 2010.

3.2 Taxation

Taxes on income in the interim periods are accrued using the tax rate that would be applicable to expected total annual earnings.

4 SEGMENTAL ANALYSIS

The chief operating decision-maker is deemed to be the Board, for whom monthly financial information is provided by division to gross profit and below this in consolidated group format. For management reporting purposes the group is organised into two operating segments (i) desalination; and (ii) monitoring.

At the Group's current stage of development the majority of the costs (business development, technical, legal, marketing, finance, facilities and directors' expenditure) are managed and reported centrally. As the commercial activities of the Group develop, this financial information is expected to evolve.

	Note	Desalination £'000	MW Monitoring £'000	Total £'000
Revenue		21	409	430
Cost of sales		(19)	(270)	(289)
Gross profit		2	139	141

5 BUSINESS COMBINATIONS

On 2 February 2011 Modern Water plc purchased the entire share capital of Cogent Environmental Limited (Cogent), for consideration of £419,110 and 642,571 newly issued 0.25p Modern Water plc shares, ranking pari passu in all respects with existing shares. The new shares represented £400,000 at the average mid-market closing price on the five previous business days, and represent 1.1% of the existing issued share capital of the Company.

Cogent contributed £338,000 revenue and £84,000 loss for the period to 30 June 2011. If the acquisition had occurred on 1 January 2011 Group revenue would have been £442,000 and Group loss £2,179,000 for the period.

At the acquisition date the fair value of the net assets and liabilities in Cogent equalled £156,306, consequently goodwill on the acquisition was £662,804. The goodwill is attributable to the acquired customer base, staff expertise and benefits resulting from combining the Cymtox and Cogent businesses. Transaction costs expensed on the acquisition were £1,500.

The following table summaries the consideration paid for Cogent, the net assets acquired and consequential goodwill recognised:

	£'000
Cash	419,110
Equity	400,000
Total consideration	819,110
Fair value of Cogent on acquisition (as below)	(156,306)
Goodwill	662,804

The fair value of the assets and liabilities acquired at the date of acquisition were:

	Book value £'000	Fair value £'000
Intangible fixed assets	-	329,693
Tangible fixed assets	39,229	39,229
Stock	83,829	83,829
Debtors	206,918	206,918
Cash	8,135	8,135
Creditors <1 year	(425,778)	(425,778)
Deferred tax liability	-	(85,720)
Net assets		156,306
Stake acquired	100%	156,306

The separable and identifiable intangible assets are:

	£'000
Customer contracts	179,702
Research and development expenditure	149,991
Intangible fixed assets	329,693

Outflow of cash to acquire the business net of cash acquired:

	£'000
Cash consideration	419,110
Cash acquired	(8,135)
Cash outflow on acquisition	410,975

6 ADMINISTRATIVE EXPENSES

	Note	**6 months ended 30 June 2011 £'000**	6 months ended 30 June 2010 £'000	Year ended 31 December 2010 £'000
Wages and salaries		**842**	766	1,437
Social security costs		**93**	110	192
Pension costs		**51**	50	99
Other employee benefits		**23**	24	41
Equity settled share-based payments	7	**126**	160	316
Depreciation, amortisation and impairment charges	10	**274**	231	492
Minimum lease payments recognised as an operating lease expense		**70**	66	139
Research and development		**181**	200	366
Other administrative expenses		**786**	634	1,407
Total administrative expenses		**2,446**	2,241	4,489

In addition to the above costs for permanent staff, the Group utilises the services of contract and agency staff as circumstances require.

7 EQUITY-SETTLED SHARE-BASED PAYMENTS

	6 months Ended 30 June 2011 £'000	6 months ended 30 June 2010 £'000	Year ended 31 December 2010 £'000
Options	**15**	84	133
Conditional share awards	**111**	68	173
Employee bonus plan	**—**	8	10
Equity-settled share-based payments	**126**	160	316
Cash-settled share-based payments	—	—	(4)
Total share-based payments changes in equity	**126**	160	312

There are two share-based payment schemes. The Management Share Incentive Scheme (MSIS) and the Modern Water Incentive Plan (MWIP). There has been no activity on MSIS during 2010 or 2011. Activity on MWIP is detailed below.

7.1 Modern Water Incentive Plan (MWIP)

The MWIP was adopted on 1 June 2007 and contains provisions relating to the making of awards in the form of options, conditional awards of ordinary shares (to be received once performance conditions are satisfied) and matching awards of ordinary shares (in respect of bonuses deferred by participants) to all employees, including executive directors. There has been no activity on the employee bonus plan during 2011. Activity on share options and conditional shares is detailed below.

(a) Options

Under this scheme share options are granted to senior management. The exercise price is equal to the market price on the date of the grant. The options may be exercised if certain TSR performance criteria are met. If the increase is not met the options lapse.

During the period the performance criteria on options over 400,000 shares lapsed. No options were granted, exercised, vested or forfeited during the period.

The fair value of the equity-settled share options granted is estimated as at the date of grant using a Black-Scholes model, taking into account the terms and conditions upon which the options were granted.

The total number of options outstanding at 30 June 2011 was 610,877 (WAEP 112p), of these 560,877 (WAEP 119p) had vested and were exercisable, but at above the current market price.

(b) Conditional share awards

The conditional share awards are provisional awards of ordinary shares in Modern Water plc, which vest three years after the date of the award to the extent that performance conditions have been met. The extent to which the award will vest depends on the Group's share price on the vesting date.

The movement in the number of conditional shares awarded is set out below:

	2011
At 1January 2011	* 1,750,000
Conditionally awarded during period	** 600,000
At 30 June 2011	2,350,000

The fair value of the award is estimated as at the date of award using a Monte Carlo model, taking into account the terms and conditions upon which the shares were awarded.

The following table lists the inputs into the model used for the shares awarded in the period.

Grant date	** 20 April 2011	* 21 April 2010	* 10 September 2009
Share price at date of award	50.5p	80.0p	72.5p
Exercise price	£nil	£nil	£nil
Assumed volatility at date of award (median of historical 50 day moving average)	43%	50%	43%
Vesting period (years)	3.0	3.0	3.0
Expected dividend yield	0%	0%	0%
Risk-free discount rate	2.0%	2.0%	2.0%
Fair value per share awarded	20p	44p	30p

Vesting criteria required on vesting date three years after grant date are set out below:

* 1,750,000 share conditionally awarded prior to 1 January 2011 will vest in full if the share price is £1.40 or more on the vesting date. If the share price is £1.00 or below the award does not vest at all. If the share price is between £1.00 and £1.40 the award partially vests, on the basis of 2.5% of the award for each £0.01 above a share price of £1.00.

** 600,000 shares conditionally awarded during the period will vest in full if the share price is £1.00 or more on the vesting date. If the share price is £0.80 the award does not vest at all. If the share price is between £0.80 and £1.00 the award partially vests, on the basis of 5% of the award for each £0.01 above a share price of £0.80.

8 TAXATION

During the period there were no taxable profits.

The deferred tax liability of £407,000 at 30 June 2011 (2010: £376,000) arises from taxable temporary differences on intangibles recognised on business combinations and is expected to unwind over the useful economic life of these assets. £29,000 has been credited to the Group Statement of Comprehensive Income to 30 June 2011 (2010: £14,000).

At the balance sheet date the Group had a deferred tax asset in respect of unutilised trading losses. This asset has not been recognised as its utilisation is not yet sufficiently certain.

9 LOSS PER SHARE

9.1 Basic

Basic loss per share is calculated by dividing the loss attributable to equity holders of the Company by the weighted average number of ordinary shares in issue during the year.

	6 months ended 30 June 2011 £'000	6 months ended 30 June 2010 £'000	Year ended 31 December 2010 £'000
Loss attributable to equity holders of the Company	**2,100**	2,026	4,051
Weighted average number of ordinary shares in issue (thousands)	**59,398**	58,863	58,863
Basic loss per share	**3.54p**	3.44p	6.88p

9.2 Diluted

As the Group is loss making, the diluted loss per share is equal to the basic loss per share.

10 CAPITAL EXPENDITURE

	Note	Property, plant and equipment £'000	Intangible assets (inc goodwill) £'000	Investments £'000	Total £'000
Six month period ended 30 June 2011					
Opening net book amount at 1 January 2011		942	14,366	215	15,523
Acquisition of subsidiary		39	993	—	1,032
Additions		106	70	—	176
Disposals		(17)	—	—	(17)
Depreciation/amortisation		(184)	(90)	—	(274)
Share of loss of joint venture		—	—	(20)	(20)
Closing net book amount at 30 June 2011		**886**	**15,339**	**195**	**16,420**

11 NET CASH FLOWS FROM OPERATING ACTIVITIES

	Note	**6 months ended 30 June 2011 £'000**	6 months ended 30 June 2010 £'000	Year ended 31 December 2010 £'000
Operating loss		**(2,305)**	(2,241)	(4,464)
Adjustments for:				
Depreciation of property, plant and equipment	10	**184**	145	312
Amortisation of intangible assets	10	**90**	86	180
(Profit)/loss on disposal of property, plant and equipment		**(6)**	—	16
Equity-settled share-based payments	7	**126**	160	316
Movements in working capital:				
Increase in inventories		**(69)**	—	(20)
Increase in trade and other receivables		**(15)**	(21)	(195)
Decrease in trade and other payables		**(136)**	(204)	(330)
Cash used in operations		**(2,131)**	(2,075)	(4,185)

12 RELATED PARTY TRANSACTIONS

IP Group plc holds 23.19% of the ordinary share capital of the Company and appoints a non-executive director, it is therefore deemed a related party. A service agreement dated 1 December 2006 was made between the Company and IP Group plc, whereby IP Group plc provides strategic, business development and administrative services to the Company. Fees for the period were £15,000 and as at 30 June 2011 £7,500 (30 June 2010: £7,500) was outstanding under this agreement.

Transactions with the Group's joint venture AguaCure Ltd are recorded using the equity method of accounting and not eliminated on consolidation and therefore require disclosure in the Group accounts. Modern Water Services Limited provided technical, management and business development services at cost to AguaCure during the period for fees of £18,510 (30 June 2010: £59,000). These fees are recorded as a credit to administrative costs and form part of the Group's share of AguaCure's loss in the statement of comprehensive income. In addition Modern Water plc and Modern Water Services Ltd provided working capital to AguaCure and at 30 June 2011 the balance outstanding was £101,000 (30 June 2010: £9,000) to Modern Water plc and £19,000 (30 June 2010: £9,000) to Modern Water Services Ltd.

Transactions between the Company and its subsidiaries, which are related parties, have been eliminated on consolidation in the Group accounts.

13 POST BALANCE SHEET EVENTS

On 29 July 2011 Modern Water plc acquired Aguahold Ltd's shareholding in AguaCure Ltd for a consideration of £25,000. This increased Modern Water's shareholding in AguaCure Ltd to 100%. Due to the timing of the transaction, the fair values of the assets and liabilities acquired are still being calculated at the date of signing of the financial statements.