

August 6, 2004

Message to shareholders,

We are very pleased to submit this report on the results for the second quarter ended June 30, 2004. This quarter saw strategic achievements made on all fronts, as the Company progressed on track to achieve the targeted milestones for the next 12 months. On the scientific front, we successfully completed our Phase IIa trial on PCK3145, advanced a step closer to filing an IND for PL-100 and completed patient enrollment for our Phase IIb trial on Fibrostat[®]. On the corporate side, Procyon raised the necessary funds to execute its two-year development strategy and increased the Company's visibility in the Canadian and US financial markets.

ONCOLOGY UPDATE – Successful completion of PCK3145 Phase IIa trial and unanimous recommendation to pursue clinical development

We were pleased to report the final positive results from the Phase IIa clinical trial with PCK3145, our therapeutic peptide indicated for metastatic hormone-refractory prostate cancer at the 2004 American Society of Clinical Oncology (ASCO) Meeting held in June in New Orleans. The final Phase IIa results confirm the safety, tolerability and the preliminary efficacy of PCK3145 at all dose levels tested. At the time of completion of the study, seven patients had stable disease and one patient showed a partial response after two cycles of treatment. In line with previously described results, a substantial reduction in levels of matrix metalloproteinase-9 (MMP-9), a gelatinase B enzyme involved in extracellular matrix degradation and tumor invasion (metastasis), was observed in all patients with elevated MMP-9 levels at baseline, while no significant change was observed after the first cycle in patients with normal baseline MMP-9 levels. This suggests that PCK3145 shows a potential dual effect by restoring normal cell growth through inducing apoptosis and inhibiting the metastatic process through regulating MMP-9 levels.

Procyon simultaneously announced the creation of a Scientific Advisory Board which is composed of 12 world-renowned oncologists and urologists. The Board met in New Orleans during the 2004 ASCO Meeting to discuss the results of the PCK3145 Phase IIa trial and unanimously concluded that the results for PCK3145 to date justify continued development of the drug candidate. We intend to initiate a North American Phase II trial during the first quarter of 2005, with the objective of demonstrating the efficacy of PCK3145 according to FDA guidelines.

VIROLOGY UPDATE – En route to a CTA/IND submission

In April, we reported the preclinical safety and pharmacokinetic profiles of PL-100, our protease inhibitor for the treatment of drug-resistant HIV/AIDS. The latest preclinical studies show that oral treatment with PL-100 is well-tolerated up to seven days at the highest doses possible. Combined with the complete lack of evidence of genotoxicity in two standard, required tests, these results suggest the safe use of PL-100 in patients. Moreover, we now have a tablet formulation of PL-100 that in animal studies shows similar bioavailability to PL-100 when administered in liquid form. PL-100 appears to have all of the requirements to provide a drug option for patients who are experiencing treatment failure due to viral resistance. We are currently completing our preclinical program and we remain on track to soon file a CTA/IND and to commence the human clinical Phase I/II trial shortly thereafter.

During the quarter, we were also invited to present a scientific poster reporting on the favorable resistance profile of PL-100 at the prestigious XIIIth International HIV Drug Resistance Workshop, in Spain. The presentation described the unique resistance profile of PL-100 in comparison with five currently-marketed protease inhibitors. On average, PL-100 showed antiviral activity superior to approved protease inhibitors when tested against 14 HIV strains that have shown resistance to the currently-available protease inhibitors. This indicates the potential for good activity against existing protease inhibitor-resistant viruses in treatment-experienced patients or in those patients newly-infected with similar resistant strains.

DERMATOLOGY UPDATE – Phase IIb patient enrollment completed

Immediately following the end of the second quarter, we completed the enrollment of the 200 patients required for the North American Phase IIb clinical trial with Fibrostat[®], our proprietary topical therapeutic intended for the treatment of hypertrophic scars resulting from surgery or burns. The placebo-controlled, double-blind, randomized Phase IIb clinical trial is currently underway at 12 centers across Canada and the United States. The primary objective of this trial is to evaluate the safety and efficacy of Fibrostat[®] 0.8% for the treatment of excessive scar formation.

This study is the first of its kind and we are pleased to act as pioneers in the management of hypertrophic scars, which represent an important area of unmet medical need. We are currently in discussions with potential partners for Europe and Japan, and hope to secure a partnering agreement once the final Phase IIb data is available. The Company expects to announce the results of the study during the fourth quarter of 2004. Following completion of the Phase IIb clinical trial of Fibrostat[®] and regulatory approval of Phase III protocols, Procyon intends to conduct separate pivotal studies in Europe and North America in collaboration with licensee partners for these respective regions.

CORPORATE UPDATE – Increasing our visibility

The second quarter was very active on the corporate front. First, we successfully completed a Unit offering at a price of \$1.00 per unit for total gross proceeds of \$17.25 million. The offering was made through a syndicate of underwriters led by Dundee Securities Corporation and including Loewen, Ondaatje, McCutcheon Limited, Research Capital Corporation and Canaccord Capital Corporation. The financing further reinforces our shareholder base with new and important European and North American institutions.

Following this financing, we increased the Company's visibility in the United States by engaging the Trout Group to provide us with institutional investor relations services. Over the years, the Trout Group has developed an exhaustive network of institutional relationships with analysts, portfolio managers, investment bankers and venture capitalists in the US biotechnology community. As we have multiple milestones to achieve within the next twelve months, we have taken the first steps to prepare Procyon for the US market.

Our visibility has also increased through André Uddin, Ph.D., Biotech Analyst at National Bank Financial, who initiated coverage of the Company. Dr. Uddin has previously written research reports on Procyon while acting as analyst with another brokerage firm. Moreover, Procyon received two prestigious awards at the 2004 Genesis Ceremony held in Montreal during the Annual BIOMEDEX Conference. The event was organized by BioQuébec and the Association of health technologies industry (AITS) in collaboration with BIOTECCanada. Procyon received the "Entrepreneurship - Biotechnology-Biopharmaceutical" award, a tribute from the Fonds de Solidarité de la FTQ, while I was personally honored with the "Brio" award, a tribute from the Royal Bank of Canada.

Finally, we appointed Jinzi J. Wu, Ph.D., as Vice-President, Preclinical and Basic Research. As our three near-term value drivers namely: PCK3145, Fibrostat[®] and PL-100, are rapidly advancing to late-stage development, it becomes crucial for Procyon to assure a constant flow of promising drug candidates in our product pipeline. In addition to overseeing the preclinical development of our early-stage candidates, Dr. Wu will add further support to our PCK3145 therapeutic peptide program by exploring its utility in other cancer types where metastases spread to the bones.

On behalf of our Board of Directors and Management Team, I would like to thank all of our shareholders and employees for your continued support.



Chairman, President & Chief Executive Officer

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, 2003 and the related notes, which are prepared in accordance with Canadian generally accepted accounting principles. Some of the statements contained in this Management's Discussion and Analysis of Financial Condition and Results of Operations constitute forward-looking statements. These statements relate to future events or to Procyon's future financial performance and involve known and unknown risks, uncertainties and other factors that may cause the Company's actual results performance or achievements to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. All amounts shown are stated in Canadian dollars. This review was prepared by management from information available to July 29, 2004. Additional information relating to the Company, including the Company's Annual Information Form and its quarterly report to shareholders for the quarter ended March 31, 2004, can be found on SEDAR at www.sedar.com.

OVERVIEW

Procyon Biopharma Inc. is a publicly-traded Canadian biotechnology company actively engaged in the discovery and development of innovative therapeutics and diagnostics in the fields of oncology and infectious diseases. The Company brings its products from the laboratory to late-stage clinical trials and licenses them to larger pharmaceutical partners for further development and commercialization. Procyon receives from licensee partners upfront and milestone payments, as well as royalty revenues upon commercialization.

Procyon's products and technologies are steadily advancing from research through development, preclinical and clinical studies. As a result, today Procyon has three near-term value drivers, namely PCK3145, a treatment for prostate cancer for which a Phase IIa trial has recently been completed; Fibrostat[®], a topical cream for hypertrophic scars licensed out to Biovail Corporation in North America currently in a Phase IIb trial; and PL-100, a very unique protease inhibitor that is currently in the pre-clinical phase. The Company is also developing a medical device, PSP⁹⁴ Serum-based immunoassay, a reliable, quick-and-easy test to detect and monitor prostate cancer, and has licensed Colopath[®], a simple screening and monitoring test for colorectal cancer, to IMI International Medical Innovations Inc. The Company is also developing two other therapeutics: ANsA, a technology platform with potential therapeutic applications to various cancers that is presently undergoing a thorough scientific review to determine its future direction; and PL-2500, an integrase inhibitor that addresses a novel mechanism of action for the treatment of HIV/AIDS.

The Company has incurred substantial losses since its inception, due primarily to its expenditures for research and development activities. We expect to incur further losses during the next several years resulting from the continuation of our ongoing clinical trials and pre-clinical development activities.

Revenues

We have not generated any significant revenues from product sales since 1997. Revenues have been earned primarily from research and development tax credits and interest on available cash balances. We expect to continue to receive such revenues during the next several years, as well as licensing revenues to be earned upon attaining certain milestones.

Research and Development Expenses

Our research and development expenses consist primarily of salaries and related personnel costs, fees paid to external service providers, laboratory supplies and costs for leasing of facilities and equipment. In the first half of 2004, fees paid to external service providers were primarily related to the Phase IIb clinical trial for Fibrostat[®], the Phase IIa trial for PCK3145 and pre-clinical costs for PL-100.

We expect our research and development expenses to increase materially during the next few years as we continue our clinical trials for our more advanced products, while continuing to advance our other research programs. However, we are unable to estimate the specific timing and future costs of our research and development programs.

Significant Projects

Each of our product candidates, which were discussed in the Overview section, will have to complete the necessary phases of clinical trials and obtain regulatory approval before they can generate significant revenues. The costs to complete these clinical trials and to obtain regulatory approval are significant and the costs associated with this process are expected to increase our research and development expenses materially over the next several years. These costs are expected to be borne to some extent by various corporate partners under research collaboration and licensing agreements.

We also have a number of other discovery and development programs to identify and develop other therapeutic and diagnostic products. This process is part of our ongoing research and development activities and, until product candidates are identified, significant clinical expenditures are not anticipated.

Segmented Information

The Company operates in only one segment, which is the sector related to the development and commercialization of diagnostic and therapeutic drugs. All revenues were earned in Canada, most operations are carried out in Canada and all assets, with the exception of certain intellectual property, are located in Canada.

RESULTS OF OPERATIONS

Quarter ended June 30, 2004 compared with the Quarter ended June 30, 2003

The Company incurred a net loss of \$4,689,259 or \$0.06 per common share for the second quarter of 2004, compared with a net loss of \$3,102,057 or \$0.05 per common share for the same quarter last year.

Revenues for the current quarter were \$101,801, compared with \$87,281 in the corresponding quarter last year. The higher revenues resulted primarily from an increase in interest income, due to the higher level of cash and short-term investments on hand following the \$17,250,000 financing that was closed on April 7, 2004, partially offset by a reduction in interest rates in the current quarter compared to the second quarter of 2003.

Research and development expenses amounted to \$3,688,384 in the second quarter of 2004, compared with \$2,382,124 in the same quarter last year. A higher level of spending on Fibrostat[®] compared with the second quarter of 2003 was the primary cause of the increase, together with increased expenditures on virology technologies in the current quarter. Tax credits increased to \$402,000 in the current quarter from \$345,307 in the same quarter last year. Research and development expenses represented 71% of total expenses before tax credits in the current quarter, compared with 67% in the corresponding quarter last year.

General and administrative expenses amounted to \$1,158,681 in the second quarter of 2004, an increase of \$285,690 or 33% over the total of \$872,991 for the same period last year. The higher expenses primarily reflected an increase in non-cash compensation and consulting fees.

Amortization expense increased to \$267,054 from \$226,897 in the second quarter of 2003. The increase resulted primarily from the amortization of purchases of equipment and intellectual property, together with the amortization of the deferred financing costs incurred for the Biolevier loan facility.

Financial charges increased to \$88,867 from \$15,335 in the second quarter last year. The increase was due to the interest on the Biolevier loan, which is being capitalized and added to the outstanding balance of the loan.

Six Months ended June 30, 2004 compared with the Six Months ended June 30, 2003

A net loss of \$7,728,534 or \$0.10 per common share was incurred during the six months ended June 30, 2004, compared with a net loss of \$4,754,377 or \$0.08 per common share for the six months ended June 30, 2003.

Revenues of \$165,480 were earned in the first half of 2004, compared with \$178,695 in the same period last year. The reduction was primarily the result of lower license revenue.

Research and development expenses for the six months ended June 30, 2004 were \$5,935,017, compared with \$3,504,584 in the corresponding period last year. The increase reflected primarily a higher level of spending on the Fibrostat[®] clinical trial, together with the increased expenditures on virology technologies, which were acquired in April 2003 through the acquisition of Pharmacor Inc. and consequently did not impact the 2003 expenses until the second quarter. Tax credits increased to \$695,000 in the first half of 2004, from \$526,307 in the same period last year. Research and development expenses represented 69% of total expenses before tax credits in the current period, compared with 64% in the corresponding period last year.

General and administrative expenses amounted to \$1,953,980 in the first half of 2004, an increase of \$404,349 or 26% over the total of \$1,549,631 for the corresponding period last year. The increase was primarily due to higher non-cash compensation and consulting fees.

Amortization expense increased to \$533,238 from \$364,583 in the same period last year. The increase resulted primarily from the full period effect in the current period of amortization of equipment and intellectual property obtained through the Pharmacor acquisition in April 2003, together with the amortization of the deferred financing costs incurred for the Biolevier loan facility.

Financial charges increased to \$182,792 from \$16,371 in the first half last year. The increase was due to the interest on the Biolevier loan, which is being capitalized and added to the outstanding balance of the loan.

LIQUIDITY AND CAPITAL RESOURCES

The Company has financed its operations and its acquisitions of technology and capital assets primarily through private placements and public issues of common shares, scientific research investment tax credits, interest income and amounts received under licensing agreements for certain of its products. In addition, a loan agreement entered into in December 2002 expanded the Company's financing base by providing it with a loan facility of \$10 million obtained under the Biolevier program of the Government of Quebec, from which an amount of \$5 million was drawn in November 2003, leaving an amount of \$5 million available for future use.

Cash and cash equivalents and short-term investments totaled \$18,124,428 at June 30, 2004, compared with \$9,917,167 at December 31, 2003. The increase of \$8,207,261 resulted from the net cash proceeds of \$15,656,846 realized from the sale on April 7, 2004 of 17.25 million Units at \$1.00 per Unit, each comprised of one common share of the Company and one-half of a common share purchase warrant. Each whole purchase warrant entitles the holder to purchase one additional common share of the Company at a price of \$1.25 at any time during the 24 months following the closing. A total of \$7,787,313 was utilized to finance operating activities for the first six months of 2004, including an increase of \$1,136,273 in non-cash working capital. In addition, \$71,758 was spent in the period for the purchase of property, plant and equipment and intellectual property. An amount of \$83,310 was generated from the issue of common shares associated with the exercise of stock options. An amount of \$330,000 was obtained through the issue of a convertible debenture to Biovail Laboratories Inc. under the Canadian licensing agreement for the development of Fibrostat[®].

The Biolevier loan does not adversely impact the Company's liquidity at this time, as no capital or interest is payable on the loan in the first three years following the initial disbursement in November 2003.

Management believes that it has sufficient funds available, including the balance of \$5 million available from the Biolevier loan facility referred to above, to support its ongoing activities through 2005.

Contractual Obligations

The only material change from the contractual obligations reported as at March 31, 2004 is in the area of purchase obligations and relates to the addition during the second quarter of 2004 of two contracts for the manufacture of drug products. These contracts can be terminated only under specific provisions and have the effect of increasing the total of contractual obligations as at June 30, 2004 by approximately \$600,000 compared to the amount reported at March 31, 2004.

There were no commitments for capital expenditures as at June 30, 2004.

Off-Balance Sheet Arrangements

The Company has not entered into any off-balance sheet arrangements during the quarter ended June 30, 2004 and does not expect to enter into any, other than in the normal course of business, in the near future.

Related Party Transactions

There has been no material change during the quarter ended June 30, 2004.

Proposed Transactions

At the present time, we do not anticipate any significant transactions involving the acquisition or disposition by the Company of assets or businesses.

Critical Accounting Estimates

The preparation of financial statements in accordance with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses and the disclosure of contingent assets and liabilities. The reported amounts and note disclosures in the consolidated financial statements are determined using management's best estimates based on assumptions that reflect the most probable set of economic conditions and planned courses of action. Actual results, however, may differ from the estimates used in the consolidated financial statements and such differences could be material. Details of the more critical estimates used were reported in the Management's Discussion and Analysis of Financial Condition and Results of Operations for the quarter ended March 31, 2004 and these continue to apply for the quarter ended June 30, 2004.

Changes in Accounting Policies

There have been no changes in accounting policies adopted by the Company during the quarter ended June 30, 2004.

Financial Instruments

The Company does not use currency or other hedging instruments.

Outstanding Share Data

As of July 29, 2004 there are 4,000,000 First Preferred Shares, Series 1 outstanding, unchanged from December 31, 2003. The number of common shares outstanding as of July 29, 2004 is 84,803,899, an increase of 17,468,000 from December 31, 2003, 17,250,000 resulting from the sale of Units on April 7, 2004 and 218,000 from the exercise of stock options. The number of stock options outstanding at July 29, 2004 is 4,844,250, an increase of 1,205,750 from December 31, 2003. In addition, 16,924,315 warrants are outstanding on July 29, 2004, compared to 6,970,897 at December 31, 2003. The increase resulted from the sale of Units on April 7, 2004, partially offset by the expiry of 482,832 Broker units issued in May 2002.

Form 52-109FT2 – Certification of Interim Filings during Transition Period

I, Hans J. Mäder, Chairman, President & Chief Executive Officer of Procyon Biopharma Inc., certify that:

1. I have reviewed the interim filings (as this term is defined in Multilateral Instrument 52-109 *Certification of Disclosure in Issuers' Annual and Interim Filings*) of Procyon Biopharma Inc., for the interim period ending June 30, 2004;
2. Based on my knowledge, the interim filings do not contain any untrue statement of a material fact or omit to state a material fact required to be stated or that is necessary to make a statement not misleading in light of the circumstances under which it was made, with respect to the period covered by the interim filings; and
3. Based on my knowledge, the interim financial statements together with the other financial information included in the interim filings fairly present in all material respects the financial condition, results of operations and cash flows of the issuer, as of the date and for the periods presented in the interim filings.



Chairman, President
& Chief Executive Officer

Date: July 29th, 2004

I, Monique Létourneau, Executive Vice-President, Finance & Chief Financial Officer of Procyon Biopharma Inc., certify that:

1. I have reviewed the interim filings (as this term is defined in Multilateral Instrument 52-109 *Certification of Disclosure in Issuers' Annual and Interim Filings*) of Procyon Biopharma Inc., for the interim period ending June 30, 2004;
2. Based on my knowledge, the interim filings do not contain any untrue statement of a material fact or omit to state a material fact required to be stated or that is necessary to make a statement not misleading in light of the circumstances under which it was made, with respect to the period covered by the interim filings; and
3. Based on my knowledge, the interim financial statements together with the other financial information included in the interim filings fairly present in all material respects the financial condition, results of operations and cash flows of the issuer, as of the date and for the periods presented in the interim filings.



Executive Vice-President Finance
& Chief Financial Officer

Date: July 29th, 2004

PROCYON BIOPHARMA INC.
CONSOLIDATED BALANCE SHEETS
(unaudited)

As at	June 30, 2004 \$	December 31, 2003 \$
ASSETS		
Current assets		
Cash and cash equivalents	13,724,428	476,673
Short-term investments	4,400,000	9,440,494
Accounts receivable	365,132	213,946
Investment tax credits recoverable	1,532,004	1,047,500
Prepaid expenses	157,205	155,093
	20,178,769	11,333,706
Property, plant and equipment	944,410	1,034,677
Intellectual property	6,967,809	7,305,837
Long-term investments (note 2)	-	7,001
Deferred financing fees	630,501	663,686
	28,721,489	20,344,907
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities		
Accounts payable and accrued liabilities	1,085,680	1,582,775
Deferred revenue	-	9,617
	1,085,680	1,592,392
Biolevier loan facility	5,223,286	5,043,223
Convertible debenture (note 3)	50,000	50,000
Preferred shares	4,000,000	4,000,000
	10,358,966	10,685,615
Shareholders' equity (note 4)		
Share capital	61,265,482	47,874,176
Warrants	2,559,254	751,292
Contributed surplus	3,452,661	2,550,164
Equity component of convertible debenture (note 3)	1,005,000	675,000
Deficit	(49,919,874)	(42,191,340)
	18,362,523	9,659,292
	28,721,489	20,344,907

See accompanying notes

PROCYON BIOPHARMA INC.
CONSOLIDATED STATEMENTS OF
OPERATIONS AND DEFICIT

(unaudited)

	Three months ended June 30,		Six months ended June 30,	
	2004	2003	2004	2003
	\$	\$	\$	\$
REVENUES				
License revenue	-	4,416	9,617	19,433
Interest and other income	101,801	82,865	155,863	159,262
	101,801	87,281	165,480	178,695
EXPENSES				
Research and development	3,688,384	2,382,124	5,935,017	3,504,584
Research and development tax credit	(402,000)	(345,307)	(695,000)	(526,307)
Net research and development	3,286,384	2,036,817	5,240,017	2,978,277
General and administrative	1,158,681	872,991	1,953,980	1,549,631
Amortization of property, plant and equipment	77,252	66,967	153,782	100,408
Amortization of intellectual property	173,210	159,930	346,271	264,175
Amortization of deferred financing fees	16,592	-	33,185	-
Interest on Biolevier loan	87,529	-	180,063	-
Write-down of investment	-	46,000	7,001	46,000
Other financial charges	1,338	15,335	2,729	16,371
Foreign exchange gains	(9,926)	(8,702)	(23,014)	(21,790)
	4,791,060	3,189,338	7,894,014	4,933,072
Net loss	(4,689,259)	(3,102,057)	(7,728,534)	(4,754,377)
Deficit, beginning of period	(45,230,615)	(33,124,658)	(42,191,340)	(31,472,338)
Deficit, end of period	(49,919,874)	(36,226,715)	(49,919,874)	(36,226,715)
Basic and diluted loss per share	(0.06)	(0.05)	(0.10)	(0.08)
Weighted average number of common shares outstanding	83,462,700	64,569,801	75,381,744	58,486,383

See accompanying notes

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

	Three months ended June 30,		Six months ended June 30,	
	2004	2003	2004	2003
	\$	\$	\$	\$
OPERATING ACTIVITIES				
Net loss	(4,689,259)	(3,102,057)	(7,728,534)	(4,754,377)
Add non-cash items				
Amortization of property, plant and equipment	77,252	66,967	153,782	100,408
Amortization of intellectual property	173,210	159,930	346,271	264,175
Amortization of deferred financing fees	16,592	-	33,185	-
Write-down of investments	-	46,000	7,001	46,000
Loan interest capitalized	87,529	-	180,063	-
Non-cash license revenues	-	(4,416)	(4,417)	(8,833)
Non-cash stock-based compensation (note 4)	300,690	80,517	361,609	80,517
	(4,033,986)	(2,753,059)	(6,651,040)	(4,272,110)
Net change in non-cash balances relating to operations	(352,570)	(969,993)	(1,136,273)	(1,930,143)
Cash flows related to operating activities	(4,386,556)	(3,723,052)	(7,787,313)	(6,202,253)
INVESTING ACTIVITIES				
Acquisition of intellectual property	(5,281)	(52,151)	(8,243)	(64,726)
Acquisition of property, plant and equipment	(39,096)	(39,710)	(63,515)	(124,852)
Cash and cash equivalents obtained on acquisition of business	-	159,832	-	159,832
Business acquisition expenses	-	(236,255)	-	(236,255)
Purchase of short-term investments	(4,400,000)	(4,957,420)	(4,400,000)	(5,949,900)
Maturities of short-term investments	5,938,210	4,451,030	9,440,494	13,359,550
Cash flows related to investing activities	1,493,833	(674,674)	4,968,736	7,143,649
FINANCING ACTIVITIES				
Issuance of units	17,250,000	3,530,000	17,250,000	3,530,000
Unit issue expenses	(1,593,154)	(317,711)	(1,593,154)	(317,711)
Issuance of common shares	-	-	83,310	-
Debt financing costs	-	(64,396)	-	(77,765)
Repayment of long-term debt assumed in an acquisition	(1,206)	(25,411)	(3,824)	(25,411)
Issuance of convertible debenture (note 3)	330,000	-	330,000	-
Cash flows related to financing activities	15,985,640	3,122,482	16,066,332	3,109,113
Net increase (decrease) in cash and cash equivalents	13,092,917	(1,275,244)	13,247,755	4,050,509
Cash and cash equivalents, beginning of period	631,511	5,704,761	476,673	379,008
Cash and cash equivalents, end of period	13,724,428	4,429,517	13,724,428	4,429,517
Supplemental cash flow information				
Cash paid during the period for interest	56	12,659	2,837	12,659

See accompanying notes

Procyon Biopharma Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2004

(unaudited)

1. Basis of presentation

These financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles applicable to interim financial statements and follow the same accounting policies and methods of application as the most recent annual financial statements. 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, 2003.

2. Long-term investments

As at June 30, 2003 the Company wrote down the carrying value of a warrant to purchase 75,000 common shares of IMI International Medical Innovations Inc. from \$53,000 to \$7,000, management's estimate of the fair value of the warrant at June 30, 2003, using the Black-Scholes option pricing model, with a volatility factor of 47% and a risk-free interest rate of 3%. The write-down was recorded as an expense during the second quarter of 2003. This warrant expired without value on March 19, 2004 and the remaining carrying value of \$7,000 was written off at that time.

3. Convertible debenture

On February 1, 2000, the Company entered into a Canadian licensing agreement with a biopharmaceutical company [the "Holder"] whereby the Holder will advance funds to the Company upon the achievement of specific scientific and regulatory milestones related to Fibrostat[®]. The funds will be advanced up to a maximum of \$1,500,000, in the form of a non-interest bearing debenture, convertible into common shares, which matures on December 31, 2049. The Holder of the debenture has a right to convert the debenture into common shares at prices ranging from 125 % to 150% of the market price of the common shares at the date regulatory approval of Fibrostat[®] is obtained. As at June 30, 2004, the Company has received \$1,055,000, including \$330,000 that was advanced during the second quarter of 2004. Of the total amount received to date, \$50,000 is included in liabilities and \$1,005,000 is recorded as the equity component of the convertible debenture. The liability component will be accreted over time by a charge to the statement of operations for interest accretion and at maturity will be equal to the face value of the debenture.

4. Share capital

Common shares

The Company is authorized to issue an unlimited number of common shares.

	Number of shares	Stated capital \$
Balance as at December 31, 2003	67,335,899	47,874,176
Issued for cash on exercise of stock options	90,500	83,310
Issued on conversion of Units	17,250,000	15,180,000
Unit issuance costs – cash	-	(1,396,023)
Unit issuance costs – broker compensation warrants	-	(475,981)
Balance as at June 30, 2004	84,676,399	61,265,482

Procyon Biopharma Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2004

(unaudited)

On April 7, 2004, the Company issued 17,250,000 Units at \$1.00 each for total cash proceeds of \$17,250,000 before issue expenses. Each Unit consisted of one common share and one-half of one common share purchase warrant for a total of 8,625,000 common share purchase warrants. Each whole common share purchase warrant entitles the holder to purchase one additional common share for \$1.25 up to April 7, 2006. In addition to the cash commission paid and other cash issue costs totaling \$1,593,154, the Company granted to the underwriters broker compensation warrants to purchase up to 1,207,500 Units at an exercise price of \$1.00 per Unit up to April 7, 2006. The fair value of these broker compensation warrants was estimated at \$540,888, determined using the Black-Scholes option pricing model with a volatility of 81%, a risk-free interest rate of 2.6%, a dividend yield of nil and an expected life of two years. This amount was recorded as Unit issue costs, which reduced the Common share and Warrant amounts by \$475,981 and \$64,907 respectively and increased Contributed Surplus by \$540,888.

Stock option plan

On June 17, 2004, the maximum number of common shares to be issued pursuant to the Company's stock option plan was increased to 8,467,639. As at June 30, 2004, there were 5,026,750 stock options outstanding, compared to 3,638,500 at December 31, 2003.

	Six months ended June 30,			
	2004	Weighted Average Exercise price	2003	Weighted Average Exercise price
	Number	\$	Number	\$
Options outstanding January 1	3,638,500	1.25	3,765,300	1.29
Granted	1,723,750	0.99	441,500	0.41
Forfeited	(245,000)	1.86	(14,900)	1.10
Expired	-	-	(288,650)	1.00
Exercised	(90,500)	0.92	-	-
Options outstanding June 30	5,026,750	1.14	3,903,250	1.21
Exercisable	3,605,501	1.25	2,992,418	1.41

All options were granted with an exercise price equal to the market price of the Company's shares at the date of grant. Compensation expense of \$310,693 has been recognized in the first half of 2004 for stock options granted to employees and directors and an additional amount of \$50,916 has been expensed for options granted to consultants. The expense was based on the fair value of the options at the date of grant determined using the Black-Scholes option pricing model with a volatility factor of from 70% to 82%, a risk-free interest rate of from 3% to 4%, a dividend yield of nil and an expected life of up to three years. Effective January 1, 2003, the Company began prospectively recording compensation expense for awards granted to employees. In 2002, the fair value of options granted to employees was not expensed. Had compensation expense for 2002 been determined based on the fair value of options as of the date of grant using the Black-Scholes option pricing model, with a volatility factor of 63%, a risk-free interest rate of 4%, a dividend yield of nil and a weighted-average expected life of the options of three years, and had the fair value been amortized over the vesting period of the options, the Company's net loss and loss per common share would have been as follows:

Procyon Biopharma Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2004

(unaudited)

	Three months ended June 30		Six months ended June 30	
	2004	2003	2004	2003
	\$	\$	\$	\$
Net loss - as reported	(4,689,259)	(3,102,057)	(7,728,534)	(4,754,377)
Net loss – pro forma	(4,702,011)	(3,117,074)	(7,756,304)	(4,784,412)
Loss per share – basic and diluted				
As reported	(0.06)	(0.05)	(0.10)	(0.08)
Pro forma	(0.06)	(0.05)	(0.10)	(0.08)

Warrants

	Number	\$
Balance as at December 31, 2003	6,970,897	751,292
Issued on conversion of Units	8,625,000	2,070,000
Unit issuance costs	-	(262,038)
Broker warrants for Units	1,207,500	-
Warrants from Broker Units	603,750	-
Expired Broker warrants	(482,832)	-
Balance as at June 30, 2004	16,924,315	2,559,254

Contributed surplus

	\$
Balance as at December 31, 2003	2,550,164
Compensation warrants issued to underwriters	540,888
Options issued to consultants	50,916
Options granted to employees and directors	310,693
Balance as at June 30, 2004	3,452,661

The fair value of options granted to employees and directors since January 1, 2003 is being recorded as an expense over their vesting period, with a corresponding credit to Contributed Surplus.

5. Comparative figures

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