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(Incorporated in the Cayman Islands with limited liability)
(Stock Code: 1129)

ANNOUNCEMENT OF UNAUDITED INTERIM RESULTS FOR THE SIX MONTHS ENDED 30 JUNE 2011

The Board of Directors (the “Board”) of China Water Industry Group Limited (the “Company”) is pleased to announce the unaudited condensed consolidated financial results of the Company and its subsidiary (collectively referred to as the “Group”) for the six months ended 30 June 2011 (the “Interim Period”), together with comparative figures for the corresponding period in 2010. These interim financial statements have not been audited but have been reviewed by the Company’s Audit Committee.

CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

For the six months ended 30 June 2011

		Six months ended 30 June	
	<i>Notes</i>	2011	2010
		HK\$’000	HK\$’000
		(Unaudited)	(Unaudited)
			(Restated)
Continuing operation			
Revenue	4	106,163	82,553
Cost of sales		(61,442)	(47,196)
Gross profit		44,721	35,357
Other operating income		5,128	4,343
Selling and distribution expenses		(5,432)	(3,601)
Administrative expenses		(38,785)	(28,894)
Finance costs	6	(15,670)	(3,879)
Change in fair value of convertible bonds	16	(7,208)	(22,385)
Change in fair value of derivative financial instruments	16	(9,847)	—
Impairment loss recognised on available-for-sale investments		(6,644)	—
Impairment loss recognised on trade and other receivables		(20,709)	—
Loss on deemed partial disposal of an associate	7	(127,836)	—
Loss on redemption of convertible bonds		(1,340)	—
Net gain on disposal of available-for-sale investments		—	3,180
Share of results of associates		(5,815)	211
Loss before tax		(189,437)	(15,668)
Income tax expense	8	(4,211)	(3,632)
Loss for the period from continuing operation	9	(193,648)	(19,300)

		Six months ended 30 June	
		2011	2010
	<i>Notes</i>	HK\$'000	HK\$'000
		(Unaudited)	(Unaudited)
			(Restated)
Discontinued operations			
Loss for the period from discontinued operations	10	–	(39,238)
Loss for the period		(193,648)	(58,538)
Other comprehensive income (expense) for the period			
Exchange difference arising on translation		7,996	2,880
Change in fair value of available-for-sale investments		(6,644)	(19,088)
Release of investment revaluation reserve upon disposal of available-for-sale investment		–	(4,346)
Share of other comprehensive income of associates		1,206	484
Other comprehensive income (expense) for the period		2,558	(20,070)
Total comprehensive expense for the period		(191,090)	(78,608)
Loss for the period attributable to:			
Owners of the Company			
From continuing operation		(200,493)	(24,757)
From discontinued operations		–	(30,847)
		(200,493)	(55,604)
Non-controlling interests			
From continuing operation		6,845	5,457
From discontinued operations		–	(8,391)
		6,845	(2,934)
		(193,648)	(58,538)
Total comprehensive income (expense) attributable to:			
Owners of the Company		(201,219)	(75,518)
Non-controlling interests		10,129	(3,090)
		(191,090)	(78,608)
Loss per share (HK cents)			
	11		
From continuing and discontinued operations			
Basic and diluted		(5.52)	(1.83)
From continuing operation			
Basic and diluted		(5.52)	(0.81)

CONDENSED CONSOLIDATED STATEMENT OF FINANCIAL POSITION

At 30 June 2011

		At 30 June 2011 HK\$'000 (Unaudited)	At 31 December 2010 HK\$'000 (Audited)
	Notes		
Non-current assets			
Property, plant and equipment	13	98,310	97,598
Prepaid lease payments		45,185	40,621
Concession intangible assets		495,000	483,829
Goodwill		142,373	142,373
Available-for-sale investments		23,254	29,898
Interest in associates		148,962	281,407
		<u>953,084</u>	<u>1,075,726</u>
Current assets			
Inventories		43,252	26,748
Trade and other receivables	14	175,528	148,900
Prepaid lease payments		1,539	1,150
Derivative financial instruments	16	392	10,239
Amounts due from customers for contract works		19,239	18,864
Cash held at financial institutions		6,507	37,724
Bank balances and cash		82,148	100,291
		<u>328,605</u>	<u>343,916</u>
Current liabilities			
Trade and other payables	15	193,342	163,572
Amounts due to customers for contract works		604	592
Bank borrowings		31,309	34,240
Other loans		42,201	39,885
Amounts due to non-controlling shareholders of a subsidiary		3,178	6,216
Loan from an associate		2,408	2,419
Convertible bonds	16	304,137	397,187
Tax payables		3,130	3,379
		<u>580,309</u>	<u>647,490</u>
Net current liabilities		<u>(251,704)</u>	<u>(303,574)</u>
Total assets less current liabilities		<u><u>701,380</u></u>	<u><u>772,152</u></u>

		At 30 June 2011 <i>HK\$'000</i> (Unaudited)	At 31 December 2010 <i>HK\$'000</i> (Audited)
	<i>Notes</i>		
Capital and reserves			
Share capital	17	410,332	324,765
Share premium and reserves		(46,075)	124,128
Equity attributable to owners of the Company		364,257	448,893
Non-controlling interests		188,576	179,164
Total equity		552,833	628,057
Non-current liabilities			
Bank borrowings		21,676	21,253
Other loans		52,218	47,487
Convertible bonds	16	–	3,000
Government grants		65,350	64,074
Deferred tax liabilities		9,303	8,281
		148,547	144,095
		701,380	772,152

NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION

For the six months ended 30 June 2011

1. COMPANY INFORMATION

China Water Industry Group Limited (the “Company”) was incorporated in the Cayman Islands as an exempted company with limited liability and its shares are listed on The Stock Exchange of Hong Kong Limited (the “Stock Exchange”).

The addresses of the registered office and principal place of business of the Company are Room 1207, 12/F, West Tower, Shun Tak Centre, 168-200 Connaught Road Central, Sheung Wan, Hong Kong.

The Company and its subsidiaries (the “Group”) are principally engaged in provision of water supply and sewage treatment as well as construction services in the People’s Republic of China (the “PRC”).

2. BASIS OF PREPARATION

The condensed consolidated interim financial information have been prepared in accordance with the applicable disclosure requirements of Appendix 16 to the Rules Governing the Listing of Securities on the Stock Exchange (the “Listing Rules”) and with Hong Kong Accounting Standard (“HKAS”) 34 “Interim Financial Reporting”, issued by the Hong Kong Institute of Certified Public Accountants (the “HKICPA”).

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 Hong Kong Financial Reporting Standards.

The Group reported an unaudited consolidated loss attributable to owners of the Company of approximately HK\$200,493,000 for the period ended 30 June 2011 and had an unaudited consolidated net current liabilities of approximately HK\$251,704,000 as at 30 June 2011. The condition indicates the existence of a material uncertainty which may cast significant doubt on the Group’s ability to continue as a going concern and therefore it may be unable to realise its assets and discharge its liability in the normal course of business. Nevertheless, the directors of the Company are of the opinion that the Group will have sufficient working capital to meet its financial obligations as and when they fall due for the next twelve months from 30 June 2011 following the repurchase of the Group’s existing convertible bonds and the issuance of new convertible bonds as disclosed in Note 20 to the condensed consolidated interim financial information.

3. PRINCIPAL ACCOUNTING POLICIES

The condensed consolidated interim financial information has been prepared on the historical cost basis, except for certain financial instruments, which are measured at fair values.

The accounting policies and methods of computation used in the condensed consolidated interim financial information for the six months ended 30 June 2011 are the same as those followed in the preparation of the Group’s annual financial statements for the year ended 31 December 2010 except as described below.

In the current interim period, the Group has applied the following new and revised standards, amendments and interpretations (“INTs”) (“new and revised HKFRSs”), issued by the HKICPA.

HKFRSs (Amendments)	Improvements to HKFRSs 2010 except of the amendments to HKFRS 3 (Revised in 2008), HKFRS 7, HKAS 1 and HKAS 28
HKFRS 1 (Amendment)	Limited Exemption from Comparative HKFRS 7 Disclosures for First-time Adopters
HKAS 24 (Revised)	Related Party Disclosures
HKAS 32 (Amendment)	Classification of Rights Issues
HK(IFRIC)-INT 14 (Amendment)	Prepayments of a Minimum Funding Requirement
HK(IFRIC)-INT 19	Extinguishing Financial Liabilities with Equity Instruments

Except as described below, the adoption of the new and revised HKFRSs had no material effect on the condensed consolidated interim financial information of the Group for the current and prior accounting periods.

The Group has not early applied the following new and revised standards, amendments or interpretations that have been issued but are not yet effective.

HKFRS 1 (Amendments)	Severe Hyperinflation and Removal of Fixed Dates for First-time Adopters ¹
HKFRS 7 (Amendments)	Disclosures – Transfers of Financial Assets ¹
HKFRS 9	Financial Instruments ⁴
HKFRS 10	Consolidated Financial Statements ⁴
HKFRS 11	Joint Arrangements ⁴
HKFRS 12	Disclosure of Interests in Other Entities ⁴
HKFRS 13	Fair Value Measurement ⁴
HKAS 1 (Revised)	Presentation of Financial Statements ³
HKAS 12 (Amendments)	Deferred Tax: Recovery of Underlying Assets ²
HKAS 19 (Revised)	Employee Benefits ⁴
HKAS 27 (2011)	Separate Financial Statements ⁴
HKAS 28 (2011)	Investments in Associates and Joint Ventures ⁴

¹ Effective for annual periods beginning on or after 1 July 2011.

² Effective for annual periods beginning on or after 1 January 2012.

³ Effective for annual periods beginning on or after 1 July 2012.

⁴ Effective for annual periods beginning on or after 1 January 2013.

HKFRS 9 Financial Instruments issued in November 2009 and amended in October 2010 introduces new requirements for the classification and measurement of financial assets and financial liabilities and for derecognition.

- HKFRS 9 requires all recognised financial assets that are within the scope of HKAS 39 Financial instruments: Recognition and Measurement to be subsequently measured at amortised cost or fair value. Specifically, debt investments that are held within a business model whose objective is to collect the contractual cash flows, and that have contractual cash flows that are solely payments of principal and interest on the principal outstanding are generally measured at amortised cost at the end of subsequent accounting periods. All other debt investments and equity investments are measured at their fair values at the end of subsequent accounting periods.
- The most significant effect of HKFRS 9 regarding the classification and measurement of financial liabilities relates to the accounting for changes in fair value of a financial liability (designated as at fair value through profit or loss) attributable to changes in the credit risk of that liability. Specifically, under HKFRS 9, for financial liabilities that are designated as at fair value through profit or loss, the amount of change in the fair value of the financial liability that is attributable to changes in the credit risk of that liability is recognised in other comprehensive income, unless the recognition of the effects of changes in the liability's credit risk in other comprehensive income would create or enlarge an accounting mismatch in profit or loss. Changes in fair value attributable to a financial liability's credit risk are not subsequently reclassified to profit or loss. Previously, under HKAS 39, the entire amount of the change in the fair value of the financial liability designated as at fair value through profit or loss was recognised in profit or loss.

HKFRS 9 is effective for annual periods beginning on or after 1 January 2013, with earlier application permitted.

The directors of the Company anticipate that HKFRS 9 that will be adopted in the Group's condensed consolidated interim financial information for the annual period beginning 1 January 2013 and that the application of the new standard may have a significant impact on amounts reported in respect of the Group's financial assets and financial liabilities. However, it is not practicable to provide a reasonable estimate of that effect until a detailed review has been completed.

The amendments HKFRS 7 *Disclosures – Transfers of Financial Assets* increase the disclosure requirements for transactions involving transfers of financial assets. These amendments are intended to provide greater transparency around risk exposures when a financial asset is transferred but the transferor retains some level of continuing exposure in the asset. The amendments also require disclosures where transfers of financial assets are not evenly distributed throughout the period.

The directors of the Company do not anticipate that these amendments to HKFRS 7 will have a significant effect on the Group's disclosures regarding transfers of trade receivables previously effected. However, if the Group enters into other types of transfers of financial assets in the future, disclosures regarding those transfers may be affected.

The five new or revised standards HKFRS 10, HKFRS 11, HKFRS 12, HKAS 27 (2011) and HKAS 28 (2011) which are standards on consolidation, joint arrangements and disclosures were issued by the HKICPA in June 2011 and are effective for annual periods beginning on or after 1 January 2013. Earlier application is permitted provided that all of the five new or revised standards are applied early at the same time. The directors of the Company anticipate that these new or revised standards will be applied in the Group's condensed consolidated interim financial information for financial year ending 31 December 2013 and the potential impact is described below.

HKFRS 10 replaces the parts of HKAS 27 *Consolidated and Separate Financial Statements* that deal with condensed consolidated interim financial information. Under HKFRS 10, there is only one basis for consolidation, that is control. In addition, HKFRS 10 includes a new definition of control that contains three elements: (a) power over an investee, (b) exposure, or rights, to variable returns from its involvement with the investee, and (c) ability to use its power over the investee to affect the amount of the investor's returns. Extensive guidance has been added in HKFRS 10 to deal with complex scenarios. Overall, the application of HKFRS 10 requires a lot of judgement. The directors of the Company is assessing the impact of the HKFRS 10 and is not in the position to comment on the impact to the interim financial information.

Other than disclosed above, the directors of the Company anticipate that the application of the other new and revised standards, amendments or interpretations will have no material impact on the condensed consolidated interim financial information.

4. REVENUE

Revenue represents revenue arising from the provision of water supply services, sewage treatment services, water supply related installation and construction income and water supply and sewage treatment infrastructure construction income.

An analysis of the Group's revenues for the period from continuing operation is as follows:

	Six months ended 30 June	
	2011	2010
	HK\$'000	HK\$'000
	(Unaudited)	(Unaudited)
		(Restated)
Water supply services	46,275	40,047
Sewage treatment services	12,305	9,088
Water supply related installation and construction income	41,765	33,418
Water supply and sewage treatment infrastructure construction income	5,818	–
	106,163	82,553

5. SEGMENT INFORMATION

The Group's operating segments, based on information reported to the chief operating decision makers who are directors of the Company for the purpose of resource allocation and performance assessment were as follows:

(a)	Provision of water supply and sewage treatment as well as construction services	Provision of water supply and sewage treatment and construction of water supply and sewage treatment infrastructure
(b)	Investments in financial products	Investments in financial and investment products
(c)	All others	Mainly represents manufacturing and trading of ceramic sewage materials and others

With effect from October 2010, the equity interest in iMerchants Limited ("iMerchants") owned by the Group was diluted to 36.57%. The investments in iMerchants were then reclassified from an investment in a subsidiary to investment in an associate. iMerchants is engaged in the business of investments in financial products and manufacturing and trading of ceramic sewage materials which was reported as a separate operating segment and a major component of the Group's other operating segment respectively for the period ended 30 June 2010. Upon the deemed partial disposal of iMerchants from a subsidiary to an associate, the operation of iMerchants was classified as discontinued operations of the Group and is described in more details in Note 10.

Segment revenues, results, assets and liabilities

Upon the deemed partial disposal of iMerchants from a subsidiary to an associate in October 2010, the Group has only one single operation, namely provision of water supply and sewage treatment and construction of water supply and sewage treatment infrastructure and accordingly no further segment information is presented.

Geographical information

No geographical information is presented as the Group's business is principally carried out in the PRC and the Group's revenue from external customers and non-current assets are in the PRC. No geographical information for other country is of a significant size to be reported separately.

Financial information and disclosures for the period ended 30 June 2010 has been restated accordingly in this condensed consolidated interim financial information.

6. FINANCE COSTS

	Six months ended 30 June	
	2011	2010
	HK\$'000	HK\$'000
	(Unaudited)	(Unaudited)
		(Restated)
Continuing operation		
Interest on:		
– Interest on convertible bonds	11,591	481
– Imputed interest charged on convertible bonds	402	–
– Bank borrowings wholly repayable within five years	1,393	1,323
– Bank borrowings wholly repayable more than five years	850	828
– Other loans wholly repayable within five years	1,028	709
– Other loans wholly repayable more than five years	87	473
– Amounts due to non-controlling shareholders of subsidiaries	155	65
– Loan from an associate	164	–
	<u>15,670</u>	<u>3,879</u>

7. LOSS ON DEEMED PARTIAL DISPOSAL OF AN ASSOCIATE

On 23 October 2009, iMerchants issued approximately 2,938,478,000 non-redeemable convertible preference shares with a par value of HK\$0.2 each (the “Convertible Preference Shares”), as a partial consideration for the acquisition of an intangible asset through the acquisition of a subsidiary.

During the six months period ended 30 June 2011, part of the Convertible Preference Shares holders, exercised their rights to convert their Convertible Preference Shares into fully paid ordinary shares of iMerchants. After the conversion, the equity interest of iMerchants owned by the Group has reduced further from 36.57% as at 31 December 2010 to 15.35% as at 30 June 2011. The loss on deemed partial disposal of an associate of HK\$127,836,000 was recognised in the condensed consolidated statement of comprehensive income of the Group for the six months period ended 30 June 2011. As at 30 June 2011, 3 out of 8 directors of iMerchants were elected by the Company and thus, in the opinion of the directors of the Company, the Company can still exercise significant influence over iMerchant’s financial and operating policy decisions.

8. INCOME TAX EXPENSE

	Six months ended 30 June	
	2011	2010
	HK\$'000	HK\$'000
	(Unaudited)	(Unaudited)
PRC Enterprise Income Tax (“EIT”)		
– current period	3,189	2,842
Deferred tax	1,022	790
	4,211	3,632

Hong Kong Profits Tax has not been provided for in the condensed consolidated interim financial information for the six months ended 30 June 2011 and 2010 as there was no estimated assessable profit derived from Hong Kong for both periods.

Pursuant to the relevant laws and regulations in the PRC, certain subsidiaries are exempted from PRC EIT for two years from the first profit making year, followed by a 50% reduction for the next three years.

Under the Law of the EIT and Implementation Regulation of the Law of the EIT, the tax rate of the other PRC subsidiaries is at 25% for both period.

9. LOSS FOR THE PERIOD FROM CONTINUING OPERATION

	Six months ended 30 June	
	2011	2010
	HK\$'000	HK\$'000
	(Unaudited)	(Unaudited)
		(Restated)
Loss for the period from continuing operation has been arrived at after charging (crediting):		
Staff costs including directors' emoluments		
– salaries, wages and other benefits	23,238	17,275
– retirement benefits scheme contributions	2,329	3,686
Total staff costs	25,567	20,961
Amortisation of prepaid lease payments	640	547
Amortisation of concession intangible assets (included in cost of sales)	7,646	7,482
Impairment loss recognised on trade and other receivables	20,709	2
Depreciation of property, plant and equipment	3,860	2,671
Gain on disposal of property, plant and equipment	(5)	(18)
Bank interest income	(501)	(79)
Net exchange loss (gain)	31	(2)

10. DISCONTINUED OPERATIONS

On 23 October 2009, iMerchants issued approximately 2,938,478,000 Convertible Preference Shares, as a partial consideration for the acquisition of an intangible asset through the acquisition of a subsidiary.

In September and October 2010, part of the Convertible Preference Shares holders exercised their rights to convert their Convertible Preference Shares in fully paid ordinary shares of iMerchants. After the conversion, the equity interest of iMerchants owned by the Group has reduced further from 67.23% to 49.23%. The investments in iMerchants were then changed from investment in a subsidiary to investment in an associate.

Analysis of profit for the period from discontinued operations

iMerchants is engaged in the business of investments in financial products and manufacturing and trading of ceramic sewage. The combined results of these discontinued operations in the condensed consolidated statement of comprehensive income and condensed consolidated statement of cash flows are set out below. The comparative loss and cash flows from the discontinued operations have been re-presented to include those operations classified as discontinued.

The loss for the period from discontinued operations is analysed as follows:

	Six months ended 30 June	
	2011	2010
	HK\$'000	HK\$'000
Loss for the period from discontinued operations		
Revenue	–	6,398
Cost of sales	–	(2,243)
Gross profit	–	4,155
Other operating income	–	344
Selling and distribution expense	–	(1,647)
Administrative expenses	–	(35,078)
Finance costs	–	(7,012)
Loss before tax	–	(39,238)
Taxation	–	–
Loss for the period from discontinued operations	–	(39,238)

Loss for the period from discontinued operations include the following:

	Six months ended 30 June	
	2011	2010
	HK\$'000	HK\$'000
Loss before tax has been arrived at after charging:		
Amortisation of an intangible asset	–	30,854
Depreciation of property, plant and equipment	–	51
Finance costs		
– Interest on other loans	–	210
– Imputed interest on convertible bonds	–	6,802
Staff costs excluding directors' emoluments		
– Salaries, wages and other benefits	–	1,691
– Retirement benefits scheme contributions	–	38
Total staff costs	–	1,729
Cash flows from discontinued operations		
Net cash inflows from operation activities	–	18,745
Net cash outflows from investing activities	–	(5,539)
Net cash outflows from financing activities	–	(15,545)
Net cash outflows	–	(2,339)

11. LOSS PER SHARE

From continuing operation

The calculation of basic and diluted loss per share attributable to the owners of the Company is based on the following data:

	Six months ended 30 June	
	2011	2010
	HK\$'000	HK\$'000
	(Unaudited)	(Unaudited)
		(Restated)
Loss		
Loss for the period attributable to the owners of the Company	(200,493)	(55,604)
Less: Loss for the period from discontinued operations	–	(30,847)
Loss for the purposes of basis and diluted loss per share from continuing operation	(200,493)	(24,757)
Number of shares	'000	'000
Weighted average number of ordinary shares for the purpose of basic and diluted loss per share	3,630,213	3,045,287

Note: The computation of diluted loss per share does not assume the exercise of the Company's outstanding share options as exercise price of those options is higher than the average market price of shares for the periods ended 30 June 2011 and 2010.

Diluted loss per share was same as the basic loss per share for the six months ended 30 June 2011 and 2010, as the effect of the conversion of the Company's outstanding share options and convertible bonds as well as the outstanding convertible bonds and non-redeemable preference shares issued by iMerchants would result in a decrease in loss per shares from continuing operation for the six months ended 30 June 2011 and 2010.

From discontinued operations

Basic and diluted earnings per share for the discontinued operations is HK\$1.01 cents per share for the six months ended 30 June 2010 (2011: Nil), based on the loss for the period from the discontinued operations of approximately HK\$30,847,000 (2011: Nil) and the denominators detailed above for both basic and diluted earnings per share.

12. DIVIDENDS

The directors of the Company do not recommend the payment of any interim dividend for the both reporting periods.

13. PROPERTY, PLANT AND EQUIPMENT

During the six months ended 30 June 2011, the Group acquired property, plant and equipment amounted to approximately HK\$2,968,000 (six months ended 30 June 2010: approximately HK\$795,000) and disposed of property, plant and equipment with carrying amount of approximately HK\$4,000 (six months ended 30 June 2010: approximately HK\$302,000).

14. TRADE AND OTHER RECEIVABLES

	At 30 June 2011 HK\$'000 (Unaudited)	At 31 December 2010 HK\$'000 (Audited)
Trade receivables	22,170	16,219
Less: impairment loss recognised	(5,350)	(5,246)
	<u>16,820</u>	<u>10,973</u>
Other receivables	41,724	22,754
Less: impairment loss recognised	(9,021)	(8,903)
	<u>32,703</u>	<u>13,851</u>
Loan receivables	148,052	129,480
Less: impairment loss recognised	(26,429)	(5,720)
	<u>121,623</u>	<u>123,760</u>
Deposits and prepayments	4,382	316
	<u><u>175,528</u></u>	<u><u>148,900</u></u>

The Group allows an average credit period of 30 days to 180 days given to the customers.

An aged analysis of trade receivables net of impairment loss recognised, based on invoice date was as follows:

	At 30 June 2011 HK\$'000 (Unaudited)	At 31 December 2010 HK\$'000 (Audited)
Within 90 days	12,553	6,517
91 to 180 days	1,883	3,537
181 to 365 days	1,672	807
Over 1 year	712	112
	<u>16,820</u>	<u>10,973</u>

15. TRADE AND OTHER PAYABLES

The following is an analysis of trade payables, presented based on the invoice date:

	At 30 June 2011 HK\$'000 (Unaudited)	At 31 December 2010 HK\$'000 (Audited)
Within 30 days	4,423	6,237
31 to 90 days	775	518
91 to 180 days	400	713
181 to 365 days	1,301	611
Over 1 year	1,832	1,018
	<u>8,731</u>	<u>9,097</u>
Other payables	104,466	79,309
Interest payables	80,145	75,166
	<u>193,342</u>	<u>163,572</u>

16. CONVERTIBLE BONDS

The Group issued two batches of convertible bonds in August 2007 ("CB1") and August 2010 ("CB2").

Movement of CB1 during the period was as follows:

	<i>HK\$'000</i> (Unaudited)
At the beginning of the period	95,526
Loss on redemption	1,340
Repayment	(18,000)
Change in fair value	7,208
	<u>86,074</u>
At the end of the period	<u>86,074</u>

Movement of CB2 during the period was as follows:

	Equity component <i>HK\$'000</i>	Liability component <i>HK\$'000</i>	Early redemption option <i>HK\$'000</i>	Total <i>HK\$'000</i>
At the beginning of the period	15,914	304,661	(10,239)	310,336
Imputed interest charged	–	402	–	402
Change in fair value	–	–	9,847	9,847
Cash paid for redemption	–	(56,000)	–	(56,000)
Conversion during the period	(1,464)	(31,000)	–	(32,464)
	<u>14,450</u>	<u>218,063</u>	<u>(392)</u>	<u>232,121</u>
At the end of the period	<u>14,450</u>	<u>218,063</u>	<u>(392)</u>	<u>232,121</u>

The following is the analysis of CB1 and CB2 for financial reporting purposes:

	At 30 June 2011 <i>HK\$'000</i>	At 31 December 2010 <i>HK\$'000</i>
Financial liabilities at fair value through profit or loss CB1	<u>86,074</u>	<u>95,526</u>
Financial liabilities at amortised cost Liability component of CB2	<u>218,063</u>	<u>304,661</u>
Analysed as:		
Current liabilities	218,063	301,661
Non-current liabilities	<u>–</u>	<u>3,000</u>
	<u>218,063</u>	<u>304,661</u>
Derivative financial instruments Early redemption option	<u>392</u>	<u>10,239</u>
Equity element Convertible bond equity reserve	<u>14,450</u>	<u>15,914</u>

17. SHARE CAPITAL

	At 30 June 2011 (Unaudited)		At 31 December 2010 (Audited)	
	Number of shares	Amount HK\$'000	Number of shares	Amount HK\$'000
Authorised capital:				
At beginning and end of the period/year				
Ordinary shares of HK\$0.1 each	8,000,000,000	800,000	8,000,000,000	800,000
Convertible preference shares of HK\$0.1 each	2,000,000,000	200,000	2,000,000,000	200,000
	10,000,000,000	1,000,000	10,000,000,000	1,000,000
Issued and fully paid:				
At beginning of the period/year	3,247,651,000	324,765	2,706,379,000	270,638
Issue of shares upon top- up placing (<i>Note 1</i>)	649,000,000	64,900	265,476,000	26,547
Issue of shares upon conversion of convertible bonds (<i>Note 2</i>)	206,666,664	20,667	–	–
Issue of shares upon placing (<i>Note 3</i>)	–	–	275,796,000	27,580
At end of the period/year	4,103,317,664	410,332	3,247,651,000	324,765

Note:

- (1) On 9 August 2010, pursuant to a placing and subscription agreement entered into with existing shareholders, the Company placed out 265,476,000 new ordinary share of HK\$0.1 each in the Company at a price of HK\$0.108 per share. A sum of net amount approximately HK\$27,851,000 after deducting related expenses of approximately HK\$820,000, was raised and used as working capital of the Group.

On 31 March 2011, pursuant to a placing and subscription agreement entered into with independent third parties, the Company placed out 324,000,000 new ordinary share of HK\$0.1 each in the Company at a price of HK\$0.128 per share. A sum of net amount approximately HK\$40,186,000 after deducting related expenses of approximately HK\$1,286,000, was raised and used for repayment of debts and for general working capital of the Group.

On 29 April 2011, pursuant to a placing and subscription agreement entered into with existing shareholders, the Company placed out 325,000,000 new ordinary share of HK\$0.1 each in the Company at a price of HK\$0.123 per share. A sum of net amount approximately HK\$38,753,000 after deducting related expenses of approximately HK\$1,222,000 was raised and used for repayment of debts and for general working capital of the Group.

- (2) On 3 March 2011, 15 March 2011 and 28 March 2011, the holder of CB2 converted an aggregate principal amount of HK\$31,000,000 of CB2 into a total of 206,666,664 ordinary shares of HK\$0.1 each in the Company. The details of conversion are as follows:

Conversion date	Number of ordinary shares of HK\$0.1 each	Conversion price per share HK\$	Conversion principal amount HK\$
3 March 2011	106,666,666	0.15	16,000,000
15 March 2011	33,333,332	0.15	5,000,000
28 March 2011	66,666,666	0.15	10,000,000
	<u>206,666,664</u>		<u>31,000,000</u>

- (3) On 9 August 2010, pursuant to a placing and subscription agreement entered into with existing shareholders, the Company placed out 275,796,000 new ordinary share of HK\$0.1 each in the Company at a price of HK\$0.108 per share. A sum of net amount approximately HK\$29,041,000 after deducting related expenses of approximately HK\$745,000, was raised and used as working capital of the Group.

All new shares issued during the period ended 30 June 2011 and the year ended 31 December 2010 rank pari passu in all respects with other shares in issue.

18. CAPITAL COMMITMENT

	At 30 June 2011 HK\$'000 (Unaudited)	At 31 December 2010 HK\$'000 (Audited)
Capital commitments contracted but not provided for, in respect of acquisition of concession intangible assets and property, plant and equipment	<u>4,642</u>	<u>7,079</u>

19. OPERATING LEASE COMMITMENTS

The Group leases certain of its factory premises, plant and staff quarters under operating lease arrangements. Leases for properties are negotiated for terms ranging from one to five years. Rental was fixed at the inception of the lease. No provision for contingent rent and terms of renewal were established in the leases.

At the end of the reporting period, the Group had future minimum lease payments under non-cancellable operating leases which fall due as follows:

	At 30 June 2011 HK\$'000 (Unaudited)	At 31 December 2010 HK\$'000 (Audited)
Within one year	1,767	3,032
In the second to fifth years, inclusive	<u>880</u>	<u>1,069</u>
	<u>2,647</u>	<u>4,101</u>

20. EVENTS AFTER THE END OF THE INTERIM PERIOD

- (1) On 29 July 2011 and 2 August 2011, the Company entered into repurchase agreements with several investors to repurchase the CB1 and CB2 at a consideration of approximately of HK\$73,096,000 and HK\$205,000,000 respectively.
- (2) On 15 August 2011, the Company entered into two subscription agreements with the subscribers to issue two convertible notes in an aggregate amount of HK\$80,000,000 and HK\$200,000,000 respectively at an initial conversion price of HK\$0.1 per share. The convertible note holder may convert at any time from one year and three years after the date of initial issue of the convertible notes respectively.
- (3) On 15 August 2011, the Company entered into a placing agreement to issue a convertible note up to a principal amount of HK\$200,000,000 at an initial conversion price of HK\$0.1 per share. The convertible note holder may convert at any time following the relevant date of issue and ending on the date that falls on the seventh day immediately before the maturity date into new shares of the Company.
- (4) On 15 August 2011, the board of directors of the Company (the “Board”) proposed to effect the share consolidation pursuant to which every 10 issued and unissued shares will be consolidated into one consolidated share with a par value of HK\$1.00 each. The authorised share capital will be increased by the creation of an additional of 1,200,000,000 consolidated shares with a par value of HK\$1.00 each.
- (5) Subject to the share consolidation as set out in (4) above, the Board proposed to effect the capital reduction pursuant to which the par value of each of the issued consolidated shares will be reduced from HK\$1.00 to HK\$0.50 each by cancelling paid-up capital to the extent of HK\$0.50 per issued consolidated share resulting in each consolidated share of HK\$1.00 each being treated as on fully paid-up new share of HK\$0.50 each in the share capital of the Company.

Details of (1) and (2) to (5) are set out in the Company’s announcement dated 2 August 2011 and 19 August 2011 respectively.

21. LITIGATION

Super Sino Investment Limited (“Super Sino”), an indirectly wholly-owned subsidiary of the Company

In November 2007, the People’s Government of Danzhou City and Super Sino entered into a net asset transfer agreement, pursuant to which all assets and liabilities of Danzhou City Water were transferred to Super Sino. On 26 June 2008, Super Sino was notified that Agricultural Bank of China, Danzhou Branch (“the Plaintiff”) filed a claim regarding the liabilities transferred by Danzhou City Water with the Court against Danzhou City Water, Super Sino, Danzhou Urban Development Corporation and the People’s Government of Danzhou City for the repayment of the loan principal of approximately HK\$31,309,000 (equivalent to RMB26,000,000) (31 December 2010: HK\$30,698,000 equivalent to RMB26,000,000) and the interests of approximately HK\$53,391,000 (equivalent to RMB44,337,000) (31 December 2010: HK\$50,972,000 equivalent to RMB43,171,000) arising from the defendants of Danzhou City Water and Super Sino to the plaintiff.

On 13 November 2009, the Court issued a civil verdict, pursuant to which Super Sino was ordered to fully repay the loan principal of RMB26,000,000 together with the interest thereon.

On 17 December 2009, the Plaintiff made on appeal to the Higher People’s Court of Hainan Province court seeking the fulfilment of the guarantee responsibility of Danzhou Urban Development Corporation.

On 15 December 2010, Higher People's Court of Hainan Province issued verdict, pursuant to which all the shares of Danzhou City Water owned by Super Sino (the "shares") have been frozen from 15 December 2010 to 14 December 2012. The Company cannot transfer or dispose of the shares during the period. According to the legal advice, the directors of the Company are of the opinion that the verdict will not impair the control of the Group over Danzhou City Water due to the following reasons:

- (1) Super Sino is still the legal owner of Danzhou City Water during the period ended 30 June 2011 and up to the date of approval of these condensed consolidated interim financial information.
- (2) As Danzhou City Water is engaged in the business of provision of water in the PRC which requires special license from the respective PRC government authorities. The procedures for the change of shareholding are complicated and require the approval from several PRC government authorities.

As at 30 June 2011, the directors of the Company are discussing the settlement arrangement with the Plaintiff and there is no demand for settlement from the Plaintiff at the moment. The principal of the said loan and the interest thereon have been included in the condensed consolidated interim financial information. The directors of the Company are of the opinion that the power to govern the financial and operating policies of Danzhou City Water are still vest on the Group.

22. RELATED PARTY TRANSACTIONS

The balances and transactions with related parties at the end of reporting period are disclosed elsewhere in the condensed consolidated interim financial information.

Compensation of key management personnel

The remuneration of directors and other members of key management during the period was as follows:

	2011 HK\$'000 (Unaudited)	2010 <i>HK\$'000</i> (Unaudited)
Short-term benefits	1,901	2,590
Post-employment benefits	43	54
	1,944	2,644

The remuneration of directors and key executives is determined by the remuneration committee having regard to the performance of individuals and market trends.

MANAGEMENT DISCUSSION AND ANALYSIS

FINANCIAL PERFORMANCE

Financial results

For the six month ended 30 June 2011, the Group recorded an unaudited consolidated net loss of HK\$193.65 million which represented a substantial increase of HK\$135.11 million compared to the consolidated net loss of HK\$58.54 million in the same period last year. The main factors contributing to the net loss for the interim period could be summarized as follows:

- Loss of HK\$127.84 million on deemed partial disposal of an associate;
- Impairment loss of HK\$20.71 million recognized in respect of trade and other receivable;
- Loss of HK\$9.85 million from the change in fair value of derivative financial instruments;
- Impairment loss of HK\$6.64 million recognized on available-for-sale investments; and
- Loss of HK\$5.82 million in sharing of results of associates.

Revenue and gross profit

For the six month ended 30 June 2011, the Group achieved a continuing growth in revenue and gross profit, which amounted to HK\$106.16 million and HK\$44.72 million respectively. This represented a growth of 28.60% in revenue and 26.48% in gross profit as compared to the corresponding period of last period. The main revenue and gross profit contributors for the period were Yichun Water Industry Co., Ltd (“Yichun Water”) and Yingtian Water Supply Co., Ltd (“Yingtian Water”), which collectively accounted for 70.93% of the consolidated revenue and 78.24% of gross profit respectively. The financial analysis of revenue and gross profit is as follows:

	Revenue				Gross Profit			
	2011		2010		2011		2010	
	HK\$'M	%	HK\$'M	%	HK\$'M	%	HK\$'M	%
Water supply services	46.27	43.58%	40.04	48.50%	16.07	35.93%	13.65	38.60%
Sewage treatment services	12.31	11.60%	9.09	11.01%	4.73	10.58%	1.85	5.23%
Construction services	47.58	44.82%	33.42	40.49%	23.92	53.49%	19.86	56.17%
Total	<u>106.16</u>	100%	<u>82.55</u>	100%	<u>44.72</u>	100%	<u>35.36</u>	100%

Other operating income

Other operating income increased by HK\$0.79 million to HK\$5.13 million (2010: 4.34 million). The income included mainly interest income of HK\$0.50 million, the guaranteed profit of HK\$1.76 million compensated by the PRC government for the respective acquired water plant, cleaning and disinfection handling fees of HK\$0.6 million and gain on disposal of wastage material of HK\$0.8 million.

Selling and distribution costs and administrative expenses

Selling and distribution costs together with administrative expenses were collectively increased by HK\$11.72 million to HK\$44.22 million (2010: HK\$32.50 million). The increase was mainly due to additional legal and professional incurred for restructuring of convertible bonds and increase in staff costs. These expenses mainly consisted of legal and professional fees of HK\$5.35 million, staff cost of HK\$17.47 million, repair and maintenance of HK\$3.14 million and depreciation of HK\$2.53 million.

Finance costs

Finance costs of HK\$15.67 million were mainly represented by interest payments to banks and other borrowings of HK\$3.51 million and to the convertible bonds (“CBs”) holders of HK\$11.59 million (2010: HK\$3.88 million). The increase of HK\$11.79 million was mainly additional interest paid to CB holders of HK\$11.11 million.

Impairment loss recognized on available-for-sale investments

This loss of HK\$6.64 million arose from the fair value of the equity investment at the end of the reporting period being less than investment cost. Pursuant to the HKFRS, the equity investment is determined to be impaired when there is a significant or prolonged decline in the fair value of that investment below its cost, this is considered to be objective evidence of impairment. The respective cumulative loss previously accumulated in the investment revaluation reserve is reclassified to loss and are recognized in Condensed Consolidated Statement of Comprehensive Income.

Impairment loss recognized on trade and other receivables

Impairment of HK\$20.71 million were provided for the other receivables covering the refundable deposit of HK\$10 million paid for the potential investment project in the PRC and loan advanced to two independent third parties (the “Borrowers”) amounting to HK\$8.20 million and HK\$2.51 million respectively. The directors of the Company has assessed these receivables individually and believed that the Company would have difficulties in recovering the above amounts. Thus, demand letters for the collection of the deposit and debts were issued to the deposit holder and the respective Borrowers and the impairment loss for the full amount was provided as these outstanding amounts were considered not recoverable.

Loss on deemed partial disposal of an associate

During the six months period ended 30 June 2011, the holders of Convertible Preference Share issued by an associate of the Group, iMerchants Limited (“iMerchants”), exercised their rights to convert the Convertible Preference Shares into fully paid ordinary shares of iMerchants. After the conversion, the equity interest of iMerchants owned by the Group has reduced further from 36.57% as at 31 December 2010 to 15.35% as at 30 June 2011. The loss on deemed partial disposal of an associate of HK\$127.84 million was recognised in the Condensed Consolidated Statement of Comprehensive Income of the Group for the six months period ended 30 June 2011. As at 30 June 2011, 3 out of 8 directors of iMerchants was elected by the Group, and thus, the Group still exercised significant influence over iMerchants’s financial and operating policy decisions.

Share of loss from associates

The Group had two associated companies, iMerchants and Jinan Hongquan Water Production Co., Ltd. (“Jinan Hongquan”). As at 30 June 2011, the Group held 15.35% equity interests in iMerchants and shared the loss of HK\$3.42 million. During the period under review, the Group shared 35% loss from Jinan Hongquan of HK\$2.40 million.

BUSINESS SEGMENTS REVIEW

Water supply business

During the interim period, the Group’s water supply business consisted of 6 water supply plants which were located in Jiangxi Province, Anhui Province, Shandong Province and Hainan Province. The total daily water supply capacities were approximately 1,960,000 tonnes contributing revenue of HK\$46.27 million, representing 43.58% of the Group’s total revenue. The average price of water supply ranged from HK\$1.51 to HK\$2.32 per tonne.

Sewage treatment business

Sewage treatment business consisted of 2 sewage treatment plants which were located in Jiangxi Province and Shandong Province. The daily disposal sewage capacities were approximately 110,000 tonnes per day contributing revenue of HK\$12.31 million, representing 11.60% of the Group’s total revenue. The average price of sewage treatment ranged from HK\$0.60 to HK\$1.43 per tonne.

Construction of water supply and sewage treatment infrastructure

Construction service comprised water meter installation, construction of pipelines and pipelines repairing. This was the Group’s major source of revenue contributing HK\$47.58 million during the period, representing 44.82% of the Group’s total revenue.

LIQUIDITY AND FINANCIAL RESOURCES

As at 30 June 2011, the Group recorded cash and bank balance including cash held at financial institutions of HK\$88.66 million (compared with HK\$138.02 million on 31 December 2010). The decrease was mainly due to repayment of a portion of the issued CBs, advances to independent third parties and an associated company of the Group. The Group has had steady cash flow generating from the water supply and sewage treatment business segments.

Total liabilities of the Group as at 30 June 2011 were HK\$728.86 million (compared with HK\$791.59 million on 31 December 2010). They mainly comprised of the CB of HK\$304.14 million (2010: HK\$400.19 million), bank and other borrowings of HK\$147.40 million (2010: HK\$142.87 million), and government grants of HK\$65.35 million (2010: HK\$64.07 million). The CBs were denominated in HK dollars, while others were denominated in Renminbi and the interest rates of which were fixed.

The Group’s gearing ratio as at 30 June 2011 was 56.87% (2010: 55.76%). The ratio was calculated by dividing total liabilities of HK\$728.86 million over total assets of the Group of HK\$1,281.69 million.

At as 30 June 2011, the Group had net current liabilities of HK\$251.70 million (2010: net current liabilities of HK\$303.57 million). The current portion of CBs amounting to HK\$304.14 million represented 52.41% of the total current liabilities.

Subsequent to the period ended, the Company entered into repurchase agreements with several CB holders to repurchase convertible bonds issued to them on 3 August 2007 (the “2007 Bonds”) and 30 September 2010 (the “2010 Bonds” and together with 2007 Bonds, the “Bonds”) at a consideration of \$73.10 million and HK\$205 million respectively. Following the repurchase, no Bonds are remained outstanding. The amount paid for the repurchasing of the Bonds was at approximately 21% discount to the accrued amounts owing to the holders if the outstanding Bonds were held to maturity, the Directors took the view that the terms for the repurchase were favorable to the Company.

To refinance the repurchase of Bonds, the Company borrowed two short-term interest bearing loans from two independent third parties, one being a 2-month unsecured loan facility of HK\$80 million and the other a 6-month secured loan facility of HK\$205 million. Both loans bear interest at rate of 12% per annum. To meet the aforesaid debts obligation when they fall due, the Company had decided to raise funds by way of debts financing through the issuance of zero interest convertible bonds. This financing structure is in the best interest of the Company to solve the imminent financial needs without incurring interest expenses.

CAPITAL RAISING AND USE OF PROCEEDS

On 31 March 2011, the Company entered into the Top up Placing and Subscription Agreement with existing shareholders and the Placing Agent pursuant to which the Company placed out a maximum of 324,000,000 new ordinary share of HK\$0.1 each at a placing price of HK\$0.128 per share, through the Placing Agent on a best effort basis. The Top-up Placing and Top-up Subscription were completed on 6 April 2011 and 8 April 2011 respectively. The net proceed of HK\$40 million from the placing are intended to be used on repayment of debts and general working capital of the Group.

On 29 April 2011, the Company entered into the Top up Placing and Subscription Agreement with existing shareholders and the Placing Agent pursuant to which the Company placed out a maximum of 325,000,000 new ordinary share of HK\$0.1 each at a placing price of HK\$0.123 per share, through the Placing Agent on a best effort basis. The Top-up Placing and Top-up Subscription were completed on 5 May 2011 and 6 May 2011 respectively. The net proceed of HK\$38.5 million from the placing are intended to be used on repayment of debts and general working capital of the Group.

In March 2011, three 2010 Bonds holders exercised their rights and converted the aggregate principle CB amount of HK\$31 million into 206,666,664 shares at the conversion price of HK\$0.15 per share. Details of the conversion were announced in the Next Day Disclosure Returns on 3 March 2011, 15 March 2011 and 28 March 2011.

During the interim period, the Group incurred capital expenditures amounting to HK\$12.86 million for acquisition of concession intangible assets, prepaid leased payment and purchase of property, plant and equipment (2010: HK\$76.47 million) .

FOREIGN EXCHANGE RISK

The Group's exposure to foreign exchange risk is minimal as most of the Group's subsidiaries operate in the PRC and most of the transactions, assets and liabilities are denominated in Renminbi. Accordingly, the Group does not have derivative financial instruments to hedge its foreign currency risks.

CAPITAL COMMITMENTS

As at 30 June 2011, the Group has the capital commitments contracted but not provided for acquisition of concession intangible assets and property, plant and equipment approximately HK\$4.64 million (2010: HK\$7.08 million).

CONTINGENT LIABILITIES

As at 30 June 2011, the group did not have any significant contingent liabilities (2010: Nil).

EMPLOYEES AND REMUNERATION POLICIES

As at 30 June 2011, the Group has employed approximately 972 full-time employees (2010: 912 full-time employees). Most of them stationed in the PRC while the remaining in Hong Kong. The remuneration package of the employees is determined by various factors including the employees' experience and performance, the market condition, industry practice and applicable employment law.

PENDING LITIGATION

(i) Technostore Limited, a subsidiary of the Company

On 30 May 2007, a Petition was filed under sections 168A and 177 of the Company Ordinance (Cap. 32) to wind-up Technostore Limited ("Technostore"), a company in which the Company held 50.01% of the issued shares. The Petition was commenced by Mr. Mao Chi Fai ("Petitioner"), the minority shareholder of Technostore holding 49.99% of the issued shares. Following court hearings regarding the winding-up proceeding in the preceding year, on 29 August 2008, the court made an order to appoint Kenny Tam & Company, Certified Public Accountant as a Liquidator of Technostore. The Liquidator, Happy Hour Limited and Mr. Mao Chi Fai to become members in the Committee of Inspection ("COI"). In October 2009, all stocks of Technostore with costs valued at approximately HK\$2.2 million transferred by the Official Receiver's Office to the Liquidator were disposed at the consideration of around HK\$0.62 million by public tender. Preferential and ordinary dividends were distributed on 10 November 2010. Further, a sum of less than HK\$1,000 was realized from the bank accounts of Technostore. On 25 August 2011, the Liquidator indicated that no additional assets of Technostore have been realised and it anticipates that there will be no further assets for realisation. The Liquidator has further indicated that it will apply to the Court for his release as the Liquidator of Technostore shortly. The directors of the Company believe that no material future outflows resources from the Group is expected and sufficient provision on assets related to Technostore have been provided. It is unlikely that there will be a material adverse financial impact on the Group.

(ii) Super Sino Investment Limited, an indirect wholly-owned subsidiary of the Company

On 6 November 2007, the People's Government of Danzhou and Super Sino Investment Limited ("Super Sino") entered into an assets and liabilities transfer agreement, pursuant to which the assets and liabilities of Danzhou City Water Company* (儋州市自來水公司) were transferred to Super Sino. On 26 June 2008, Agricultural Bank of China Danzhou Branch instituted proceedings with Hainan Intermediate People's Court against Danzhou City Water Company, Super Sino and the People's Government of Danzhou (a third party) regarding the abovementioned transfer of the relevant liabilities, claiming for the principal of RMB26 million and the interest thereon of RMB43.17 million repayable by Danzhou City Water Company and Super Sino (as defendants). On 13 November 2009, the First Intermediate People's Court of Hainan Province issued a civil verdict, pursuant to which Super Sino was ordered to fully repay the loan principal of RMB26 million together with the interest thereon. On 17 December 2009, the Plaintiff made an appeal to the Higher People's Court of Hainan Province court seeking the fulfilment of the guarantee responsibility of Danzhou Urban Development Corporation. On 15 December 2010, Higher People's Court of Hainan Province issued verdict, pursuant to which all the shares of Danzhou City Water owned by Super Sino (the "shares") have been freezed from 15 December 2010 to 14 December 2012. The Company cannot transfer or dispose of the shares during the period. According to the legal advice, the directors of the Company are of the opinion that the verdict will not impair the control of the Group over Danzhou City Water due to the following reason:

- (1) Super Sino is still the legal owner of Danzhou City Water during the period ended 30 June 2011 and up to the reporting date.
- (2) As Danzhou City Water is engaged in the business of provision of water in the PRC which requires special license from the respective the PRC government authorities. The procedures for the change of shareholding is complicated and require the approval from several the PRC government authorities.

As at the date of this announcement, the directors of the Company are discussing the settlement arrangement with the Plaintiff and there is no demand for settlement from the Plaintiff at the moment. The principal of the said loan and the interest thereon have been included in the condensed consolidated interim financial statements of the Group. The directors of the Company are of the view that the aforesaid litigation is unlikely to have any significant material financial impact on the Group.

Save and except for this, the Company is not aware of any other significant proceedings instituted against the Company.

MAJOR EVENTS SUBSEQUENT TO THE PERIOD UNDER REVIEW

Repurchase of Bonds

On 2 August 2011 and 29 July 2011, the Company entered into repurchase agreements with several CB holders to repurchase convertible bonds issued to them on 3 August 2007 and on 30 September 2010 respectively (“Bonds”). The total consideration paid for the Bonds was HK\$73,096,098 and HK\$205,000,000, respectively. The Bonds were repurchased with the proceeds from short term interest bearing loans on an arm’s length basis, entered into by the Company and Independent third party lenders on 28 July 2011 and 3 August 2011 respectively. The repurchased Bonds were settled on 8 August 2011 and then all Bonds were cancelled pursuant to the terms and conditions of the Bonds. Following such cancellation, no Bonds are remained outstanding.

Issue of Convertible Notes under General Mandate, Issue of Convertible Notes under Specific Mandate, Placing of Convertible Notes and Capital Reorganization

On 15 August 2011, the Company entered into Subscription Agreement I (“Subscription I”) and Subscription Agreement II (“Subscription II”) with Honghu Capital Co. Ltd (the “Subscriber”), under which the Company has agreed to issue, and the Subscriber has agreed to subscribe for, the zero interest Convertible Notes I due 2012 (“Convertible Notes I”) and the zero interest Convertible Notes II due 2014 (“Convertible Note II”) to be issued by the Company in an aggregate principal amount of HK\$80 million and HK\$200 million respectively.

For Convertible Notes I, a total of 800,000,000 Conversion Shares I will be allotted and issued under general mandate to Subscriber at Conversion Price I of HK\$0.10 per Share.

For Convertible Notes II, a total of 2,000,000,000 Conversion Shares II will be allotted and issued under the Specific Mandate to Subscriber at the initial Conversion Price II of HK\$0.10 per Share (being the current par value of the Shares) but assuming the Capital Reorganisation has not been completed. The Specific Mandate will be sought from Shareholders at the Extraordinary General Meeting (“EGM”).

At the same date, the Company entered into the Placing Agreement (“Placing”) with Kingston Securities Limited (the “Placing Agent”), pursuant to which the Placing Agent agreed to procure placees to subscribe for HK\$200,000,000 of the zero interest Convertible Notes III 2014 (“Convertible Notes III”) on a best endeavours basis, at the initial Conversion Price III of HK\$0.10 per Share (being the current par value of the Shares) but assuming the Capital Reorganisation has not been completed. For the Convertible Notes III fully placed, a total of 2,000,000,000 Conversion Shares III will be allotted and issued at the Conversion Price III but subject to the approval by shareholders at the EGM.

To comply with the trading requirements of the Rules Governing the Listing of Securities on the Stock Exchange (the “Listing Rules”), the Board proposed to effect the Share Consolidation for every 10 issued and unissued Shares be consolidated into one Consolidated Share. To cater for additional new Shares to be allotted and issued for Convertible Note I, II and III, the authorised share capital will be increased by the creation of an additional 1,200,000,000 Consolidated Shares with a par value of HK\$1.00 each immediately following the Share Consolidation. Subject to the Share Consolidation becoming effective, the Board proposed to effect the Capital Reduction to reduce the par value of each of the issued Consolidated Shares from HK\$1.00 to HK\$0.50 each. The Share Consolidation, the increase of Share Capital and the Capital Reduction (collectively referred to as the “Capital Reorganisation”) are subject to the approval by shareholders at EGM.

Upon the completion of the Subscription I, II and the Placing and assuming the Capital Reorganization becoming effective, a total of 80,000,000 Conversion Shares I, 400,000,000 Conversion Shares II and 400,000,000 Conversion Shares III will be allotted and issued by the Company to Subscriber and Placees respectively.

Acquisition of subsidiaries

On 1 December 2010, Mark Profit Group Holdings Limited (“Mark Profit”), a wholly owned subsidiary of the Company, entered into the Sales and Purchase Agreement (“Agreement”) with Vendor A – Top Vision Management Limited (“Top Vision”) and Vendor B – Da Xin Waterworks Management (Huizhou) Co., Ltd.* (“Da Xin Waterworks”) (達信水務管理(惠州)有限公司), pursuant to which the Mark Profit has conditionally agreed to acquire 70% of the registered capital of Foshan City Gaoming Huaxin Sewage Treatment Company Ltd.* (“Gaoming Huaxin”) (佛山市高明區華信污水處理有限公司); 100% of the registered capital of Sihui South China Waterworks Development Co., Ltd.* (“Sihui South China”) (四會華南水務發展有限公司), 100% interest of Boluo Da Xin Sewage Treatment Company Ltd.* (“Boluo Daxin”) (博羅達信污水處理有限公司) respectively, at a consideration of HK\$50 million. The consideration of HK\$6.5 million will be paid in cash for refundable deposit before completion and the remaining balance of HK\$43.5 million will be offset by the loan which was owed by Top Vision. The negotiation for the acquisition of Gaoming Huaxin is at the final stage. The management and the Vendor A is arranging for the handover matter. The acquisition is expected to be completed in September 2011. But the acquisition of Sihui South China and Boluo Daxin have not been completed up to the reporting date. The application of share transfer relating to the sale interest of Sihui South China was submitted to the Foreign Trade & Economic Cooperation Bureau* (對外貿易經濟合作局) and the Administration for Industry and Commerce* (工商行政管理局), the PRC. In view of the current progress of relevant governmental or regulatory authorities, it is expected that additional time will be required for obtaining regulatory approval of shares transfer. Furthermore, the Sale Interests relating to Boluo Daxin is subject to prior encumbrance in favour of third party, such encumbrance has to be released before Completion. The Vendor B is arranging for the release of the encumbrance over the Sale Interests to facilitate the Completion. As more time than expected is required for arranging a proper release of the encumbrance and in view of the current progress, it is expected that additional time will be required before Completion can take place. Pursuant to the Agreement, the acquisition is subject to the satisfaction (or waiver, where applicable) of the condition precedents set forth therein on or before 31 May 2011. In this connection, the responsible directors are under negotiation with the Vendors relating to the extension of long stop date of the acquisition of the Sale Interests. Further announcement will be made once the Supplemental Agreement regarding the extension of long stop date has been entered into by the relevant parties.

PROSPECTS

After years of efforts and developments, the Group has realized certain economy of scale in terms of water supply in mainland China, and also accumulated some experiences in terms of sewage treatment, which promises that the water business would be identified as the principal business yielding continuously increasing income and bringing us profit thereafter. However, the Company will incur losses this year due to the limited profit improvement of the water supply plants which were challenged with rising operating costs arising from excessively fast climbing commodity prices and excessively growing consumer price index and with restriction in raising water prices, together with certain issues left over from history.

Currently, since the new management is in place, the Company will conduct a strategic adjustment shortly. The Board believes that the Company is going to enjoy a bright prospect in future upon settling the problems left over from history through such adjustment.

SUPPLEMENTARY INFORMATION

INTERIM DIVIDENDS

The Board does not recommend the payment of interim dividend for the six month ended 30 June 2011 (six months ended 30 June 2010: Nil)

DIRECTORS' AND CHIEF EXECUTIVE'S INTERESTS IN SECURITIES

As at 30 June 2011, the interests and short positions of each Director and Chief Executive of the Company, or their associates in the shares, underlying shares and debentures of the Company and its associated corporations (within the meaning of the Securities and Futures Ordinance ("SFO") which (a) had been notified of the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests and short positions in which Directors have taken or deemed to have under such provisions of the SFO) or which (b) were required pursuant to section 352 of the SFO, to be entered in the register referred to therein; or which (c) were required, pursuant to the Model Code for Securities Transactions by Directors of Listed Companies (the "Model Code") contained in Appendix 10 to the Listing Rules to be notified to Company and the Stock Exchange were as follows:

(i) Interest in the Shares

Name of director	Nature of interest	Number of issued ordinary shares held	Total interest	Percentage of the issued share capital of the Company
Chu Yin Yin, Georgiana	Beneficial owner	5,432,000	5,432,000 (L)	0.13%
Yang Bin	Interest of controlled corporation	450,479,000	450,479,000 (L) (Note)	10.98%

For the purpose of this section, the shareholding percentage of the Company is calculated on the basis of 4,103,317,664 Shares in issue as at 30 June 2011.

The letter "L" denotes a long position in shares of the Company

Note: These China Water Shares are held by Boost Skill Investments Limited (as to 265,479,000 China Water Shares) and its wholly owned subsidiaries, Favor Jumbo Investments Limited (as to 130,000,000 China Water Shares) and Sure Ability Limited (as to 55,000,000 China Water Shares). Mr. Yang Bin is interested in 60% of the equity interest in Boost Skill Investments Limited.

(ii) Interest in underlying Shares

Name of director	Exercise Price	Exercise Period	Number of underlying Shares (under share options of the Company)			Approximate shareholding
			Outstanding as at 1 January 2011	Lapsed during the year	Outstanding as at 30 June 2011	
	(HK\$)					%
Chu Yin Yin, Georgiana	0.335	11 January 2007 to 10 January 2017	3,000,000	(3,000,000)	–	–

Note: Owing to the termination of the Existing Share Option Scheme and adoption of the New Share Option Scheme at the Annual General Meeting held on 3rd June 2011, those share options granted under the Existing Share Option Scheme were lapsed accordingly.

Save as disclosed above, as at 30 June 2011, none of the Directors or Chief Executive of the Company had any interest or short position in any shares, underlying shares or debenture of the Company or any of its associated corporations (within meaning of the SFO) which (a) were required to be notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests and short positions which Directors have taken or deemed to have under such provisions of SFO) or (b) were required pursuant to section 352 of the SFO, to be entered in the register referred to therein; or which (c) were required, pursuant to the Model Code to be notified to Company and the Stock Exchange.

SUBSTANTIAL SHAREHOLDERS

As at 30 June 2011, the following persons and entities, other than a Director or chief executive of the Company disclosed under the section “Directors’ and Chief executive’s interests in Securities” above) had interest or short positions in the shares and underlying shares of the Company as recorded in the register required to be kept under Section 336 of SFO:

Name of shareholder	Capacity	Number of issued Shares held	Approximate percentage of the issued share capital of the Company
Li Jian Ping	Interest of controlled corporation	450,479,000 (Note 1)	10.98%
Boost Skill Investments Limited	Interest of controlled corporation	185,000,000 (Note 2)	4.51%
	Beneficial owner	265,479,000	6.47%
Abax Arhat Fund	Interest of controlled corporation	228,873,239	5.58%
Abax Claremont Ltd.	Interest of controlled corporation	228,873,239 (Note 3)	5.58%
Abax Global Capital	Interest of controlled corporation	228,873,239 (Note 3)	5.58%
Abax Global Opportunitites Fund	Interest of controlled corporation	228,873,239 (Note 3)	5.58%
Abax Upland Fund, LLC	Interest of controlled corporation	228,873,239 (Note 3)	5.58%
Abax Lotus Ltd.	Beneficial owner	228,873,239 (Note 3)	5.58%

Note 1: These China Water Shares are held by Boost Skill Investments Limited (as to 265,479,000 China Water Shares), Favor Jumbo Investments Limited (as to 130,000,000 China Water Shares) and Sure Ability Limited (as to 55,000,000 China Water Shares). Mr. Yang Bin, an executive Director, and Mr. Li Jian Ping is interested in 60% and 40% respectively of the equity interest in Boost Skill Investments Limited.

Note 2: These China Water Shares are held by Favor Jumbo Investments Limited (as to 130,000,000 China Water Shares) and Sure Ability Limited (as to 55,000,000 China Water Shares). Favor Jumbo Investments Limited and Sure Ability Limited are wholly-owned subsidiaries of Boost Skill Investments Limited.

Note 3: These 228,873,239 underlying Shares are those Shares which would be issued upon exercise of the convertible rights attaching to the convertible bonds issued by the Company as disclosed in the announcement of the Company dated 31 July 2007. As the issued share capital of Abax Lotus Limited is held indirectly or directly by Abax Arhat Fund, Abax Claremont Limited, Abax Global Capital, Abax Global Opportunities Fund and Abax Upland Fund, LLC, they are deemed to be interested in the underlying Shares under SFO.

Note 4: The shareholding percentage in China Water is calculated on the basis of 4,103,317,664 China Water Shares in issue as at 30 June 2011.

Save as disclosed above, as at 30 June 2011, the Company has not been notified of any person or entity who had interests and short position in the shares and underlying shares of the Company as recorded in the register required to be kept under Section 336 of the SFO.

DIRECTORS' RIGHTS TO ACQUIRES OR DEBENTURES

Save as disclosed under the heading "Share Option Scheme" below, at no time during the period were the rights to acquire benefits by means of the acquisition of shares in or debentures of the Company Granted to any Director or Chief Executive of the Company or their respective spouse or children under 18 years of age, or were any such rights exercised by them; or was the Company and its subsidiaries a party to any arrangement to enable the Directors to acquire such rights in any other body corporate.

SHARE OPTION SCHEME

At the Annual General Meeting of the Company held on 3 June 2011, the shareholders of the Company approved the adoption of the Company's New Share Option Scheme ("Scheme") and the termination of the Company's then Existing Share Option Scheme. Options granted under the Existing Share Option Scheme but not exercised or lapsed in accordance with the terms of the New Scheme were cancelled by the Company with the approval of the Option Holders. The Scheme was adopted for the primary purpose of providing incentives or rewards to selected eligible participants for their contributions to the Group, and will expire on 2 June 2021.

Details of the movements in the share options during the period ended 30 June 2011 under the Existing Share Option Scheme are as follows:

Name or category of participant	Date of grant	Outstanding as at 1 January 2011	Granted during the period	Exercised during the period	Lapsed during the period	Outstanding as at 30 June 2011	Exercisable period	Exercise Price per share of the Company HK\$
<i>Directors</i>								
Chu Yin Yin, Georgiana (Note 1)	11 January 2007	3,000,000	-	-	(3,000,000)	-	11 January 2007 to 10 January 2017	0.335
Other eligible participant (Note 1, 2)	17 January 2007	5,000,000	-	-	(5,000,000)	-	17 January 2007 to 16 January 2017	0.420
Total as at 30 June 2011		<u>8,000,000</u>	<u>-</u>	<u>-</u>	<u>(8,000,000)</u>	<u>-</u>		

Note 1 : Owing to the termination of the Existing Share Option Scheme and adoption of the New Share Option Scheme at the Annual General Meeting held on 3 June 2011, those share options granted under the Existing Share Option Scheme were lapsed accordingly.

Note 2: Liu Bai Yue resigned all position in the Group in June 2011.

PRE-EMPTIVE RIGHTS

There are no provisions for pre-emptive rights under the Company's articles of association or the laws of the Cayman Islands which would oblige the Company to offer new shares on a pro rata basis to its existing shareholders.

PURCHASES, REDEMPTIONS OR SALES OF COMPANY'S LISTED SECURITIES

During the six months ended 30 June 2011, the Company had not redeemed, and neither the Company nor any of its subsidiaries had purchased or sold any of the Company's listed securities.

SUFFICIENT OF PUBLIC FLOAT

As far as the information publicly available to the company is concerned and to the best knowledge of the Directors of the Company, at least 25% of the Company's issued share capital were held by members of the public as at the date of this announcement.

CORPORATE GOVERNANCE

The Group recognizes the importance of transparency and accountability to shareholders. The Board will continually review and enhance its corporate governance practices to ensure that they meet shareholder's expectation and comply with relevant standards.

During the six months ended 30 June 2011, the corporate governance practices adopted by the Company has complied with the code provisions set out in the Code of Corporate Governance Practices contained in Appendix 14 of the Listing Rules (the "CGP Code") except the following deviation from the following provisions of the CGP Code:

- Code provision A4.1 stipulates that non-executive Directors including independent non-executive Directors should be appointed for a specific term, subject to re-election while all directors should be subject to the retirement by rotation at least once every three years. However, none of the existing independent non-executive Directors of the Company are appointed for a specific term since all independent non-executive Directors of the Company are subject to retirement by rotation and re-election at annual general meetings for the Company in line with the Company's Articles of Association. The Company considers that sufficient measures have been taken to ensure that the Company's corporate governance practices are no less exacting than those in the CGP Code.

MODEL CODE FOR SECURITIES TRANSACTIONS BY DIRECTORS

The Company has adopted the full set of Model Code set out in Appendix 10 of the Listing Rules as the code of the conduct for securities transactions by directors (the "Model Code"). The prohibitions on securities dealing and disclosure requirements in the Model Code apply to specified individuals including the Group's senior management and also persons who are privy to price sensitive information of the Group. Having made specific enquiry of all directors, the Board confirmed that directors of the Company had complied with the Model Code regarding directors' securities transactions throughout the six months ended 30 June 2011.

AUDIT COMMITTEE

The Audit Committee comprises 3 independent non-executive Directors of the Company, has reviewed with the management of the Company the accounting principles and practices adopted by the Group and discussed auditing, internal controls and financial reporting matters including the review of the unaudited interim financial statements for the six months ended 30 June 2011.

REMUNERATION COMMITTEE

The Remuneration Committee comprises 2 independent non-executive Directors of the Company and 1 executive Director of the Company, is responsible for reviewing and evaluating the remuneration policies of executive Directors and senior management and making recommendations to the Board from time to time.

INVESTMENT COMMITTEE

The Investment Committee consists of 4 executive Directors and 1 independent non-executive Director. The role of Investment Committee is to oversee the Company's strategic and investment policy on a regular basis and to advise the Board on the investment of the Company including asset allocation and new investment proposal.

PUBLICATION OF THE INTERIM RESULTS AND REPORT

The interim results announcement is published on the websites of the Company (www.chinawaterind.com) and The Stock Exchange of Hong Kong Limited (<http://www.hkex.com.hk>). The interim report of the Company for 2011 containing all information required by the Listing Rules will be dispatched to Shareholders and made available on the above websites in due course.

APPRECIATION

Finally, I would like to take this opportunity to express my gratitude to my fellow Directors, management and employees for their contributions and dedication to the development of the Group and deep thanks to our shareholders, customers, suppliers and business partners for their continued supports.

By order of the Board
China Water Industry Group Limited
Wang De Yin
Chairman

Hong Kong, 29 August 2011

As at the date of this announcement, the board of directors of the Company comprises Mr. Wang De Yin, Mr. Yang Bin, Mr. Liu Feng, Mr. Lin Yue Hui, Mr. Tang Hui Ping and Ms. Chu Yin Yin, Georgiana, all being executive Directors, and Mr. Chang Kin Man, Mr. Wu Tak Lung and Mr. Gu Wen Xuan, all being independent non-executive Directors.

** for identification purpose only*