



Phoslock Water Solutions Ltd.
ABN 88 099 555 290

Phoslock Water Solutions Limited and controlled entities

A.B.N. 88 099 555 290

APPENDIX 4D

HALF YEAR REPORT FOR THE PERIOD ENDED 31 DECEMBER 2017

Previous Corresponding Reporting Period: 31 December 2016

| Results for Announcement to the Market: | | | | A\$'000 |
|--|----|------|----|---------|
| Revenue from Ordinary Activities | Up | 226% | to | 6,196 |
| Earnings before depreciation, tax and interest (EBITDA) | Up | 252% | to | 1,010 |
| Profit from ordinary activities after tax attributable to members (NPAT) | UP | 169% | to | 528 |
| Net Profit for the period attributable to members | UP | 169% | to | 528 |

The company does not propose to pay any dividends for the six months ended 31 December 2017 (2016: Nil).

NTA Backing:

Net tangible asset backing per ordinary security (cents per share):

| | |
|--------------------|------|
| - 31 December 2017 | 2.56 |
| - 31 December 2016 | 0.05 |

Commentary on Results:

Detailed commentary on results contained in attached Interim Financial Statements

(Company Secretary)
Robert Schuitema

Dated: 22 February 2018



**Phoslock Water Solutions Limited and Controlled Entities
A.B.N. 88 099 555 290
INTERIM FINANCIAL REPORT
FOR THE HALF YEAR ENDED 31 DECEMBER 2017**

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Phoslock Water Solutions Limited and Controlled Entities
A.B.N. 88 099 555 290
Interim Financial Report

DIRECTORS' REPORT

Your directors present their report on the Company and its controlled entities ("the Group" or "PWS") for the half year ended 31 December 2017.

Directors

The names of directors in office at anytime during the year or since the end of the half year are:

Mr Laurence Freedman AM
Mr Robert Schuitema
The Hon. Pam Allan (retired on 23 November 2017)
Mr Zhigang Zhang
Ms Brenda Shanahan (appointed on 15 September 2017)

Review of Operations

- * Revenue and Other Income for the 6 months totalled \$6,196,354 – up 226% Half Year on Half Year (HOH)
- * Adverse weather affected two projects, resulting in Sales of approx. \$3m being pushed in the second half of FY17-18
- * EBITDA⁽¹⁾ for the 6 months of \$1,009,669 versus ((\$663,238) for Dec 16 period) – an improvement of \$1.7m HOH

| | 2017 | 2016 |
|-----------------------------|-----------|-----------|
| Profit before tax | 904,322 | (759,626) |
| Less : interest income | (3,744) | (1,356) |
| Add : finance cost | 84,418 | 59,499 |
| depreciation & amortization | 24,673 | 38,245 |
| EBITDA | 1,009,669 | (663,238) |

- * Maiden profit after tax of \$527,868 (after tax provision of \$376,454 in China)
- * Forecast sales⁽²⁾ for FY17-18 of \$21 - \$23m
- * Balance sheet in a strong position - largely debt free with cash on hand of \$7m and debtors and inventories of \$5.9m (2016: cash on hand \$0.4m; debtors and inventories \$1.6m)

2017 was a transformation year for PWS. The catalyst to the transformation has been the strategic agreement with BHZQ Environmental and the setting up of the Phoslock Beijing office with an experienced executive team of water industry professionals. Phoslock Beijing has broadened PWS's business base, which now includes design, engineering, implementation and contract management of water related projects.

A large manufacturing facility in Changxing, China, 150 kilometres inland from Shanghai was completed in August 2017. The project cost came within budget. After an initial commissioning period, the manufacturing facility has consistently produced over 40 tons of Phoslock per day or an annualised rate around 15,000 tons per annum (tpa). The manufacturing facility is wholly owned and will massively increase production of our core product, Phoslock, along with our growing suite of water treatment products. Significant economies of scale provides the Group with a substantial cost saving. Phoslock production is managed to meet current and anticipated demand.

The Company's business mix is rapidly changing. From only selling Phoslock material internationally in FY16-17, the Group is progressing to an estimated mix of 30% international materials, 40% China contracting business and 30% China materials for the current financial year. Revenue for this financial year is currently forecast to increase by over 400% from FY16-17 to \$22 million⁽²⁾.

These dramatic changes have resulted in major additions to the PWS Board and management team; the Group currently have nearly 50 employees in China, with half in our Beijing office and the other half at the Changxing factory. The Changxing factory is highly mechanised resulting in a significant reduction in factory floor workers. The factory has state of the art waste water treatment facilities which not only treats the water but also allows the recovery of our key active ingredient which can be added back into the production process to reduce operating costs. PWS Changxing receives a range of incentives and rebates from the local government as part of the Group's Investment Agreement. A video of the Changxing factory can be seen on www.phoslock.com.au

A large investment is currently being made to our product development facilities in Changxing and building a skilled team and state of the art facilities. The key focus is providing a range of products for black odorous and other types of highly polluted water bodies in China. This comes at a time when "China is working to ensure that over 80 percent of the country's water meets at least the Level III standard by 2020" (Chinese Ministry of Environmental Protection). PWS is already working on black odorous canal projects in China and is tailoring its products to meet the challenges of different projects.

Outside of China, the international materials business had a record 6 months with sales and other revenue of \$2.8m, an increase of 45% HOH. Major projects were undertaken in Canada, Poland, two projects in Brazil, along with a number of smaller projects in the United States, UK, Belgium, Germany and Australia. PWS has ongoing work in a number of countries including Poland, Brazil, Netherlands, Germany, Belgium and Australia. In addition, the pipeline for international materials business is very strong. After 12 years of commercial sales in over 20 countries, over 300 projects, and over 70 peer reviewed technical scientific papers, Phoslock is now regarded internationally as a proven treatment solution to reduce excess phosphorus from water bodies.

Financial Review

The July to December 2017 six months period produced both record Sales and record Cash Receipts from customers for the Company. Revenue and other income for the period of \$6.2 million was an 226% increase over the corresponding six month period. \$3.4m or 55% of revenues came from Chinese projects and 45% from International projects.

Phoslock Beijing formally commenced business on 1 July 2017. Within a couple of months of commencement of operations, PWS was awarded its largest project to date, providing materials and services to a canal project in northern China. Work commenced in September 2017, however very cold weather in northern China from mid November to February 2018 has affected the application of materials to this canal project. Approx \$2.5m of sales were recorded for this project to December 2017 with the balance, \$2.5m of revenue to be taken up into the second half of FY17-18. The Beijing team are currently working on two large engineering projects with a value of approx. \$15m, the first of which is expected to be formally contracted in March 2018 and the second project in the middle of 2018. It is expected that approx. \$8m of sales revenue from these projects will be booked to 30 June 2018⁽²⁾.

Phoslock Water Solutions Limited and Controlled Entities
A.B.N. 88 099 555 290
Interim Financial Report

DIRECTORS' REPORT (continued)
Financial Review (continued)

The Net Profit before Tax for the 6 months of the consolidated entity was \$904,322 (2016: loss of \$759,626). The Group is taking up a provision of \$376,454 for tax for our Chinese businesses. Net Profit after Tax was \$527,868 (2016: loss of \$759,626). Earnings before interest, tax, depreciation and amortisation (EBITDA) for the 6 months was \$1,009,669 (HY2016: negative \$663,238). This is a \$1.7m improvement in operating performance for the 6 month HoH period. The Group is currently looking at a range of options to manage its group tax liability.

Expenses (excluding depreciation, amortization and finance) for the 6 months increased by 81% to \$2,746,891 (HY2016:\$1,514,330). The main changes were higher employee, marketing and administration costs. The expenses relating to the China operations accounted for most of the increase in employee, marketing and administration costs. The investment in the Chinese business has already generated \$3.4m of sales in the six months to 31 December 2017, and forecast to increase significantly in future periods⁽²⁾.

The Changxing factory primarily manufactures water treatment products for PWS international and Phoslock Beijing. Phoslock Changxing produced approx. 2,000 tons of Phoslock during the December 2017 six month period.

The Company lodged patent applications covering 50 countries in 2013 for the core Phoslock technology, which would extend patent coverage until 2033. The patent applications are currently in examination stage. During the first six months of FY2017-18, the Company spent significant management time and \$39,821 on approval of the new patents in various countries. Significant progress was made during this period with the various patent offices on getting the Phoslock patent approved in various countries.

In the December 2017 half year, the Group raised \$8.0m (net of expenses) via a Share Placement and very successful Share Purchase Plan (SPP), with 24% of shareholders taking up shares in the SPP. In addition, \$1.5m was raised through the exercise of options, including \$1.3m from PWS employees. The majority of PWS employees retained as many shares as possible from the option exercise showing their support for the future potential of the Group. As at 31 December 2017 the Group has Net Assets of \$12.3m (30 June 2017:\$1.9m); Cash of \$7m (June 2017: \$1.2m); Debtors of \$4.3m (June 2017: \$1.2m) and Inventories of \$1.5m (June 2017: \$0.9m). Since 31 December 2017, the Company has received over A\$1.5m in debtor payments including A\$1.1m from Chinese debtors.

The Group liabilities as at 31 December 2017 were \$2.3m (June 2017: \$2.6m) made up of Trade Creditors \$1.3m (June 2017: \$0.4m); Tax Payable \$0.4m (June 2017: nil) External Loans and financial liabilities nil (June 2017: \$1.5m); employee provisions \$0.3m (June 2017: \$0.3m) and loan from European JV partner \$0.3m (June 2017: \$0.3m).

The Company had 67.5m options outstanding as at 31 December 2017 which if exercised over the next 2 years could raise \$7m. These include 65m Performance Options exercisable when the vesting conditions are met at 10.5 cents per option. Once the Performance Options have met the vesting conditions, the holders can make payment to PWS for the option premium and convert these from options to fully paid PHK shares.

The Group improved Balance Sheet showing Net Assets of \$12.3m, including \$7m of cash, has significantly improved the Group's operating flexibility. The Group has sufficient financial resources to expand its existing businesses of as well as the ability to look at potential add on businesses in the water industry segment. The outlook for the Group looks very promising in both China and its International business⁽²⁾

Lead Auditor's Independence Declaration

The lead auditor's independence declaration is set out on page 5 and forms part of the directors' report for the six months ended 31 December 2017.

Signed in accordance with a resolution of the Board of Directors of Phoslock Water Solutions Limited and Controlled Entities.



Mr Robert Schuitema
Managing Director

Dated at Sydney, 22nd February 2018

⁽¹⁾ EBITDA = Earnings Before Interest, Taxation, Depreciation and Amortization

⁽²⁾ The Directors' Report contains forward-looking statements. Forward-looking statements are not guarantees or predictions of future performance, and involve known and unknown risks, uncertainties and other factors, many of which are beyond our control, and which may cause actual results to differ materially from those expressed in the statements contained in this report.



Lead Auditor's Independence Declaration under Section 307C of the Corporations Act 2001

To the Directors of Phoslock Water Solutions Limited

I declare that, to the best of my knowledge and belief, in relation to the review of Phoslock Water Solutions Limited for the half-year ended 31 December 2017 there have been:

- i. no contraventions of the auditor independence requirements as set out in the *Corporations Act 2001* in relation to the review; and
- ii. no contraventions of any applicable code of professional conduct in relation to the review.

KPMG

KPMG

Sarah Cain

Partner

Sydney

22 February 2018

Phoslock Water Solutions Limited and Controlled Entities
A.B.N. 88 099 555 290
INTERIM FINANCIAL REPORT
CONSOLIDATED STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME
FOR THE HALF YEAR ENDED 31 DECEMBER 2017

| | NOTE | Half Year Ended 31.12.2017 \$ | Half Year Ended 31.12.2016 \$ |
|--|------|-------------------------------------|-------------------------------------|
| Sales Revenue | 2 | 6,004,822 | 1,702,511 |
| Cost of sales | | <u>(2,436,048)</u> | <u>(1,046,704)</u> |
| Gross profit | | 3,568,774 | 655,807 |
| Other income | 2 | 191,532 | 196,642 |
| Distribution expenses | | (219,158) | (17,673) |
| Marketing expenses | | (114,407) | (140,593) |
| Occupancy expenses | | (148,243) | (50,234) |
| Administrative expenses | | (856,244) | (479,795) |
| Employee benefit expenses | 3 | (1,280,457) | (814,291) |
| Depreciation and amortisation | | <u>(24,673)</u> | <u>(38,245)</u> |
| Operating Profit | | 1,117,124 | (688,382) |
| Finance costs | 3 | (84,418) | (59,499) |
| Foreign exchange losses | | (14,725) | (11,745) |
| Options expenses | | <u>(113,659)</u> | <u>-</u> |
| PROFIT / (LOSS) BEFORE INCOME TAX | | 904,322 | (759,626) |
| Income tax expense | | <u>(376,454)</u> | <u>-</u> |
| PROFIT / (LOSS) FOR THE PERIOD | | 527,868 | (759,626) |
| OTHER COMPREHENSIVE INCOME | | | |
| Exchange differences arising on translation of foreign controlled entities | | <u>131,186</u> | <u>35,753</u> |
| TOTAL COMPREHENSIVE INCOME / (LOSS) FOR THE PERIOD | | <u>659,054</u> | <u>(723,873)</u> |
| Profit / (Loss) for the period attributable to: | | | |
| - Owners of parent entity | | 470,767 | (760,122) |
| - Non-controlling interest | | <u>57,101</u> | <u>496</u> |
| Total profit/(loss) for the period | | <u>527,868</u> | <u>(759,626)</u> |
| Total comprehensive income/(loss) for the period attributable to: | | | |
| - Owners of parent entity | | 601,953 | (724,369) |
| - Non-controlling interest | | <u>57,101</u> | <u>496</u> |
| Total comprehensive income/(loss) for the period | | <u>659,054</u> | <u>(723,873)</u> |
| Earnings per share | | | |
| Basic earnings per share (cents per share) | | 0.12 | (0.21) |
| Diluted earnings per share (cents per share) | | 0.11 | (0.21) |

The accompanying notes form part of these financial statements

Phoslock Water Solutions Limited and Controlled Entities
A.B.N. 88 099 555 290
INTERIM FINANCIAL REPORT
CONSOLIDATED STATEMENT OF FINANCIAL POSITION

AS AT 31 DECEMBER 2017

| | NOTE | 31.12.2017 | 30.06.2017 |
|--|------|-------------------|------------------|
| | | \$ | \$ |
| CURRENT ASSETS | | | |
| Cash and cash equivalents | | 7,035,983 | 1,234,243 |
| Trade and other receivables | | 4,344,777 | 1,172,751 |
| Inventories | | 1,515,063 | 897,336 |
| Other assets | | 424,873 | 141,601 |
| TOTAL CURRENT ASSETS | | <u>13,320,696</u> | <u>3,445,931</u> |
| NON-CURRENT ASSETS | | | |
| Financial assets | | 31,258 | 25,000 |
| Plant and equipment | | 1,253,653 | 1,038,093 |
| TOTAL NON-CURRENT ASSETS | | <u>1,284,911</u> | <u>1,063,093</u> |
| TOTAL ASSETS | | <u>14,605,607</u> | <u>4,509,024</u> |
| CURRENT LIABILITIES | | | |
| Trade and other payables | | 1,277,838 | 330,443 |
| Other liability | | - | 89,830 |
| Tax payable | | 382,945 | - |
| Financial liabilities | 4 | 301,191 | 1,792,241 |
| Short term provisions | | 353,416 | 352,134 |
| TOTAL CURRENT LIABILITIES | | <u>2,315,390</u> | <u>2,564,648</u> |
| NON-CURRENT LIABILITIES | | | |
| Long term provisions | | 11,664 | 8,707 |
| TOTAL NON-CURRENT LIABILITIES | | <u>11,664</u> | <u>8,707</u> |
| TOTAL LIABILITIES | | <u>2,327,054</u> | <u>2,573,355</u> |
| NET ASSETS | | <u>12,278,553</u> | <u>1,935,669</u> |
| EQUITY | | | |
| Issued capital | 6 | 51,121,283 | 41,551,112 |
| Reserves | | 650,741 | 405,896 |
| Accumulated losses | | (39,350,936) | (39,821,703) |
| Total equity attributable to owners of the Company | | 12,421,088 | 2,135,305 |
| Non-controlling interest | | (142,535) | (199,636) |
| TOTAL EQUITY | | <u>12,278,553</u> | <u>1,935,669</u> |

The accompanying notes form part of these financial statements

Phoslock Water Solutions Limited and Controlled Entities
A.B.N. 88 099 555 290
INTERIM FINANCIAL REPORT
CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
FOR THE HALF YEAR ENDED 31 DECEMBER 2017

| | Issued capital \$ | Option Reserve \$ | Foreign currency translation reserves \$ | Non- controlling interest \$ | Accumulated losses \$ | Equity \$ |
|---|----------------------|-------------------------|--|---------------------------------------|-----------------------------|-------------------|
| Balance at 1 July 2016 | 38,465,112 | 277,391 | 133,950 | (244,318) | (37,983,793) | 648,342 |
| Total comprehensive income/(loss) for the period | | | | | | |
| Profit / (Loss) for the period | - | - | - | 496 | (760,122) | (759,626) |
| Other comprehensive income | - | - | 35,753 | - | - | 35,753 |
| Total comprehensive income/(loss) for the period | - | - | 35,753 | 496 | (760,122) | (723,873) |
| Transactions with owners in their capacity as owners | | | | | | |
| Shares issued during the period | 265,000 | - | - | - | - | 265,000 |
| Reserves | - | - | 150 | - | - | 150 |
| Total transactions with owners in their capacity as owners | 265,000 | - | 150 | - | - | 265,150 |
| Balance at 31 December 2016 | 38,730,112 | 277,391 | 169,853 | (243,822) | (38,743,915) | 189,619 |
| Balance at 1 July 2017 | 41,551,112 | 283,814 | 122,082 | (199,636) | (39,821,703) | 1,935,669 |
| Total comprehensive income/(loss) for the period | | | | | | |
| Profit / (Loss) for the period | - | - | - | 57,101 | 470,767 | 527,868 |
| Other comprehensive income | - | - | 131,186 | - | - | 131,186 |
| Total comprehensive income for the period | - | - | 131,186 | 57,101 | 470,767 | 659,054 |
| Transactions with owners in their capacity as owners | | | | | | |
| Shares issued during the period | 9,570,171 | - | - | - | - | 9,570,171 |
| Share based payments | - | 113,659 | - | - | - | 113,659 |
| Total transactions with owners in their capacity as owners | 9,570,171 | 113,659 | - | - | - | 9,683,830 |
| Balance at 31 December 2017 | 51,121,283 | 397,473 | 253,268 | (142,535) | (39,350,936) | 12,278,553 |

The accompanying notes form part of these financial statements

Phoslock Water Solutions Limited and Controlled Entities
A.B.N. 88 099 555 290
INTERIM FINANCIAL REPORT
CONSOLIDATED STATEMENT OF CASH FLOWS
FOR THE HALF YEAR ENDED 31 DECEMBER 2017

| | Half Year Ended | Half Year Ended |
|---|------------------------|------------------------|
| | 31.12.2017 | 31.12.2016 |
| | \$ | \$ |
| CASH FLOWS FROM OPERATING ACTIVITIES | | |
| Receipts from customers | 3,096,639 | 1,353,433 |
| Receipt from government grants | 361,980 | 373,313 |
| Payments to suppliers and employees | (5,400,323) | (3,203,214) |
| Interest received | 3,744 | 948 |
| Finance costs | (84,418) | (56,792) |
| Intellectual property cost | (39,821) | (44,434) |
| | <hr/> | <hr/> |
| NET CASH USED IN OPERATING ACTIVITIES | (2,062,199) | (1,576,746) |
| CASH FLOWS FROM INVESTING ACTIVITIES | | |
| Purchase of property, plant and equipment | (200,412) | (32,983) |
| | <hr/> | <hr/> |
| NET CASH USED IN INVESTING ACTIVITIES | (200,412) | (32,983) |
| CASH FLOWS FROM FINANCING ACTIVITIES | | |
| Proceeds from share issue | 8,139,609 | 265,000 |
| Proceeds from exercise of share options | 1,595,000 | - |
| Transaction costs related to share issue | (184,938) | - |
| Repayment of borrowings | (1,500,000) | (280,000) |
| Proceeds from borrowings | - | 690,000 |
| | <hr/> | <hr/> |
| NET CASH FROM FINANCING ACTIVITIES | 8,049,671 | 675,000 |
| Net increase/(decrease) in cash and cash equivalents held | 5,787,060 | (934,729) |
| Cash and cash equivalents at the beginning of the half year | 1,234,243 | 1,306,865 |
| Effect of exchange rates on cash holdings in foreign currencies | 14,680 | (18,446) |
| | <hr/> | <hr/> |
| CASH AND CASH EQUIVALENTS AT THE END OF THE PERIOD | 7,035,983 | 353,690 |

The accompanying notes form part of these financial statements

Phoslock Water Solutions Limited and Controlled Entities

A.B.N. 88 099 555 290

INTERIM FINANCIAL REPORT

NOTES TO THE CONSOLIDATED INTERIM FINANCIAL STATEMENTS
FOR THE HALF YEAR ENDED 31 DECEMBER 2017

NOTE 1 BASIS OF PREPARATION

Reporting entity

Phoslock Water Solutions Limited (the "Company") is a company domiciled in Australia. These condensed consolidated interim financial statements ("interim financial statements") as at and for the six months ended 31 December 2017 comprise the Company and its subsidiaries (together referred to as the "Group"). The Group primarily is involved in the sale and marketing of patented product "Phoslock" and providing design & engineering solutions for environmental projects in China. The consolidated annual financial report of the Group as at and for the year ended 30 June 2017 is available upon request from the Company's registered office at Suite 403, 25 Lime Street, Sydney, New South Wales, Australia or on the Company's website www.phoslock.com.au.

Statement of compliance

These interim financial statements are general purpose financial statements prepared in accordance with AASB 134 Interim Financial Reporting and the Corporations Act 2001, and with IAS 34 Interim Financial Reporting.

These interim financial statements do not include all of the information required for a complete set of annual financial statements, and should be read in conjunction with the consolidated annual financial statements of the Group as at and for the year ended 30 June 2017. However, selected explanatory notes are included to explain events and transactions that are significant to an understanding of the changes in the Group's financial position and performance since the last annual consolidated financial statements as at and for the year ended 30 June 2017.

These interim financial statements were approved by the Board of Directors on 22 February 2018.

New Accounting Standards and Interpretation

The Group has adopted all of the new and revised standards issued by the AASB that are relevant to its operations and effective for the period. Details of the impact of adoption of these new AASB's, where applicable, are set out in the individual accounting policy notes.

Certain new accounting standards and interpretations have been published by the AASB that are not mandatory for this reporting period and have not been adopted early but the Group. The Group does not expect that the adoption of the Standards will have a material impact on the financial statements of the Group in future periods except for AASB 16 Leases and AASB 15 Revenue from contracts with customers. The Group's assessment of the impact of these new standards and interpretations is set out below:

AASB 16 removes the lease classification test for lessees and requires all the leases (including operating leases) to be brought onto the balance sheet.

AASB 16 is effective for annual reporting periods beginning on or after 1 January 2019, with early adoption permitted where AASB 15 Revenue from Contracts with Customers is adopted at the same time.

AASB 15 establishes a comprehensive framework for determining whether, how much and when revenue is recognised. It replaces existing revenue recognition guidance including AASB 118 Revenue. AASB 15 is effective for annual reporting periods beginning on or after 1 January 2018, with early adoption permitted.

The Group is still assessing the potential impact on its financial statements resulting from the application of AASB 16 and AASB 15. Beyond the information above, it is not practicable to provide a reasonable estimate of the effect of AASB 16 and IFRS 15 until a detailed review has been completed.

Financial Instruments

The Group's financial instruments consist of cash and cash equivalents, trade and other receivables, refundable security deposits, trade and other payables, related party short-term loan and an unsecured subordinated non-interest bearing loan from Bentophos GmbH (which holds a non-controlling interest in Phoslock Europe GmbH, Zug). These financial instruments are measured at fair value initially, then subsequently at amortised cost, less any impairment. The carrying amount of the financial assets and liabilities approximate their fair value.

| NOTE 2 REVENUE | 31.12.2017 | 31.12.2016 |
|------------------------------------|-------------------|-------------------|
| | \$ | \$ |
| Sales Revenue | | |
| - sale of goods | 5,824,166 | 1,697,857 |
| - provision of services | 180,656 | 4,654 |
| | <u>6,004,822</u> | <u>1,702,511</u> |
| Other Income | | |
| - interest received | 3,744 | 1,356 |
| - research & development grants | 161,980 | 195,286 |
| - other income | 25,808 | - |
| | <u>191,532</u> | <u>196,642</u> |
| Total Sales Revenue & Other Income | <u>6,196,354</u> | <u>1,899,153</u> |

NOTE 3 EXPENSES FOR THE PERIOD

Expenses for the period includes the following specific items:

| | | |
|--|-------------|-----------|
| Employee benefit expenses | (1,280,457) | (814,291) |
| No. of employees at end of reporting period | 59 | 18 |

Employee benefit expenses include salaries to employees, director fees, superannuation, annual and long service leave costs for the period, cost of any options or shares issued to employees, fringe benefit taxes and workers compensation.

Phoslock Water Solutions Limited and Controlled Entities

A.B.N. 88 099 555 290

INTERIM FINANCIAL REPORT

NOTES TO THE CONSOLIDATED INTERIM FINANCIAL STATEMENTS
FOR THE HALF YEAR ENDED 31 DECEMBER 2017

NOTE 3 EXPENSES FOR THE PERIOD (continued)

Finance costs

| | | |
|---|-----------------|-----------------|
| - Convertible Notes issued to related parties | - | (49,253) |
| - Interest on loans provided by related parties | (84,161) | (7,729) |
| - other interest & fees | (257) | (2,517) |
| Total Finance Cost | <u>(84,418)</u> | <u>(59,499)</u> |

Finance costs include all interest, derivative, and upfront expenses for loans and bank charges.

| | 31.12.2017 | 30.06.2017 |
|--|----------------|------------------|
| | \$ | \$ |
| - Related party borrowings - loan (unsecured) | - | 1,000,000 |
| - Related party borrowings - debtor factoring (secured) | - | 500,000 |
| - Related party subordinated loan (unsecured, interest free) | 301,191 | 292,241 |
| | <u>301,191</u> | <u>1,792,241</u> |

NOTE 5 SEGMENT REPORTING

Segment Information

Identification of reportable segments

The Group has identified its operating segments based on the internal reports that are reviewed and used by the Board of Directors (chief operating decision makers) in assessing performance and determining the allocation of resources.

The group is managed primarily on the basis of geographical areas – Australia/NZ, Europe/UK, North & South America, and China/Asia. The Group's operations (except China) inherently have similar profiles and performance assessment criteria. China operations include design, engineering and project implementation.

Types of products and services by segment

The Group has three business segments:

- (1) Sale of Phoslock granules and application services and lake restoration consulting services in Australia/NZ, Europe/UK and North & South America.
- (2) Sale of Phoslock granules and other water treatment materials, and application services in China/Asia.
- (3) Design, engineering & project implementation services for canal, river, lake & wetland projects in China/Asia.

Basis of accounting for purposes of reporting by operating segments

Accounting policies adopted

Unless stated otherwise, all amounts reported to the Board of Directors as the chief operating decision makers with respect to operating segments are determined in accordance with accounting policies that are consistent to those adopted in the annual financial statements of the Group.

Inter-segment transactions

An internally determined transfer price is set for all inter-entity sales. This price is based on what would be realised in the event the sale was made to an external party at arm's-length. All such transactions are eliminated on consolidation for the Group's financial statements.

Corporate charges are allocated to reporting segments based on the segments' overall proportion of revenue generation within the Group. The Board of Directors believes this is representative of likely consumption of head office expenditure that should be used in assessing segment performance and cost recoveries. Inter-segment loans payable and receivable are initially recognised at the consideration received net of transaction costs and then revalued to the exchange rate used at the end of the current accounting period.

Segment assets

Where an asset is used across multiple segments, the asset is allocated to the segment that receives the majority of economic value from the asset. In the majority of instances, segment assets are clearly identifiable on the basis of their nature and physical location.

Unless indicated otherwise in the segment assets note and investments in financial assets have not been allocated to operating segments.

Segment liabilities

Liabilities are allocated to segments where there is direct nexus between the incurrence of the liability and the operations of the segment. Borrowings and tax liabilities are generally considered to relate to the Group as a whole and are not allocated. Segment liabilities include trade and other payables and certain direct borrowings.

Unallocated items

The following items of revenue, expense, assets and liabilities are not allocated to operating segments as they are not considered part of the core operations of any segment:

- income tax expense;
- corporate income and finance costs
- corporate charges
- option expenses

Phoslock Water Solutions Limited and Controlled Entities

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INTERIM FINANCIAL REPORT

NOTES TO THE CONSOLIDATED INTERIM FINANCIAL STATEMENTS
FOR THE HALF YEAR ENDED 31 DECEMBER 2017

(i) Segment performance

| | Australia/NZ | Europe/UK | N&S America | China/Asia | Total | Eliminations | Total |
|---|-----------------|-----------------|------------------|------------------|------------------|--------------------|------------------|
| Six months ended 31 December 2017 | | | | | | | |
| Revenue | | | | | | | |
| External sales | 218,719 | 623,842 | 1,744,777 | 3,417,484 | 6,004,822 | - | 6,004,822 |
| Inter-segment sales | 446,161 | 57,129 | - | 1,008,196 | 1,511,486 | (1,511,486) | - |
| Other revenue | 162,237 | - | - | 25,551 | 187,788 | - | 187,788 |
| Total segment revenue | 827,117 | 680,971 | 1,744,777 | 4,451,231 | 7,704,096 | (1,511,486) | 6,192,610 |
| <i>Reconciliation of segment revenue to group revenue</i> | | | | | | | |
| Unallocated interest income | | | | | | | 3,744 |
| Total group revenue | | | | | | | <u>6,196,354</u> |
| Segment profit / (loss) before tax | 45,117 | 143,434 | 200,000 | 1,298,603 | 1,687,154 | - | 1,687,154 |
| <i>Reconciliation of segment result to group net profit/(loss) before tax</i> | | | | | | | |
| Amounts not included in segment result but reviewed by the Board | | | | | | | |
| - Depreciation and amortisation | (14,595) | - | - | (10,078) | (24,673) | - | (24,673) |
| Unallocated items: | | | | | | | |
| - Corporate charges | | | | | | | (560,080) |
| - Option expense | | | | | | | (113,659) |
| - Finance costs | | | | | | | (84,418) |
| Profit before income tax from continuing operations | | | | | | | <u>904,324</u> |
| Six months ended 31 December 2016 | | | | | | | |
| Revenue | | | | | | | |
| External sales | 27,001 | 35,877 | 1,520,110 | 119,523 | 1,702,511 | - | 1,702,511 |
| Inter-segment sales | - | 15,257 | - | - | 15,257 | (15,257) | - |
| Other revenue | 195,286 | - | - | - | 195,286 | - | 195,286 |
| Total segment revenue | 222,287 | 51,134 | 1,520,110 | 119,523 | 1,913,054 | (15,257) | 1,897,797 |
| <i>Reconciliation of segment revenue to group revenue</i> | | | | | | | |
| Unallocated interest income | | | | | | | 1,356 |
| Total group revenue | | | | | | | <u>1,899,153</u> |
| Segment loss before tax | (28,126) | (10,405) | 162,309 | (305,863) | (182,085) | - | (182,085) |
| <i>Reconciliation of segment result to group net profit/(loss) before tax</i> | | | | | | | |
| Amounts not included in segment result but reviewed by the Board | | | | | | | |
| - Depreciation and amortisation | (38,245) | - | - | - | (38,245) | - | (38,245) |
| Unallocated items: | | | | | | | |
| - Corporate charges | | | | | | | (479,797) |
| - Finance costs | | | | | | | (59,499) |
| Loss before income tax from continuing operations | | | | | | | <u>(759,626)</u> |

| | Australia/NZ | Europe/UK | N&S America | China/Asia | Total | Eliminations | Total |
|----------------------------------|--------------|-----------|-------------|------------|------------|--------------|-------------------|
| (ii) Segment assets | | | | | | | |
| 31 December 2017 | | | | | | | |
| Segment assets | 13,149,777 | 252,992 | - | 10,184,112 | 23,586,881 | (8,981,274) | 14,605,607 |
| Total group assets | | | | | | | <u>14,605,607</u> |
| 30 June 2017 | | | | | | | |
| Segment assets | 5,724,549 | 251,459 | - | 2,423,493 | 8,399,501 | (3,890,476) | 4,509,025 |
| Total group assets | | | | | | | <u>4,509,025</u> |
| (iii) Segment liabilities | | | | | | | |
| 31 December 2017 | | | | | | | |
| Segment liabilities | 517,398 | 991,850 | - | 1,542,504 | 3,051,752 | (724,699) | 2,327,053 |
| Total group liabilities | | | | | | | <u>2,327,053</u> |
| 30 June 2017 | | | | | | | |
| Segment liabilities | 2,255,608 | 329,356 | - | 11,167 | 2,596,131 | (22,776) | 2,573,355 |
| Total group liabilities | | | | | | | <u>2,573,355</u> |
| (iv) Major customers | | | | | | | |

The Group has a number of customers to which it provides both products and services. The Group's largest external customer accounts for 41% of external revenue (2016:77%)

Phoslock Water Solutions Limited and Controlled Entities

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INTERIM FINANCIAL REPORT

NOTES TO THE CONSOLIDATED INTERIM FINANCIAL STATEMENTS
FOR THE HALF YEAR ENDED 31 DECEMBER 2017

NOTE 6 SHARE CAPITAL

| | 31.12.2017 | | 30.06.2017 | |
|--|-------------|------------|-------------|------------|
| | No. | \$ | No. | \$ |
| At the beginning of the period | 413,084,403 | 41,551,112 | 362,953,968 | 38,465,112 |
| Contributions and distributions during the period | | | | |
| - 18 July, 2016 - conversion of options | - | - | 5,000,000 | 265,000 |
| - 9 May, 2017 - conversion of options | - | - | 1,000,000 | 71,000 |
| - 15 May, 2017 - issue of shares under a Placement | - | - | 15,000,000 | 1,050,000 |
| - 31 May, 2017 - issue of shares under a Placement | - | - | 15,000,000 | 1,050,000 |
| - 31 May, 2017 - shares issued under Conversion of \$0.65m Convertible Notes | - | - | 14,130,435 | 650,000 |
| - Option Exercise (July 2017) | 1,000,000 | 71,000 | - | - |
| - Option Exercise (August 2017) | 5,000,000 | 300,000 | - | - |
| - Employee Option Exercise (July-Sept 2017) | 13,600,000 | 1,224,000 | - | - |
| - Placement (Sept 2017) | 22,960,071 | 4,018,012 | - | - |
| - Share Purchase Plan (October 2017) | 20,169,327 | 3,529,598 | - | - |
| - Placement (Dec 2017) | 3,500,000 | 612,500 | - | - |
| Transaction cost arising from Placements | - | (184,939) | - | - |
| Balance at the end of the period | 479,313,801 | 51,121,283 | 413,084,403 | 41,551,112 |

Ordinary shares participate in dividends and the proceeds on winding up of the parent entity in proportion to the number of shares held.

At shareholder meetings each ordinary share is entitled to one vote when a poll is called, otherwise each shareholder has one vote on a show of hands.

OPTIONS OUTSTANDING

| | 31.12.2017 | | 30.06.2017 | |
|--|--------------|---------------------------------|-------------|---------------------------------|
| | No. | Weighted Average Exercise Price | No. | Weighted Average Exercise Price |
| Options balance at the beginning of the period | 87,100,000 | 0.100 | 28,100,000 | 0.078 |
| Options issued during the period | - | - | 65,000,000 | 0.082 |
| Options exercised during the period | (19,600,000) | 0.081 | (6,000,000) | 0.059 |
| Options where vesting conditions not met | - | - | - | - |
| Options balance at the end of the period | 67,500,000 | 0.104 | 87,100,000 | 0.100 |

All options are unlisted.

During the period, 19.6 million options were exercised raising \$1,595,000.

NOTE 7 COMMITMENTS AND CONTINGENT LIABILITIES

The Group has three non-cancellable operating lease commitments with future rental payments and insurance funding of \$673,850 (30 June 2017 \$711,496). There has been no significant contingent liabilities since the last annual reporting date to 31 December, 2017.

NOTE 8 EVENTS SUBSEQUENT TO THE REPORTING DATE

There are no material events subsequent to 31 December, 2017.

NOTE 9 DIVIDENDS PAID OR PAYABLE

No dividends have been paid or declared during the period (2016: \$nil).

NOTE 10 RELATED PARTY TRANSACTIONS

| | 31.12.2017 | 31.12.2016 |
|---|------------|------------|
| | \$ | \$ |
| | 6 months | 6 months |
| Transaction with related parties: | | |
| (a) Relatives of Specified Executives | | |
| Services provided on a normal commercial basis by parties related to specified executives | | |
| Margaret Schuitema – part time employment (1)) | 37,976 | 34,615 |
| Yolanda Winks – part time employment (2) | 19,039 | 17,308 |
| Ben Schuitema – part time employment (1) | 3,256 | 11,385 |
| Martin Schuitema – part time employment (1) | 8,910 | 16,935 |
| (b) Transactions with related parties | | |
| Link Traders (Aust) Pty Ltd – rental costs for Sydney Office (3) | 50,229 | 49,390 |
| Link Traders (Aust) Pty Ltd – interest on loans (3) (6) | 84,161 | 55,068 |
| Sail Ahead Pty Ltd – interest on loans (4) (6) | - | 1,825 |
| Wentworth Place Group Ltd - investor relations (7) | 42,000 | 24,000 |
| Contribution to self-managed superannuation funds managed by related parties (3) (4) | 24,862 | 33,856 |
| (c) Transactions with other related parties | | |
| BHZQ Environmental - sale of goods & services (8) | 2,425,963 | - |
| Bentophos GmbH - purchase of goods & services (9) | 28,330 | 2,947 |

Phoslock Water Solutions Limited and Controlled Entities

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INTERIM FINANCIAL REPORT

NOTES TO THE CONSOLIDATED INTERIM FINANCIAL STATEMENTS
FOR THE HALF YEAR ENDED 31 DECEMBER 2017

| NOTE 10 RELATED PARTY TRANSACTIONS (continued) | 31.12.2017 | 31.12.2016 |
|--|---------------|------------|
| | \$ | \$ |
| | 6 months | 6 months |
| (d) Balances with related parties | | |
| Link Traders (Aust) Pty Ltd – Convertible Notes (3) (5) | - | 650,000 |
| Link Traders (Aust) Pty Ltd – loan to Phoslock Pty Ltd (3) | - | 400,000 |
| Sail Ahead Pty Ltd – loan to Phoslock Pty Ltd (4) | - | 10,000 |
| Bentophos GmbH - subordinated loan to Phoslock Europe GmbH (9) | 301,191 | 286,218 |
| Bentophos GMBH - creditor balance (9) | 18,991 | - |
| BHZQ Environmental - debtor balance net of VAT (8) | (A) 2,031,264 | - |

(1) related party of Robert Schuitema

(2) related party of Andrew Winks

(3) Laurence Freedman is a director of this company

(4) Robert Schuitema is a director of this company

(5) Convertible Notes issued by Phoslock Water Solutions Ltd converted on 30 June, 2017; interest rate – 15%

(6) interest paid on loans, debt factoring to Phoslock Pty Ltd (interest rate 15-18%) and Convertible Notes to Phoslock Water Solutions Ltd (interest rate 15%)

(7) related party by of Laurence Freedman

(8) Zhigang Zhang is a senior executive of BHZQ Environmental

(9) Bentophos GmbH holds 40% interest in subsidiary Phoslock Europe GmbH.

(A) BHZQ Environmental debtor is for goods & services provided in November & December 2017 with payment terms of 120 days. As of 22 February 2018, the BHZQ debtor balance was approx. \$1.5m with approx. \$0.5m received since 31 December 2017



Phoslock Water Solutions Limited and Controlled Entities

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DIRECTORS' DECLARATION

The Directors of Phoslock Water Solutions Limited and Controlled Entities declare that:

- 1 The financial statements and notes set out on pages 6 to 14 are in accordance with the *Corporations Act 2001*; including:
 - (a) complying with Australian Accounting Standard *AASB 134: Interim Financial Reporting and the Corporations Regulations*
 - (b) giving a true and fair view of the Group's financial position as at 31 December 2017 and its performance for the half-year
- 2 In the directors opinion there are reasonable grounds to believe that the company will be able to pay its debts as and when they become become due and payable.

This declaration is made in accordance with a resolution of the Board of Directors of Phoslock Water Solutions Limited and Controlled Entities.

On behalf of the directors

A handwritten signature in black ink, appearing to read "R. Schuitema", is written over a horizontal line.

Robert Schuitema
Director

Dated this 22nd day of February 2018



Independent Auditor's Review Report

To the shareholders of Phoslock Water Solutions Limited

Report on the Interim Financial Report

Conclusion

We have reviewed the accompanying **Interim Financial Report** of Phoslock Water Solutions Limited.

Based on our review, which is not an audit, we have not become aware of any matter that makes us believe that the Interim Financial Report of Phoslock Water Solutions Limited is not in accordance with the *Corporations Act 2001*, including:

- giving a true and fair view of the **Group's** financial position as at 31 December 2017 and of its performance for the half-year ended on that date; and
- complying with *Australian Accounting Standard AASB 134 Interim Financial Reporting* and the *Corporations Regulations 2001*.

The **Interim Financial Report** comprises:

- Consolidated statement of financial position as at 31 December 2017
- Consolidated statement of profit or loss and other comprehensive income, Consolidated statement of changes in equity and Consolidated statement of cash flows for the half-year ended on that date
- Note 1 comprising a summary of significant accounting policies and other explanatory information
- The Directors' Declaration.

The **Group** comprises Phoslock Water Solutions Limited (the Company) and the entities it controlled at the half year's end or from time to time during the half-year.

Responsibilities of the Directors for the Interim Financial Report

The Directors of the Company are responsible for:

- the preparation of the half-year Financial Report that gives a true and fair view in accordance with *Australian Accounting Standards* and the *Corporations Act 2001*
- for such internal control as the Directors determine is necessary to enable the preparation of the Interim Financial Report that is free from material misstatement, whether due to fraud or error.



Auditor's responsibility for the review of the Interim Financial Report

Our responsibility is to express a conclusion on the Interim Financial Report based on our review. We conducted our review in accordance with *Auditing Standard on Review Engagements ASRE 2410 Review of a Financial Report Performed by the Independent Auditor of the Entity*, in order to state whether, on the basis of the procedures described, we have become aware of any matter that makes us believe that the Interim Financial Report is not in accordance with the *Corporations Act 2001* including: giving a true and fair view of the Group's financial position as at 31 December 2017 and its performance for the half-year ended on that date; and complying with *Australian Accounting Standard AASB 134 Interim Financial Reporting* and the *Corporations Regulations 2001*. As auditor of Phoslock Water Solutions Limited, *ASRE 2410* requires that we comply with the ethical requirements relevant to the audit of the annual financial report.

A review of an Interim Financial Report consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with *Australian Auditing Standards* and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

In conducting our review, we have complied with the independence requirements of the *Corporations Act 2001*.

KPMG

Sarah Cain

Partner

Sydney

22 February 2018