

# Phylogica Limited

ACN 098 391 961

## Interim Financial Report

31 December 2007

# Phylogica Limited

ACN 098 391 961

## Directors

Mr Joachim von Roy  
Executive Chairman

Mr Harry Karelis  
Deputy Chairman

Mr Bruce McHarrie  
Non-executive Director

Dr Mark Pierce  
Non-executive Director

Dr Douglas Wilson  
Non-executive Director

Dr Stewart Washer  
Executive Director

Dr Paul Watt  
Executive Director

## Company Secretary

Graeme R Boden  
Telephone: 08 9321 9888  
Facsimile: 08 9321 6666  
Email: gboden@bigpond.net.au

## Share Registry

PO Box 535  
Applecross  
Western Australia 6953  
770 Canning Highway  
Applecross  
Western Australia 6153  
Telephone: 08 9315 2333  
Facsimile: 08 9315 2233  
Email: registrar@securitytransfer.com.au

## Bankers

National Australia Bank  
Subiaco Branch  
464 Hay Street  
Subiaco  
Western Australia 6008

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## Registered Office & Principal Place of Business

105 Hay Street  
Subiaco  
Western Australia 6008  
Telephone: 08 9423 8888  
Facsimile: 08 9423 8899  
Website: www.phylogica.com

## Auditors

KPMG  
Central Park  
152 - 158 St Georges Terrace  
Perth  
Western Australia 6000

Incorporated in Western Australia, October 2001  
Listed on the Australian Stock Exchange (ASX)  
Home Exchange: Perth  
**Code: PYC** ordinary shares

## Phylogica Limited

### Directors report

The directors present their report on Phylogica Limited (referred to in these financial statements as ~~the~~ ~~Company~~ or ~~Phylogica~~) together with the financial report for the half-year ended 31 December 2007 and the review report thereon.

## Directors

The Directors of the Company at any time during or since the end of the half-year are:

### Non-executive

Mr Harry Karelis

Mr Bruce McHarrie

Dr Mark Pierce

Dr Doug Wilson

Appointed 20 February 2007

Appointed 10 December 2007

### Executive

Mr Joachim von Roy

Dr Stewart Washer

Dr Paul Watt

Unless otherwise indicated, all Directors held their position as a Director throughout the entire half year and up to the date of this report.

Dr Stewart Washer has announced his intention to resign as a Director and Chief Executive Officer with effect from the end of February 2008.

## Review of operations

The principal activity of Phylogica during the period was the discovery and development of novel therapeutics directed at proteins and their interactions.

Activities continue to progress rapidly for Phylogica with the past 6 months seeing important and significant technology and research results.

The Company recorded a loss of \$2,297,203 for the six months to 31 December 2007 (31 December 2006: \$1,754,838). Expenditure continues to be in line with budget.

Highlights of the period include:

- In August 2007, the expiry date of \$0.25 options was reached with the vast majority of option holders choosing to exercise their options, leaving a shortfall of only \$685,999 which was covered under the company's underwriting agreement with Australian Heritage Group.
- Phylogica expanded its product pipeline to include acute lung distress. New Phylomer peptide PYC 38 was found to protect against acute respiratory distress in animals. In collaboration with the internationally renowned asthma and respiratory researchers at the Telethon Institute for Child Health Research in Perth, Phylogica demonstrated that several Phylomer peptides, when delivered intra-nasally, significantly reduced lung inflammation in animals with acute respiratory distress.
- Phylogica entered into an agreement with Dynamic Microbials Limited to license anti-microbial applications of its proprietary Phylomer technology.

## Review of operations (continued)

- Phylogica signed a research collaboration agreement with Swiss Institute of Allergy & Asthma Research (SIAF). The research involves the screening of Phylogica proprietary Phylomer libraries for potential vaccine leads for the treatment of allergies and asthma.
- Phylogica has demonstrated biological activity with its lead Rheumatoid Arthritis (RA) compounds developed during its Commercial Ready grant funded program. Phylomers are now considered proven to work for disease targets both inside and outside the cell.
- Phylogica is to take its innovative burns drug into human trials. Pre-clinical data for Phylomer drug candidate PYC35B demonstrates convincing in-vivo efficacy at low dose. Skin healing was accelerated and scar formation significantly reduced with low concentrations of the drug applied topically after injury in animal models and positive effects on healing were maintained after treatment. Phylogica has committed to exploit this exciting opportunity by taking lead Phylomer PYC35B into the clinic in 2008.

Phylogica continues to build on its strategy of collaboration with Australian and internationally recognised centres of excellence and scientists in the pursuit of its objectives.

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

The lead auditor's independence declaration is set out on page 3 and forms part of the Directors' report for the half-year ended 31 December 2007.

Signed in accordance with a resolution of the directors:



Harry Karelis  
Director

Perth  
26 February 2008

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

To: the directors of Phylogica Limited

I declare that, to the best of my knowledge and belief, in relation to the review for the half-year ended 31 December 2007 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

T R Hart  
*Partner*

Perth  
26 February 2008

# Phylogica Limited

## Interim income statement

For the half year ended 31 December 2007

	<i>Note</i>	31 Dec 2007	31 Dec 2006
		\$	\$
Commercial income		74,422	208,344
Government grant income		325,434	317,600
<b>Gross profit</b>		<b>399,856</b>	<b>525,944</b>
Contract research costs		1,125,709	757,225
Personnel expenses		939,836	726,166
Depreciation, amortisation and impairment		47,684	12,500
Professional services		195,553	207,671
Travel and accommodation		165,606	94,708
Licenses		8,135	6,789
Intellectual property maintenance		83,648	182,728
Laboratory consumables		124,155	134,030
Occupancy costs		49,045	34,977
Other operating expenses		118,616	215,743
<b>Results from operating activities</b>		<b>(2,458,131)</b>	<b>(1,846,593)</b>
Interest income		160,928	91,755
<b>Loss before income tax</b>		<b>(2,297,203)</b>	<b>(1,754,838)</b>
Income tax benefit	3	-	-
<b>Loss for the period attributable to the members of Phylogica Limited</b>		<b>(2,297,203)</b>	<b>(1,754,838)</b>
		Cents	Cents
Basic earnings per share		<b>(1.7)</b>	<b>(1.6)</b>

Diluted earnings per share are not shown because potential ordinary shares on issue at the comparative balance dates are not considered dilutive.

The income statement is to be read in conjunction with the notes to the interim financial statements set out on pages 8 to 12

# Phylogica Limited

## Interim balance sheet

For the half year ended 31 December 2007

	<i>Note</i>	<b>31 Dec 2007</b>	30 June 2007
		\$	\$
<b>Current assets</b>			
Cash and cash equivalents		<b>5,364,415</b>	3,369,322
Trade and other receivables		<b>92,607</b>	29,570
Other		<b>9,625</b>	20,549
<b>Total current assets</b>		<b>5,466,647</b>	3,419,441
<b>Non-current assets</b>			
Property, plant and equipment	4	<b>150,164</b>	114,543
<b>Total non-current assets</b>		<b>150,164</b>	114,543
<b>Total assets</b>		<b>5,616,811</b>	3,533,984
<b>Current liabilities</b>			
Trade and other payables		<b>458,156</b>	830,632
Non Interest-bearing liabilities		<b>11,165</b>	9,679
Employee benefits	9	<b>90,352</b>	246,287
Deferred government grants		<b>168,509</b>	239,516
<b>Total current liabilities</b>		<b>728,182</b>	1,326,114
<b>Non-current liabilities</b>			
Employee benefits		<b>7,820</b>	11,208
<b>Total non-current liabilities</b>		<b>7,820</b>	11,208
<b>Total liabilities</b>		<b>736,002</b>	1,337,322
<b>Net assets</b>		<b>4,880,809</b>	2,196,662
<b>Equity</b>			
Issued capital	2	<b>16,675,573</b>	11,709,889
Accumulated losses	2	<b>(11,794,764)</b>	(9,513,227)
<b>Total equity attributable to members of Phylogica Limited</b>		<b>4,880,809</b>	2,196,662

The balance sheet is to be read in conjunction with the notes to the interim financial statements set out on pages 8 to 12

# Phylogica Limited

## Interim statement of cash flows

For the half year ended 31 December 2007

	<i>Note</i>	<b>31 Dec 2007</b>	31 Dec 2006
		\$	\$
<b>Cash flows from operating activities</b>			
Income received		470,863	470,936
Cash paid to suppliers and employees		<u>(3,517,590)</u>	<u>(2,246,796)</u>
Cash used in operations		<u>(3,046,727)</u>	<u>(1,775,860)</u>
Interest received		159,442	108,281
<b>Net cash from operating activities</b>		<u><b>(2,887,285)</b></u>	<u><b>(1,667,579)</b></u>
<b>Cash flows from investing activities</b>			
Acquisition of property, plant and equipment	4	(83,305)	(30,546)
Acquisition of other investments		-	-
<b>Net cash from investing activities</b>		<u><b>(83,305)</b></u>	<u><b>(30,546)</b></u>
<b>Cash flows from financing activities</b>			
Proceeds from the issue of share capital	2	5,172,691	3,769,583
Repayment of borrowings		-	-
Payment of transaction costs	2	<u>(207,008)</u>	<u>(206,250)</u>
<b>Net cash from financing activities</b>		<u><b>4,965,683</b></u>	<u><b>3,563,333</b></u>
Net decrease in cash and cash equivalents		1,995,093	1,865,208
Cash and cash equivalents at 1 July		<u>3,369,322</u>	<u>2,638,872</u>
<b>Cash and cash equivalents at 31 December</b>		<u><b>5,364,415</b></u>	<u><b>4,504,080</b></u>

This statement of cash flows is to be read in conjunction with the notes to the interim financial statements set out on pages 8 to 12

## Phylogica Limited

### Statement of changes in equity

For the half year ended 31 December 2007

	<i>Note</i>	<b>31 Dec 2007</b> \$	31 Dec 2006 \$
Total equity at the beginning of the period		<b>2,196,662</b>	2,114,304
Loss for the period		<b>(2,297,203)</b>	(1,754,838)
Issue of capital	2	<b>5,172,691</b>	3,769,583
Share capital transaction costs	2	<b>(207,008)</b>	(206,250)
Share based payments expense for the period		<b>15,666</b>	98,985
<b>Total equity at the end of the half year</b>		<b>4,880,809</b>	4,021,784

This statement of changes in equity is to be read in conjunction with the notes to the interim financial statements set out on pages 8 to 12

## Notes to the interim financial statements

### 1. Significant accounting policies

Phylogica Limited is a company domiciled in Australia.

The annual financial report of the Company as at and for the year ended 30 June 2007 is available upon request from the Company's registered office at the address or at the Web site shown earlier in this report.

#### (a) Statement of compliance

The interim financial report is a general purpose financial report which has been prepared in accordance with Australian Accounting Standards AASB 134: Interim financial reporting and the Corporations Act 2001.

The interim financial report does not include all of the information required for a full annual financial report, and should be read in conjunction with the annual financial report of the Company as at and for the year ended 30 June 2007.

The interim financial report of the Company for the six months ended 31 December 2007 was authorised for issue by the directors on 18<sup>th</sup> February 2008.

#### (b) Significant accounting policies

The accounting policies applied by the Company in this interim financial report are the same as those applied by the Company in its financial report as at and for the year ended 30 June 2007.

#### (c) Estimates

The preparation of an interim financial report in conformity with AASB 134 *Interim Financial Reporting* requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. These estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

In preparing this interim financial report, the significant judgements made by management in applying the Company's accounting policies and the key sources of estimation uncertainty were the same as those that applied to the financial report as at and for the year ended 30 June 2007.

#### (d) Financial Risk Management

The Company's financial risk management objectives and policies are consistent with that disclosed in the financial report as at and for the year ended 30 June 2007.

## Notes to the interim financial statements (continued)

### 2 Issued capital and accumulated losses

#### (i) Issued and paid up capital

	31 Dec 2007	30 June 2007
143,501,764 ordinary shares fully paid	16,675,573	11,709,889

The following movements in ordinary shares were recorded from 1 July 2007:

	Number of shares	\$
Balance brought forward as at 1 July 2007	122,810,999	11,709,889
Options exercised for cash	17,946,768	4,486,692
Issue of shares for cash	2,743,997	685,999
Transaction costs	-	(207,008)
Balance carried forward as at 31 December 2007	<b>143,501,764</b>	<b>16,675,573</b>

#### (ii) Accumulated losses

	31 Dec 2007	30 June 2007
	\$	\$
Opening balance as at 1 July 2007 / 1 July 2006	(9,513,227)	(5,706,148)
Loss for the period	(2,297,203)	(3,888,673)
Share based compensation	15,666	81,594
Closing balance as at 31 December 2007 / 30 June 2007	<b>(11,794,764)</b>	<b>(9,513,227)</b>

#### (iii) Options

564,000 options to acquire ordinary shares were issued during the half year ended 31 December 2007 under and in accordance with the Phylogica Employee Share Option Plan (ESOP). One third vested on the grant date and one third of the remainder will vest on each of the next two anniversaries of issue, subject to the optionholders remaining employees.

No options to acquire ordinary shares were issued to directors during the half year ended 31 December 2007.

Total number of options on issue as at 31 December 2007 is 7,734,000:

<u>Description</u>	<u>Options on Issue</u>	<u>Expiry Date</u>	<u>Exercise Price</u>
Unquoted Options	6,650,000	30 June 2010	\$0.25 ea
Unquoted Options	520,000	30 June 2010	\$0.30 ea
Unquoted Options	564,000	31 July 2010	\$0.30 ea

## Notes to the interim financial statements (continued)

### 3 Income tax expense/benefit

The company was not eligible for the research and development tax rebate for the half year ended 31 December 2007 because its expenditure exceeded the eligibility threshold.

Deferred tax assets have not been recognised as at 31 December 2007 because, at this stage of the Company's development, it cannot be considered as probable that future taxable profit will be available against which the Company can utilise the benefits.

### 4 Property, plant and equipment

#### Acquisitions and disposals

During the six months ended 31 December 2007, the Company acquired assets with a cost of \$83,305 (six months ended 31 December 2006: \$30,546).

### 5 Segment information

The Company comprises a single business segment comprising discovery and development of novel therapeutics and a single geographical location being Australia. The segment details are therefore fully reflected in the results and balances reported in the interim income and balance sheet statements.

### 6 Events subsequent to balance date

Subsequent to the interim balance sheet and up to the date of this report, there has not arisen any item, transaction or event of a material and unusual nature likely, in the opinion of the directors of the Company, to affect significantly the operations of the Company, the results of those operations, or the state of the affairs of the Company in future financial years.

### 7 Contingent liabilities and contingent assets

There are no known significant liabilities or contingent assets as at the date of this report.

### 8 Earnings per share

#### Basic earnings per share

The calculation of basic earnings per share for the six months ended 31 December 2007 was based on the loss attributable to ordinary shareholders of \$2,297,203 (six months ended 31 December 2006: \$1,754,838) and a weighted average number of ordinary shares outstanding during the six months ended 31 December 2007 of 136,382,237 (six months ended 31 December 2006: 110,890,264), calculated as follows:

## Notes to the interim financial statements (continued)

### (i) Profit attributable to ordinary shareholders

	<b>31 Dec 2007</b>	31 Dec 2006
Loss for the period:	<b>\$</b>	<b>\$</b>
Basic earnings	<b>(2,297,203)</b>	(1,754,838)

### (ii) Weighted average number of ordinary shares

Number of ordinary shares	<b>122,810,999</b>	108,572,271
Effect of shares issued	<b>13,571,238</b>	2,317,993
Weighted average number of ordinary shares at 31 December 2007	<b>136,382,237</b>	110,890,264

## 9 Employee Benefits

### (i) Details of total employee benefits as at balance sheet date

	<b>31 Dec 2007</b>	30 June 2007
	<b>\$</b>	<b>\$</b>
<b>Current</b>		
Liability for annual leave	<b>90,353</b>	80,051
Incentive provision	-	166,236
<b>Non Current</b>		
Liability for long service leave	<b>7,820</b>	11,208
Total employee benefits	<b>98,173</b>	257,495

### (ii) Share-based payments

In 2005 the Company established a employee share option programme (ESOP) that entitles key management personnel and senior employees to purchase shares in the Company. The terms and conditions of the share option programme are disclosed in the ESOP rules approved by the General Meeting of shareholders held in November 2006. During the six months ended 31 December 2007, 564,000 options were granted under the ESOP.

The terms and conditions of the grants made during the six months ended 31 December 2007 are as follows:

Grant date	Number of instruments	Vesting conditions	Contractual life of options
Option grant at 23 November 2007	450,000	Two years of service	2.69 years
Option grant at 23 November 2007	84,000	Two years of service	2.69 years
Option grant at 23 November 2007	30,000	Two years of service	2.69 years

### (iii) Fair value of share options and assumptions for the six months ended 31 December 2007:

Number of Options	Grant Date	Expiry Date	Fair Value Per Option	Exercise Price	Price of Shares on grant date	Risk Free Interest Rate (%)	Estimated Volatility (%)	Number Vested at 31/12/07
450,000	23 Nov 07	31 Jul 10	\$0.015	\$0.30	\$0.18	6.44	30	150,000
84,000	23 Nov 07	31 Jul 10	\$0.015	\$0.30	\$0.18	6.44	30	28,000
30,000	23 Nov 07	31 Jul 10	\$0.015	\$0.30	\$0.18	6.44	30	10,000

## Notes to the interim financial statements (continued)

188,000 options vested immediately and of the remaining two thirds vest equally on the two subsequent anniversaries of grant.

The basis of measuring fair value is consistent with that disclosed in the financial report as at and for the year ended 30 June 2007.

### 10 Key management personnel expense

Key management personnel receive compensation in the form of short-term employee benefits, post-employment benefits and equity compensation benefits. Key management personnel received total compensation of \$711,059 for the six months ended 31 December 2007 (six months ended 31 Dec 2006: \$536,187). Total remuneration is included in share based payment expense, administration expenses, research and development expenses and other operating expenses in the income statement.

### 11 Related parties

Arrangements with related parties continue to be in place. For details of these arrangements, refer to the 30 June 2007 annual financial report.

## Directors' declaration

In the opinion of the directors of Phylogica Limited (the Company)

1. the financial statements and notes set out on pages 4 to 12 are in accordance with the Corporations Act 2001 including:
  - (a) giving a true and fair view of the financial position of the Company as at 31 December 2007 and of its performance, as represented by the results of its operations and cash flows for the half-year ended on that date; and
  - (b) complying with Australian Accounting Standard AASB 134 *Interim Financial Reporting* and the Corporations Regulations 2001; and
2. there are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable.

Signed in accordance with a resolution of the directors:



Harry Karelis  
*Director*

Perth  
26 February 2008



## **Independent auditor's review report to the members of Phylogica Limited**

### **Report on the financial report**

We have reviewed the accompanying interim financial report of Phylogica Limited, which comprises the interim balance sheet as at 31 December 2007, income statement, statement of changes in equity and cash flow statement for the half-year ended on that date, a description of accounting policies and other explanatory notes 1 to 11 and the directors' declaration at the half-year's end or from time to time during the half-year.

#### *Directors' responsibility for the financial report*

The directors of the Company are responsible for the preparation and fair presentation of the interim financial report in accordance with Australian Accounting Standard AASB 134 *Interim Financial Reporting* and the *Corporations Act 2001*. This responsibility includes establishing and maintaining internal control relevant to the preparation and fair presentation of the interim financial report that is free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

#### *Auditor's responsibility*

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 an Interim 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 Company's financial position as at 31 December 2007 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 Phylogica Limited, ASRE 2410 requires that we comply with the ethical requirements relevant to the audit of the annual financial report.

A review of a 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.

#### *Conclusion*

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 Phylogica Limited is not in accordance with the *Corporations Act 2001*, including:

- (a) giving a true and fair view of the Company's financial position as at 31 December 2007 and of its performance for the half-year ended on that date; and



- (b) complying with Australian Accounting Standard AASB 134 *Interim Financial Reporting* and the Corporations Regulations 2001.

KPMG

KPMG

A handwritten signature in blue ink, appearing to be 'T R Hart', written in a cursive style.

T R Hart  
*Partner*

Perth  
26 February 2008