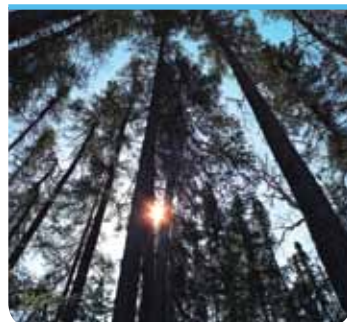




MODERNWATER



HIGHLIGHTS

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- 04 Group statement of financial position (unaudited)
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OPERATIONAL

Agreement with Oman based Omzest to assist market development



Winner of the AIM Sustainability Award 2009



Winner of the AIM Sustainability Award 2009



Evaporative cooling system proving plant to be installed in Oman by mid-2010



FINANCIAL

Cymtox achieves first revenue; further proof of commercialisation



Patent portfolio significantly increased



Balance of shares acquired in Cymtox Ltd



Strong financial position with £23.1 million cash and no debt



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- Cooling tower plant fully commissioned in Oman;
- Oman desalination plant trial extension and tariff approved;
- Cymtox extends reach across UK with trials at Bristol Water;
- Directorate changes; and
- Strong cash position with £21.2 million in hand and no debt at 30 June 2010.

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NEIL MCDOUGALL
Executive Chairman
15 September 2010

GROUP STATEMENT OF COMPREHENSIVE INCOME (UNAUDITED)

FOR THE SIX MONTH PERIOD ENDED 30 JUNE 2010

	Note	6 months ended 30 June 2010 £000	6 months ended 30 June 2009 £000	Year ended 31 December 2009 £000
Revenue	4	1	—	56
Cost of sales		(1)	—	(21)
Gross profit		—	—	35
Administrative expenses	6	(2,241)	(2,500)	(4,380)
Other income	4	—	—	6
Operating loss		(2,241)	(2,500)	(4,339)
Finance income		286	524	849
Finance costs		—	(23)	(21)
Share of loss of joint venture	10	(93)	(61)	(145)
Loss on ordinary activities before taxation		(2,048)	(2,060)	(3,656)
Taxation	8	14	15	29
Loss and total comprehensive loss for the period		(2,034)	(2,045)	(3,627)
Attributable to:				
Equity shareholders of the Company		(2,026)	(2,012)	(3,547)
Minority interest		(8)	(33)	(80)
		(2,034)	(2,045)	(3,627)
Loss per share attributable to the equity holders of the Company				
Basic loss per share	9	3.44p	3.42p	6.03p
Diluted loss per share	9	3.44p	3.42p	6.03p

The notes on pages [•] to [•] 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)

FOR THE SIX MONTH PERIOD ENDED 30 JUNE 2010

	Note	30 June 2010 £000	30 June 2009 £000	31 December 2009 £000
Assets				
Non-current assets				
Property, plant and equipment	10	1,068	1,029	1,148
Intangible assets	10	14,391	14,182	14,412
Investments	10	253	420	246
		15,712	15,631	15,806
Current assets				
Trade and other receivables		457	327	557
Cash and cash equivalents		21,225	25,325	23,123
		21,682	25,652	23,680
Total assets		37,394	41,283	39,486
Equity and liabilities				
Equity				
Called up share capital		147	147	147
Share premium account		30,532	30,532	30,532
Merger reserve		12,782	12,782	12,782
Retained earnings		(7,260)	(3,985)	(5,394)
		36,201	39,476	38,067
Minority interest		6	84	14
Total equity		36,207	39,560	38,081
Liabilities				
Non-current liabilities				
Deferred tax liability	8	376	404	390
Current liabilities				
Trade and other payables		811	1,315	1,015
Borrowings		—	4	—
		761	1,319	1,015
Total liabilities		1,187	1,723	1,405
Total equity and liabilities		37,394	41,283	39,486

The notes on pages [•] to [•] form an integral part of this condensed consolidated interim financial information.

GROUP STATEMENT OF CHANGES IN EQUITY (UNAUDITED)

FOR THE SIX MONTH PERIOD ENDED 30 JUNE 2010

	Note	Called up share capital £'000	Share premium account £'000	Merger reserve £'000	Retained earnings £'000	Total £'000	Minority interest £'000	Total equity £'000
Period ended 30 June 2009								
Balance as at 1 January 2009		147	30,532	12,782	(2,105)	41,356	34	41,390
Loss and total comprehensive loss for the period ended 30 June 2009		—	—	—	(2,012)	(2,012)	(33)	(2,045)
Transaction with minority interest		—	—	—	—	—	83	83
Share-based payment schemes	7	—	—	—	132	132	—	132
Balance as at 30 June 2009		147	30,532	12,782	(3,985)	39,476	84	39,560
Period ended 30 June 2010								
Balance as at 1 January 2010		147	30,532	12,782	(5,394)	38,067	14	38,081
Loss and total comprehensive loss for the period ended 30 June 2010		—	—	—	(2,026)	(2,026)	(8)	(2,034)
Share-based payments	7	—	—	—	160	160	—	160
Balance as at 30 June 2010		147	30,532	12,782	(7,260)	36,201	6	36,207

The notes on pages [•] to [•] form an integral part of this condensed consolidated interim financial information.

GROUP STATEMENT OF CASH FLOWS (UNAUDITED)

FOR THE SIX MONTH PERIOD ENDED 30 JUNE 2010

	Note	6 months ended 30 June 2010 £000	6 months ended 30 June 2009 £000	Year ended 31 December 2009 £000
Cash flows from operating activities				
Cash used in operations	11	(2,075)	(1,897)	(3,648)
Net cash flows used in operating activities				
Cash flows from investing activities				
Purchase of property, plant and equipment	10	(65)	(316)	(540)
Purchase of patents and development costs	10	(65)	(52)	(100)
Acquisition of subsidiaries, net of cash acquired		—	—	(285)
Investment in joint venture	5	(100)	—	—
Interest received		395	762	875
Net cash flows generated from/(used in) investing activities				
Cash flows from financing activities				
Cash-settled share-based payments		—	—	(5)
Repayments of borrowings		—	(4)	(8)
Net cash flows from financing activities				
Net decrease in cash and cash equivalents				
Cash and cash equivalents at start of period		23,123	26,855	26,855
Exchange gains/(losses) on bank balances		12	(23)	(21)
Cash and cash equivalents at end of period				

The notes on pages [•] to [•] form an integral part of this condensed consolidated interim financial information.

NOTES TO THE CONSOLIDATED INTERIM FINANCIAL STATEMENTS (UNAUDITED)

FOR THE SIX MONTH PERIOD ENDED 30 JUNE 2010

1. GENERAL INFORMATION

Modern Water plc ("the Company") and its subsidiaries (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 15 September 2010.

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 2009 were approved by the board of directors on 10 March 2010 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 2010 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 2009, which have been prepared in accordance with International Financial Reporting Standards (IFRS).

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 2009, except as described below.

(a) Standards, amendments and interpretations to existing standards effective in 2010

The following new standards and amendments to standards are mandatory for the first time for the financial year beginning 1 January 2010:

- IFRS 3 (revised) 'Business combinations', and consequential amendments to IAS 27, 'Consolidated and separate financial statements', IAS 28, 'Investments in associates', and IAS 31, 'Interests in joint ventures'. The revised standard continues to apply the acquisition method to business combinations, with some significant changes. Changes to measurement of the fair value of payments made to acquire a business and the goodwill arising. Transaction costs are expensed. The effect of all transactions with non-controlling interests are recorded in equity if there is no change in control and these transactions will no longer result in goodwill gains and losses. The investment in Aguacure on 5 February 2010 was not impacted as the consideration was for the issue of new shares and not a transaction with a non-controlling interest. Effective from annual reporting periods commencing on or after 1 July 2009;
- IFRS 5 (amendment), 'Non-current assets for sale and discontinued operations'. Clarification on disclosures. This has no impact on these interim financial results. Effective for annual reporting periods commencing on or after 1 January 2010;
- IAS 1 (amendment), 'Presentation of financial statements'. Clarification on the potential settlement of a liability by the issue of equity. This has no impact on these interim financial results. Effective for annual reporting periods commencing on or after 1 January 2010;
- IAS 38 (amendment), 'Intangible assets'. The amendment clarifies guidance in measuring the fair value of an intangible asset acquired in a business combination. This has no impact on these interim financial results. Effective for annual reporting periods commencing on or after 1 January 2010;
- IFRIC 17, 'Distributions of non-cash assets to owners'. Guidance on accounting for distribution of non-cash assets to shareholders. This has no impact on these interim financial results. Effective for annual reporting periods commencing on or after 1 July 2009; and
- IFRIC 18, 'Transfers of assets from customers'. This has no impact on these interim financial results. Effective for annual reporting periods commencing on or after 1 July 2009.

NOTES TO THE CONSOLIDATED INTERIM FINANCIAL STATEMENTS (UNAUDITED) CONTINUED

FOR THE SIX MONTH PERIOD ENDED 30 JUNE 2010

(b) Standards, amendments and interpretations to existing standards that are not yet effective and have not been early adopted by the Group

The following new standards, amendments to standards and interpretations have been issued, but are not effective for the financial reporting period beginning 1 January 2010:

- IFRS 9, 'Financial instruments'. This addresses the classification and measurement of financial assets. This is not expected to impact the Group. Effective for annual reporting periods commencing on or after 1 January 2013;
- IAS 24 (revised), 'Related party disclosures'. This supersedes IAS 24. This is not expected to impact the Group. Effective for annual reporting periods commencing on or after 1 January 2011;
- IAS 32 (amendment), 'Classification of rights issues'. This is not expected to impact the Group. Effective for annual reporting periods commencing on or after 1 February 2010;
- IFRIC 14 (amendment), 'Prepayments of a minimum funding requirement'. This is not expected to impact the Group. Effective for annual reporting periods commencing on or after 1 January 2011; and
- IFRIC 19, 'Extinguishing financial liabilities with equity instruments'. This clarifies the requirements of IFRSs when an entity renegotiates the terms of a financial liability with its creditor and the creditor agrees to accept the entity's shares to settle the liability. This is not expected to impact the Group. Effective for annual reporting periods commencing on or after 1 July 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 in consolidated group format.

Revenue and gross profit during the period were from consumable sales by Cymtox Ltd. Revenue and gross profit during 2009 were from royalty, consumables and consultancy sales by Cymtox Ltd. Other income in 2009 was from the reimbursement of expenses relating to the consultancy sales.

At the Group's current stage of development the majority of the costs (business development, technical, legal, marketing, finance, facilities and directors' expenditure), including those relating to Cymtox Ltd, are managed and reported centrally.

As the commercial activities of the group develop, this financial information is expected to evolve.

The business is not considered to be seasonal.

5. INVESTMENT IN JOINT VENTURE

At 31 December 2009 Modern Water plc owned 45% of AguaCure Limited (AguaCure), which it accounted for as a joint venture. On 5 February 2010, Modern Water plc invested £100,000 for 20 newly issued AguaCure shares. This increased the Group's shareholding to 54%. AguaCure is deemed to remain under joint control of Modern Water plc and Aguahold Ltd and therefore continues to be accounted for as a joint venture by Modern Water plc.

6. ADMINISTRATIVE EXPENSES

	Note	6 months ended 30 June 2010 £000	6 months ended 30 June 2009 £000	Year ended 31 December 2009 £000
Wages and salaries		766	814	1,530
Social security costs		110	83	166
Pension costs		50	43	96
Other employee benefits		24	17	34
Equity settled share-based payments	7	160	132	263
Depreciation, amortisation and impairment charges	10	231	154	429
Minimum lease payments recognised as an operating lease expense		66	65	133
Research and development		200	161	336
Other administrative expenses		634	1,031	1,393
Total administrative expenses		2,241	2,500	4,380

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

NOTES TO THE CONSOLIDATED INTERIM FINANCIAL STATEMENTS (UNAUDITED) CONTINUED

FOR THE SIX MONTH PERIOD ENDED 30 JUNE 2010

7. EQUITY-SETTLED SHARE-BASED PAYMENTS

	6 months ended 30 June 2010 £000	6 months ended 30 June 2009 £000	Year ended 31 December 2009 £000
Options	84	124	214
Conditional share awards	68	—	34
Employee bonus plan	8	8	15
Total share-based payments	160	132	263

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 2009 or 2010. 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 2010. 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 560,877 shares vested. No options were granted, exercised, lapsed 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 directors' and employees' holdings of options over ordinary shares issued under MWIP were as follows:

Grant date	Earliest exercise date	Expiry date	Exercise price	Number of options			Exercisable at below market price 30 June 2010
				Outstanding at 1 January 2010	Outstanding at 30 June 2010	Vested and exercisable at 30 June 2010	
Neil McDougall*							
12.06.07	12.06.10	12.06.17	119.0p	186,959	186,959	186,959	—
Simon Humphrey*							
12.06.07	12.06.10	12.06.17	119.0p	373,918	373,918	373,918	—
Employees							
13.12.07**	13.12.10	13.12.19	97.0p	500,000	500,000	—	—
26.02.08**	26.02.11	26.02.20	87.5p	200,000	200,000	—	—
02.06.08**	02.06.11	02.06.20	112.5p	200,000	200,000	—	—
21.04.09***	21.04.12	21.04.19	35.0p	50,000	50,000	—	—
Total Options				1,510,877	1,510,877	560,877	—
WAEP				104p	104p	119p	—

TSR performance criteria required on the earliest exercise date. If this is not met the options lapse.

* Options vested during the period, as total shareholder return was at least equal to 10% for the 12 months preceding the vesting date. Since vesting the share price on the stock market has been lower than the option exercise price, therefore these options are currently 'underwater'.

** Options will vest subject to total shareholder return being at least equal to 30% for the 3 years between grant and vesting.

*** Options will vest subject to total shareholder return being at least equal to 200% for the 3 years between grant and vesting.

NOTES TO THE CONSOLIDATED INTERIM FINANCIAL STATEMENTS (UNAUDITED) CONTINUED FOR THE SIX MONTH PERIOD ENDED 30 JUNE 2010

(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. If the share price is £1.40 or more the award will vest in full. 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.

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

	2010
At 1 January 2010	1,000,000
Conditionally awarded during period	750,000
At 30 June 2010	1,750,000

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

8. TAXATION

During the period there were no taxable profits.

The deferred tax liability of £376,000 at 30 June 2010 (2009: £404,000) arises from taxable temporary differences on intangibles recognised on business combinations and is expected to unwind over the useful economic life of these assets. £14,000 has been credited to the Group Statement of Comprehensive Income to 30 June 2010 (2009: £15,000).

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 earnings 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 2010 £000	6 months ended 30 June 2009 £000	Year ended 31 December 2009 £000
Loss attributable to equity holders of the Company	2,026	2,012	3,547
Weighted average number of ordinary shares in issue (thousands)	58,863	58,863	58,863
Basic loss per share	3.44p	3.42p	6.03p

9.2 Diluted

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

NOTES TO THE CONSOLIDATED INTERIM FINANCIAL STATEMENTS (UNAUDITED) CONTINUED

FOR THE SIX MONTH PERIOD ENDED 30 JUNE 2010

10. CAPITAL EXPENDITURE

	Note	Property, plant and equipment £'000	Intangible assets £'000	Investments £'000	Total £'000
Period ended 30 June 2010					
Opening net book amount at 1 January 2010		1,148	14,412	246	15,806
Investment in joint venture	5	—	—	100	100
Additions		65	65	—	130
Depreciation/amortisation		(145)	(86)	—	(231)
Share of loss of joint venture		—	—	(93)	(93)
Closing net book amount at 30 June 2010		1,068	14,391	253	15,712

11. NET CASH FLOWS FROM OPERATING ACTIVITIES

	Note	6 months ended 30 June 2010 £000	6 months ended 30 June 2009 £000	Year ended 31 December 2009 £000
Operating loss		(2,241)	(2,500)	(4,339)
Adjustments for:				
Depreciation of property, plant and equipment	10	145	66	171
Amortisation of intangible assets	10	86	88	168
Impairment of investment		—	—	90
Equity-settled share-based payments	7	160	132	263
Movements in working capital:				
(Increase) in trade and other receivables		(21)	(47)	(65)
(Decrease)/Increase in trade and other payables		(204)	364	64
Cash used in operations		(2,075)	(1,897)	(3,648)

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

12. POST BALANCE SHEET EVENTS

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