



synairgen plc

Interim Report 2006

Synairgen is a drug discovery company focused on identifying and out-licensing new pharmaceutical products which address the underlying causes of asthma and chronic obstructive pulmonary disease

Highlights

for the six months ended 31 December 2006

Financial highlights

- Turnover for the period: £54k (2005: £77k);
- Research and development expenditure for the period: £682k (2005: £494k);
- Retained loss for the period: £746k (2005: loss of £558k); and
- Net funds at 31 December 2006 of £6.7 million (2005: £8.2 million)

Operational highlights

- Phase I clinical trial of Interferon beta ('IFN β ') for asthma progressing in the clinic in line with expectations;
- Validation of *in vitro* data supporting use of IFN β in treatment of COPD complete;
- Exclusive rights to a novel peptide which inhibits IL-4 and IL-13 signalling in-licensed from the University of Southampton. Validation programme is underway;
- Development programme commenced for growth factor with potential for restoration of barrier function in asthma; and
- Collaboration with undisclosed North American biotechnology company extended.

Chairman's Statement

Introduction

The first six months of the financial year have seen considerable progress on all fronts.

We now have four valuable proprietary programmes underway as well as our proteomics pipeline technology and barrier function screening assay.

Candidate	Indication	Programme status		
		Lead Selection	Preclinical Development	Clinical Phase I
Interferon beta	Asthma			●
Interferon beta	COPD		●	
Growth Factor	Asthma		●	
IL-13R α 2 Peptide	Asthma	●		

During the period, we were delighted to introduce two new proprietary programmes to our research portfolio: a growth factor (borne out of the barrier function programme) and a novel peptide inhibitor of IL-4 and IL-13. Both of these programmes are focused exclusively on asthma.

The interferon beta ('IFN β ') programme for asthma has been progressed in the clinic and Synairgen has completed successful validation of the COPD data presented at the American Thoracic Society meeting in May 2006.

In addition, we have also extended the collaboration with our unnamed North American biotechnology research partner, and we maintain a dialogue with potential licensees for our programmes.

Operating Review

Proprietary programmes

IFN β for asthma

Synairgen's lead programme is the development of inhaled IFN β as a therapy to prevent and treat asthma exacerbations caused by the common cold. Our aim remains to progress the programme to a proof of concept Phase IIa clinical trial. During the period under review, we have continued our Phase I safety study in allergic individuals without asthma and the last volunteer was enrolled into the study on 6 February 2007. Our next study, the first in asthmatics, is anticipated to commence in the autumn.

Chairman's Statement - continued

IFN β for COPD

COPD patients consume approximately twice as much healthcare resource as asthma patients, primarily due to unplanned hospitalisations caused by exacerbations. Up to 60% of all COPD exacerbations are preceded by the common cold.

In May 2006, we presented preliminary data at the American Thoracic Society conference, indicating that IFN β may have a place in the treatment of COPD. During the period, these data have been validated, showing that the susceptibility of COPD epithelial cells to the common cold virus is between 10 and 100 times greater than cells from non-smoking healthy control subjects. The addition of low levels of IFN β to the COPD epithelial cell models was protective against the common cold virus.

The opportunity for IFN β in COPD is a very significant addition to the Company's portfolio as there have been relatively few successful developments for COPD, despite it being the fifth leading cause of death worldwide and a great consumer of healthcare resource. We are continuing to discuss the IFN β programme with potential out-licensing partners.

During the period, Synairgen in-licensed intellectual property from Imperial Innovations Ltd relating to the use of interferon lambda, which appears to function in a similar manner to IFN β .

Barrier Function - Growth Factors

One of Synairgen's pipeline platforms is borne out of an observation that the asthmatic epithelium is 'leaky' due to the poor formation of tight junction proteins between cells. This defect in barrier function may be a key contributor to asthma susceptibility to environmental insults enabling pro-inflammatory allergens, pollutants and viruses to penetrate through the epithelium to the underlying tissue. Synairgen uses this patented observation as a platform to test for products which might restore tight junction integrity in asthma. To date, we have identified two growth factors selective for epithelial cells that could be developed as potential therapies. We are reviewing manufacture and further development of one of these growth factors, with a view to commencing clinical studies during 2009.

'Natural' inhibitor of IL-4 and IL-13

As announced in November 2006, we have in-licensed exclusive rights to a novel peptide which mimics the body's own intracellular inhibition of IL-4 and IL-13 signalling. The peptide was discovered at the University of Southampton by Dr Allison Lynn Andrews, Dr John Holloway and Professor Donna Davies (a co-founder of Synairgen) and the in-licensing of this programme to Synairgen is another example of the strong collaborative relationship between Synairgen and the University. A number of large pharmaceutical and biotechnology companies are known to be developing therapies designed to counter the adverse

Chairman's Statement - continued

effects of these cytokines, which are considered central to the development of allergic asthma. Synairgen's peptide potentially has a number of advantages, such as being easier to manufacture, being deliverable by aerosol, and most importantly, the ability to inhibit both IL-4 and IL-13 signalling. In January 2007, we commenced a validation programme, which will take approximately six months.

Pipeline platform technology

Synairgen uses its *in vitro* models to screen for new compounds and targets which reverse poor barrier function in asthma. We also continue to make progress in our proteomics programme, where we have observed a number of secreted proteins which are altered at baseline in asthma. By focussing on secreted proteins we increase the relative drugability of the targets. These proteins will be identified during the next year and will be evaluated as drug targets for further development.

Collaborative programmes

Further to an interim analysis of data in the programme we were delighted to have extended the collaboration with our target discovery programme with our unnamed North American biotechnology partner.

Staff

During the period, we announced the appointment of Dr Phillip Monk from Cambridge Antibody Technology ('CAT') as Head of Bioscience Development. Phill was previously Director of the

Respiratory and Inflammation Biology group at CAT and led the scientific development of CAT-354, an anti-IL-13 antibody being developed for the treatment of severe asthma.

In addition to Phill's appointment, we continue to strengthen our research and clinical resource to meet the needs of our proprietary and collaborative programmes.

Financial Review

Profit and loss account

Revenue for the six months to 31 December 2006 was £54k (six months ended 31 December 2005: £77k) and was primarily generated from the extended discovery collaboration with our unidentified international biotechnology partner. The operating loss for the period was £1,011k (2005: loss of £756k). Research and development expenditure increased from £494k to £682k as the Company increased its number of proprietary research programmes to four. Our R&D expenditure will continue to increase further as we progress the IFN β programmes and scale up the level of activity on the growth factor and peptide projects. Other administrative costs increased from £325k to £368k. Interest receivable decreased from £198k to £174k on account of lower deposit balances. Following the receipt of our first research and development tax credit in respect of the year ended June 2005, a tax credit of £91k for the period (2005: £nil) has been accounted for. The retained loss was £746k (2005: loss of £558k) and the loss per share was 3.4p (2005: loss of 2.6p).

Chairman's Statement - continued

Balance sheet and cash flow

At 31 December 2006, net assets amounted to £7.1 million (31 December 2005: £8.3 million), including net funds of £6.7 million (2005: £8.2 million).

Cash outflow for the six months to 31 December 2006 was £746k (six months ended 31 December 2005: £438k), underpinned by the increase in operating loss from £756k to £1,011k.

Adoption of Financial Reporting Standard 20 ('FRS 20')

As of 1 July 2006, the Company has adopted FRS 20 "Share-based Payment" in place of UITF 17 "Employee Share Schemes". FRS 20 requires fair value accounting for options and LTIPs granted after 17 November 2002 which have not vested by 30 June 2006. In accordance with standard practice, prior period results are restated as if the standard had always been in force. For the period up to 30 June 2006 the additional charge booked to the Profit and Loss Account following the adoption of FRS 20 amounted to £41,000. The FRS 20 charge for the six months ended 31 December 2006 was £33,000.

Adoption of International Financial Reporting Standards ('IFRS')

The Company will adopt IFRS on 1 July 2007 and has commenced a project to facilitate conversion from UK GAAP. Disclosure will be made in the annual accounts of the likely impact of conversion.

Outlook

We have made great progress in our primary research and development programmes. We look forward to completing the first safety study of inhaled IFN β , and the commencement of the first study in asthma. We also anticipate progress relating to a lead growth factor compound, and the results of the IL-4 and IL-13 inhibiting experiments which validate the recently licensed peptide. We have focused on assembling a strong intellectual property portfolio in our core areas and we continue to discuss potentially attractive out-licensing opportunities.

Simon Shaw
Chairman

Unaudited Consolidated Profit and Loss Account

for the six months ended 31 December 2006

	Notes	Six months ended 31 December 2006 £000	Restated (See Note 1) Six months ended 31 December 2005 £000	Restated (See Note 1) Year ended 30 June 2006 £000
Turnover		54	77	82
Cost of sales		(15)	(14)	(15)
Gross profit		39	63	67
Administrative expenses				
Research and development expenditure		(682)	(494)	(1,083)
Other		(368)	(325)	(664)
Total		(1,050)	(819)	(1,747)
Operating loss		(1,011)	(756)	(1,680)
Interest receivable		174	198	376
Loss on ordinary activities before taxation		(837)	(558)	(1,304)
Tax on loss on ordinary activities	2	91	–	255
Loss on ordinary activities after taxation and retained loss for the period		(746)	(558)	(1,049)
Loss per ordinary share				
Basic and diluted loss per share (pence)	3	(3.44)p	(2.57)p	(4.84)p

All amounts relate to continuing activities. There were no other recognised gains and losses during any of the periods presented.

Unaudited Consolidated Balance Sheet

as at 31 December 2006

	Notes	31 December 2006 £000	Restated (See Note 1) 31 December 2005 £000	Restated (See Note 1) 30 June 2006 £000
Fixed assets				
Intangible assets		91	26	36
Tangible assets		143	157	157
		234	183	193
Current assets				
Stocks		85	88	68
Debtors		421	211	423
Investments: short-term deposits		6,624	8,165	7,464
Cash at bank and in hand		127	80	33
		7,257	8,544	7,988
Creditors: amounts falling due within one year		(359)	(421)	(334)
Net current assets		6,898	8,123	7,654
Total assets less current liabilities		7,132	8,306	7,847
Creditors: amounts falling due after more than one year		(8)	–	(10)
Net assets		7,124	8,306	7,837
Capital and reserves				
Called up share capital		217	217	217
Share premium account		8,903	8,903	8,903
Merger reserve		483	483	483
Share-based payment reserve		113	58	80
Profit and loss account		(2,592)	(1,355)	(1,846)
Shareholders' funds	4	7,124	8,306	7,837

Unaudited Consolidated Cash Flow Statement

for the six months ended 31 December 2006

	Notes	Six months ended 31 December 2006 £000	Six months ended 31 December 2005 £000	Year ended 30 June 2006 £000
Net cash outflow from operating activities	5	(940)	(621)	(1,530)
Returns on investments and servicing of finance				
Interest received		180	213	397
Taxation				
Research and development tax credit received		89	–	–
Capital expenditure and financial investment				
Purchase of intangible fixed assets		(59)	(6)	(17)
Purchase of tangible fixed assets		(14)	(24)	(35)
Net cash outflow from capital expenditure		(73)	(30)	(52)
Net cash outflow before management of liquid resources and financing		(744)	(438)	(1,185)
Management of liquid resources				
Decrease in short-term deposits		840	440	1,141
Financing				
Repayment of capital element of finance leases and hire purchase contracts		(2)	–	(1)
Increase/(Decrease) in cash in period	6	94	2	(45)

Notes to the Financial Statements

for the six months ended 31 December 2006

1. Basis of preparation

The accounting policies and presentation applied to half-yearly figures are consistent with those applied in the last published accounts except where the accounting policies and presentation are to be changed in the next annual financial statements (see below re FRS 20), in which case the new accounting policies and presentation are followed.

All AIM-quoted companies are required to implement Financial Reporting Standard (“FRS”) 20 “Share-based Payment” for accounting periods beginning on or after 1 January 2006. Adoption of FRS 20 supersedes UITF Abstract 17 (revised 2003) “Employee Share Schemes”, under which the Company had previously accounted for shares and share options awarded to employees. FRS 20 requires that options awards and awards made under the Company’s Long-Term Incentive Plan (“LTIP”) granted after 7 November 2002 which had not vested by 1 July 2006 be fair valued and charged to the profit and loss account over the period from grant to vesting. The Company has valued option awards using the Black-Scholes model and awards under the LTIP using the Stochastic model. In common with the implementation of all accounting standards, prior year results must be restated as if the accounting standard has always been in force. This change in accounting policy does not result in any change to the Profit and Loss charge for the six months ended 31 December 2006 (six months ended 31 December 2005: increase of £15,000; year ended 30 June 2006: increase of £8,000). Under UITF 17, the credit for the charge was taken to the Profit and Loss reserve and reported in the reconciliation of movements in shareholders’ funds. Under FRS 20 the credit for the charge is taken to the Share-based payment reserve. The restatement has no impact on net assets in the periods presented in these interim results.

The Interim Report was approved by the Board of Directors on 16 March 2007. The financial information for the six months ended 31 December 2006 is unaudited, but has been reviewed in accordance with Auditing Practices Board guidance by BDO Stoy Hayward LLP. The interim results do not constitute statutory financial statements within the meaning of Section 240(5) of the Companies Act 1985.

The comparatives for the full year ended 30 June 2006 are not the Company’s full statutory accounts for that year. A copy of the statutory accounts for that year has been delivered to the Registrar of Companies. The auditors’ report on those accounts was unqualified and did not contain a statement under section 237(2)-(3) of the Companies Act 1985.

2. Taxation

The credit of £91,000 represents an estimate of the research and development tax credit receivable in respect of the six months ended 31 December 2006.

Notes to the Financial Statements - continued

for the six months ended 31 December 2006

3. Loss per ordinary share

	Six months ended 31 December 2006	Restated Six months ended 31 December 2005	Restated Year ended 30 June 2006
Loss on ordinary activities after taxation (£000)	(746)	(558)	(1,049)
Weighted average number of ordinary shares in issue	21,692,308	21,692,308	21,692,308

The loss attributable to ordinary shareholders and weighted average number of ordinary shares for the purpose of calculating the diluted earnings per ordinary share are identical to those used for basic earnings per share. This is because the exercise of share options would have the effect of reducing the loss per ordinary share and is therefore not dilutive under the terms of Financial Reporting Standard 22.

4. Reconciliation of movements in shareholders' funds

	Share capital £000	Share premium account £000	Merger reserve £000	Share-based payment reserve £000	Profit and loss account £000	Shareholders' funds £000
At 30 June 2005 (as originally stated)	217	8,903	483	–	(763)	8,840
FRS 20 charge	–	–	–	34	(34)	–
At 30 June 2005 (restated)	217	8,903	483	34	(797)	8,840
Loss for the period (restated)	–	–	–	–	(558)	(558)
Reversal of FRS 20 charge	–	–	–	24	–	24
At 31 December 2005 (restated)	217	8,903	483	58	(1,355)	8,306
Loss for the period (restated)	–	–	–	–	(491)	(491)
Reversal of FRS 20 charge	–	–	–	22	–	22
At 30 June 2006 (restated)	217	8,903	483	80	(1,846)	7,837
Loss for the period	–	–	–	–	(746)	(746)
Reversal of FRS 20 charge	–	–	–	33	–	33
At 31 December 2006	217	8,903	483	113	(2,592)	7,124

Notes to the Financial Statements - continued

for the six months ended 31 December 2006

5. Reconciliation of operating loss to net cash outflow from operating activities

	Six months ended 31 December 2006 £000	Restated Six months ended 31 December 2005 £000	Restated Year ended 30 June 2006 £000
Operating loss	(1,011)	(756)	(1,680)
Depreciation & amortisation	32	22	48
FRS 20 charge	33	24	46
Increase in stocks	(17)	(33)	(13)
(Increase)/Decrease in debtors	(2)	99	136
Increase/(Decrease) in creditors	25	23	(67)
Net cash outflow from operating activities	(940)	(621)	(1,530)

6. Reconciliation of net cash flow to movement in net funds

	Six months ended 31 December 2006 £000	Six months ended 31 December 2005 £000	Year ended 30 June 2006 £000
Increase/(Decrease) in cash in period	94	2	(45)
Decrease in short-term deposits	(840)	(440)	(1,141)
Cash use to repay capital element of finance leases and hire purchase contracts	2	-	1
Change in net funds resulting from cash flows	(744)	(438)	(1,185)
New finance leases and hire purchase contracts	-	-	(14)
Movement in net funds	(744)	(438)	(1,199)
Net funds at start of period	7,484	8,683	8,683
Net funds at end of period	6,740	8,245	7,484

Independent Review Report to Synairgen plc

Introduction

We have been instructed by the company to review the financial information for the six months ended 31 December 2006 which comprises the unaudited group profit and loss account for the six months ended 31 December 2006, the unaudited group balance sheet as at 31 December 2006, the unaudited group cash flow statement for the six months ended 31 December 2006 and the related notes. We have read the other information contained in the interim report and considered whether it contains any apparent misstatements or material inconsistencies with the financial information.

Our report has been prepared in accordance with the terms of our engagement to assist the company in meeting the requirements of the rules of the London Stock Exchange for companies trading securities on the Alternative Investment Market and for no other purpose. No person is entitled to rely on this report unless such a person is a person entitled to rely upon this report by virtue of and for the purpose of our terms of engagement or has been expressly authorised to do so by our prior written consent. Save as above, we do not accept responsibility for this report to any other person or for any other purpose and we hereby expressly disclaim any and all such liability.

Directors' responsibilities

The interim report, including the financial information contained therein, is the responsibility of, and has been approved by the directors. The directors are responsible for preparing the interim report in accordance with the rules of the London Stock Exchange for companies trading securities on the Alternative Investment Market which require that the half-yearly report be presented and prepared in a form consistent with that which will be adopted in the company's annual accounts having regard to the accounting standards applicable to such annual accounts.

Review work performed

We conducted our review in accordance with guidance contained in Bulletin 1999/4 issued by the Auditing Practices Board for use in the United Kingdom by auditors of fully listed companies. A review consists principally of making enquiries of management and applying analytical procedures to the financial information and underlying financial data and based thereon, assessing whether the accounting policies and presentation have been consistently applied unless otherwise disclosed. A review excludes audit procedures such as tests of controls and verification of assets, liabilities and transactions. It is substantially less in scope than an audit performed in accordance with International Standards on Auditing (United Kingdom and Ireland) and therefore provides a lower level of assurance than an audit. Accordingly we do not express an audit opinion on the financial information.

Review conclusion

On the basis of our review we are not aware of any material modifications that should be made to the financial information as presented for the six months ended 31 December 2006.

BDO Stoy Hayward LLP
Chartered Accountants
Southampton
16 March 2007



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