



25 June, 2020

Reference: ODIN19684

Mr Elvis Onyura
Senior Adviser – Listing Compliance
ASX Compliance Pty Limited
20 Bridge Street
Sydney NSW 2000

By email:

Dear Elvis,

Thank you for your letter titled Phoslock Environmental Technologies Limited ('PET'): Query letter dated 22 June 2020.

Having regard to the queries contained in your letter, please see below PET's detailed response which addresses each of the following questions and requests for information.

Question 1: Please outline specifically what the material changes were, and which forecasts are affected.

Sales forecasts for the PET group are updated monthly by the Heads of the Chinese and International businesses and provided to the Managing Director and Company Secretary four to five days prior to PET's monthly Board Meeting.

These reports are collated and provided to the PET Board for discussion.

The initial FY2020 sales forecast of \$50-70 million was provided to the ASX on 3 December, 2019. The sales forecast of \$50 - \$70 million had assumed active remediation work of the Shilongba Reservoir and Xingyun Lake projects from June to mid-December 2020. These two projects accounted for a significant portion of the Chinese business's revenue forecast of \$40-\$55 million. International sales accounted for \$10-15m range; the aggregation of which made up the Group forecast range of \$50 - \$70 million. The above forecast was reaffirmed at the 17 December 2019 and 14 January 2020 Board Meetings.

Whilst there was no board meeting in February, in early February, the company received confirmation of a new treatment in Rio de Janeiro which generated substantial media coverage. This coupled with interest in general activities in China promoted us to release the update of 17th of February to the market.

The next PET Board Meeting was on 3 March 2020. Reports from the team in China suggested that the virus curve was trending downward and that restrictions were easing. This was evidenced by our Changxing factory restarting on 17 February 2020 and by early March was producing at record production levels. Our GM China reported business as getting back to normal. There was no information suggesting a requirement to restate the prior sales forecast. This was around the time 'Covid-19' (meaning economic dislocation issues due to virus response) in US and Europe were becoming apparent.

The next PET Board Meeting was 14 April 2020. The team in China reported that the factory was operating well and that the supply chain in and out of the factory was operating as normal. The GM China reported that all major projects were on track, albeit with some small delays in commencement dates. The GM International reported that delay's due to Covid-19 would affect first half 2020 projects, and these were being pushed into the second half of 2020. Of note also was the significant devaluation of the \$A versus the ¥CNY and \$US (¥4.35/\$A1 and \$US0.62/\$A1 at the time of publishing reports). A devaluation of the \$A vs both currencies represents an uplift in the Group's revenues in \$A terms.

The next PET Board Meeting was 20 May 2020. Reports were provided on 15 May. Our GM China reported that all projects were on track, although commencement dates for Shilongba and Xingyun were still being determined. Separately, the GM China had advised that government approval had been obtained to commence a trial in Lake Dianchi, China's eighth largest freshwater lake. This was a positive development. The amount forecasted in the Groups FY2020 sales forecast for Dianchi was low. A successful trial could lead to meaningful project work by Q4 2020. The GM International reported that Covid 19 delays has affected first half 2020 projects, albeit work on several Brazilian and US projects had been undertaken. The remainder of International projects were being pushed into the second half of 2020 and potentially FY2021, however remained within the Groups guidance range.

The June 2020 Board Meeting was on 17 June. The GM China report was received late evening Thursday 11 June and translated into English for review on Friday 12 June. The report advised of delays in finalising orders for Shilongba and Xingyun projects. The report suggested that there was now a possibility that a material portion of the Shilongba and Xingyun projects may move into FY2021 estimated at \$20 million. It also noted that some of the smaller projects in China had also been affected. The report detailed that government officials were reprioritising some short-term emergency resources away from projects such as lake restoration toward immediate health resources (ie for the potential of a second Covid-19 outbreak). This report contained material new information to the prior forecast, and was distributed to the Board over this weekend. The Company decided to suspend PET shares on Monday 15 June to verify the nature of the report and to enable a concise picture of the restated June forecast to be given to shareholders.

Question 2 - Noting that:

- a. **PET released the June Forecast 16 business days after releasing the May Forecast.**
- b. **The June Forecast represents a 20-57% reduction in PET's forecast revenue, please explain in detail what led to the changes reflected in the June Forecast.**

Please ensure your answer addresses:

- i. **what specific matters came to the attention of PET;**
- ii. **when those matters came to the attention of PET;**
- iii. **why PET considered those matters to warrant the material changes; and**
- iv. **how PET arrived at the \$30 million to \$40 million guidance**

As referenced in the final paragraph answering question 1 above, the report from the GM China received late evening Thursday 11 June and translated into English for review on Friday 12 June contained material new information to the prior forecast, requiring a new/updated forecast. (Reference i & ii above)

The new/updated June Forecast was arrived by accepting timing delays in the Shilongba and Xingyun projects - estimated at approx. \$20 million revenue and other smaller projects in China to the end of the year. The new \$30 - \$40 million range also considers the increasingly likely delays to proposed work on Lake Dianchi through the rest of this year, while acknowledging our ongoing trial work.

Furthermore, it should also be noted that the A\$ had appreciated materially and was now ¥4.9/\$A1 and \$US0.69/\$1. An appreciation of the \$A vs both currencies represents a decline in the Group's revenues in \$A terms.

In summary, taking into consideration potential delays in China sales, particularly in the Shilongba and Xingyun projects, combined with the earlier stated delays in International sales with some projects moving into FY2021 and the recent strength in the A\$, the board of PET decided to reduce FY2020 forecast sales to \$30-40 million. (Reference iii & iv above)

Question 3 - To the extent not already dealt with in PET's answers to questions 1 and 2:

a. Have any projects been delayed?

Answered in Question 2 (2nd Paragraph)

b. If the answer to question 3.a is "yes", please identify which projects have been delayed and the expected change in their contribution to total revenue

Answered in Question 2 (2nd Paragraph)

Trust this sufficiently answers your queries

Yours sincerely



Lachlan McKinnon
Managing Director
Phoslock Environmental Technologies Limited



22 June 2020

Reference: ODIN19684

Mr Matthew Parker
Chief Financial Officer & Company Secretary
Phoslock Environmental Technologies Limited
Suite 403
25 Lime Street
Sydney NSW 2000

By email:

Dear Mr Parker

Phoslock Environmental Technologies Limited ('PET'): Query Letter

ASX refers to the following:

A. PET's announcement titled "Business Update" released on the ASX Market Announcements Platform ('MAP') on 31 January 2020, which disclosed:

i. *"On 3 December 2019 PET advised shareholders that the sales forecast for FY2020 was in the range of \$50-70m, a 100% increase on FY2019."*

ASX notes there was no revision to the sales forecast within the announcement.

ii. *"Although we have experienced some delays in the last quarter due to slower than anticipated government action on some projects, all are continuing and will commence or be completed in the current financial year. Overall, therefore, we expect to see no change in the total volume of business.*

The Company and its personnel are unaffected by the coronavirus outbreak and at this stage we expect to see no change in the overall contract position."

B. PET's announcement titled "China Update and new Brazil Project" released on MAP on 17 February 2020 which disclosed:

"No treatments in China planned until late March/April and no delays expected; no effect on FY2020 sales guidance"

C. PET's announcement titled "Business Update" released on MAP on 26 March 2020 which disclosed (emphasis added):

*"PET has reviewed its plans for FY2020 in light of the current Coronavirus COVID 19 crisis that is affecting most parts of the world. China is a key part of PET's business, both manufacturing and projects. The Company has been forecasting 85% of FY2020 revenue from its China business. **All projects in the company's FY2020 business plan, except several lakes in Hubei province, are forecast to proceed as planned.***

*PET's International Business was forecast to make up 15% of FY2020 sales. Some 40% of the International sales (\$5m) are for existing projects and customers. A number of deliveries have already been made to customers in January and February. **PET expects that most of the sales to existing projects and customers should proceed in FY2020.** The balances of planned International Sales (\$7m) are new projects mainly in Europe and North America. Given that most of Europe and North America is currently in lock-down, first half projects will be moved into the second half of FY2020 and potentially some could move into FY2021.*

Based on the above, PET maintains its FY2020 Revenue Forecast* in the range \$50m - \$70m, up some 100% on FY2019. In light of measures to limit the spread of Coronavirus COVID 19, PET will continue to review its forecast, and amend if business conditions change.

- D. PET's announcement titled "AGM Presentation" released on MAP on 25 May 2020 which disclosed on:
- i. slide 9 that "COVID-19 has a significant impact on the world's economy. The economic downturn was inevitable, and PET business in China was also affected"; and
 - ii. slide 34 that anticipated revenue for 2020 would be between \$50 million and \$70 million, broken down by each project's contribution to total revenue (the '**May Forecast**').
- E. PET's announcement titled "Market Update" released on MAP on 16 June 2020 which disclosed that:
- i. Anticipated revenue for 2020 would be between \$30 million and \$40 million (the '**June Forecast**').
 - ii. *"Material changes to forecasts over the weekend prompted this revision."*
 - iii. *"While no projects have been cancelled – and, in our opinion, are unlikely to be affected in size or scope, there are concerns that, in the event of substantial secondary outbreaks, some projects will be delayed in order for governments to deal with more immediate health problems."*

Request for Information

Having regard to the above, ASX asks PET to respond separately to each of the following questions and requests for information:

1. Please outline specifically what the material changes were, and which forecasts are affected.
2. Noting that:
 - a. PET released the June Forecast 16 business days after releasing the May Forecast.
 - b. The June Forecast represents a 20-57% reduction¹ in PET's forecast revenue,please explain in detail what led to the changes reflected in the June Forecast. Please ensure your answer addresses:
 - what specific matters came to the attention of PET;
 - when those matters came to the attention of PET;
 - why PET considered those matters to warrant the material changes referred to in paragraph E.ii; and
 - how PET arrived at the \$30 million to \$40 million guidance.
3. To the extent not already dealt with in PET's answers to questions 1 and 2:
 - a. Have any projects been delayed?
 - b. If the answer to question 3.a is:
 - i. "yes", please identify which projects have been delayed and the expected change in their contribution to total revenue; or
 - ii. "no", please explain the rationale behind the downgrade.

¹ Representing the smallest change (from \$50 million to \$40 million) to largest change (from \$70 million to \$30 million).

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- c. Noting:
- i. the evident impact of the coronavirus pandemic on the global economy in the first half of calendar year 2020;
 - ii. that PET's forecast revenue was consistent across its 3 December 2019, 31 January 2020, 17 February 2020, 26 March 2020 and 25 May 2020 announcements;
 - iii. that the announcement dated 26 March 2020 (see paragraph C), when maintaining its earlier guidance, provided the following particulars:
 - PET anticipated that its China-based operations, accounting for 85% of forecast revenue, would not be materially affected.
 - 6% of PET's forecast revenue, derived from its non-China operations, was from existing projects and customers and expected to be fulfilled that year.
 - 9% of PET's forecast revenue was from "planned" sales to new projects outside China and was likely to be delayed by at least half a year.
 - PET would "continue to review its forecast, and amend if business conditions change" on the basis of "measures to limit the spread of coronavirus".
 - iv. PET released the June Forecast 16 business days after releasing the May Forecast, how has PET concluded that "concerns ... of substantial secondary outbreaks" is a reasonable basis on which to downgrade its revenue forecast by 20-57%?

When and where to send your response

This request is made under Listing Rule 18.7. Your response is required as soon as reasonably possible and, in any event, by no later than 4:00 PM **AEST Thursday, 25 June 2020**.

You should note that if the information requested by this letter is information required to be given to ASX under Listing Rule 3.1 and it does not fall within the exceptions mentioned in Listing Rule 3.1A, PET's obligation is to disclose the information "immediately". This may require the information to be disclosed before the deadline set out in the previous paragraph and may require PET to request a trading halt immediately.

If you wish to request a trading halt, you must tell us:

- the reasons for the trading halt;
- how long you want the trading halt to last;
- the event you expect to happen that will end the trading halt;
- that you are not aware of any reason why the trading halt should not be granted; and
- any other information necessary to inform the market about the trading halt, or that we ask for.

We require the request for a trading halt to be in writing. The trading halt cannot extend past the commencement of normal trading on the second day after the day on which it is granted.

You can find further information about trading halts in Guidance Note 16 *Trading Halts & Voluntary Suspensions*.

ASX reserves the right to release a copy of this letter and your response on MAP under Listing Rule 18.7A. Accordingly, your response should be in a form suitable for release to the market.

Your response should be sent to me by e-mail at ListingsComplianceSydney@asx.com.au. It should not be sent directly to the ASX Market Announcements Office. This is to allow me to review your response to confirm that it is in a form appropriate for release to the market, before it is published on MAP.

Listing Rules 3.1 and 3.1A

In responding to this letter, you should have regard to PET's obligations under Listing Rules 3.1 and 3.1A and also to Guidance Note 8 *Continuous Disclosure: Listing Rules 3.1 – 3.1B*. It should be noted that PET's obligation to disclose information under Listing Rule 3.1 is not confined to, nor is it necessarily satisfied by, answering the questions set out in this letter.

Suspension

If you are unable to respond to this letter by the time specified above ASX will likely suspend trading in PET's securities under Listing Rule 17.3.

Enquiries

If you have any queries or concerns about any of the above, please contact me immediately.

Kind regards

Elvis Onyura
Senior Adviser, Listings Compliance (Sydney)