

discovery

human health

Mycobacterium phlei

innovation

technology

bladder cancer

hyaluronans

food safety

prostate cancer

animal health

MCC

apoptosis

vaccines

2005

After six months, the Board of Directors and management of Bioniche Life Sciences understand that this will not be a year without its challenges, but we continue to make progress toward important milestones.

In the meantime, the Company continues to be recognized by peers in the industry. Most recently, the Ottawa Life Sciences Council selected Bioniche as one of Canada's top 10 life science companies. The Top 10 companies were selected from a pool of entrants by a jury of senior venture capitalists from across the U.S. and Canada. The quality investment and partnership opportunities were a key factor in their selection. The award was presented at BioNorth 2004, Canada's international biotechnology and life sciences conference and exhibition in Ottawa in November, 2004.

Bioniche continues to demonstrate its innovation. A recent example is the approval by the U.S. Department of Agriculture (USDA) to market our proprietary product, *SETTLE*TM, for the treatment of equine endometritis caused by *Streptococcus zooepidemicus*. This is a product that was developed from our core Mycobacterial Cell Wall technology, the same basic technology that was first utilized as an immunomodulator/anticancer product for animals and has since been developed into our proprietary bladder cancer product for humans (Mycobacterial Cell Wall-DNA Complex — MCC). MCC has now been utilized in a small study on advanced canine cancers with significant success. The talented research and development team at Bioniche are not satisfied to simply look at a technology for a single purpose. Instead, they continue to explore new applications, while ensuring the protection and long-term value of the technology by way of patents.

Our list of approved patents grew in this quarter with the addition of three new patents (one in the U.S. and two in Europe) for our Mycobacterial Cell Wall-DNA Complex (MCC). Bioniche makes a significant investment in patent protection each year. This ensures that we will be well-protected in key therapeutic areas and will be able to provide the best possible return on our research and development investment.

Technology	No. of Patent Applications	No. of Patents Issued or in EP Validation Stage	Total No. of Patents and Applications
MCC	35	62	97
MCWE	12	26	38
ODN	63	0	63
Hyaluronan	7	50	57
Botanical	6	0	6
Reproductive	6	7	13
Total	129	145	274

It takes pharmaceutical products an average of 10 to 12 years of development and testing before they are ready to be licensed. The process of review and approval by regulators can take another 618 days in Canada and 510 days in the U.S. on average.¹

Great rewards can be obtained by staying involved with products through to their end point, yet this requires significant patience on the part of everyone — both inside and outside the Company. The highly-regulated world in which we operate helps to ensure that pharmaceutical products are of the highest quality and efficacy when they reach the market. At the same time, regulators present us, on a routine basis, with hurdles that cause delays in reaching the end points. We try to be realistic in our timelines, yet we cannot always anticipate these regulatory challenges.

It should be noted that very few Canadian biotechnology companies have to date successfully taken a product from inception to marketplace. Instead, many establish partnerships with large pharmaceutical companies to take a product through the manufacturing process development, final clinical development, and commercialization. By retaining ownership and control of our products through to late stage, when marketing or distribution deals might be considered, Bioniche retains the greatest possible return for investors.

Our state-of-the-art, fully validated MCC manufacturing facility in Montreal, Quebec, Canada is manufacturing both the raw material and the final dosage form of *Urocidin* for the Phase III clinical trial and the commercial product that will follow its registration. We are committed to completing the development of this product ourselves, turning to external partners for marketing and/or distribution support at the appropriate time.

The investment community continues to show its support of, and confidence in, Bioniche. The latest evidence of this occurred in late October, 2004, with the announcement of \$12 million in financing by the Fonds de Solidarité des Travailleurs du Québec ("FSTQ") and the Bio-Food Investment Fund. The FSTQ has invested \$10 million in the development of the MCC bladder cancer program, while the Bio-Food Investment Fund has invested \$2 million for animal health applications of the same technology. These are key business areas for the Company.

Bladder Cancer Phase III Clinical Trial with *Urocidin*

The skilled clinical development team at Bioniche Therapeutics has been diligently working with expert urologists internationally to finalize the Phase III pivotal trial protocol for *Urocidin* in the treatment of bladder cancer. Our staff are liaising with regulatory authorities to finalize the details of the protocol prior to formal submission of a Special Protocol Assessment and Investigational New Drug (IND) application.

This trial will involve patients in both North America and Europe and, therefore, the protocol must be approved by regulatory agencies on both continents (Health Canada, the U.S. Food and Drug Administration (FDA), and the European Medicines Agency (EMA)).

The Phase III clinical trial will use *Urocidin* in direct comparison with the current standard treatment — Bacille Calmette-Guérin (BCG) — for the treatment of high-risk, superficial bladder cancer.

The \$10 million investment by the FSTQ will be used to partially finance the Phase III clinical trial. Bioniche is engaged in discussions with potential marketing partners who would participate in funding the trial in return for an opportunity to share in the revenues of the commercialized product.

E. coli O157:H7 Food Safety Vaccine

As discussed earlier, there can be regulatory challenges in the process of bringing a product to market. A good example is our *E. coli* O157:H7 cattle vaccine. The Canadian Food Inspection Agency (CFIA) — the Canadian regulatory authority responsible for licensing the vaccine — recently asked us to provide additional safety data after reviewing data we submitted in 2003. The Veterinary Biologics Section of the CFIA, after consultations with Health Canada, expressed concerns about potential health risks associated with accidental injection of the vaccine into the administrator.

In order to provide the requested data to the CFIA, Bioniche will be conducting an additional animal safety study. We are committed to ensuring the safety of our vaccine before it reaches the market, and we are working diligently with the regulators to ensure their satisfaction with every aspect of this product. The vaccine has consistently shown efficacy and safety in North American field and challenge studies involving approximately 20,000 head of cattle over three consecutive years.

¹ Patient Pathways — www.canadapharma.org

In the meantime, our two Natural Science and Engineering Research Canada (NSERC)/Bioniche Industrial Research Chairs in vaccines to reduce food and water contamination have been hard at work at the University of Saskatchewan. Dr. Andy Potter (Senior Chair) and Dr. Wolfgang Köster (Associate Chair) were officially appointed in October, 2004. Beyond the *E. coli* O157:H7 vaccine, they are investigating vaccines to combat such infectious diseases as *Salmonella enteritidis*, *Campylobacter jejuni*, and *Cryptosporidium parvum*.

Second Quarter Financial Results

The Company's consolidated revenues for the second quarter of fiscal year 2005 decreased by 24% over the same period last year, reaching \$10.2 million as compared to \$13.5 million. For the first six months of the year, consolidated revenues are down 13% compared to the same period in fiscal 2004. The downturn came primarily from the Company's total Human Health division, which suffered a year-to-date decline of 20% in sales as compared to the same period in fiscal 2004. This can be attributed to softening sales in both the Osteoarthritis and the Specialty Pharmaceutical areas, where increased competition in terms of pricing and the delays in market launch of a key product factored into our results.

Revenues from the Company's proprietary urological product — *Cystistat* — almost doubled in the first six months of fiscal 2005 as compared to the same period last year. Sales of *Cystistat* reached \$1.9 million at December 31, 2004. *Cystistat* is a treatment that provides relief from the symptoms of multiple forms of cystitis, including interstitial, bacterial, and radiation-induced cystitis. It is a sterile sodium hyaluronan solution that serves as a temporary replacement of the glycosaminoglycan (GAG) layer in the bladder.

On the Animal Health side of our business, we have experienced a year-to-date decline in revenues of 6% over last year, primarily involving our reproductive products in Canada. Our Canadian animal health product sales continue to feel the adverse affect of the Bovine Spongiform Encephalopathy (BSE — "mad cow") crisis. The beef industry estimates its losses due to the crisis at more than \$11 million for each day that the U.S. border remains closed to exports.² As key suppliers to the industry, we are feeling the affects of the beef producers' reduced income. We are working diligently to offset this downturn by pursuing new markets for our products, including China and Europe. China, in particular, is a growing economy where there is governmental interest in increasing the number of beef and dairy cattle. This bodes well for the Company's cattle reproductive products.

Activities of Note in the Quarter

Animal Health Leadership Changes

In December, we announced the move of our Managing Director, Australian/Asian Animal Health operations to Europe. Andrew Grant is leading the launch of *Folltropin-V*, in Europe, in addition to promoting sales of other Bioniche Animal Health products.

Andrew has been replaced in Australia by Chris O'Callaghan — General Manager for the Australia/Asia Animal Health operations effective January 4, 2005. Mr. O'Callaghan has ten years of experience in sales and management with the agricultural and animal health industries in Australia. He has a Masters degree in Marketing from Monash University and a B.Agr.Sc. from La Trobe University.

New Animal Health Product Launched

As mentioned earlier in this letter, our new animal health product, *SETTLE*TM was officially launched at the Conference of the American Association of Equine Practitioners in Denver, Colorado, in December 2004. Bioniche received approval from the U.S. Department of Agriculture (USDA) to market this product, for the treatment of equine endometritis caused by *Streptococcus zooepidemicus* in November 2004. We intend to register this product in other jurisdictions as well.

SETTLE has been clinically proven as a fast-acting, specific endometritis therapy for broodmares. It is the end result of clinical research conducted over a period of five breeding seasons. Endometritis is a non-life threatening disease that affects 25% to 40% of broodmares worldwide. The disease results in low conception rates or loss of pregnancies if conception occurs.

Animal Reproduction Newsletter

The Bioniche Animal Health Division produced an Animal Reproduction newsletter earlier this winter that was widely distributed to food animal and equine reproduction practitioners worldwide. The newsletter includes information about trends in global consumption of livestock products; current technology related to reproduction and embryo transfer; expert opinions about Bioniche products; and a feature about the Bioniche contribution to the survival of endangered species.

There are approximately 110 animal species classified as "endangered" in Australia. Bioniche Animal Health A/Asia Pty., based in Armidale, New South Wales, has contributed financially to the University of Sydney's Assisted Reproductive Technology (ART) course, where veterinary science students are learning about artificial insemination, embryo transfer, and related technologies. One ART initiative supported by Bioniche involves 113 Northern Hairy-Nosed Wombats, Queensland's most endangered mammal. Research staff are using traditional cattle breeding methods of superovulation and embryo transfer to increase the number of wombat offspring from the breeding-age females.

Continued Product Development

Bioniche's Human Health Pharma Division received approval in November 2004 for an Abbreviated New Drug Application (ANDA) from the U.S. Food and Drug Administration (FDA) for *Sotradecol* Injection (Sodium Tetradecyl Sulfate Injection) for the treatment of varicose veins. The product is being manufactured at our Galway, Ireland facility and will soon be available in the U.S.

Ongoing Research with Proprietary Technology

In November 2004, Bioniche researchers presented further positive data demonstrating the unique anticancer activity profile of MCC for the treatment of bladder — the 47th scientific presentation showing the unique profile of this technology. The data was presented at the 98th Annual Meeting of l'Association Française d'Urologie (AFU), held in Paris, France. The results demonstrated MCC's ability to induce urinary cytokines and apoptotic markers following intravesical administration to patients with bladder cancer. The urinary cytokine profile induced by intravesical treatment with MCC reinforces its distinctiveness from BCG (as evidenced also in our clinical trials to date). BCG is the recognized standard therapy for the treatment of human bladder cancer.

Looking Ahead

Our Board of Directors and management are always considering ways in which to streamline our business activities to optimize the return to our shareholders. Given the scope of our areas of strategic focus, this is not a simple task. We are confident in the abilities of our highly skilled employees at all levels to bring our business objectives to fruition this fiscal year and beyond.



Graeme McRae
President & CEO
Bioniche Life Sciences Inc.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITIONS AND RESULTS FROM OPERATIONS

The following discussion and analysis is the responsibility of management. It should be read in conjunction with the accompanying consolidated financial statements and associated notes. The discussion in this report contains forward-looking statements that involve risks and uncertainties, such as statements of the Company's plans, objectives, expectations, and intentions. The cautionary statements made in this report should be read as applying to all related forward-looking statements wherever they appear. The Company's actual results could differ materially from those discussed here. Factors that could cause or contribute to these differences include those discussed in the "Annual Report for fiscal 2004". All amounts are in Canadian dollars unless otherwise indicated.

OVERVIEW

Bioniche is a research-based, technology-driven Canadian biopharmaceutical company that discovers, develops, manufactures, and markets proprietary products for human and animal health markets worldwide. The fully-integrated Company employs approximately 300 people and has four reportable segments: Bioniche Animal Health, Bioniche Food Safety, Bioniche Therapeutics, and Bioniche Pharma (the two latter segments fall under the Company's Human Health division). Corporate headquarters are located in Belleville, Ontario, Canada, with research, manufacturing, and marketing/sales facilities in Belleville, Ontario, Canada; Montréal, Québec, Canada; Armidale, New South Wales, Australia; Athens, Georgia, U.S.A.; Pullman, Washington, U.S.A.; and Galway, Republic of Ireland.

Bioniche has an expanded global presence and a portfolio of products and technologies in development that promise to have a profound impact on the converging world of human and animal health. Effective therapies for bladder cancer and potentially other cancers; a cattle vaccine to help prevent *E. coli* O157:H7 contamination of food and water; technologies to improve livestock reproduction; and technologies that could replace the use of antibiotics in livestock: these are the key areas of strategic focus for Bioniche.

HIGHLIGHTS FOR THE SECOND QUARTER

The Company reported several operating highlights in the course of its second fiscal quarter. These events and highlights are summarized as follows:

- On November 29th, the Company announced receiving the approval from the U.S. Department of Agriculture (USDA) to market its proprietary product, *SETTLE*(TM), for the treatment of Equine Endometritis caused by *Streptococcus zooepidemicus*. This new treatment for Equine Endometritis is now being made available to U.S. equine veterinarians. It is the Company's intention to register this product in other jurisdictions as well.

- On November 22nd, the Company announced that it received approval for an Abbreviated New Drug Application (ANDA) from the U.S. Food and Drug Administration (FDA) for *Sotradecol* Injection (Sodium Injection) for the treatment of varicose veins.
- On November 3rd, the Company completed an equity financing of \$10,000,000 with the Fonds de Solidarité des Travailleurs du Québec ("FSTQ") and \$2,000,000 with the Fonds d'investissement Bioalimentaire, sec ("Fonds Bio"). The financing consists of a private placement offering of 12,000,000 newly created Series 2 preferred shares to FSTQ and Fonds Bio for a subscription price of \$12,000,000. Proceeds from this financing are to be used for the development of the bladder cancer program with the Company's proprietary technology — Mycobacterial Cell Wall — DNA complex (MCC), *E. coli* O157:H7 vaccine development, and for other animal health applications of the same technology. More financial disclosure is presented under Note 2[c] in the financial statements.

THREE-MONTH PERIOD ENDED DECEMBER 31, 2004 COMPARED TO THE SAME PERIOD ENDED DECEMBER 31, 2003

The Company experienced a soft quarter in terms of consolidated revenues for both its Animal and Human Health divisions. For the first time, the Company is reporting lower revenues both quarterly and for the first six months of fiscal 2005 as compared to previous periods (first quarter of fiscal 2005 and first six months of fiscal 2004).

In previous reporting, the Company has discussed the negative impact on its Canadian animal health business caused by the Bovine Spongiform Encephalopathy (BSE — "mad cow") crisis, and the negative foreign currency impact caused by the sharp increase of the Canadian dollar. This quarter, the Company is also facing: worldwide competition that has negatively impacted the Osteoarthritis and Specialty Pharmaceutical businesses of Bioniche Pharma, resulting in price erosion, and delays in government approvals. More information on the quarterly and six month revenue variances can be found below.

REVENUES

The Company's consolidated revenues for the second quarter of fiscal year 2005 reached \$10.2 million as compared to \$13.5 million for the same quarter of fiscal year 2004, a decrease of \$3.3 million, or 24%. Adjusted for currency fluctuations, revenues for the second quarter of fiscal year 2005 would have reached \$10.9 million, for a net decrease of 19% as compared to fiscal 2004.

Total consolidated revenues for the six months ending December 31, 2004 were \$20.4 million. This compares to \$23.3 million reported in the same period last year, a decrease of \$2.9 million, or 13%. Adjusted for currency fluctuations, revenues for the six months ending December 31, 2004 would have reached \$21.4 million, for a net decrease of 8% compared to December 31, 2003.

REVENUES BY REPORTING SEGMENT

(number in millions & % variation over 2004)

	2005				2004	
	Q2		YTD		Q2	YTD
	\$	%	\$	%	\$	\$
Animal Health	5.6	-15%	11.5	-6%	6.6	12.2
Food Safety	—		—		—	—
Human Health – Pharma	3.7	-39%	7.0	-30%	6.1	10.0
Human Health – Therapeutics	0.9	13%	1.9	73%	0.8	1.1
Total Revenues	10.2	-24%	20.4	-13%	13.5	23.3

This decrease in consolidated revenues are mainly attributable to the Company's Human Health division.

In the Animal Health division, the declines in total revenues of \$1.0 million for the second quarter and \$0.7 million for the first six months of the fiscal year were due directly to the BSE situation in Canada.

In the Human Health division, the declines in total revenues of \$2.3 million for the second quarter and \$2.2 million for the first six months of the fiscal year are mostly attributable to the Osteoarthritis and Specialty Pharmaceutical areas of Bioniche Pharma.

Revenues from the Company's proprietary urological product — *Cystistat* — doubled in the first six months of 2005 as compared to the same period last year. Sales of *Cystistat* reached \$2.0 million at December 31, 2004. *Cystistat* is a treatment that provides relief from the symptoms of multiple forms of cystitis, including interstitial, bacterial, and radiation-induced cystitis. It is a sterile sodium hyaluronan solution that serves as a temporary replacement of the glycosaminoglycan (GAG) layer in the bladder.

More explanation regarding revenues can be found in the section entitled, "Areas of Market Focus" below.

The Company's revenues have historically been softer in the first two quarters of the fiscal year due to the seasonality of the business. Therefore, the results of operations for the three and six months ended December 31, 2004 are not necessarily indicative of annual results.

The Company has four reportable segments, described in Note 3 of the financial statements. These are: Bioniche Animal Health, Bioniche Food Safety, Bioniche Therapeutics, and Bioniche Pharma (the two latter segments fall under the Company's Human Health division).

The Company's revenues are primarily derived from a number of products sold under the areas of market focus shown in the following chart:

REVENUES FROM SPECIFIC AREAS OF MARKET FOCUS

(expressed in millions of Canadian dollars and % variation over 2004)

	2005				2004	
	Q2		YTD		Q2	YTD
	\$	%	\$	%	\$	\$
Human Health						
Bioniche Therapeutics						
Urology	0.9	13%	1.9	73%	0.8	1.1
Bioniche Pharma						
Osteoarthritis	2.5	-26%	3.8	-31%	3.4	5.5
Specialty Pharmaceutical (ANDA)	0.5	-58%	1.7	-19%	1.2	2.1
	3.9	-28%	7.4	-15%	5.4	8.7
Animal Health						
Reproduction	3.9	-17%	7.5	-10%	4.7	8.3
Immune Stimulants	0.9	13%	1.6	7%	0.8	1.5
Osteoarthritis	0.1	9%	0.3	50%	0.1	0.2
	4.9	-13%	9.4	-6%	5.6	10.0
Food Safety	—		—		—	—
Revenues from Areas of Market Focus	8.8	-20%	16.8	-10%	11.0	18.7
% of Total Sales	86%		82%		82%	80%
Others	1.4	-44%	3.6	-22%	2.5	4.6
Total Revenues	10.2	-24%	20.4	-13%	13.5	23.3

The revenues derived from the Company's specific areas of market focus for the second quarter comprised 86% of total revenues and, for the first six months comprised 82% of total revenues, showing an increase over the same periods last year and reflecting the Company's continuing focus on these areas. The remaining revenues were derived from non-branded generic human and animal health product sales, included above under the heading "Others".

The declines in both the second quarter and the first six months of fiscal 2005 — 20% and 10% respectively — in areas of market focus are less dramatic than the declines of 44% and 22% respectively under "Others".

The steeper decline of "Others" is a result of reduced sales of various non-branded human and animal generic products.

HUMAN HEALTH DIVISION

Bioniche Pharma: Bioniche Pharma's products are classified under the following categories: Osteoarthritis, Specialty Pharmaceutical, and other non-branded generics.

Osteoarthritis

Suplasyn is the Company's main product in this category. The sales of *Suplasyn* reached \$3.8 million for the first half of fiscal 2005, compared with \$5.5 million for the same period in 2004. The 31% revenue decrease is attributable primarily to competitive pricing in our largest marketplace — Germany. *Suplasyn* is a sterile, sodium hyaluronan solution injected into synovial joints such as the knee to replace or augment synovial fluid, the naturally occurring lubricant in the joints. *Suplasyn* is now recognized as one of the leading hyaluronan products in Europe.

In the third quarter of fiscal 2005, the Company plans to launch a new dosage formula of *Suplasyn* — *SuplasynMD* — in most countries in Europe. *SuplasynMD* targets smaller human joints. The Company believes this will help differentiate Bioniche from the competition and improve the brand's profitability.

Specialty Pharmaceutical (ANDA)

Over the past four years, the Bioniche Pharma business unit has evolved into a Specialty Pharmaceutical company, identifying niche segments, and developing and obtaining product approvals for promising Specialty Pharmaceutical products. The Company files the Abbreviated New Drug Applications (ANDAs), and manufactures and markets the products after approval.

At the end of December 2004, eight products were approved by the U.S. Food and Drug Administration (FDA), generating sales of \$1.7 million for the first half of fiscal 2005, compared with \$2.1 million for the same period in 2004, a decrease of 19%. This decrease is attributed for the most part to sales of *Amiodorone* that were stronger in the first half of last year following its market launch.

At this time, the Company is not forecasting any gains in its sterile injectables business for fiscal 2005 due primarily to delays experienced with new ANDA approvals and launches, as well as price and volume erosion on a specific product. The Company is currently finalizing production of its new ANDA *Sotradecol* Injection (Sodium Tetradecyl Sulfate Injection) for the treatment of varicose veins, announced this quarter.

Bioniche Therapeutics: Revenues from sales of the Company's Urology product are reported under Bioniche Therapeutics.

Urology

Cystistat is currently the Company's only product in this category. The sales of *Cystistat* reached \$1.9 million for the first half of fiscal 2005, compared with \$1.1 million in the same period last year due to increased sales volume. *Cystistat* is a treatment that provides relief from the symptoms of multiple forms of cystitis, including interstitial, bacterial, and radiation-induced cystitis. *Cystistat* is a sterile sodium hyaluronan solution that serves as a temporary replacement of the glycosaminoglycan (GAG) layer in the bladder.

Building core expertise in the Urology field is one of the Company's key priorities. During 2005, the Company will continue to develop its own Canadian sales force, while maintaining a network of distributors elsewhere in the world. By doing so, the Company will experience increased margins and establish key contacts within the Urology field, which will also help advance the Company's key R&D platform (MCC — *Urocidin*) for use in bladder cancer. The Company expects current product sales in the Urology sector to continue to increase in 2005 compared to 2004, due to further expansion of its direct sales force and increased market acceptance of *Cystistat*.

ANIMAL HEALTH DIVISION

The Company's Canadian animal health product sales continue to feel the adverse affect of the Bovine Spongiform Encephalopathy (BSE — "mad cow") crisis. The BSE impact for the Company accounts for a loss of approximately \$0.7 million in sales from 2003 fiscal sales levels.

The Animal Health business experienced an additional decrease in Canadian sales of \$1.0 million, or 25%, for the first half of fiscal 2005 as compared to the same period last year. Over and above the impact of the BSE crisis, the Company experienced a loss of \$0.9 million due to the expiry of the Canadian distribution rights to *CIDR*[™], a reproductive product. The Company has acquired the *Cue-Mate* device to replace the *CIDR* product. *Cue-Mate* is currently registered in Australia and New Zealand, and the Company has a strategy to expand registrations of this product in the future.

Fortunately, Bioniche Animal Health U.S.A. sales are continuing to grow, recording an increase of \$0.5 million, or 9%, for the first half of fiscal 2005 over the same period last year, despite the strengthening of the Canadian currency. The acquisition of the AB Technology product line has provided increased sales of \$0.7 million for the first half of fiscal 2005 over the same period last year. The Australian and European Animal Health operations recorded little variation as compared with the previous period end. Animal Health export sales are down \$0.6 million over last year due to decreased demand from China.

The Company expects its current product sales in the animal health market to show growth in the U.S., Australia, Europe, and China in the next six months. Animal Health sales are not expected to increase in Canada until the ban on beef exports associated with the BSE crisis is lifted. European animal health sales are expected to grow as a result of new product registrations.

Reproduction Products

The Company's Animal Health division has developed the original proprietary platforms and expertise employed today. Over the years, Bioniche Animal Health has achieved a significant leadership presence in the livestock reproduction segment. Revenues from animal health reproduction products were \$7.5 million for the six months ending Dec. 31, 2004 as compared with \$8.3 million in the same period last year. In 2004, the Company made two important strategic acquisitions to complement its reproductive franchise. Gross sales contribution from these newly-acquired products was \$1.3 million in the first half of fiscal 2005.

The Company's Animal Health team is working diligently to offset the revenue downturn in Canada by pursuing new markets for its reproductive products, including China and Europe. China, in particular, is a growing economy where there is governmental interest in increasing the number of beef and dairy cattle. This bodes well for sales of the Company's bovine reproductive products. Subsequent to the quarter, the

Company announced the launch of its *Folltropin*^{®-V} embryo transfer technology in additional European Union (EU) countries — specifically, in the United Kingdom, the Netherlands, and Spain. Registrations will be sought in other EU countries as well. The product was already being sold in Ireland.

At the same time, Canadian product lines are being diversified. The latest market offering is for the swine industry — the use of *Pregnecol*, a superovulatory gonadotropin, and *Lutropin-V*, a purified lutenizing hormone for induction of ovulation. *Pregnecol* stimulates the ovary to develop follicles and *Lutropin-V* stimulates the release of ova from the follicles. Together, these products narrow the ovulation window and make the timing of ovulation specific and predictable. This increases conception rates in sows and reduces the time and cost involved for breeders. Research studies conducted in Canada and Brazil using this product combination resulted in an 89% pregnancy rate with a single, timed insemination.

Immune Stimulant Products

A core research focus of the Company is the area of immune stimulants, particularly how they can offer an alternative to the use of antibiotics in livestock. At the end of December, 2004, the Company had a total of five products sold in this category, generating \$1.7 million in revenue, compared with \$1.5 million in revenue for the same period last year.

As well, during the second quarter, the Company launched *SETTLE*[™] in the United States for the treatment of Equine Endometritis caused by *Streptococcus zooepidemicus*. This product, developed from the Company's Mycobacterial Cell Wall technology, has been clinically proven as a fast-acting, specific endometritis therapy for broodmares. It is the end result of clinical research conducted over a period of five breeding seasons.

Osteoarthritis Products

This is the first quarter in which the Company has reported its Animal Health Osteoarthritis products as an area of market focus. Bioniche Animal Health markets its proprietary product, *Enhance*[®], for intra-articular injection in horses in Australia and New Zealand. *Enhance*[®] is used to treat synovitis and/or osteoarthritis. It is a sterile sodium hyaluronate solution, obtained from a selective fermentation source using a manufacturing process that is free from thermal degrading effects. It is manufactured at the facility in Galway, Ireland.

FOOD SAFETY DIVISION

E. coli O157:H7 Cattle Vaccine

No revenues are reported for the first quarter of fiscal 2005. However, upon registration of the *E. coli* O157:H7 vaccine, we anticipate revenues to grow quickly after product introduction. The first target market is Canada, followed by the United States and Europe.

OTHER NON-BRANDED GENERIC PRODUCTS

The Company experienced a decline of 44% in second quarter sales of non-branded human and animal generic products as compared to the same quarter last year. For the fiscal year-to-date, this decline was 20% compared to fiscal 2004.

COSTS OF GOODS SOLD AND GROSS PROFIT

Gross profit was \$5.7 million, or 56%, on sales of \$10.2 million this quarter compared to \$7.6 million, or 56%, on sales of \$13.5 million in the same period last year. In the first six months of fiscal 2005, gross profit reached \$11.2 million, or 55%, on sales of \$ 20.4 million as compared to \$12.9 million, or 55%, on sales of \$23.3 million in the same period last year. Overall, gross profit margins were maintained by sales of high margin products such as *Cystistat*, which contributed to offset the negative impact of the strengthening of the Canadian dollar.

The Company expects future gross margins to deteriorate if the strengthening of the Canadian dollar continues. New product approvals and pending applications are anticipated to contribute higher margins than the current average.

OPERATING EXPENSES

Total operating expenses were \$7.9 million for the second quarter of fiscal 2005, compared with \$7.1 million for the same period in 2004. For the first six months of fiscal 2005, total operating expenses were \$15.1 million after six months, compared with \$13.7 million excluding the one time gain on debt settlement for the same period in 2004. The increase of \$1.4 million came primarily in the areas of sales, marketing, and quality assurance. This relates to the Company's increasing efforts to expand market potential for its products through expanded product registrations and entry into new global markets, including the AB Technology and *Cue-Mate* product lines.

The Company expects selling, general, and administrative expenses to increase proportionally in 2005 compared to 2004 due to its continuing investment in global commercial operations, as well as higher sales and marketing costs to distribute its products in global markets. This investment in building a multinational infrastructure is in line with the Company's business plan, which focuses on commercializing the Company's own proprietary technologies to maximize returns.

(expressed in millions of Canadian dollars & % of revenue)

	Operating Expenses					
	2005			2004		
	Q2	YTD		Q2	YTD	
	\$	\$	%	\$	\$	%
Revenues	10.2	20.4	100%	13.5	23.3	100%
Administration	2.3	4.2	21%	2.3	4.1	18%
Marketing and selling	2.3	4.5	22%	2.1	4.0	17%
Quality Assurance	0.9	1.9	9%	0.8	1.6	7%
Sub total	5.5	10.6	52%	5.2	9.7	42%
Non cash items						
Share ownership and bonus	0.2	0.4	2%	0.2	0.4	2%
Amortization	0.8	1.5	7%	0.6	1.3	5%
Imputed Interest expense						
on convertible debentures	0.3	0.5	3%	0.2	0.5	2%
Sub total	1.3	2.4	12%	1.0	2.2	9%
Other Items						
Interest	0.6	1.2	6%	0.7	1.4	6%
Gain on Debt Settlement	—	—	0%	—	(1.7)	-8%
Foreign Exchange loss	0.5	0.9	4%	0.2	0.4	2%
Sub total	1.1	2.1	10%	0.9	0.1	0%
Total Operating Expenses	7.9	15.1	74%	7.1	12.0	51%

EBITDA BEFORE RESEARCH & DEVELOPMENT

(expressed in millions of Canadian dollars)

	2005		2004	
	Q2	YTD	Q2	YTD
Human Health – Pharma	(1.0)	(2.2)	1.1	0.9
Human Health – Therapeutics	0.5	1.1	0.4	0.5
Animal Health	0.5	1.2	0.7	1.5
Food Safety	—	—	—	—
EBITDA* before Research and Development	(0.0)	0.1	2.2	2.9

*EBITDA means earnings before interest, taxes, depreciation, and amortization. For more information, please refer to the section, "Non-GAAP & Other Measures" below.

EBITDA before Research and Development was break even for the second quarter of fiscal 2005 compared with \$2.2 million for the same period in 2004. The decrease of \$2.2 million came primarily from the Bioniche Pharma division, more specifically, in the areas of Osteoarthritis and Specialty Pharmaceutical. As well, economic factors such as the strengthening of the Canadian currency and the Canadian BSE situation affecting the Animal Health division contributed to this decline in profitability before Research and Development.

RESEARCH & DEVELOPMENT

Gross research and development expenses were \$3.2 million for the second quarter of fiscal 2005, compared with \$3.0 million for the same period in 2004. Looking at the first six months of fiscal 2005, total gross research and development expenses were \$6.5 million compared with \$5.8 million for the same period in 2004. This increase of \$0.7 million reflects higher investment into the Food Safety division. Key expenditures during this period include \$0.2 million in support of the Industrial Research Chairs at the University of Saskatchewan, along with continuing *E. coli* O157:H7 vaccine clinical trials.

The Company expects research and development expenses to increase during the remainder of 2005 due to an anticipated increase in clinical activity related to the start of the Phase III clinical trial with Mycobacterial Cell Wall-DNA complex (MCC) for bladder cancer. The future level of research and development expenditures will depend upon, among other things, the outcome of clinical testing of current products under development, delays or changes in government-required testing and approval procedures, technological and competitive developments, strategic marketing decisions, and availability of funds.

RESEARCH & DEVELOPMENT EXPENDITURES

(expressed in millions of Canadian dollars)

	Key Areas					
	2005			2004		
	Q2	YTD		Q2	YTD	
	\$	\$	%	\$	\$	%
Animal Health	0.6	1.3	20%	0.6	1.1	19%
Food Safety	0.3	0.7	11%	0.2	0.2	3%
Human Health – Therapeutics	2.1	4.1	63%	2.0	3.8	66%
Human Health – Pharma	0.2	0.4	6%	0.2	0.7	12%
Research and Development, Gross	3.2	6.5	100%	3.0	5.8	100%

RESULTS OF OPERATIONS

The Company's net loss for the second quarter of fiscal 2005 was \$4.9 million, or (\$0.14) per share, compared with \$2.2 million, or (\$0.07) per share, for the same period in 2004. For the first six months of fiscal 2005, total net loss was \$9.6 million, or (\$0.27) per share, compared with \$4.3 million, or (\$0.14) per share, for the same period in 2004.

The current loss is due partly to the substantial ongoing investment in research and development, predominantly in the area of bladder cancer, as the Company prepares for its upcoming Phase III clinical trial with MCC (*Urocidin*) as well as further clinical studies related to its *E. coli* O157:H7 cattle vaccine. The increase in net loss over last year is also due to the one-time gain recorded last year of \$1.7 million resulting from the settlement of the long-term debt. In addition, the Company also expanded its operational base in preparation for anticipated market growth as new technologies come to market.

LIQUIDITY, FINANCING, AND CAPITAL RESOURCES

As of December 31, 2004, the Company's consolidated cash and cash equivalents were \$13.4 million, of which the Bioniche Pharma business unit held \$4.5 million. This \$4.5 million is to be used to directly develop the Bioniche Pharma business. Working capital at December 31, 2004 and December 31, 2003 was \$23.7 million and \$12.5 million respectively.

The cash flow used in operations (before change in non-cash working capital balances related to operations) was \$6.6 million for the six months ended December 31, 2004. This represents a burn rate* of approximately \$1.1 million per month on average. This is a significant increase from \$3.2 million for the six-month period ended December 31, 2003 and can be attributed to the Company's revenue decrease and modest investment in marketing activities. As a result, the Company does not anticipate having positive cash flows from operations in 2005.

The Company believes that it will be able to continue to support its current corporate objectives, including research and clinical development programs in both animal and human health, by obtaining long-term equity capital as required. In the event that such resources are not forthcoming, corporate objectives will be revisited accordingly.

* Burn rate means cash flow used in operations. For more information, please refer to the section, "Non-GAAP Measures" below.

Quarterly Variation from Previously Reported Commitments

In February 2004, the Company acquired the net assets of AB Technology Inc., an American veterinary product company in Pullman, Washington, U.S.A. which is a leader in the development of embryo transfer media, materials, and equipment for the bovine and equine markets. As part of the acquisition, the Company paid monthly installments totaling \$4 million (or \$32 million USD) for the six-month period ending December 31, 2004. A balance of \$1.13 million (or \$1.11 million USD) remains payable under the terms of the agreement, in two equal monthly installments.

On March 29, 2004, the Company acquired from Pfizer Inc. the intellectual property and other assets of the *Cue-Mate* business, an innovative livestock reproductive technology. At the end of December, 2004, the Company is obligated to pay the balance of the purchase price of \$361,000 (or \$300,000 USD) to Pfizer Inc.

On May 20, 2004, Bioniche Pharma Group Limited entered into a financing agreement with the Bank of Ireland for the purchase and building of an expanded facility in Galway, Ireland for the manufacture of pharmaceutical injectable products. During the quarter, the Company drew 3.1 million Euro (\$5.1 million CDN) against Facilities 1 and 2 with the Bank of Ireland, bringing the total drawn at December 31, 2004 to 6.7 million Euro (\$10.9 million CDN).

On November 3, 2004 the Company completed a financing totaling \$12,000,000 with the Fonds de Solidarité des Travailleurs du Québec (FSTQ) and with the Fonds d'investissement Bioalimentaire (Fonds Bio). The financing consists of a private placement offering of 12,000,000 newly created Series 2 preferred shares to FSTQ and Fonds Bio. These preferred shares can convert into common shares over a period of five years according to a predefined formula. For more financial disclosure, please see Note 2[c] in the financial statements.

OUTSTANDING SHARE DATA

The Company has total common shares outstanding at February 8, 2005 of 36,124,918 and 12,000,000 Series 2 Preferred Shares. In addition, the Company has 3,506,250 outstanding warrants and 2,910,001 outstanding options, exchangeable for one common shares upon exercise. Outstanding conversion rights on convertible debentures are exchangeable for no more than 8.9 million common shares. The Company also has a commitment to issue warrants to Technology Partnerships Canada (TPC).

NON-GAAP MEASURES

The following measures included in the report do not have a standardized meaning under Canadian Generally Accepted Accounting Principles (GAAP) and, therefore, are unlikely to be comparable to similar measures presented by other companies:

EBITDA

“EBITDA” means “Earnings Before Interest, Taxes, Depreciation, and Amortization”. The Company considers EBITDA to be an effective measure of each segment’s contribution to the Company on an operational basis, before allocating the cost of income taxes and capital investments. It is management’s understanding that this measure is used by analysts and shareholders to evaluate the Company’s operations.

Burn Rate

“Burn Rate” means “cash flow used in operations”. This information can be found in the Consolidated Statements of Cash Flows under “Operating Activities”. It shows the cash flow used in operations (before change in non-cash working capital balances related to operations).

RISKS AND UNCERTAINTIES

Early Stage Development

Several of the Company’s products or processes are at an early stage of development. A commitment of substantial time and resources is required to conduct research and clinical trials if the Company is to complete the development of any product or process for commercialization. It is not known whether any of these product or process candidates will meet applicable health regulatory standards and obtain required

regulatory approvals, whether such products or processes can be produced in commercial quantities at reasonable costs and be successfully marketed, or if the Company’s investment in any such product or process candidate will be recovered through sales or royalties.

Government Regulations

The manufacture and sale of animal and human therapeutic products is governed by numerous statutes and regulations in the United States, Canada, Ireland, and other countries where the Company sells or intends to market its products. The subject matter of such legislation includes approval of manufacturing facilities, controlled research and testing procedures, review and approval of manufacturing, pre-clinical and clinical data prior to marketing approval, including adherence to good manufacturing practices (GMP) during production and storage, and regulation or marketing activities, notably advertising and labelling.

The products and procedures to be developed by the Company require lengthy development, pre-clinical and clinical testing, and investment of significant funds prior to their commercialization. There can be no assurance that any such products will actually reach the marketplace. The process of completing clinical testing and obtaining required approvals is likely to take several years and require the expenditure of substantial resources. Furthermore, there can be no assurance that the regulators will not require modification to any submissions that may result in delays or failure to obtain regulatory approvals. Any delay or failure to obtain regulatory approval could adversely affect the ability of the Company to utilize its technology, thereby adversely affecting operations. Further, there can be no assurance that the Company’s product candidates will prove to be safe and effective in clinical trials, or that they will receive the requisite regulatory approval. Foreign markets, other than the United States and Canada, impose similar restrictions.

Key Personnel

The Company’s success is also dependent upon its ability to attract and retain a highly-qualified work force, and to establish and maintain close relations with research centres. Competition is intense and the Company’s success will depend, to a great extent, on its senior executive, scientific staff, and collaborators. The loss of key personnel could compromise the timing and ultimate success of product development.

Foreign Currency Risk

The Company operates internationally, therefore, a substantial portion of revenues and expenses is translated in Canadian dollars. The Company’s exposure to exchange rate fluctuation is reduced by the Company’s revenues dominated in currencies other than Canadian dollars matched by a corresponding amount of cost denominated in the same currency.

Volatility of Share Prices

Share prices are subject to change due to numerous factors related to business activity, including reports of new information, changes in the Company's financial situation, the sale of shares in the market, the Company's failure to obtain results in line with the expectations of analysts, or an announcement by the Company or any of its competitors concerning technological innovation. During the past few years, shares of Bioniche Life Sciences Inc., other biopharmaceutical companies, and the investment market in general have been subjected to extreme fluctuations that were unrelated to the operational results of the companies affected. There is no guarantee that the market price of Company shares will be protected from any such fluctuations in the future.

Intellectual Property Infringement Claims

Third parties may claim that we infringe on their intellectual property. Any such claims, with or without merit, could materially harm our business and operating results.

Government Incentives and Contracts

The Company relies, in part, on government incentives and contracts to fund its research and development program as well as to expand its facilities. Such incentives are subject to interpretation and estimation as to their presentation in the financial statements; however, they are subject to the terms and conditions of the various agreements and the continuing support of the government agencies. It is not possible to guarantee that the terms and conditions will not be changed or interpreted in a different manner that could have a material impact on the financial position of the Company. One such program, which provides material financial assistance to the Company's research and development program, is currently subject to a government audit.

FORWARD-LOOKING STATEMENTS

This discussion and analysis contains certain forward-looking statements that are subject to risks and uncertainties that may cause the results or events predicted in this document to differ materially from actual results or events. No assurance can be given that results, performance, or achievement expressed in, or implied by, forward-looking statements within this disclosure will occur, or, if they do, that any benefit may be derived from them.

Additional information relating to the Company, including the Annual Information Form (AIF), is available on SEDAR at www.sedar.com.



Patrick Montpetit, CA
 Vice-President, and Chief Financial Officer
 February 8, 2005

Bioniche Life Sciences Inc.
 Amalgamated under the laws of Ontario

CONSOLIDATED BALANCE SHEETS

	<i>Unaudited</i> As at Dec. 31 2004 \$	<i>Unaudited</i> As at Dec. 31 2003 \$	<i>Unaudited</i> As at June 30 2004 \$
ASSETS			
Current			
Cash and cash equivalents	13,397,654	4,583,666	8,245,118
Accounts receivable	11,823,751	11,122,603	16,582,146
Inventories	11,654,864	12,093,820	11,059,212
Prepaid expenses and deposits	881,309	498,881	590,028
	37,757,578	28,298,970	36,476,504
Long-term			
Capital assets	31,713,991	17,492,220	23,548,199
Goodwill	5,553,798	5,553,798	5,553,798
Intangible assets, net	11,231,360	11,719,602	11,672,718
Deferred financing fees, net	1,316,882	1,552,647	1,485,624
Other assets – deferred costs	576,000	—	576,000
	88,149,609	64,617,237	79,312,843
LIABILITIES AND SHAREHOLDERS' EQUITY			
Current			
Accounts payable and accrued liabilities	12,292,032	13,906,199	15,063,137
Income taxes payable	710,013	811,881	833,443
Current portion of senior and other long-term debt <i>[note 4]</i>	1,029,088	1,098,919	1,510,666
	14,031,133	15,816,999	17,407,246
Long-term			
Senior debt <i>[note 4]</i>	13,677,279	3,571,531	6,933,854
Other long-term debt	22,779,633	20,032,747	22,339,900
Deferred government incentives	6,020,497	2,860,910	4,131,237
Future income taxes	387,000	374,000	387,000
	56,895,542	42,656,187	51,199,237
Non-controlling interest	3,032,396	3,939,121	3,079,640
Commitments and contingencies <i>[note 5]</i>			
Shareholders' equity			
Share capital <i>[note 2]</i>	69,964,120	49,097,155	57,666,956
Other paid-in capital <i>[note 2]</i>	3,773,836	1,340,247	3,310,345
Deficit	(46,701,503)	(33,591,523)	(37,123,268)
Cumulative translation amount	1,185,218	1,176,050	1,179,933
	28,221,671	18,021,929	25,033,966
	88,149,609	64,617,237	79,312,843

See accompanying notes

Bioniche Life Sciences Inc.

CONSOLIDATED STATEMENTS OF LOSS

For the three and six months ended December 31

	Unaudited Current Quarter 2004 \$	Unaudited Last Year Quarter 2003 \$	Unaudited Current Year to Date 2004 \$	Unaudited Last Year Year to Date 2003 \$
REVENUE				
Sales	10,232,417	13,476,677	20,364,270	23,273,723
Cost of sales	4,526,099	5,890,323	9,158,539	10,323,803
Gross profit	5,706,318	7,586,354	11,205,731	12,949,920
OPERATING EXPENSES				
Administration	2,281,107	2,297,376	4,255,843	4,121,156
Marketing and selling	2,357,236	2,085,513	4,520,499	3,980,557
Quality assurance	868,833	827,996	1,860,846	1,631,822
Interest	618,074	702,876	1,240,538	1,373,428
Imputed interest expense on convertible debentures	242,633	168,379	468,085	516,454
Share ownership and bonus – operating	214,182	211,260	430,023	368,568
Amortization	773,454	656,277	1,471,005	1,341,435
Gain on debt settlement	—	—	—	(1,744,835)
Foreign exchange loss	510,888	203,304	838,203	392,811
	7,866,407	7,152,981	15,085,042	11,981,396
Income (loss) before research and development	(2,160,089)	433,373	(3,879,311)	968,524
Research and development expenses, gross	(3,158,007)	(2,978,613)	(6,451,725)	(5,828,304)
Less government incentives	354,989	681,033	690,677	942,330
Loss before income taxes	(4,963,107)	(1,864,207)	(9,640,359)	(3,917,450)
Income tax (expense) recovery				
Current	72,970	(313,700)	14,970	(388,700)
Future	—	—	—	25,000
	72,970	(313,700)	14,970	(363,700)
	(4,890,137)	(2,177,907)	(9,625,389)	(4,281,150)
Non-controlling interest	26,914	—	47,154	—
Net loss for the period	(4,863,223)	(2,177,907)	(9,578,235)	(4,281,150)
Basic and fully diluted net loss per share	(0.14)	(0.07)	(0.27)	(0.14)

See accompanying notes

Bioniche Life Sciences Inc.

CONSOLIDATED STATEMENTS OF DEFICIT

For the three and six months ended December 31

	Unaudited Current Quarter 2004 \$	Unaudited Last Year Quarter 2003 \$	Unaudited Current Year to Date 2004 \$	Unaudited Last Year Year to Date 2003 \$
Balance, beginning of period	(41,838,280)	(31,413,616)	(37,123,268)	(30,936,563)
Settlement of convertible debentures	—	—	—	1,626,190
Net loss for the period	(4,863,223)	(2,177,907)	(9,578,235)	(4,281,150)
Balance, end of period	(46,701,503)	(33,591,523)	(46,701,503)	(33,591,523)

See accompanying notes

Bioniche Life Sciences Inc.

CONSOLIDATED STATEMENTS OF CASH FLOWS

For the three and six months ended December 31

	<i>Unaudited Current Quarter 2004 \$</i>	<i>Unaudited Last Year Quarter 2003 \$</i>	<i>Unaudited Current Year to Date 2004 \$</i>	<i>Unaudited Last Year Year to Date 2003 \$</i>
OPERATING ACTIVITIES				
Net loss for the period	(4,863,223)	(2,177,907)	(9,578,235)	(4,281,150)
Add (deduct) non-cash items:				
Amortization	773,454	656,277	1,471,005	1,341,435
Non-cash interest expense	242,633	168,379	468,085	516,454
Foreign exchange	—	(121,805)	—	(12,024)
Share and option compensation	126,492	82,000	132,836	110,000
Non-controlling interest	(26,914)	—	(47,154)	—
Non-cash bonus	284,000	350,000	673,000	660,482
Employee share ownership plan	145,225	118,271	279,967	232,945
Dividends on preferred shares	23,224	7,877	44,803	15,714
Gain on debt settlement	—	—	—	(1,744,835)
Future tax recovery	—	—	—	(25,000)
Cash flow used in operations	(3,295,109)	(916,908)	(6,555,693)	(3,185,979)
Net changes in non-cash working capital balances related to operations	(790,127)	667,363	1,996,025	1,041,607
Cash used in operating activities	(4,085,236)	(249,545)	(4,559,668)	(2,144,372)
INVESTMENT ACTIVITIES				
Acquisition of net assets	—	(45,150)	—	(45,150)
Payment on balance of acquisitions	(806,560)	—	(1,019,163)	—
Government incentives received on account of capital assets	—	9,400	6,458	18,462
Purchase of capital assets	(5,522,589)	(1,718,712)	(9,058,353)	(2,456,877)
Cash used in investing activities	(6,329,149)	(1,754,462)	(10,071,058)	(2,483,565)

Bioniche Life Sciences Inc.

CONSOLIDATED STATEMENTS OF CASH FLOWS *CONTINUED*

	<i>Unaudited Current Quarter 2004 \$</i>	<i>Unaudited Last Year Quarter 2003 \$</i>	<i>Unaudited Current Year to Date 2004 \$</i>	<i>Unaudited Last Year Year to Date 2003 \$</i>
FINANCING ACTIVITIES				
Proceeds of senior debt	5,132,184	298,495	6,620,464	298,495
Common shares issued, net	—	(17,734)	—	(17,734)
Preferred shares issued, net	11,674,854	—	11,674,854	—
Financing fees – debt	30,886	(119,658)	(20,968)	(239,376)
Proceeds on debenture loans	—	—	—	9,450,000
Increase in deferred government incentives	1,759,927	164,401	1,954,446	332,111
Repayment of long-term debt	(247,558)	(264,044)	(495,001)	(10,932,534)
Cash provided by (used in) financing activities	18,350,293	61,460	19,733,795	(1,109,038)
Effect of foreign currency translation	310,902	369,210	49,467	472,231
Net increase (decrease) in cash during the period	8,246,810	(1,573,337)	5,152,536	(5,264,744)
Cash, beginning of period	5,150,844	6,157,003	8,245,118	9,848,410
Cash, end of period	13,397,654	4,583,666	13,397,654	4,583,666

See accompanying notes

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Unaudited — December 31, 2004

1. SIGNIFICANT ACCOUNTING POLICIES

These interim financial statements do not contain all disclosures required by Canadian generally accepted accounting principles for annual financial statements and, accordingly, these financial statements should be read in conjunction with the most recently prepared annual financial statements for the year ended June 30, 2004. These unaudited interim consolidated financial statements follow the same accounting policies and methods of their application as outlined in the most recent annual consolidated financial statements.

Business is typically weaker in the first two quarters of the Company's fiscal year. Consequently, due to the seasonality of the business, the results of operations for the three and six months ended December 31, 2004 are not necessarily indicative of annual results.

2. SHARE CAPITAL AND OTHER PAID-IN CAPITAL

Issued share capital consists of:

	December 2004	December 2003	June 2004
	\$	\$	\$
Preferred shares — Series 1 – 167 [June 2004 – 167]	161,000	161,000	161,000
Preferred shares — Series 2 [c] — 12,000,000 [June 2004 – Nil]	11,674,854	—	—
Common shares — 36,066,349 [June 2004 – 35,681,029]	58,128,266	48,936,155	57,505,956
	69,964,120	49,097,155	57,666,956

At December 31, 2004 the Company has issued 180,875 shares under the employee share ownership plan in the current fiscal year valued at \$278,168, of which \$45,450 relates to the accrued balance at June 30, 2004 included in Other paid-in capital. In addition, the Company has issued 49,413 shares to directors in lieu of payment of fees, valued at \$84,000 and issued 155,032 shares under the share bonus plan (a).

Other paid-in capital consists of:

	December 2004	December 2003	June 2004
	\$	\$	\$
Accrued share bonus [a]	834,038	835,055	421,181
Accrued employee share ownership plan	47,248	40,842	45,450
Warrants	1,570,714	436,350	1,570,714
Accrued warrants	1,200,000	—	1,200,000
Options [b]	121,836	28,000	73,000
	3,773,836	1,340,247	3,310,345

(a) Share Bonus

The Company has accrued an estimated bonus of \$673,000 in the current fiscal year for all of its eligible employees which is expected to be settled by issuing the Company's common shares subsequent to the year

end. At December 31, 2004 the Company issued 155,032 shares in settlement of a portion of last years estimated bonus, valued at \$260,142. The balance of the share bonus at June 30, 2004 will be satisfied by the issuance of an additional 81,000 common shares based on management's estimate.

(b) Options

During the current fiscal year, 420,000 stock options were granted at \$1.58 per share, 954,500 stock options were granted at \$4.40 per share and 15,000 stock options were granted at \$1.68 per share to employees and directors. Under the Company's share option plan, options may be granted with an exercise price not less than the market price on the date of the grant. The fair value of these 1,389,500 stock options, determined using the fair value method, was \$742,125. These options will be expensed over the vesting period. The amount of compensation expense in the current quarter is \$42,492 [2003 – nil] and year to date is \$48,836 [2003 – \$28,000].

The following weighted average assumptions were used to determine the fair value of these options: risk-free interest rate of 3.75%, expected dividend yield of 0%, average expected volatility of 0.566 and expected option life of three and five years resulting in a weighted fair value per option of \$0.534. The Company uses the Black-Scholes model to calculate the fair value of options awarded.

(c) Preferred Shares - Series 2

On November 3, 2004 the Company issued 12,000,000 shares of Series 2 convertible preferred stock for gross consideration of \$12,000,000. The proceeds are to be used for the Phase III clinical trial with MCC for the treatment of bladder cancer, MCC for animal health applications, and the *E. coli* O157:H7 vaccine development. The Series 2 preferred shares are convertible at the option of the holder into common shares for five years plus one day at a conversion ratio which is obtained by dividing the fully-accreted value by the applicable conversion price as follows: 25% at \$1.45; 50% at \$2.50; and 25% at \$3.75. The fully-accreted value is calculated as the aggregate subscription price of the preferred shares plus 6% per annum until the earlier of conversion or five years from the date of issuance. Costs of completion for this private placement, estimated at approximately \$325,000, were netted against the share capital of the Series 2 preferred shares.

After the initial five-year plus one-day term, any Series 2 preferred shares outstanding are convertible, at the option of the holder, into common shares at the fully accreted value divided by the average market price of the common shares less the greater of 5% or the maximum discount permitted by the Toronto Stock Exchange (subject to the issuance of a maximum of 8,910,000 common shares in the aggregate on conversion of all Series 2 preferred shares).

If the trading price of the common shares exceeds \$13.50 for 60 consecutive days, the Company may require the holders to convert the preferred shares into common shares at the conversion ratio applicable on the date of conversion.

The preferred shares have voting rights on the basis of the number of common shares that the holder would have if the preferred shares were converted into common shares on the date of the applicable shareholders' meeting.

3. SEGMENTED FINANCIAL INFORMATION

The Company's four reportable segments: Pharma, Animal Health, Therapeutics, and Food Safety are strategic business units that offer different products and require different technology and marketing strategies. The manufacturing operations for both the Pharma and Therapeutics segments are carried out at the plant in Galway, Ireland.

The accounting policies of the segments are the same as those described in the summary of significant accounting policies in note 2 of the annual consolidated financial statements for the year ended June 30, 2004. The Company accounts for inter-segment sales on a cost plus basis.

The Company evaluates performance and allocates resources based on profit or loss from operations before interest, income taxes, depreciation, and amortization.

Current Quarter December, 2004

	Human		Animal	Food	Total
	Pharma	Therapeutics	Health	Safety	
Sales	3,657,118	932,817	5,642,482	—	10,232,417
Cost of sales	2,154,636	93,954	2,277,509	—	4,526,099
Operating expenses	2,512,326	373,296	2,835,736	—	5,721,358
EBITDA before Research and Development	(1,009,844)	465,567	529,237	—	(15,040)
Research and					
Development expenses	196,443	2,101,062	581,467	279,035	3,158,007
Less Government Incentives	—	(284,093)	(31,684)	(39,212)	(354,989)
Net Research and Development expenses	196,443	1,816,969	549,783	239,823	2,803,018
Interest expense, net	389,087	376,245	95,375	—	860,707
Amortization expense	252,778	298,090	216,906	5,680	773,454
Foreign exchange (gain) loss					510,888
Gain on settlement of debt					—
Segment income (loss) before taxes and non-controlling interest	(1,848,152)	(2,025,737)	(332,827)	(245,503)	(4,963,107)
Inter-segment sales	916,831	1,132	—	—	917,963

Last Year Quarter December, 2003

	Human		Animal	Food	Total
	Pharma	Therapeutics	Health	Safety	
Sales	6,078,723	750,470	6,647,484	—	13,476,677
Cost of sales	2,494,706	74,257	3,321,360	—	5,890,323
Operating expenses	2,468,728	275,464	2,677,953	—	5,422,145
EBITDA before Research and Development	1,115,289	400,749	648,171	—	2,164,209
Research and					
Development expenses	208,301	2,029,993	571,349	168,970	2,978,613
Less Government Incentives	(190,100)	(361,775)	(12,796)	(116,362)	(681,033)
Net Research and Development expenses	18,201	1,668,218	558,553	52,608	2,297,580
Interest expense, net	285,177	465,524	120,554	—	871,255
Amortization expense	259,276	276,294	117,944	2,763	656,277
Foreign exchange (gain) loss					203,304
Gain on settlement of debt					—
Segment income (loss) before taxes and non-controlling interest	552,635	(2,009,287)	(148,880)	(55,371)	(1,864,207)
Inter-segment sales	843,249	—	3,658	—	846,907

Current Year to Date December, 2004

	Human		Animal	Food	Total
	Pharma	Therapeutics	Health	Safety	
Sales	6,926,449	1,941,775	11,496,046	—	20,364,270
Cost of sales	3,939,471	194,178	5,024,890	—	9,158,539
Operating expenses	5,201,952	639,130	5,226,129	—	11,067,211
EBITDA before Research and Development	(2,214,974)	1,108,467	1,245,027	—	138,520
Research and					
Development expenses	428,637	4,029,575	1,310,628	682,885	6,451,725
Less Government Incentives	—	(521,982)	(31,684)	(137,011)	(690,677)
Net Research and Development expenses	428,637	3,507,593	1,278,944	545,874	5,761,048
Interest expense, net	755,428	756,890	196,305	—	1,708,623
Amortization expense	453,389	587,218	419,978	10,420	1,471,005
Foreign exchange (gain) loss					838,203
Gain on settlement of debt					—
Segment income (loss) before taxes and non-controlling interest	(3,852,428)	(3,743,234)	(650,200)	(556,294)	(9,640,359)
Inter-segment sales	1,583,674	1,132	—	—	1,584,806

Last Year to Date December, 2003

	Human		Animal	Food	Total
	Pharma	Therapeutics	Health	Safety	
Sales	10,004,325	1,045,279	12,224,119	—	23,273,723
Cost of sales	4,309,384	104,528	5,909,891	—	10,323,803
Operating expenses	4,808,643	450,870	4,842,590	—	10,102,103
EBITDA before Research and Development	886,298	489,881	1,471,638	—	2,847,817
Research and					
Development expenses	723,561	3,775,301	1,130,450	198,992	5,828,304
Less Government Incentives	(190,100)	(598,519)	(12,796)	(140,915)	(942,330)
Net Research and Development expenses	533,461	3,176,782	1,117,654	58,077	4,885,974
Interest expense, net	560,247	1,049,185	280,450	—	1,889,882
Amortization expense	499,800	580,613	255,498	5,524	1,341,435
Foreign exchange (gain) loss					392,811
Gain on settlement of debt					(1,744,835)
Segment income (loss) before taxes and non-controlling interest	(707,210)	(4,316,699)	(181,964)	(63,601)	(3,917,450)
Inter-segment sales	1,944,696	—	3,658	—	1,948,354

4. SENIOR DEBT

The Company's affiliate, Bioniche Pharma Group Limited, entered into an interest rate swap agreement with the Bank of Ireland as contemplated in Facility 3 of their agreement in order to reduce the impact of fluctuating interest rates on this debt. Under the terms of this agreement, the Company is required within a reasonable period of time to exchange at least one-half of the outstanding floating rate debt under Facilities 1 and 2 of the loan agreement to a notional fixed interest rate of 5.315%. The swap agreement requires the periodic exchange of payments without the exchange of the notional principal amount on which the payments are based. The balance of this loan facility not subject to the swap agreement will be subject to a floating interest rate of Euribor plus 1.825% and 1.75% covering Facility 1 and 2 respectively.

The Company designates its interest rate swap agreements as hedges of the underlying debt. Interest expense on the debt is adjusted to include the payments made or received under the interest rate swaps. At December 31, 2004, the Company had a notional principal amount of 2,099,833 Euro (\$3,421,048 CDN) outstanding on the interest rate swap with a negative fair value of 70,223 Euro (\$114,407 CDN).

During the quarter, the Company drew 3,117,000 Euro (\$5,078,216 CDN) against Facilities 1 and 2 with the Bank of Ireland, bringing the total drawn at December 31, 2004 to 6,667,000 Euro (\$10,861,922 CDN). These facilities are for the purchase and building of an expanded facility in Galway, Ireland. Interest capitalized during the current fiscal year totals 188,699 Euro (CDN \$307,428).

In addition, the Company's affiliate in Australia agreed to repayment terms pursuant to a mortgage arrangement in regards to the \$547,185 AUS (\$514,572 CDN) loan facility. It will be repaid over a 15-year term with monthly principal and interest payments of \$5,295 AUS (\$4,979 CDN) and interest. Interest is variable and is calculated at the mortgage index rate as published by the bank.

5. COMMITMENTS AND CONTINGENCIES

On July 2, 2004, the Company initiated, as planned, the funding of the Industrial Research Chairs after the Vaccine & Infectious Disease Organization (VIDO), jointly with Natural Science and Engineering Research Canada (NSERC), confirmed two appointments for this role. Under this agreement, the Company receives the first commercial rights to new food safety vaccines to fight infectious diseases of animals, including Salmonella enteritidis, Campylobacter and Cryptosporidium parvum. The Company's financial commitment is \$200,000, payable at the beginning of each six-month period commencing July, 2004. At the end of December 2004, the Company has expensed \$200,000 in Research and Development.

The Company participates in research and development funding arrangements, some of which, based on management's best estimates, are recorded as a reduction in the related cost and some as a deferred government incentives obligation. The funding arrangements are subject to audit by the contributors and the Company was notified that it would be audited under the terms of one of its funding arrangements subsequent to the end of the second quarter. If there are any material adjustments required, they will be made in the period in which they are known.

7. COMPARATIVE AMOUNTS

Certain comparative figures have been reclassified to conform to the financial statement presentation adopted in the current year.

P.O. Box 1570
Belleville, Ontario
Canada, K8N 5J2

Tel: (613) 966-8058
Fax: (613) 966-4177

www.Bioniche.com

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