



16 November 2016

Flowgroup plc
("Flow" or the "Company" or the "Group")

Update

Flowgroup plc (AIM: FLOW), which provides a range of innovative energy technologies, energy supply and energy services, announces an update on its home energy, smart boiler and microCHP businesses.

Flow Energy

Our Flow Energy business continues to perform well and in line with management expectations. We have delivered greater than 150% growth in customer fuel accounts this year and it is pleasing to note that this part of the Group is achieving over £127million revenue in annualised sales.

Consumers are facing price rises this winter as the energy market is experiencing a significant rise in wholesales costs, with electricity prices having risen by around 65% since August for this winter period, accompanied by a 30% rise in winter gas prices since the middle of the year. Our hedging strategy provides protection against rising wholesale energy prices for both our customer base and our business. We have also taken steps to protect our gas costs against adverse weather conditions over this winter when demand is most volatile, either as a result of cold or warm periods.

We believe that current market conditions favour more established providers like Flow with more robust energy trading strategies, systems and processes, and we believe we can continue to grow this part of the business in 2017.

Smart boiler

Following the launch of the Flow Eco RF in September 2016, we have been pursuing sales through our Flow Brand Ambassador (FBA) network, via our energy customers and with social housing networks. Whilst still at an early stage in the launch cycle, sales via our FBA network have started satisfactorily and management will provide further updates in due course.

The feedback from our FBAs on the quality of the product and the benefit of our heating and home energy bundles has been consistently positive. A test campaign to target our energy customers for Flow Eco RF sales has produced positive results, supporting our belief that our energy customer base has the potential to be a sustainable channel to generate boiler sales. The social housing market is producing significant opportunities where we believe the Flow Eco RF can deliver benefits to both social and private landlords, with substantial savings for large landlords due to the increased efficiency and reliability of the product, as well as the remote diagnostic capability, which reduces servicing costs. We are in active discussions with a range of social housing providers all with networks of thousands of homes.

MicroCHP update

DECC review

In May 2016, the then Department of Energy and Climate Change (DECC), now part of the Department for Business, Energy and Industrial Strategy (BEIS), published a consultation document (the "Consultation") which included a review of support for the microCHP Feed-in-Tariff (FiT), whereby the number of qualifying microCHP units would be capped at a much lower level, thereby reducing the support significantly.

Due to the implications of this Consultation, coupled with increasing manufacturing costs due to the fall in the value of Sterling against the Euro and US Dollar, in the Company's half year report announced on 5 September, we stated that we had initiated a strategic review of the microCHP business. We also announced that we had slowed down the production of the Flow microCHP boiler and reduced the level of sales and marketing activity to offset the risks of carrying a large inventory of boilers that could be potentially uneconomic to support in the UK.

We had expected clarity from Government in early Q4 2016 on the scope of ongoing FIT support for microCHP. However, this has not been forthcoming and indications from BEIS are that any revised scheme will now not come into place until April 2017, which suggests that the review is taking longer than expected and may not report back this year. This continues to be a frustration, as our manufacturing relationship with Jabil Inc. is good and our teams continue to work closely together with Jabil's production facility in Livingston, Scotland, which is fully operational and producing Flow microCHP boilers.

During the Consultation and after it closed we made strong representations to BEIS to promote the benefits to the UK of our technology and had several meetings with them. BEIS also visited Jabil's facility in Scotland to see Flow microCHP boilers being made and the investment in production facilities. We have been encouraged by the level of engagement by BEIS and remain optimistic of a positive outcome to the Consultation. However, alongside discussions with Jabil, the Board is considering the options for microCHP should the conclusion to the Consultation be adverse or further delayed. These include:

1. Continue reducing production while we await the BEIS announcement and accelerating our plans to launch in Europe, where the financial support offered favours microCHP

Due to the proposed reduction in the UK FIT, plus higher production costs due to the weakness of Sterling, we are evaluating a plan to support a reduction in boilers produced on a monthly basis for the remainder of 2016 and into the majority of 2017.

This option prioritises the commercialisation and support of our technology in Europe ahead of the UK, and Flow is engaged in active discussions with French, Italian and German market players for the distribution of our technology.

We would then re-focus on the UK market once the boiler economics are more favourable following cost reduction at volume manufacture. We will continue to explore the feasibility of this approach, both in terms of manufacturing, distribution logistics and financing.

2. Sale or exit of the microCHP business

In the event that the above approach is found not to be feasible the Board would explore the sale of the microCHP business to a third party. In the event that no sale is achieved, the remaining option would be to exit our microCHP business. This would have a material effect on Flowgroup both in terms of the strategic direction of the Group and also the cost to exit this part of the business.

We will continue to explore the options and report back to shareholders when we are able to recommend a preferred option.

Update on Europe

As stated above, we have reduced production levels to a minimum and, as a result, we have now built up an inventory of over 800 fully functional Flow microCHP boilers. In order to recoup manufacturing costs, continue to learn from real-world installations and continue to create case studies and generate performance data, we will now increase our marketing to offer these for sale both in the UK and Europe.

Whilst the uncertainty of the outcome of the Consultation and the weakness of Sterling has created issues, support for the technology in Europe remains very strong. Potential incentives vary across Europe, with Italy understood to offer personal tax rebates, while Germany provides grants and other tax incentives to support deployment of the technology. The Board believes that consumer demand is also potentially strong.

As announced previously, a large European utility has been testing our Flow microCHP boiler. The first phase of these tests is now complete and we are pleased to be in a position to be able to announce that the company we have been working with is Gaz réseau distribution France (GRDF), the French gas distributor and a branch of ENGIE, which employs 154,950 people worldwide, achieved revenues of €69.9 billion in 2015, and which provides individuals, cities and businesses with efficient and innovative solutions to take on the challenges of energy's transition to a low-carbon economy.

We are delighted with the findings from GRDF's testing of the performance of our technology. GRDF checked the performance of our microCHP boiler as specified and analysed the technology to confirm that it was relevant for the French market. For both these objectives, our technology met GRDF's criteria. GRDF also noted that we had a clear advantage on performance against competing technologies when measured in time from switch-on to generation of electricity, thereby giving an advantage in the heating market where heating systems cycle throughout daily operation.

Additionally, a recent report by GRDF stated that some 80 per cent of people surveyed across France are attracted by the idea of microCHP. We believe that the European combination of financial support and consumer demand could lead to significant adoption of microCHP technology in Europe, as suggested by the previously quoted Cogeneration Observatory and Dissemination Europe (CODE) report in 2014 which indicated microCHP could take one third of the European boiler market by 2030, a market with an installed base of over 100 million.

Outlook

Whilst the previously announced reduction in microCHP production has inevitably had a corresponding effect on our expectations for turnover, it is pleasing to note that the Group's diverse model is robust. With the rest of the business trading well and costs being monitored closely, the Board expects the other key metrics of EBITDA and cash for the financial year ending December 2016 to be in line with market expectations.

Tony Stiff, Group Chief Executive Officer of Flowgroup plc, commented: *"The ongoing uncertainty around our microCHP business is frustrating. However, we are taking positive steps to find a solution that works for our business and for our shareholders. While we do that, we are continuing to grow the business as a whole, producing good results in our energy business and generating the first sales of the Flow Eco RF boiler, both to new leads and to existing energy customers. This element of our strategy is very clear – to take advantage of a seismic shift in the energy market, and a heating market that is ripe for disruption, to deliver a successful company that spans both markets and generates significant value for customers and shareholders.*

"As discussed in our half Yearly report, while our microCHP technology platform has significant potential value for our business, and we will pursue every opportunity to realise that value, we have built an organisation that can flourish without it, should that be necessary, and believe that diversification remains one of Flowgroup's fundamental strengths. That said, we remain positive about the potential for microCHP. GRDF's testing of our technology produced good results which confirmed our own data on performance and which compared our technology favourably with that of our competitors. It was pleasing to have such a large and successful business as GRDF be supportive of our product, particularly considering our potential focus on the European market."

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