



**BONE MEDICAL LIMITED
AND CONTROLLED ENTITIES**

ABN 70 009 109 755

INTERIM FINANCIAL REPORT

For the Half-Year ended

31 DECEMBER 2007

BONE MEDICAL LIMITED and Controlled Entities
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DIRECTORS' REPORT

Your directors present their report on the consolidated entity consisting of Bone Medical Limited and the entities it controlled at the end of, or during, the half-year ended 31 December 2007.

DIRECTORS

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

Mr. Troels Jordansen

Dr. Roger New

Mr. Leon Ivory

Mr. Barry Walker, M.D.

Prof. Peter Brooks (appointed 25 July 2007)

Mr. Leif Jensen (appointed 10 September 2007)

Mr. Paul Hopper (resigned 16 July 2007)

Mr. Gabriel Chiappini (resigned 10 September 2007)

Directors have been in office since the start of the financial year to the date of this report unless otherwise stated.

COMPANY SECRETARIES

The following persons held the position of Company Secretary during the year:

Mr. Gabriel Chiappini (resigned 14 December 2007)

Mr. Mark Clements (appointed 14 December 2007)

FINANCIALS

The consolidated loss after income tax for the financial half year was \$1,464,646 (2006: \$1,330,950) after providing for an income tax rebate benefit of \$312,688 (2006: \$249,000). The loss was in line with expectations, with major expenses broadly in line with previous years relating to research and development of the Company's two primary drug candidates in the clinic, Calcitonin (sCT) for osteoporosis and potentially osteoarthritis, CaPTHymone™ Parathyroid Hormone (PTH) for osteoporosis and BN006, its anti TNF down-regulator for Rheumatoid Arthritis, and administrative overheads.

OPERATIONS

Bone Medical has made good progress during the period:

- **Successful capital raising of \$1.245m** – commenced in December 2007 and completed in January 2008, the raising was well supported by existing shareholders as well as new institutional investors;
- **Capsitonin® Positive Phase II results** – Oral Calcitonin formulation demonstrated biological efficacy on the basis of change in Calcium levels & primary endpoint CTX-1 levels which were equivalent to commercially available nasal spray.
- **Patent Notice of Allowance** – In-licensed drug discovery technology Axxess I and Mozaic have been given Notice of Allowance by the US patent office.

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DIRECTORS' REPORT (continued)

- **Commenced Phase I/IIa oral PTH clinical trial** – an important trial to evaluate two different formulations of oral CaPTHymone™ for future Phase II clinical trials. Results currently under analysis.
- **Advanced pre-clinical animal studies on promising TNF down-regulator for rheumatoid arthritis in Germany & UK** – early data from this pre-clinical candidate has provided encouragement to progress to the next stage of testing.
- **Strengthened Board** – appointment of Prof Peter Brooks in Queensland and Mr. Leif Jensen in Denmark as non-executive directors & appointment of Mr. Mark Clements in Perth as Company Secretary.
- **Receipt of Australian Government grants totaling A\$ 313,000.**

EVENTS POST BALANCE DATE

On the 7th January 2008 Bone Medical completed a private placement raising \$1.245m. 2,723,350 ordinary shares were issued at \$0.30 each with an additional 1,427,253 ordinary shares to be issued subject to a General Meeting of shareholders to be held on the 5th March 2008. Each share qualifies for one free attaching option exercisable at \$0.40 expiring 18 months from the date of issue.

On the 17th January 2008 Bone Medical engaged Intersuisse Bioscience Managers and PhillipCapital Australia as corporate advisors. This engagement is a precursor to detailed research, raising awareness and ultimately Australian and Asian investor and fund raising programs.

On the 28th January 2008 Bone Medical announced new data that its lead drug candidate BN006 is capable not only of down-regulating TNF secretion, but also inhibiting secretion of IL6 an agent instrumental in creating the vicious cycle of inflammatory events in Rheumatoid Arthritis.

On the 1st February 2008 Bone Medical announced positive data from its second clinical trial conducted to test CaPTHymone™. Two formulations of oral parathyroid hormone (PTH) were tested with both treatments demonstrating increases in calcium after six hours equivalent to that seen previously for the injectable Forteo comparator.

CURRENT OUTLOOK

Bone's clinical programme continues to progress according to plan and valuable clinical data is being generated. Capsitonin® will be presented to the FDA in the 1st half of 2008 with the objective of identifying the regulatory requirements for taking the product into Phase III. CaPTHymone™ has just successfully matched the only PTH product on the market, namely Forte from Eli Lilly (injectable only). The clinical data is still being analysed, but Bone is likely to request a Pre-IND meeting with the FDA to better understand the FDA's view on the regulatory pathway. BN006 has recently proven not only to down regulate TNF, but also to have a significant effect on IL-6, both significant markers for Rheumatoid Arthritis. With appropriate funding, Bone will be able to progress BN006 into its first in man study at the end of 2008 or early 2009.

Last year's fund raising was another strong indication of the value of Bone's pipeline. With sophisticated European institutional investors and representation of current large investors, Bone raised A\$ 1.245 in a tough market. From 2008 Bone will have research coverage from Intersuisse and Bone' continues to develop its relationship with a major European banker with special focus on the European market.

In the coming 6 months Bone will focus on FDA meetings and further corporate development and the Board remains positive on the prospects of the Company.


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Auditors Declaration

The Auditors Independence Declaration under section 307C of the Corporations Act 2001 is set out on page 6 for the half year ended 31 December 2007.

This report is signed in accordance with a resolution of the Board of Directors.

Director:



Leon Ivory

Date: 29TH February 2008



BDO Kendalls

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29 February 2008

The Directors
Bone Medical Ltd
PO Box 1110
BENTLEY DC WA 6983

Dear Sirs

DECLARATION OF INDEPENDENCE BY BRAD MCVEIGH TO THE DIRECTORS OF BONE MEDICAL LIMITED

As lead auditor for the review of Bone Medical Limited for the half-year ended 31 December 2007, I declare that to the best of my knowledge and belief, there have been:

- no contraventions of the auditor independence requirements of the *Corporations Act 2001* in relation to the review; and
- no contraventions of any applicable code of professional conduct in relation to the review.

This declaration is in respect of Bone Medical Limited and the entities it controlled during the period.

BG McVeigh
Director

BDO Kendalls Audit & Assurance (WA) Pty Ltd
Perth, Western Australia

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Consolidated Income Statement For the half year ended 31st December, 2007	Economic Entity	
	31.12.2007	31.12.2006
	\$	\$
Revenue from Continuing Operations	22,385	21,035
Research & Development	(1,049,673)	(1,054,014)
Employee Benefits	(249,062)	(155,701)
Professional Consultants	(141,220)	(104,120)
Depreciation & Amortisation	(3,355)	(3,602)
External Consultants	(77,737)	(128,031)
Legal Fees	(84,826)	(6,214)
Travel	(21,843)	(13,846)
Business Development	(15,511)	(17,950)
Public Relations	(16,500)	-
Other Expenses	(139,992)	(117,507)
Loss before Income Tax	(1,777,334)	(1,579,950)
Income Tax Benefit	312,688	249,000
Loss for the year	(1,464,646)	(1,330,950)

Earnings per share for profit from continuing operations attributable to the ordinary equity holders of the company

	Cents	Cents
Basic loss per share (cents per share)	(1.92)	(1.97)
Diluted loss per share (cents per share)	N/A	N/A

The consolidated income statement should be read in conjunction with the accompanying notes

BONE MEDICAL LIMITED and Controlled Entities
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Consolidated Balance Sheet	Economic Entity	
For the half year ended 31st December, 2007	31.12.2007	30.06.2007
	\$	\$
<u>ASSETS</u>		
CURRENT ASSETS		
Cash & cash equivalents	1,361,365	1,478,640
Trade and other receivables	34,652	43,640
TOTAL CURRENT ASSETS	1,396,017	1,522,280
NON-CURRENT ASSETS		
Property, plant & equipment	17,995	21,350
Intangible assets	1,956,599	1,956,599
TOTAL NON-CURRENT ASSETS	1,974,594	1,977,949
TOTAL ASSETS	3,370,611	3,500,229
<u>LIABILITIES</u>		
CURRENT LIABILITIES		
Payables	1,938,502	603,474
TOTAL CURRENT LIABILITIES	1,938,502	603,474
TOTAL LIABILITIES	1,938,502	603,474
NET ASSETS	1,432,109	2,896,755
<u>EQUITY</u>		
Contributed Equity	12,232,626	12,232,626
Accumulated losses	(11,241,543)	(9,776,897)
Reserves	441,026	441,026
TOTAL EQUITY	1,432,109	2,896,755

The consolidated balance sheet should be read in conjunction with the accompanying notes

BONE MEDICAL LIMITED and Controlled Entities
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Consolidated Statement of Changes in Equity
For the half-year ended 31 December 2007

	Issued Capital Ordinary	Retained Earnings	Option Reserve	Total
	\$	\$	\$	\$
Balance at 1st July 2006	8,274,883	(6,359,934)	309,000	2,223,949
Loss attributable to members of parent entity	-	(1,330,950)	-	(1,330,950)
Total recognised income & expense for the year	-	(1,330,950)	-	(1,330,950)
Ordinary shares issued under placement	1,783,107	-	-	1,783,107
Options issued during the year	-	-	8,200	8,200
Balance at 31st December 2006	10,057,990	(7,690,884)	317,200	2,684,306
Balance at 1st July 2007	12,232,626	(9,776,897)	441,026	2,896,755
Loss attributable to members of parent entity	-	(1,464,646)	-	(1,464,646)
Total recognised income & expense for the year	-	(1,464,646)	-	(1,464,646)
Balance at 31st December 2007	12,232,626	(11,241,543)	441,026	1,432,109

The above consolidated statement of changes in equity should be read in conjunction with the accompanying notes

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Consolidated Cash Flow Statement
for the half-year ended 31 December 2007

	Economic Entity	
	31.12.2007	31.12.2006
	\$	\$
CASH FLOWS FROM OPERATING ACTIVITIES		
Receipts from government grants	312,688	291,236
Payments to suppliers & employees	(1,452,525)	(1,531,315)
Interest received	26,458	21,035
Net cash (outflow) from operating activities	(1,113,379)	(1,219,044)
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of property, plant & equipment	-	(2,608)
Net cash (outflow) from investing activities	-	(2,608)
CASH FLOWS FROM FINANCING ACTIVITIES		
Proceeds from issue of shares & other equity securities	996,104	1,783,107
Net cash inflow from financing activities	996,104	1,783,107
Net increase (decrease) in cash & cash equivalents	(117,275)	561,455
Cash & cash equivalents at beginning of the half year	1,478,640	220,559
Cash & cash equivalents at the end of half year	1,361,365	782,014

The above consolidated cash flow statements should be read in conjunction with the accompanying notes.

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NOTES TO FINANCIAL REPORTS

1 Basis of Preparation

This general purpose financial report for the interim half-year reporting period ended 31 December 2007 has been prepared in accordance with Accounting Standard AASB 134 *Interim Financial Reporting* and *Corporations Act 2001*.

This interim financial report does not include all the notes of the type normally included in an annual financial report. Accordingly, this report is to be read in conjunction with the annual report for the year ended 30 June 2007 and any public announcements made by Bone Medical Limited during the interim reporting period in accordance with the continuous disclosure requirements of the Corporations Act 2001.

The accounting policies adopted are consistent with those of the previous financial year and corresponding interim reporting period.

Accounting Policies

(a) Going Concern

The accounts have been prepared on a going concern basis. Future capital raisings will be required in order to continue the research and development of the company's products and technology to achieve a position where they can commercialise or market the products and technology.

In common with biotechnology companies, the company's operations are subject to risk & uncertainty due primarily to the nature of research, development and commercialisation to be undertaken.

The ability of the company to continue as a going concern is dependent upon the company raising further capital sufficient to meet the company's expenditure commitments.

The company is required to raise significant additional funding in order to continue to research and develop the company's products and technology to achieve a position where they can commercialise or market the products and technology.

The Directors and senior management have prepared a cash flow forecast for the foreseeable future reflecting the above mentioned expectations and their effect upon Bone Medical Limited or controlled entities. The achievement of the forecast is dependant upon future capital raising, the outcome of which is uncertain.

In the event that sufficient capital raising at an amount and timing necessary to meet the future budgeted operational and investing activities of the company is unfavourable the Directors believe that they will be able to contain the operating and investment activities sufficiently to ensure that Bone Medical Limited or controlled entities can meet its debts as and when they become due and payable.

In the unlikely event that the events referred to above result in a negative outcome, then the going concern basis of accounting may not be appropriate with the result that the Group may have to realise its assets and extinguish its liabilities other than in the normal course of business and in amounts different from that stated in the financial report.

The financial report does not include any adjustments relating to the recoverability or classification of recorded asset amounts or classification of liabilities that might be necessary should Bone Medical Limited or controlled entities not be able to continue as a going concern.

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NOTES TO FINANCIAL REPORTS (continued)

2 Loss for the half-year

There were no items included in the loss for the half-year that that were considered to be unusual because of their nature, size or incidence

3 Segment Information

In the half-year ending 31st December 2007 & 31st December 2006, the Company has predominantly undertaken all its business activities in the biopharmaceutical segment in Australia.

4 Contingent Liabilities

Licence agreement obligations:-

Under the licence agreement between Bone Limited and Axxess Limited the following terms apply:

£1,030,000 is payable to Axxess Limited as a lump sum payment upon any of the following events occurring:-

- The completion of a \$15 million fundraising,
- Any licence transaction involving upfront or milestone payments of equal to or more than \$10 million.
- The commencement of a pivotal Phase III study (or the study prior to lodgement for regulatory approval from the FDA or EMEA) for any project in Bone Medical Limited, subject to the company having at least \$5 million in the bank.

As the licence payment has not been paid in full by the 4th January 2006, a monthly interest charge is payable on the unpaid balance at a rate equal to the 30 day London Interbank Offering Rate (LIBOR) on the 4th day of each month plus 2%.

5 Dividends

No dividends were declared during the half year.

6 Discontinued Operation

2007

There were no discontinued operations in the half-year ended 31st December, 2007

2006

There were no discontinued operations in the half-year ended 31st December, 2006.

7 Trade and Other Liabilities

CURRENT	31.12.2007	30.6.2007
Trade Payables	259,635	275,198
Sundry payables and accrued expenses	94,219	60,048
Other related parties	588,544	254,130
Key management personnel related entities	-	14,098
Receipts for un-allotted shares	996,104	-
	<u>1,938,502</u>	<u>603,474</u>

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NOTES TO FINANCIAL REPORTS (continued)

8 Events occurring after the balance sheet date

On the 7th January 2008 Bone Medical Limited completed a private placement raising \$1.245m. 2,723,350 ordinary shares were issued at \$0.30 each with an additional 1,427,253 ordinary shares to be issued subject to a General Meeting of shareholders to be held on the 5th March 2008. Each share qualifies for one free attaching option exercisable at \$0.40 expiring 18 months from the date of issue.

9 Equity securities issued

Issues of ordinary shares during the half-year	2007 Shares	2006 Shares	2007 \$	2006 \$
Ordinary shares issued by private placement	-	6,604,101	-	1,783,107

10 Recoverability of Goodwill

The recoverability of the amount of goodwill is based upon Bone Medical Limited and controlled entities being able to continue as a going concern, by way of raising further capital in order to meet expenditure commitments to be able to successfully exploit the company's products & technologies in excess of the carrying value of the goodwill.

(a) Impairment tests for goodwill

The goodwill acquired through a business combination of \$1.957m relates to novel technology for the oral delivery of peptides for the treatment of Osteoporosis & Osteoarthritis.

The recoverable amount of goodwill is determined based on value-in-use calculations. These calculations use cash flow projections based on financial budgets approved by management covering a five-year period.

(b) Key assumptions used for value-in-use calculations

The cash flow projections rely upon the successful commercialisation of Bone Medicals' two lead projects, Oral Sct & Oral Pth, which are now entering a phase of development whereby commercialisation is possible by way of licencing deals, consisting of both milestone payments and royalties payments typical of the Biotech Industry, with large pharmaceutical company's. The discount rate used being 30.48% reflects the high level of risk associated with biotechnology research and development staged companies.

(c) Impact of possible changes in key assumptions

The calculated recoverable amount of goodwill based on the cash flow projections is significantly greater than the carrying value of goodwill. If the discount factor applied is raised to 50%, the calculated recoverable amount remains considerably greater than the carrying value of goodwill.

(d) Impairment Charge

In the opinion of the board there have been no events that have occurred during or since the reporting period that is likely to have a negative effect on the carrying value of goodwill. Therefore no impairment to goodwill has been charged.

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Directors' Declaration

In the directors' opinion:

- (a) the financial statements and notes set out on pages 6 to 12 are in accordance with the *Corporations Act 2001*, including:
 - (i) complying with Accounting Standards, the *Corporations Regulations 2001* and other mandatory professional reporting requirements; and
 - (ii) giving a true and fair view of the consolidated entity's financial position as at 31 December 2007 and of its performance for the half-year ended on that date; and
- (b) there are reasonable grounds to believe that Bone Medical Limited will be able to pay its debts as and when they become due and payable.

This declaration is made in accordance with a resolution of the directors.



Leon Ivory
Director

Perth, Western Australia
29th February, 2008



INDEPENDENT AUDITOR'S REVIEW REPORT TO THE MEMBERS OF BONE MEDICAL LIMITED

We have reviewed the accompanying half-year financial report of Bone Medical Limited, which comprises the condensed balance sheet as at 31 December 2007, and the condensed income statement, condensed statement of changes in equity and condensed cash flow statement for the half-year ended on that date, a statement of accounting policies, other selected explanatory notes and the directors' declaration of the consolidated entity comprising the disclosing entity and the entities it controlled at the half-year end or from time to time during the half-year in order for the disclosing entity to lodge the half-year financial report with the Australian Securities and Investments Commission.

Directors' Responsibility for the Half-Year Financial Report

The directors of the disclosing entity are responsible for the preparation and fair presentation of the half-year financial report in accordance with Australian Accounting Standards (including the Australian Accounting Interpretations) and the *Corporations Act 2001*. This responsibility includes designing, implementing and maintaining internal control relevant to the preparation and fair presentation of the half-year financial report that is free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's Responsibility

Our responsibility is to express a conclusion on the half-year financial report based on our review. We conducted our review in accordance with Auditing Standard on Review Engagements ASRE 2410 *Review of an Interim Financial Report Performed by the Independent Auditor of the Entity*, in order to state whether, on the basis of the procedures described, we have become aware of any matter that makes us believe that the financial report is not in accordance with the *Corporations Act 2001* including: giving a true and fair view of the disclosing entity's financial position as at 31 December 2007 and its performance for the half-year ended on that date; and complying with Accounting Standard AASB 134 *Interim Financial Reporting* and the *Corporations Regulations 2001*. As the auditor of Bone Medical Limited, ASRE 2410 requires that we comply with the ethical requirements relevant to the audit of the annual financial report.

A review of a half-year financial report consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with Australian Auditing Standards and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Independence

In conducting our review, we have complied with the independence requirements of the *Corporations Act 2001*. We confirm that the independence declaration required by the *Corporations Act 2001* would be in the same terms if it had been given to the directors at the time that this auditor's review report was made.

Conclusion

Based on our review, which is not an audit, we have not become aware of any matter that makes us believe that the half-year financial report of Bone Medical Limited is not in accordance with the *Corporations Act 2001* including:

- (a) giving a true and fair view of the consolidated entity's financial position as at 31 December 2007 and of its performance for the half-year ended on that date; and
- (b) complying with Accounting Standard AASB 134 *Interim Financial Reporting* and Corporations Regulations 2001.

Material Uncertainty Regarding Continuation as a Going Concern

Without qualifying our conclusion, we draw attention to Note 1 in the interim financial report. As a result of the matters described in Note 1, there is significant uncertainty whether Bone Medical Limited and controlled entities will be able to continue as a going concern and therefore whether it will realise its assets and extinguish its liabilities in the normal course of business and at amounts stated in the financial report.

Material Uncertainty Regarding Recoverability of Goodwill

Without qualifying our conclusion, we draw attention to Note 10 in the interim financial report. As indicated in Note 10 to the financial statements, Bone Medical Limited has goodwill as at 31 December 2007 with a carrying value of \$1,956,599. This amount is recoverable based upon Bone Medical Limited and controlled entities being able to continue as a going concern as outlined in the above paragraph. This amount is also dependent upon Bone Medical Limited and controlled entities being able to successfully exploit the company's products and technology at amounts in excess of the carrying value.

BDO Kendalls Audit & Assurance (WA) Pty Ltd

BDO Kendalls
BG McVeigh

BG McVeigh
Director

Perth, Western Australia
Dated this 29th day of February 2008