



Message to shareholders,

August 15, 2002

We are pleased to submit this report on the activities of the Company during the second quarter ended June 30, 2002, an important period during which Procyon further solidified its position scientifically and clinically, as well as financially.

During the quarter, two major milestones were achieved, one dealing with the bought deal financing and the other with the reporting of Phase II results of the Canadian clinical study for our scar treatment product FIBROSTAT[®]. As reported previously, we were able to successfully complete a \$10 million equity financing in May in spite of relatively poor market conditions which worsened subsequently. This financing, underwritten by a syndicate of Dundee Securities Corporation and Research Capital Corporation as co-leads and including Yorkton Securities Inc. and Desjardins Securities Inc., was predominantly institutional and we were very pleased that several prominent Canadian institutions participated. The proceeds of the financing, together with the Company's existing cash reserves, will ensure stability of financial resources for the next 2 years to enable us to move forward expeditiously with the clinical programs in our cancer technologies. We also expect the Company's cash resources to facilitate the acquisition of new and synergistic cancer technologies.

In June, we announced the results of the multi-center Canadian Phase II trial for FIBROSTAT[®]. While the "placebo" effect was found to be higher than expected, we were able to show clearly the safety of the product as well as the appropriate dose for future clinical studies. The safety of FIBROSTAT[®] is confirmed, particularly with the 0.8% concentration which was first used by the inventor, Dr. Kenneth N. Dolynchuk of the University of Manitoba, to show both the safety and efficacy of FIBROSTAT[®]. It is also important that we were able to demonstrate evidence of a more favourable effect for the 0.8% concentration in sub-group analyses of patients with the more serious scars. With these results and the recommendations of our Medical Advisors, who are acknowledged leaders in this field, we are now moving forward to set up the next Phase II development study, which we plan to carry out in North America together with our partner Biovail Corporation.

We are continuing discussions with potential licensing partners in Europe and the rest of the world and were very pleased to announce recently the granting of the patent for FIBROSTAT[®] in Europe.

During the quarter we also made significant progress in the scientific and clinical development of our PSP⁹⁴ (Prostate Secretory Protein) technology for prostate cancer. Earlier this year we had announced the clearance by the U.K. Medicines Control Agency for conducting human Clinical Phase IIa trials with our lead compound, the peptide PCK3145 for treating late stage hormone refractory prostate cancer patients. All required institutional approvals have now been obtained and the trial will commence imminently, following the summer break. At a major cancer conference in April, our collaborators from McGill University reported on the effect of PCK3145 in reducing hypercalcemia resulting from metastasis of prostate cancer, an important finding that may expand the potential utility of our lead compound for treating both primary tumor as well as metastatic cancer. We also recently announced the extension of the License Option Agreement for PSP⁹⁴ with Chiron Corporation, to September 30, 2002.

In May, our scientists reported on the purification and identification of a novel PSP⁹⁴ binding protein found in the serum, a significant achievement as this discovery will be important for the development of a novel diagnostic/prognostic test for determining the presence as well as aggressivity of prostate cancer.

We are actively pursuing the pre-clinical development program with our ANA (Antinucleosome Antibody) based chimeric monoclonal antibody candidate c2C5 and GMP grade material is currently being produced by our contractor, Goodwin Biotechnology, Inc. At the prestigious American Society of Clinical Oncologists (ASCO) meeting in May our scientists reported on the efficacy of c2C5 in Small Cell Lung cancer animal model, an important finding further confirming the pan-carcinoma effect of the antibody, since previously we have shown effects on other animal cancer models.

I am particularly pleased to welcome Dr. Daniel Böck, who joined us during the quarter as Vice President, Business Development, replacing Dr. Naveen Anand who resigned to join a large pharma company in May. I would like to thank Dr. Anand for his extensive services to Procyon. On June 5, 2002, we held our Annual General Meeting and are pleased to announce the re-election of the Board of Directors, following which the Management team was endorsed.

Signed : "Hans J. Mäder"
Chairman, President & CEO

Management's Discussion and Analysis of Financial Condition and Results of Operations

The following information should be read in conjunction with the Company's unaudited consolidated financial statements and related notes included herein, together with our audited consolidated financial statements for the year ended December 31, 2001 and the related notes, which are prepared in accordance with Canadian generally accepted accounting principles.

RESULTS OF OPERATIONS

Quarter ended June 30, 2002 compared with the Quarter ended June 30, 2001

The Company incurred a net loss of \$1,621,350 or \$0.03 per common share during the second quarter of 2002, compared with a net loss of \$2,536,905 or \$0.06 per common share for the corresponding quarter last year.

Revenues for the current quarter were \$90,080, compared with \$157,759 in the second quarter last year. The reduced revenues reflected a decrease in interest income due to the decline in interest rates compared with the second quarter of 2001, partially offset by license revenue generated in the second quarter of 2002.

Research and development expenses amounted to \$1,039,238 in the second quarter of 2002, compared with \$1,950,638 in the same quarter last year, a decrease of 47%. The higher level of spending in the second quarter of 2001 primarily reflected significant expenditures on the PSP⁹⁴ and ANA technologies. Expenses in the current quarter were temporarily lower pending the commencement of the clinical studies for the PSP⁹⁴ technology and the production of antibodies for the ANA technology. Research and development spending is projected to increase materially by the fourth quarter of 2002. Tax credits increased to \$190,000 in the current quarter from \$157,000 in the same quarter last year due to a higher level of research salaries and payments to Quebec-based consultants qualifying for the tax credit. Research and development expenses represented 55% of total expenses before tax credits in the current quarter, compared with 68% in the corresponding period last year.

General and administrative expenses decreased to \$741,714 in the second quarter of 2002, from the total of \$798,512 for the same quarter last year, primarily as a result of a reduction in professional fees.

Amortization expense increased to \$120,478 from \$102,514 in the second quarter of 2001. The increase resulted from the higher level of investment on intellectual property during the second half of 2001.

Six Months ended June 30, 2002 compared with the Six Months ended June 30, 2001

A net loss of \$3,234,185 or \$0.07 per common share was incurred in the first half of 2002, compared with a net loss of \$4,505,122 or \$0.10 per common share in the first six months of 2001.

Revenues earned during the first half of 2002 declined to \$161,417 from the amount of \$334,862 in the same period last year. The reduction was the result of a decrease in interest income due to the decline in interest rates compared with the first half of 2001 and to lower average levels of cash and short-term investments, partially offset by license revenue earned in the current period.

Research and development expenses amounted to \$2,274,523 in the first six months of 2002, compared with \$3,360,077 in the corresponding period last year, a decrease of 32%. The higher spending during the first half of 2001 reflected primarily the significant research and pre-clinical testing on the PSP⁹⁴ and ANA technologies. Tax credits increased to \$369,000 in the current period from \$316,000 in the first half of 2001 due to a higher level of research salaries and payments to Quebec-based consultants. Research and development expenses comprised 60% of total expenses before tax credits for the first half of 2002, compared with 65% in the same period last year.

General and administrative expenses for the six months ended June 30, 2002 amounted to \$1,248,947, a reduction of 22% from the amount of \$1,591,091 in the first half of 2001. The reduced expenses were primarily for professional fees and employee compensation.

Amortization expense in the first half of 2002 amounted to \$241,132, compared with \$204,816 in the corresponding period last year. The increase reflected primarily the amortization on the additional investment on intellectual property during the past year.

LIQUIDITY AND CAPITAL RESOURCES

Cash and cash equivalents and short-term investments at June 30, 2002 totaled \$15,011,740 compared with \$5,566,152 at December 31, 2001. The increase of \$9,445,588 resulted primarily from two major events. Cash proceeds of \$10,001,520 were realized on May 10, 2002 from the issue of Units, each comprised of one common share and one-half of a common share purchase warrant, before cash expenses of \$936,097 related to the transaction. An additional \$4,000,000 was generated from the issue of First Preferred Shares, Series 1 on January 4, 2002 in connection with the licensing agreement granting the United States marketing rights for FIBROSTAT® to Biovail Corporation. These amounts were supplemented by proceeds of \$510,860 from the issue of common shares during the period, primarily resulting from the exercise of stock options. A total of \$4,053,774 of the cash and short-term investments was utilized to finance operating activities for the first half of 2002, including an increase of \$1,150,721 in non-cash working capital. Expenditures on intellectual property and equipment during the first six months of 2002 totaled \$76,921.

The cash and short-term investments on hand are expected to be sufficient to support the Company's activities for at least two years.

Safe Harbour Statement

Certain matters discussed in this management's discussion and analysis of financial condition and results of operations are, by their nature, forward-looking. For a number of reasons, actual results could differ materially.

PROCYON BIOPHARMA INC.
CONSOLIDATED BALANCE SHEETS

As at

	June 30,	December 31,
	2002	2001
	(unaudited)	(audited)
	\$	\$
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ASSETS		
Current assets		
Cash and cash equivalents	9,548,925	540,934
Short-term investments	5,462,815	5,025,218
Accounts receivable	264,653	324,922
Investment tax credits recoverable	1,587,537	1,806,064
Prepaid expenses	67,236	33,263
	<hr/>	<hr/>
	16,931,166	7,730,401
Property, plant and equipment	478,168	494,103
Intellectual property	4,697,642	4,845,918
Investments	53,001	53,001
	<hr/>	<hr/>
	22,159,977	13,123,423
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LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities		
Accounts payable and accrued liabilities	638,642	1,994,153
Deferred revenue	77,917	117,950
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	716,559	2,112,103
Convertible debenture	50,000	50,000
Preferred shares (note 3)	4,000,000	-
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	4,766,559	2,162,103
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Shareholders' equity (note 3)		
Share capital	42,106,431	33,498,087
Other paid-in capital	1,538,588	862,000
Warrants	965,038	233,687
Equity components of convertible debenture	612,500	612,500
Deficit	(27,829,139)	(24,244,954)
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	17,393,418	10,961,320
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	22,159,977	13,123,423
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See accompanying notes

PROCYON BIOPHARMA INC.
CONSOLIDATED STATEMENTS OF
OPERATIONS AND DEFICIT
(unaudited)

	Three months ended June 30,		Six months ended June 30,	
	2002	2001	2002	2001
	\$	\$	\$	\$
REVENUES				
License revenue	20,016	-	40,033	-
Interest and other income	70,064	157,759	121,384	334,862
	90,080	157,759	161,417	334,862
EXPENSES				
Research and development	1,039,238	1,950,638	2,274,523	3,360,077
Research and development tax credit	(190,000)	(157,000)	(369,000)	(316,000)
General and administrative	741,714	798,512	1,248,947	1,591,091
Amortization of property, plant and equipment	19,947	20,412	39,852	40,611
Amortization of intangibles	100,531	82,102	201,280	164,205
	1,711,430	2,694,664	3,395,602	4,839,984
Net loss	(1,621,350)	(2,536,905)	(3,234,185)	(4,505,122)
Adjustment to terms of outstanding warrants (note 3)	(350,000)	-	(350,000)	-
Deficit, beginning of period	(25,857,789)	(16,861,008)	(24,244,954)	(14,892,791)
Deficit, end of period	(27,829,139)	(19,397,913)	(27,829,139)	(19,397,913)
Basic and diluted loss per share	(0.03)	(0.06)	(0.07)	(0.10)
Weighted average number of common shares outstanding	49,283,344	43,855,158	47,258,008	43,783,815

See accompanying notes

PROCYON BIOPHARMA INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited)

	Three months ended June 30,		Six months ended June 30,	
	2002	2001	2002	2001
	\$	\$	\$	\$
OPERATING ACTIVITIES				
Net loss	(1,621,350)	(2,536,905)	(3,234,185)	(4,505,122)
Add non-cash items				
Amortization	120,478	102,514	241,132	204,816
Services paid by issuance of stock options (note 3)	90,000	77,000	90,000	77,000
	(1,410,872)	(2,357,391)	(2,903,053)	(4,223,306)
Net change in non-cash working capital balances related to operations	(282,947)	(92,689)	(1,150,721)	(241,832)
Cash flows related to operating activities	(1,693,819)	(2,450,080)	(4,053,774)	(4,465,138)
INVESTING ACTIVITIES				
Acquisition of intellectual property	(50,119)	(84,154)	(53,004)	(164,976)
Acquisition of property, plant and equipment	(21,387)	(41,896)	(23,917)	(70,868)
Purchase of short-term investments	(5,462,815)	-	(5,462,815)	-
Sale of short-term investments	2,082,480	11,712,988	5,025,218	11,912,880
Cash flows related to investing activities	(3,451,841)	11,586,938	(514,518)	11,677,036
FINANCING ACTIVITIES				
Issuance of units	10,001,520	-	10,001,520	-
Unit issue expenses	(936,097)	-	(936,097)	-
Issuance of common shares	63,610	1,135,572	510,860	1,168,288
Share issue expenses	-	(21,192)	-	(21,192)
Issuance of preferred shares	-	-	4,000,000	-
Issuance of convertible debenture	-	256,250	-	318,750
Cash flows related to financing activities	9,129,033	1,370,630	13,576,283	1,465,846
Net increase in cash and cash equivalents	3,983,373	10,507,488	9,007,991	8,677,744
Cash and cash equivalents, beginning of period	5,565,552	320,546	540,934	2,150,290
Cash and cash equivalents, end of period	9,548,925	10,828,034	9,548,925	10,828,034

Supplemental cash flow information

Cash paid during the period for interest	-	-	-	-
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See accompanying notes

Procyon Biopharma Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2002

(unaudited)

1. Basis of presentation

These financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles and follow the same accounting policies and methods of application as the most recent annual financial statements, except for the changes in accounting policies described in note 2. The interim financial statements do not include all disclosures required for annual financial statements and should be read in conjunction with the most recent annual financial statements as at and for the year ended December 31, 2001.

2. Changes in accounting policies

(i) Intangible assets

Effective January 1, 2002, the Company prospectively adopted the new recommendations published by the Canadian Institute of Chartered Accountants relating to the method of valuation and the presentation and disclosure requirements for intangible assets. The new recommendations require recognized intangible assets to be amortized over their useful life to an enterprise, unless the life is determined to be indefinite. When an intangible asset is determined to have an indefinite useful life, it should not be amortized until its life is determined to be no longer indefinite. The amortization method and estimate of the useful life of an intangible asset should be reviewed annually. Intangible assets that are subject to amortization are tested for impairment by comparing the net carrying amount with the net recoverable amount whereas for intangible assets not subject to amortization, the net carrying amount is compared to the asset's fair value. The impact of the adoption of the new recommendations will not result in any change to the recognized intangible assets of the Company because its intangible assets are not considered to have an indefinite life. However, the Company will have additional disclosure requirements relating to its intangible assets.

Procyon Biopharma Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2002

(unaudited)

(ii) Stock-based compensation and other stock-based payments

Effective January 1, 2002, the Company also adopted the new CICA recommendations relating to stock-based compensation and other stock-based payments. As permitted, the Company has applied this change prospectively for new awards granted on or after January 1, 2002. The Company has chosen to recognize no compensation when stock options are granted to employees and directors under stock option plans with no cash settlement features. However, direct awards of stock to employees and stock and stock option awards granted to non-employees will be accounted for in accordance with the fair value method of accounting for stock-based compensation. The fair value of direct awards of stock are to be determined based on the quoted market price of the Company's stock and the fair value of stock options are to be determined using the Black-Scholes Option Pricing Model. In periods prior to January 1, 2002, the Company recognized no compensation when stock or stock options were issued to employees. Pro forma information regarding net income is required to be determined as if the Company had accounted for its employee stock options granted after December 31, 2001 under the fair value method. The fair value of these options is to be estimated at the date of grant using a Black-Scholes Option Pricing Model with assumptions for the weighted-average risk-free interest rates, dividend yields, weighted-average expected volatility of the market price of the Company's common shares and a weighted-average expected life of the options in years. For purposes of pro forma disclosures, the estimated fair value of the options is amortized to expense over the options' vesting periods on a straight-line basis.

3. Share capital

Common shares

The Company is authorized to issue an unlimited number of common shares. As at June 30, 2002, 52,411,708 common shares valued at \$42,106,431 were issued and outstanding (45,114,008 common shares valued at \$33,498,087 at December 31, 2001). On May 10, 2002, the Company issued 6,897,600 Units at \$1.45 each for total cash proceeds of \$10,001,520, before cash expenses of \$936,097. Each Unit consisted of one common share and one-half common share purchase warrant. Each whole common share purchase warrant entitles the holder to purchase one additional common share for \$1.75 up to November 10, 2003. Also, during the six months ended June 30, 2002 a total of 400,100 common shares were issued for cash consideration of \$410,860 on exercise of stock options and a \$100,000 shareholder loan was repaid.

Procyon Biopharma Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2002

(unaudited)

Preferred shares

The Company is authorized to issue an unlimited number of non-voting First Preferred Shares and Second Preferred Shares, each without par value.

On January 4, 2002, the Company issued 4,000,000 First Preferred Shares, Series 1 for total consideration of \$4,000,000. From January 1, 2004 to December 31, 2006, the holder of these shares may elect (i) to convert them into common shares at two times the market price on the date of conversion, or (ii) to require Procyon to redeem them for cash, in which case Procyon must redeem the shares if it has received sufficient cash to do so, pursuant to a licensing agreement with the holder, and, if not, Procyon may convert such shares into common shares at the market price at the date of conversion. If no election is made prior to December 31, 2006, Procyon may redeem the shares on or prior to January 30, 2007 for cash or convert them into common shares at the market price on the date of conversion. Since these shares are retractable, they have been included with liabilities on the balance sheet.

Stock option plan

On June 5, 2002, the maximum number of common shares to be issued pursuant to the Company's stock option plan was increased to 4,545,900. As at June 30, 2002, 3,808,832 stock options were outstanding compared to 3,958,932 as at December 31, 2001. During the six months ended June 30, 2002, 335,000 options were granted, 400,100 options were exercised and 85,000 options were forfeited. The Company applies the intrinsic value based method of accounting for stock-based compensation awards granted to employees. Accordingly, no compensation cost has been recognized for stock options granted to employees and directors. Had compensation cost been determined based on the fair value at the date of grant of options granted, the fair value of the options would have been amortized over the vesting period of the options and the Company's net loss and loss per common share would have been amended as follows:

		Three months ended June 30, 2002	Six months ended June 30, 2002
Net loss	As reported	\$(1,621,350)	\$(3,234,185)
	Pro forma	(1,623,616)	(3,236,451)
Earnings per share Basic and diluted	As reported	\$(0.03)	\$(0.07)
	Pro forma	(0.03)	(0.07)

Procyon Biopharma Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2002

(unaudited)

Warrants

As at June 30, 2002, there were 8,919,425 common shares reserved for issuance upon the exercise of warrants, compared to 5,470,625 at December 31, 2001. The increase of 3,448,800 resulted from the issue of 6,897,600 Units discussed under “ Common shares ” above, each of which included one-half of a common share purchase warrant. On April 5, 2002, the Company amended the terms of the common share purchase warrants issued on July 31, 2000 to lower the exercise price to \$2.62 per common share from \$3.93 per common share and to extend the time up to which the warrants may be exercised until April 10, 2003. As a result of these amendments, other paid-in capital was increased by \$350,000, with an offsetting charge to the deficit.

Other paid-in capital

As at June 30, 2002, other paid-in capital amounted to \$1,538,588, compared to \$862,000 at December 31, 2001. On April 5, 2002, the terms of the common share purchase warrants issued on July 31, 2000 were amended, resulting in an increase of \$350,000 in other paid-in capital. The fair value of the broker warrants associated with the issue of Units on May 10, 2002 amounted to \$236,588, while the fair value of stock options granted to a consultant on June 17, 2002 was \$90,000.

4. Comparative figures

Certain comparative figures have been reclassified to conform to the presentation in the current period.

5. Subsequent events

On July 12, 2002, the Company extended the license option agreement with Chiron Corporation for an evaluation of its Prostate Secretory Protein (PSP⁹⁴) technology. The extension gives Chiron an exclusive option for the evaluation of the program until September 30, 2002, during which time the Company has committed to not out-license the technology to another party.