

Annual Report 2004

Highlights

Corporate

- Fully underwritten Rights Issue and Issue for Cash raised £14.4m net
- Further divestments of non-core assets

Commercial

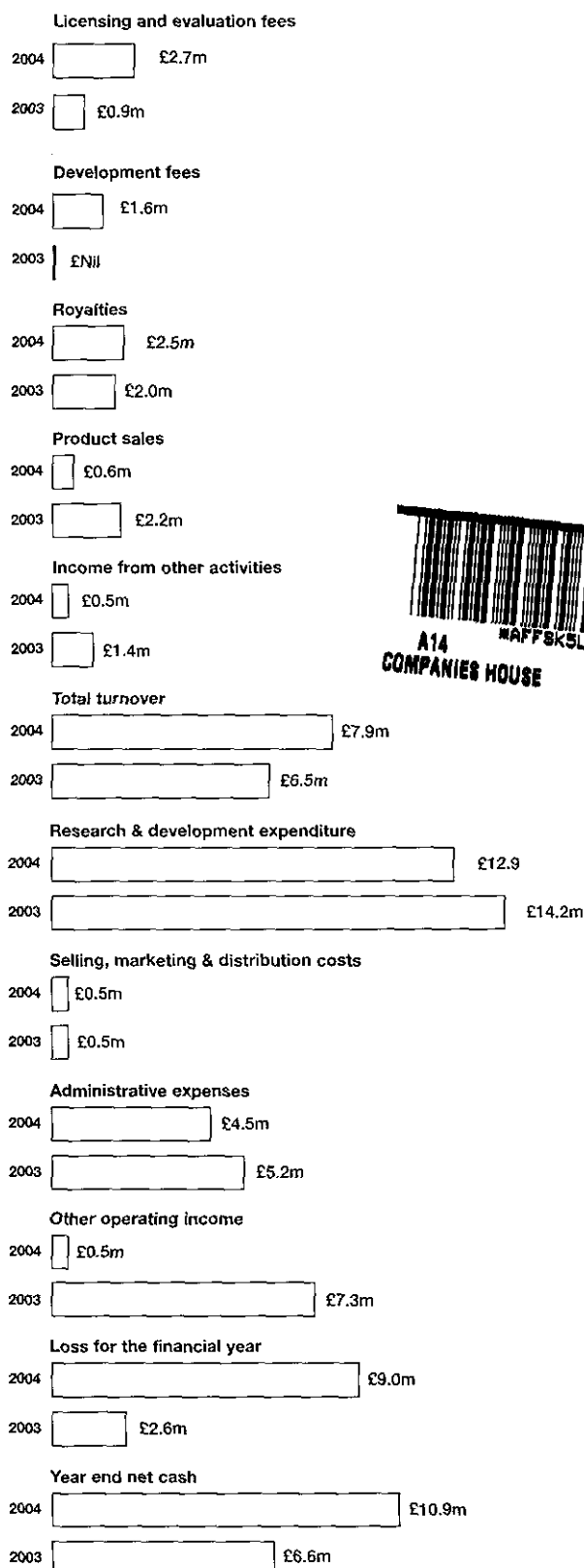
- First licence agreement for an NCE in Clickhaler
- First licence agreement for C200 combination inhaled therapy
- Second licence agreement for Clickhaler in Japan

Product development progress

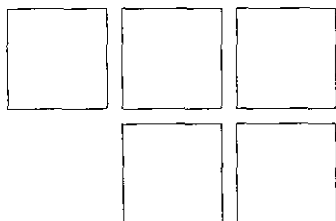
- Adept - US Phase III study preliminary results
- Alpharen™* commenced Phase IIa study
- Formoterol Clickhaler - regulatory filing in Canada
- Budesonide Clickhaler - regulatory filing in EU
- Meptin Clickhaler - regulatory filing in Japan
- CTL 102
 - Prostate cancer - Phase II study commenced
 - Prosthesis repair - Phase I/II study commenced
- CTL 901
 - Melanoma - Phase I/II study commenced

* Alpharen is a trade mark of Ineos Silicas Healthcare Limited

Summary Financial Performance



Chairman's Statement



In January 2004 we successfully raised £14.4m by way of a fully underwritten Rights Issue and an issue for Cash. At that time we issued a circular describing how the Board intended to use those proceeds and I am pleased to report on our progress towards achieving the objectives identified.

Throughout the financial year ended 30th September 2004 and the subsequent period to date, we have made considerable progress in the development and commercialisation of our portfolio of pharmaceutical products and technologies which resulted in the following principal outcomes:

Clinical and regulatory progress -

• ADEPT -

In December 2004 we announced the preliminary unaudited results of our pivotal Phase III US multi-centre clinical trial of Adept, our adhesion reduction therapy. This clinical trial was a landmark study as it was the first double-blind randomised controlled clinical study with an adhesion reduction agent, and the largest clinical laparoscopic second-look adhesions study ever undertaken.

The data analysis demonstrated that those patients who received Adept showed improvement over the comparator group in all measurements of efficacy whilst maintaining a similar safety profile.

We therefore plan to file an application with the US Food and Drug Administration ('FDA') for a US marketing authorisation in the first quarter of 2005. The outcome of the application is anticipated in 2006 and, if successful, will be followed by launch in the US subject to the appointment of a licensee for that territory.

We consider it is likely that Japanese marketing approval will be facilitated by data generated by the US study. Consequently, we are in discussions with potential licensees for the US, Japanese and other Asian markets and we anticipate that the appointment of licensees for these valuable territories should generate

substantial milestone receipts during 2005.

We are excited by the prospects for Adept and believe it has the potential to be used routinely in all abdominal surgery due to its safety profile, ease of use and potential cost advantage.

• ALPHAREN™* -

Our collaboration with Ineos Silicas Healthcare Limited to develop its novel compound for the treatment of hyperphosphataemia in kidney failure patients saw the encouraging initial results of the Phase I study presented at both the American Society of Nephrology in November 2003 and the European Dialysis and Transplant Association meeting in May 2004. In addition we commenced a Phase IIa clinical study in the period and progressed the design of the Phase IIb study.

We consider Alpharen could be a significant entrant to this rapidly growing market segment given its substantial phosphate binding activity as demonstrated in the Phase I study.

• FORMOTEROL CLICKHALER -

Dialogue with the regulators regarding our application for European marketing authorisation continued in the period and outcome is anticipated shortly. Approval of the product will trigger a significant milestone receipt from our licensee, as will European marketing launch which is anticipated in H1 2005.

Application for marketing authorisation was also filed in Canada and launch of the product in that country, which is anticipated in H2 2006, will trigger a further significant milestone receipt. The product launches will be followed by royalties on sales.

• BUDESONIDE CLICKHALER -

The application for European marketing authorisation was filed in November 2003 triggering a significant milestone receipt from our licensee. European marketing approval of this product is also anticipated shortly enabling

* ALPHAREN is a trade mark of Ineos Silicas Healthcare Ltd.

launch in H1 2005. Both events will trigger further significant milestone receipts and will be followed by royalty income post launch.

- MEPTIN CLICKHALER -

Otsuka Pharmaceutical Co. Ltd., a leading Japanese healthcare company, has an exclusive licence for the delivery of Meptin, its asthma treatment, in Clickhaler in Japan and Spain. In May 2004 we announced that data produced by Otsuka had been filed with the Japanese regulator triggering a further milestone receipt. Approval and launch of Meptin Clickhaler in Japan are anticipated in 2005 which will trigger further milestone receipts and income from the supply of Clickhalers to Otsuka.

- CTL102 in Prostate Cancer -

We commenced the treatment phase of our *Phase II study to evaluate the efficacy and safety* of our novel treatment of prostate cancer during the year. The trial, which is the first of its kind in prostate cancer in the UK, has progressed during the period and we anticipate reporting the outcome in H1 2006.

- CTL102 in Prosthesis Repair -

In collaboration with the University of Leiden, we commenced a Phase I/II study to evaluate the potential for the cell killing capability of CTL102 to be used in prosthesis revision surgery to facilitate the refixing of loosened prostheses.

The object of study, which will be undertaken in 12 inoperable patients, is to assess the response to therapy in respect of mobility and pain, and we expect the study will complete in H2 2005.

- CTL901 -

In December 2003 the first patient was entered into the Phase I/II clinical trial of our treatment of skin cancer (advanced melanoma) by our collaborators at Birmingham University. Recruitment has continued and we expect the trial to complete in H1 2005.

Commercialisation progress -

Innovata Biomed ('IB'), our respiratory drug delivery subsidiary, achieved considerable commercial success in the period which, significantly, included the signing of both the first commercialisation agreement for our new C200 combination inhaler and the first agreement for a New Chemical Entity ('NCE') to be delivered in Clickhaler.

- C200 multi-dose breath-actuated inhaler -

Combination delivery of inhaled drugs is increasingly being seen as the most effective means of controlling asthma and the C200 device, coupled with IB's formulation expertise, provides a fast development route to this rapidly growing sector. The market for combination asthma therapy is currently valued globally at over \$5 billion p.a. and projected to exceed \$6 billion p.a. by 2006 (Source: Datamonitor).

In June 2004 we announced an exclusive agreement with a global pharmaceutical group whereby IB will develop a respiratory treatment comprising a combination of two established respiratory medications in C200. Our licensee will market and distribute the product in Europe and certain other specified countries with IB having retained the rights for all other territories including the US and Japan.

The agreement, which is the second with this licensee, provides for IB to receive access fees and milestone receipts totalling £7.5m. In addition, IB will conduct the development programme on behalf of the licensee which could generate development fees of up to a further £9m. IB will receive royalties on sales, with first launch anticipated in 2008, and will supply C200 inhalers to the licensee on commercial terms.

We believe the C200 technology could be used to deliver a number of inhaled products in combination with new, or established, molecules and IB continues to seek collaborations with other pharmaceutical companies with the object of securing further valuable licensing deals for the C200 device.

Chairman's Statement

• CLICKHALER -

Budesonide Clickhaler Japan -

In September 2004 we announced that IB had signed an exclusive agreement with a Japanese pharmaceutical company for marketing rights to budesonide Clickhaler for that territory. We are delighted that following extensive evaluation the company selected IB's budesonide Clickhaler.

Under the terms of the agreement, IB received an access fee and will receive subsequent milestone receipts. IB will provide assistance to the company in completing the necessary clinical studies to obtain regulatory approval in Japan, where the company expects to launch the product in 2008. IB will supply the product to the company on commercial terms thereafter.

This agreement is the second licence of Clickhaler in Japan and should generate important income for the Group.

PLIVA Clickhaler -

In December 2003 IB entered into an agreement with PLIVA, a multi-national pharmaceutical company, to develop a novel asthma medication based on PLIVA's NCE steroid and Clickhaler. Under the agreement, IB will receive development fees, milestone receipts and royalties on sales. In addition, IB will supply Clickhalers on commercial terms.

This agreement is significant in that it represents the first agreement for an NCE to be delivered in Clickhaler and sets IB on the pathway to achieving its objective of becoming a leading independent provider of dry powder inhalation technologies for the delivery of NCE respiratory compounds.

Disposals

In December 2003 we sold the balance of our shareholding in Cobra Biomanufacturing Plc ('CBM') realising a further £1.2m, net of expenses, bringing the total gross sum realised from the divestment of that business to circa £8.2m. In February 2004 we disposed of our loss making

educational training business where the consideration received was in the form of shares in the purchaser which we have retained as a £0.2m investment.

Financial results

The loss before tax in the year of £10.9m compares with a loss of £2.8m in the previous year which reflected the benefit of £7.3m resulting from accounting for transactions with Paul Capital and profit on divestments of £5.7m compared with £0.5m and £0.8m respectively in the year under review. The financial results are fully described in the Financial Review.

Funding

Our activities in the year were financed by a combination of the fundraising of £14.4m, net of expenses, royalty and milestone income generated by those of our products that have been commercialised, and proceeds from the disposal of assets.

Working capital

The cash flow projections of the Group include significant receipts of milestone income and proceeds from the potential disposal of assets. Historically we have demonstrated that we are able to generate receipts from such sources and we anticipate that we will continue to be able to do so. Consequently, we have a reasonable expectation that the Group will have sufficient working capital for the foreseeable future. However, given the difficulty in predicting accurately the timing and amount of such future receipts we will continue to keep the adequacy of our working capital under regular review.

Panos acquisition

In January 2004 we informed shareholders that we had agreed an arrangement whereby we may, in due course, acquire Panos, from whom we license our interest in Devacade, for a consideration to be paid in shares.

This arrangement remains in place, albeit still subject to contract.

Prospects

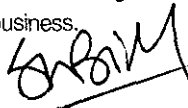
ML is currently generating income from products it has successfully developed and licensed to other pharmaceutical companies which we have achieved by utilising our core skills in clinical development, regulatory affairs and product commercialisation. Our development activities are focused on products and technologies with the potential to produce income in the relatively near term. We continue to believe that each of our products in development is of potentially high value with an acceptable risk profile and, accordingly, has a reasonable probability of generating income for the Group. Our potential for growth is supported by our established track record of sourcing a development pipeline through in-house initiatives, in-licensing and joint development agreements, all of which we will continue to pursue actively. Consequently we believe that the business is capable of achieving profitability in the near term and delivering value to shareholders over the long term. Therefore the Directors view the future prospects of the Group with confidence.

Corporate objective

Our objective is to develop and commercialise pharmaceutical products and technologies for specialist markets derived from intellectual property generated by our own research, in-licensed from third parties and through joint development programmes.

In the January 2004 circular to shareholders we stated that providing milestone income is received in line with current projections ML would be in a position to consider developing certain products through Phase III, adopting alternative commercialisation strategies and/or seeking to expand the pharmaceutical portfolio by in-licensing additional appropriate products, and I can confirm that this continues to be the case.

I would like to take this opportunity to thank all shareholders for their continuing support of the company and our employees whose hard work and dedication continue to deliver the products and technologies essential for the progress of the business.



S. W. Sim

Executive Chairman

25th January 2005

ML Pharmaceuticals

	"The clinical development and commercialisation of pharmaceutical products and technologies derived from intellectual property generated by our own research, in-licensed from third parties and resulting from joint development agreements."									

ML Pharmaceuticals is a pharmaceutical product development business with a track record of successful clinical development, regulatory approval and licensing of pharmaceutical products and a development pipeline of future products targeted at specialist markets. Its activities are supported by revenue streams from products which have been successfully developed and licensed to other pharmaceutical companies. In addition ML also generates income by licensing patented technologies resulting from its research to third parties for use in the discovery and manufacture of biotechnology products.

In-market products

	Research	Pre-clinical	Phase I	Phase II	Phase III	Regulatory approval	Marketed
EXTRANEAL*/RENAL							
ADEPT/ADHESIONS (EUROPE)							

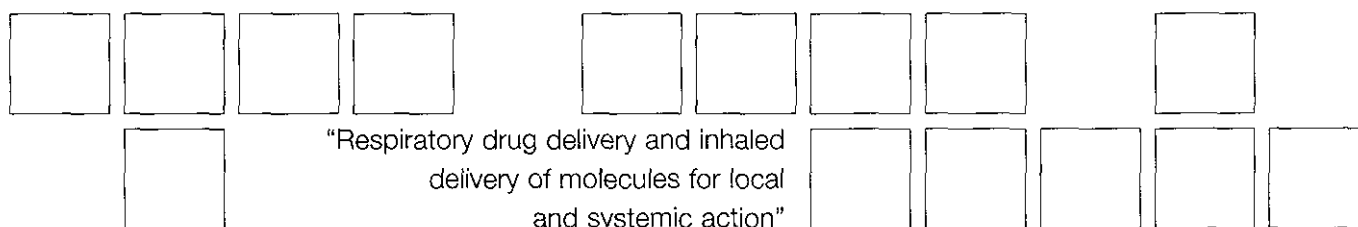
Products in development

	Research	Pre-clinical	Phase I	Phase II	Phase III	Regulatory approval	Marketed
DEXEMEL - ONCOLOGY & GENE THERAPY							
ADEPT/ADHESIONS (US)							
ALPHAREN*/PHOSPHATE BINDER - HYPERPHOSPHATAEMIA							
DEVACADE - PAIN MANAGEMENT							
CTL102 - PROSTATE CANCER							
CTL 901 - MELANOMA							
CTL 102 - PROSTHESIS REPAIR							
EMMELLE - CHLAMYDIA							

* Trademark of Baxter Healthcare

+ Trademark of Ineos Silicas Healthcare Limited

Innovata Biomed



Innovata Biomed's core competency is in the design, formulation, development and industrialisation of innovative technologies for delivering compounds to the lung. Its unique strengths lie in the ability to provide inhaled drug delivery solutions to the global pharmaceutical industry based on a proven track record of regulatory approvals and volume manufacture of its founding technologies which are inhalation devices for the administration of drugs for respiratory disease.

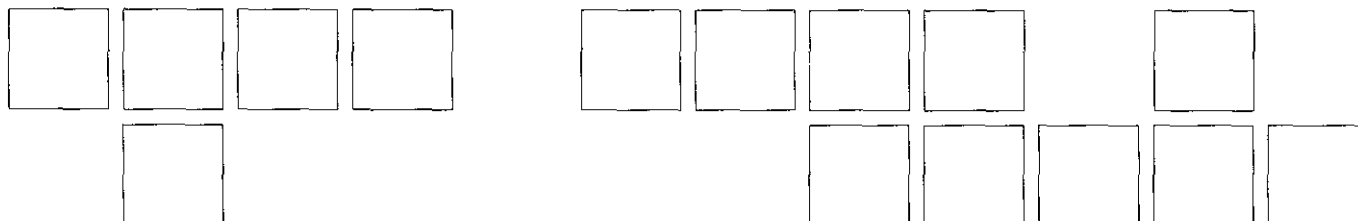
In-market products

Research	Pre-clinical	Phase I	Clinical trials Phase II	Phase III	Regulatory approval	Marketed
ASMASAL CLICKHALER						
ASMABEC CLICKHALER						

Products in development

Research	Pre-clinical	Phase I	Clinical trials Phase II	Phase III	Regulatory approval	Marketed
BUDESONIDE CLICKHALER						
FORMOTEROL CLICKHALER						
OTSUKA CLICKHALER						
PLIVA CLICKHALER						
C200 COMBINATION						
BUDESONIDE CLICKHALER JAPAN						

Operational Review



OPERATIONAL STRUCTURE

The Group's activities are organised into two principal operations - ML Pharmaceuticals and Innovata Biomed, the Group's respiratory subsidiary.

ML Pharmaceuticals is a pharmaceutical product development business with a track record of successful clinical development, regulatory approval and licensing of pharmaceutical products and a development pipeline of future products targeted at specialist markets. Its activities are supported by revenue streams generated from products which have been successfully developed and licensed to other pharmaceutical companies.

Innovata Biomed is an independent provider of inhaled drug delivery technology to the pharmaceutical industry. IB's proven delivery technology is available for proof of principle testing and as a "fast-to-market" drug delivery solution. Existing licence agreements generate development fees, royalty income and milestone receipts which support the business's ongoing development programmes.

Both businesses operate as distinct divisions with their own research, clinical development and business development capabilities, supported by centrally provided services which include regulatory affairs, intellectual property management, finance and administration.

PRODUCT DEVELOPMENT REVIEW

ML PHARMACEUTICALS

EXTRANEAL - a solution of Icodextrin for use in Peritoneal Dialysis treatment

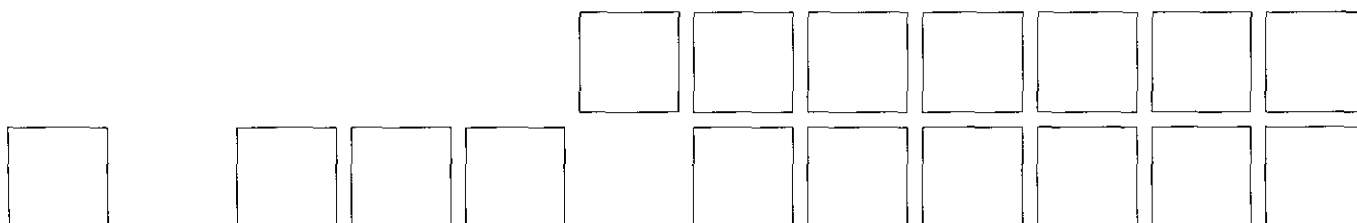
Icodextrin solution is used in peritoneal dialysis for the treatment of renal failure patients, wherein waste products and excess fluid pass from the patient's blood into a dialysis solution which has been infused into the abdominal cavity, all of which is subsequently drained out. ML holds patents over Icodextrin, the active ingredient, in all appropriate major countries.

The product has been licensed on an exclusive worldwide basis to Baxter Healthcare, a market leader in renal disease treatments. Baxter has launched the product under its trade name, Extraneal, firstly in the UK in 1996 and subsequently in a further 35 countries, including the two major markets of USA and Japan in 2003, which offer the prospect of significant royalty income. As a result Extraneal is now commercially available in all of the world's major pharmaceutical markets.

Currently more than 15,000 patients worldwide are using the solution on a daily basis and over 50,000 patient-years experience in routine clinical use has been gained to date.

ADEPT - a solution of Icodextrin for the reduction of post-operative adhesions

Adhesions are a serious and frequent complication following abdominal and gynaecological surgery and are acknowledged as a major surgical problem. Adhesions are expensive to treat, often requiring further surgery



and hospitalisation. Currently available treatments are both expensive and difficult to administer, often requiring specific training. Adept offers significant advantages in that it is an easy to use, low viscosity solution which can be delivered via a laparoscope in minimally invasive (keyhole) surgery and is readily incorporated into routine surgical procedures.

Shire Pharmaceuticals PLC ('Shire'), our licensee for Europe, is achieving growing use of this product with gynaecologists and with general surgeons carrying out colorectal operations. ML retains all rights to Adept for the rest of the world.

The clinical development of Adept has been concentrated in the US where we recently completed the pivotal Phase III clinical trial, ('the PAMELA study'), the object of which was to *determine the efficacy and safety of Adept in the reduction of post surgical adhesions after laparoscopic surgery*. The preliminary results of this study were announced in December 2004 and confirmed that Adept demonstrated significant benefits over the control therapy in reducing adhesions and improving the status of gynaecological patients.

The analysis demonstrated that those patients who received Adept showed improvement over the comparator group in all measurements of efficacy whilst maintaining a similar safety profile. We therefore have sufficient confidence to progress the filing of an application with the US Food and Drug Administration ('FDA') for a US marketing authorisation.

The PAMELA study was an evaluation of Adept as an adjunct to adhesiolysis surgery conducted in 16 gynaecology units in the US. The study was a double blind comparison of Adept and an

optimised control therapy using Ringer's lactate solution ('RLS'). A total of 449 patients were randomised to treatment.

The detailed analysis demonstrated that Adept *significantly reduced the number of adhesions* in patients undergoing adhesiolysis. Adept demonstrated a 30% improvement when compared to the control patients who received the optimised therapy using RLS. In addition, Adept treatment resulted in significantly fewer patients with newly formed adhesions.

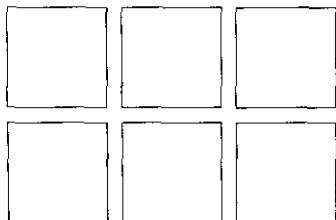
In routine clinical use the safety of Icodextrin, the active ingredient in Adept, has been firmly established in peritoneal dialysis (over 50,000 patient-years experience worldwide) and in adhesion reduction in over 100,000 surgical patients in Europe. In addition, the PAMELA study showed that *the overall incidence of adverse events in the Adept and control groups was similar*.

Unusually, the study protocol included several statistically defined primary endpoints. Whilst not all were achieved, the significant benefits demonstrated and the positive responses of the clinical investigators have confirmed to us that Adept represents a valuable therapeutic product.

In addition, the PAMELA trial data will form the basis for advanced stage ongoing negotiations with potential licensees for the US and Japan and for the negotiation of the remaining milestone payment from Shire.

Our view is that uptake of available competitive treatments for adhesions has been hampered by their complexity of use and cost. We consider that an ideal anti-adhesion agent should be safe, cost effective, easy to use and capable of

Operational Review



reducing adhesion formation at the operating site and throughout the peritoneal cavity. The preliminary results of the PAMELA study suggest that Adept fits this profile and can assist in reducing the burden of adhesions.

We anticipate filing an application with the FDA for a US marketing authorisation in the first quarter of 2005 following completion and audit of the full statistical analysis and compilation of the final clinical report of the study.

ALPHAREN™ - a Phosphate Binder for the treatment of Hyperphosphataemia

Abnormally high and damaging levels of phosphate in the blood occur when failing kidneys are unable to rid the body of excess phosphate absorbed from food. Patients suffering from end-stage renal failure usually need to take a phosphate binding product to prevent absorption of phosphate and reduce blood concentrations. The novel compound we are co-developing with Ineos Silicas Healthcare Limited has been shown in pre-clinical and Phase I human volunteer tests to have substantial phosphate binding activity. Furthermore, the product does not contain aluminium or calcium ions which could cause safety concerns in long term use, therefore also rendering Alpharen potentially applicable for use in pre-dialysis renal failure patients.

A Phase I study has demonstrated that healthy volunteers were able to tolerate the drug in doses sufficient to cause a significant reduction in phosphate absorption from the diet. A Phase IIa study is underway.

This product meets our product selection criteria ideally, as its clinical efficacy can be readily demonstrated in a relatively small number of kidney failure patients.

Gene Therapy Products

CTL102 in Prostate Cancer -

Prostate cancer is the most common cancer in men in the UK with over 24,700 new cases a year. The lifetime risk for being diagnosed with prostate cancer is 1 in 14*. The treatment technique uses gene therapy technology to deliver a cancer killing toxin direct to the tumour site in a two stage

process. The mode of action is the delivery of the gene for a bacterial enzyme, nitroreductase, to cancer cells such that a separately administered, relatively harmless drug, CB1954, will be activated in the tumour to kill the cancer cells. In November 2003 we announced the commencement of the treatment stage of our Phase II clinical trial of prostate cancer and we expect to report the outcome of the trial in H1 2006.

We are hopeful that the novelty of the product could establish a marketable platform from which gene therapy products can be developed by third party licensees for the treatment of other tumours.

CTL 102 in Prosthesis repair -

In collaboration with the University of Leiden, we are evaluating the potential for the cell killing capability of CTL 102 to be used in prosthesis revision surgery.

Patients with artificial joints have a tendency for the prosthesis to work loose over time. The consequences of such loosening include pain and discomfort and often result in the patient having to undergo further lengthy operations to repair or replace the prosthesis. Many patients, particularly the elderly, may be unable to be subjected to such operations which are also very expensive. In some countries, prosthetic implants such as hips are not offered to younger patients because of the frequency with which they become loose and the cost of subsequent surgery.

The product concept is designed to enable orthopaedic surgeons to destroy the rubbery interface tissue surrounding loose prostheses which cannot otherwise be easily removed. Once destroyed, the tissue can be aspirated to enable replacement bone cement to be injected into the area, thereby refixing the prosthesis.

A Phase I/II study is underway to assess the response to therapy of 12 inoperable patients in respect of mobility and pain. The study is expected to complete in H2 2005.

CTL901 in Melanoma -

A Phase I/II clinical trial is being conducted by

*Source: Statistics from Cancer Research UK

our collaborators at the Cancer Research UK Institute for Cancer Studies at Birmingham University on our treatment for malignant melanoma. This treatment is based on the delivery of genes encoding tumour associated antigens to antigen presenting cells known as dendritic cells, a component of the immune system. In the trial, dendritic cells isolated from the patients' blood are modified using our proprietary antigen delivery system, CL22. The modified dendritic cells are returned to the patients by injection in order to induce the patients' immune system to attack tumour cells. Pre-clinical data suggest that this treatment will specifically attack skin cancers as well as the cancerous cells which leave the tumour and spread the disease throughout the body. We consider that our CL22 system is a platform technology that may prove to be capable of modifying dendritic cells for the treatment of other advanced forms of cancer for which no effective treatments are available.

Gene Expression Technology

Agreements have been signed with a number of biotechnology and pharmaceutical companies to evaluate the UCOE technology for facilitating gene expression and thereby increasing the efficiency of therapeutic protein production. In addition we have an agreement with Medarex to apply our UCOE gene expression technology for antibody production. We consider that the licensing of this technology will continue to generate revenues in the near term in the form of licence fees and potentially, in the long term, in the form of royalties on the sale of products using this technology.

DEVACADE - for enhancing the pain relief produced by morphine

Pre-clinical studies with Devacade demonstrated that this new chemical entity ('NCE') has the ability to enhance the pain relieving properties of drugs such as morphine without increasing the disturbing and dangerous side-effects experienced with such drugs. In a Phase II programme Devacade, when given as an adjunct to those drugs, reduced pain levels and patients reported reduced levels of sleep disturbance from their pain and reduced interference in

activities owing to pain.

Further clinical programmes are being designed to assess the efficacy and required dose levels for the use of Devacade as an adjunct to opioid analgesia in a number of pain states.

We continue actively to seek a licensee who is able to complete the required clinical programme and market this novel product.

EMMELLE intravaginal gel

In September 2004 we announced that the Medical Research Council was not prepared to take Emmelle forward into its Phase III microbicide programme for the prevention of transmission of HIV. Therefore, given the poor potential for an acceptable financial return to ML were it to take the product forward, we discontinued our activities related to this programme.

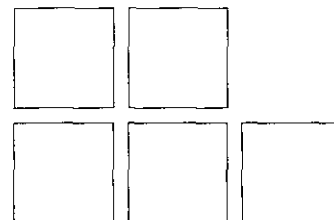
A pre-clinical programme is underway to evaluate the activity of Emmelle against chlamydia and herpes simplex virus.

INNOVATA BIOMED

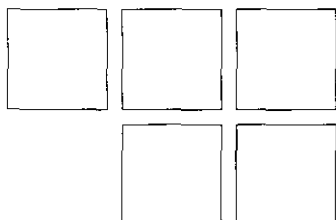
CLICKHALER - a fast-to-market dry powder inhaler for new asthma therapies.

Clickhaler is a proven, industrialised dry powder inhaler ('DPI') with many established advantages over standard asthma inhalers. Clickhaler has been extensively studied and shown to be highly acceptable to patients, regulators and potential licensees. Furthermore, it is already marketed by Celltech with standard asthma therapies (salbutamol and beclomethasone) in the UK, Ireland and France.

In September 2002 we announced that we had entered into an exclusive licence agreement with a major global pharmaceutical group for the rights to market the two asthma therapy molecules, budesonide and formoterol, in Clickhaler in Europe and a number of other territories. Taking into account monies already received we anticipate this agreement will generate £10m in access fees and milestone receipts plus double digit royalties on future product sales.



Operational Review



In November 2002 the first application for marketing authorisation for formoterol Clickhaler in Europe was submitted, which was followed by application to the Canadian regulators in November 2003. We anticipate reaching the European and Canadian markets through our licensee in 2005 and 2006 respectively. The application for European marketing authorisation for budesonide Clickhaler was filed in November 2003 with launch expected in 2005. Revenues from both budesonide and formoterol Clickhaler are expected to flow from sales for the commercial life of the products.

Negotiations were completed in March 2003 for the delivery of Otsuka Pharmaceutical Company's established drug, Meptin, using IB's Clickhaler, in Japan and Spain. This drug is already being sold by Otsuka in a CFC metered dose inhaler format and they expect to be able to commence substitution of sales of their existing product with Clickhaler once approval is granted by the Japanese regulators, which we anticipate will be received in H1 2005.

In December 2003 an agreement was entered into with PLIVA to develop a novel asthma medication based on PLIVA's NCE steroid and Clickhaler.

In September 2004 an agreement was entered into with a Japanese company for the rights to budesonide Clickhaler for Japan. We believe this agreement further cements Clickhaler's reputation as a leading independently provided dry powder inhaler.

In addition, further formulation studies have been undertaken by IB, both alone and with potential partner companies, to evaluate the performance of Clickhaler in the laboratory. These studies include the assessment of novel and established molecules as well as new formulation technologies designed to enhance the performance of the device with certain drugs.

IB continues to build a library of data on the capabilities of its own device and formulation technologies, as well as third party formulation technologies, to enable it to provide an enhanced offering to the global pharmaceutical industry.

C200 Device – building on the CLICKHALER technology

IB has recognised the opportunity offered by developments in the treatment of asthma by combining two drugs in the same inhaler.

Patents have already been granted in Europe on the C200 device, which is a novel adaptation of the proven dose-metering 'engine' of Clickhaler, whereby in the same device two separate drug reservoirs feed two separate drug formulations to separate metering chambers from which they are delivered to the patient in the same breath. The ability to formulate the drugs separately permits optimisation of each individually, thereby offering the potential to overcome significant formulation challenges.

This concept allows for flexibility in the formulation of each active ingredient and enables IB to develop a portfolio of formulations which can be tailored to fit with New Chemical Entities ('NCE') from its partners' research and development programmes.

The C200 technology is designed to assist a number of established and new drugs to compete in the lucrative combination inhaled drug sector using device and formulation technologies being developed by IP.

In June 2004 IB announced an exclusive agreement with a major global pharmaceutical group to market and distribute a combination of two established respiratory medications in the C200 dry powder inhaler. The agreement covers Europe and certain other specified countries, with IB having retained the rights for all remaining territories including the US and Japan.

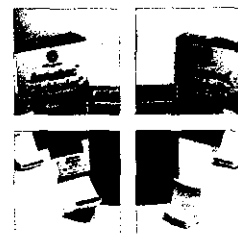
During the period under review, IB has worked with a number of drug formulations and device designs in order to optimise the first product which is planned to enter clinical trials in early 2006.

This agreement for our new C200 platform is significant for IB as we consider it represents a further step towards fulfilling IB's objective of becoming the leading, independent provider of dry powder inhalation solutions to the global pharmaceutical industry.

We believe that this advance in the core technology offering of IB presents an exciting opportunity to partner companies by providing a device which can deliver either more dose units or a larger dose payload (thereby reducing cost to the manufacturer and healthcare provider), or can deliver a novel molecule in combination with an established drug to address the rapidly growing inhalation market.

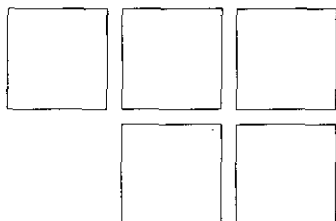
P.J. Shennan

Chief Operating Officer and Finance Director
25th January 2005



Financial Review

For the year ended 30th September 2004



Group operating results for both the year and the comparative year have been analysed in the consolidated profit and loss account between continuing activities and those discontinued as a result of the divestment of the educational training and Icodextrin manufacturing businesses in February 2004 and April 2003 respectively.

Turnover and gross profit

Turnover includes income from royalties and pharmaceutical product sales, which are stated *net of the entitlements of Paul Capital Royalty Acquisition Fund ('PCRAF')* where appropriate, and fee income from licensing, evaluation and development agreements.

Total turnover in the year was £7.9m (2003: £6.5m) of which £0.2m (2003: £2.8m) related to discontinued businesses. The increase in turnover included an increase in licensing and evaluation fees to £2.7m (2003: £0.9m). Such 'milestone' receipts under licensing deals are typically triggered by regulatory or commercial events and as such are irregular in timing and subject to substantial variation from one period to another.

Development fees charged to licensees for conducting development programmes under licence agreements were £1.6m (2003: £nil). These relate to development programmes under the C200 and PLIVA licences entered into during the year.

Royalty income increased to £2.5m (2003: £2.0m) despite being further adversely affected by movements in the dollar/pound exchange rate.

Pharmaceutical products sales were £0.6m (2003: £2.2m), reflecting the divestment of the Icodextrin manufacturing business. Non-pharmaceutical turnover from "other activities" was reduced to £0.5m (2003: £1.4m) following the sale of the educational training business.

The increase in turnover resulted in an increase in gross profit to £5.4m (2003: £3.9m).

Operating costs

The categorisation of operating costs has been changed during the year to include within research and development expenditure certain indirect costs related to such activities previously classified as administrative expenses. The Group believes that this reclassification more appropriately reflects the nature of the Group's activities and is more comparable with practice elsewhere in the sector. Comparative figures for 2003 have also been reclassified.

Research and development expenditure at £12.9m (2003: £14.2m) was reduced from the comparative period. Selling, marketing and distribution costs of £0.5m (2003: £0.5m) were at a similar level. Administrative expenses were reduced to £4.5m (2003: £5.2m) reflecting the divestment of the educational training business and further reductions in the Group's cost base.

Other operating income of £0.5m (2003: £7.3m) comprised the release to the consolidated profit and loss account of the final portion of the deferred element of funds received from PCRAF in 2001, which related specifically to the clinical development of Adept in the US. The comparative figure included the release to the consolidated profit and loss account of £5m of PCRAF funding received in 2002, together with the relevant portion of the deferred element of PCRAF funding. The effect of this is that the total funding of £22.5m received from PCRAF in 2001 and 2002 has now been recognised in full in the consolidated profit and loss account.

Loss before taxation

The operating loss for the period was £12.0m (2003: £8.7m). An exceptional profit of £0.8m arose on the disposal of the balance of the shares held by the Group in Cobra Biomanufacturing Plc ('CBM') in December 2003. The disposal of the educational training business in February 2004 gave rise to neither a profit nor a loss as the consideration, received in the form of shares in Bridgehead International Limited ('Bridgehead'), has a fair value in the balance sheet equal to the net assets divested. The profit on divestments in 2003 of £5.7m

arose on the disposal of the foodextrin manufacturing business and the sale of five million of the Group's holding of six million CBM shares. After net interest income, the loss before taxation was £10.9m (2003: £2.8m).

Taxation

Tax credits in relation to eligible research and development expenditure estimated to be receivable less withholding taxes suffered on income received, were £1.9m (2003: £0.2m). This figure includes £0.6m arising from the difference between the tax credits actually received for 2003 and the estimates included in the consolidated profit and loss account for that year.

Loss after taxation

The loss for the period after taxation was £9.0m (2003: £2.6m), giving a loss per ordinary share of 4.48p (2003: 1.61p).

Net assets

Net assets at 30th September 2004 were £12.9m compared with £7.6m at 30th September 2003, a net increase of £5.3m. The increase resulted from the net proceeds of the Rights Issue and the Issue for Cash announced on 28th January 2004 of £14.4m offset by the loss for the period of £9.0m.

Intangible assets of £3.1m comprise goodwill, which continues to be amortised over 20 years.

Expenditure on fixed assets of £1.8m, net of depreciation charges, disposals and divestments, resulted in an increase in the net book value of fixed assets to £2.9m (2003: £1.9m). Expenditure on fixed assets related principally to the tooling programme on Innovata Biomed's C200 device, the relocation of the Group's Liverpool facility and the replacement of motor vehicles.

Fixed asset investments of £0.2m comprise the carrying value of the Group's shares in Bridgehead, as noted above.

Stocks of £0.3m were reduced from £0.7m at 30th September 2003, while debtors increased

over the same period to £5.5m from £3.2m, principally as a result of development fee income arising in the period and an increase in the level of R&D tax credits receivable. Total creditors of £9.3m (2003: £7.8m) increased as a result of an increase in leasing liabilities related to the C200 tooling programme and the inclusion of a further milestone which is repayable if contractually specified conditions are not met.

Deferred income of £0.7m represents licensing and evaluation fees and development income received, the revenue recognition of which it has been appropriate to defer in accordance with our accounting policy on turnover.

Cash balances and cash flow

Cash consumed in the year by operations (excluding milestone receipts), capital expenditure and net finance lease repayments, offset by net interest income, amounted to £15.8m. This was offset by milestone receipts of £3.7m (which form part of the 'Net Cash Outflow from Operating Activities' in note 29 to the Financial Statements), proceeds from the sale of Cobra Biomanufacturing Plc shares of £1.2m, tax credits of £0.8m and the net proceeds of the Rights Issue and the Issue for Cash of £14.4m, which totalled £20.1m, resulting in an increase in cash and short term deposits of £4.3m. We ended the period with a net cash balance of £10.9m, compared with £6.6m at 30th September 2003.



P.J. Shennan

Chief Operating Officer and Finance Director
25th January 2005

Directors, Secretary and Advisers

Directors

S. W. Sim (Executive Chairman)
P. J. Ballington
Dr. R. N. Boyes
Prof. D. S. Davies
Prof. A. D. Dayan (Non-Executive)
Dr. T. Medinger (Non-Executive)
P. J. Shennan

Secretary and registered office

David Smith, Stringer Saul,
17 Hanover Square, London, W1S 1HU.

Principal bankers

Barclays Bank PLC, Barclays Business Centre,
Manchester City Office, P.O. Box 357, 51 Mosley
Street, Manchester, M60 2AU

Registrars and transfer office

Capita Registrars, The Registry, 34 Beckenham
Road, Beckenham, Kent, BR3 4TU

Registered auditors

PricewaterhouseCoopers LLP, Chartered
Accountants, 8 Princes Parade, St. Nicholas Place,
Liverpool, L3 1QJ.

Financial adviser & stockbroker

Panmure Gordon,
a division of Lazard & Co., Limited,
50 Stratton Street,
London,
W1J 8LL

Directors

S. W. Sim, FCA

Executive Chairman (Age 53)
Stuart Sim qualified as a Chartered Accountant in 1975 following which he held a number of senior financial and general management positions in a variety of industries. He joined the Group as Finance Director in 1988 and he was appointed Chief Executive in June 1997. He became Executive Chairman in October 2002. He is a non-executive Director of Heritage Great Britain Plc and Haline Properties Limited.

P. J. Ballington, BSc

Director of Business Development and Managing Director, Innovata Biomed Limited (Age 50)
Paul Ballington was appointed to the ML Board in June 2004 having joined the Group in 1994 from Abbott Laboratories Inc. where he held senior positions in European and UK country management. Paul is responsible for co-ordinating the commercial and business development efforts of the Group and, in addition, is the Managing Director of Innovata Biomed Limited, the Group's respiratory drug delivery subsidiary.

Dr. R. N. Boyes, PhD

Director North America (Age 64)
Nick Boyes joined the Group in 1990 when it acquired 75% of the equity of his company, Innovata Biomed Limited, and he became a Director in 1993. He has over thirty years experience of the pharmaceutical industry, much of which was gained with the Astra Pharmaceutical Group in the USA, Sweden and the UK, during which time he carried out a number of senior functions at director level. He is an expert in respiratory diseases. Nick spends a substantial part of his time in North America where his primary responsibility is to negotiate collaborations with US companies and search out additional opportunities.

Prof. D. S. Davies, BSc, PhD, FRSC, FRCP, FRCPPath

Group Director of R&D (Age 64)
Donald Davies was appointed Group Director of Research and Development and an Executive Director in October 2002. He had been a Non-Executive Director since the formation of the Company in 1987. In his current role Professor Davies is responsible for co-ordinating research and regulatory policy and strategy and providing scientific evaluation of new product and research opportunities. He was previously Head of Clinical Pharmacology at Imperial College, Hammersmith Hospital, where he is retained as Professor of Biochemical Pharmacology. He is a former member of the Committee on Safety of Medicines and has served on other expert committees in the UK, Europe and the USA. He has had more than 200 papers published on mechanisms of drug action and toxicity and drug safety evaluation.

Prof. A. D. Dayan, LIB, MD, FRCP, FRCPPath Non-Executive Director (Age 69)

Anthony Dayan joined the Board in March 1998. He is a leading toxicologist and has published more than 150 research papers and has edited or contributed to almost 50 books on toxicology, drug development, pathology, neuropathology and the risk sciences. He has been a member of a number of UK and other government advisory committees including the Medicines Commission, an adviser to the World Health Organisation and a consultant on toxicology, biotechnology and drug development to UK, European, US and Japanese pharmaceutical companies. Professor Dayan was Professor of Toxicology at St Bartholomew's and the Royal London School of Medicine and Dentistry, London until 1st October 1998. Prior to that he was with the Wellcome Foundation for eleven years where, latterly, he held the position of Group Adviser in Toxicology and Project Co-ordinator for the Group R & D Director.

Dr. T. Medinger MA, DPhil (Oxon)

Non-Executive Director (Age 64)
Till Medinger joined the Board in March 1999. He was until November 1999 Senior Vice President Corporate Strategy at AstraZeneca PLC and formerly Zeneca Pharmaceuticals International Business Director. As its International Marketing Director he launched several products that have enjoyed major global success. He was President of the Association of the British Pharmaceutical Industry from 1994 to 1996 and served on the Boards of both the European and the International Pharmaceutical Industry Federations. His business career has spanned research and development, licensing and acquisition, strategic planning, territorial and marketing management and public and government affairs. He is non-executive Chairman of PhotoBiotics Limited and a non-executive Director of Peptech Limited (Australia) and Datapharm Communications Limited. He has also acted as corporate consultant to a number of private UK and US biotech companies.

P. J. Shennan, BA, FCA, MSI

Chief Operating Officer and Finance Director (Age 54)
Peter Shennan became Finance Director in November 1997. He qualified as a Chartered Accountant in 1977 and is a member of the Securities Institute. He joined the Group in June 1997 from Coopers & Lybrand. In October 2002 he was appointed Chief Operating Officer in addition to his duties as Finance Director.

The Directors present their Annual Report and the audited Group financial statements for the year ended 30th September 2004.

Principal activities

To date, the Group has successfully developed and commercialised a number of its pharmaceutical products. During the year it has continued to develop its portfolio of such products and its patented technologies with a view to commercialising them on a world wide basis.

Business review

The Chairman's Statement, the Operational Review and the Financial Review on pages 2 to 15 should be read in conjunction with this Directors' Report as they include a review of the development of the business of the Group including its principal activities in research and development and likely future developments.

Results and dividends

The Group loss on ordinary activities before taxation amounted to £10,905,000 (2003 £2,830,000). The Group loss for the year after taxation and minority interests of £9,046,000 (2003 £2,596,000) has been added to the deficit brought forward on profit and loss account reserves as shown in note 20 on page 47. The Directors do not recommend the payment of a dividend.

Research and development

The Group is engaged in the research into, and development of, a portfolio of pharmaceutical and medical products and technologies.

The loss for the year is stated after charging research and development expenditure of £12,903,000 (2003 £14,223,000).

Directors

The Directors who held office during the year were :

S. W. Sim (Executive Chairman)
P. J. Ballington (Appointed 29th June 2004)
Dr. R. N. Boyes
Prof. D. S. Davies
Prof. A. D. Dayan (Non-Executive)
Dr. T. Medinger (Non-Executive)
P. J. Shennan

Under the Articles of Association Mr. P.J. Ballington, Dr. R.N. Boyes and Prof. A.D. Dayan retire from office, and, being eligible, offer themselves for re-election at the forthcoming Annual General Meeting.

Details of the Directors' service contracts are shown in the Remuneration Report on pages 22 to 26.

Directors' share options

Details of the Directors' Share Options are shown in the Remuneration Report on pages 22 to 26.

Directors' interests

The interests (beneficial unless otherwise stated) in the shares of the Company of the Directors who held office at 30th September 2004, were as follows:

	2004 Number of Ordinary Shares	2003 Number of Ordinary Shares	2004 Percentage of Ordinary Share Capital	2003 Percentage of Ordinary Share Capital
S.W. Sim	1,299,117 ⁽¹⁾	1,039,569 ⁽¹⁾	0.57%	0.66%
P. J. Ballington	25,000	500 ⁽²⁾	0.01%	-
Dr. R.N. Boyes	235,625	188,500	0.10%	0.12%
Prof. D.S. Davies	491,531	393,225	0.21%	0.25%
T. Medinger	67,155	53,724	0.03%	0.03%
Prof. A.D. Dayan	41,806 ⁽³⁾	22,500 ⁽³⁾	0.02%	0.01%
P. J. Shennan	25,000	20,000	0.01%	0.01%

1. Mr. S.W. Sim's holding includes 1,375 shares held non-beneficially.

2. Holding as at date of appointment, 29th June 2004.

3. These shares are held jointly with Mrs. H. Dayan.

At 30th September 2004, Dr. R. N. Boyes owned 7,500 shares in Innovata Biomed Limited (2003 7,500 shares) representing 18.75% of that company's issued share capital. Innovata Biomed Limited is a subsidiary of the Company.

There were no changes to the above holdings between 30th September 2004 and 25th January 2005.

As set out in note 33 on page 51, prior to the disposal of Healthcare Education Services Limited, a subsidiary of the Company, the Group acquired the shareholding of Dr. R. N. Boyes in that company representing 18.75 per cent. of its issued share capital, for a nominal consideration.

Substantial interests

As at 25th January 2005, the Company has been notified of the following interests in 3% or more, or in the case of fund managers, 10% or more, of its share capital. The holdings shown are as notified under the Companies Act 1985:

Shareholder	No. of ordinary shares	% of share capital
Channel Hotels & Properties Limited	22,500,000	9.84
Diarmuid Investments Limited	14,000,000 ⁽¹⁾	6.12
Mourant & Co. Trustees Limited	14,000,000 ⁽¹⁾	6.12
Colin Blackburn	9,750,000	4.26
State Street Nominees Limited (for BP Pensions Trustees Limited)	7,967,511	3.48

1. The Company understands that the interests of Diarmuid Investments Limited and Mourant & Co. Trustees Limited are in the same holding of 14,000,000 ordinary shares.

Creditor payment policy

The Group's policy and practice in relation to the payment of its creditors is to make payments in accordance with appropriate payment terms for each business transaction. At 30th September 2004 trade creditors for the Group represented 56 days of amounts invoiced by suppliers (2003 53 days) and for the Company represented 53 days (2003 50 days).

Charitable and political donations

During the year the Group made no charitable donations (2003 £Nil) and no contributions were made to political organisations (2003 £Nil).

Environmental, health and safety policies

The Group recognises its responsibility for safeguarding the environment and where practically and economically possible seeks to manage its activities efficiently so as to minimise any adverse environmental effects. The Group also recognises its obligations for the health and safety of its employees in the workplace and has made an assessment of risks at the various sites at which the Group's activities are undertaken and has in place formal procedures for managing, co-ordinating and reporting to the Board on health and safety matters. The Group has provided training to individuals who are responsible for health and safety. The Group continues to keep environmental, health and safety practices under review.

Ethical and social policies

The Group's principal activities are undertaken within the pharmaceutical industry which is subject to a highly regulated ethical framework with which the Group complies. In addition, the Group seeks to conduct its activities generally in accordance with good business ethics. The Group does not consider it appropriate at its current stage of development to make significant financial donations to charitable, community or social activities, but considers that its most important contribution to the communities within which it operates is to provide high quality employment opportunities and, to society generally, to develop new therapies for serious diseases.

Employees

The Group recognises that in an industry based on innovation, research and development, its employees are one of its biggest assets and seeks to communicate and, where appropriate, consult with them on matters affecting them as employees, in the most appropriate manner. The Group operates a policy of equal opportunities with no discrimination on race, sex, disability or any other grounds. The Group provides training and development appropriate to individual needs and offers remuneration packages, including pensions, life and permanent health insurance, and a working environment which are designed to be both fair and competitive with larger companies within the industry. Participation in the Group's share option scheme is extended to the majority of the Group's employees.

Auditors

The auditors have indicated their willingness to continue in office and a resolution to re-appoint PricewaterhouseCoopers LLP as auditors to the Company will be proposed at the Annual General Meeting.

Annual General Meeting

Notice of the 2005 Annual General Meeting ("AGM") of M L Laboratories PLC is enclosed with this document.

Resolution 7 in the notice of the AGM is a resolution to renew the general authority of the Directors to issue relevant securities (as defined in the Companies Act 1985 ("the Act")). It is proposed that such authority be granted over shares with an aggregate nominal value of £762,369.01, being approximately one-third of the current issued share capital, and that the authority should continue until the 2006 AGM, or 15 months from the date of the resolution if earlier. This resolution will be proposed as an ordinary resolution.

Resolution 8 in the notice of the AGM is a resolution to disapply the statutory pre-emption rights on the allotment for cash of equity securities (as defined in the Act). The extent of the proposed disapplication is set out in the text of the resolution, and it is proposed that the disapplication should take effect until the 2006 AGM, or 15 months from the date of the resolution if earlier. This resolution will be proposed as a special resolution.

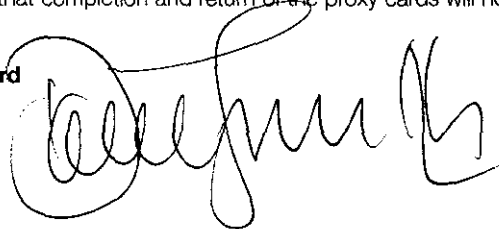
The Directors believe that it is important that they are granted these powers and authorities so as to enable them to take advantage of commercial opportunities as they arise. Accordingly the Directors unanimously recommend that you vote in favour of these resolutions, as they and those connected with them intend to do in respect of a total of 2,185,234 ordinary shares (representing approximately one per cent. of the current issued ordinary shares).

In addition to the ordinary business set out in the notice of the AGM, an advisory resolution (resolution 2) will be proposed to approve the Remuneration Report, set out on pages 22 to 26.

You will find enclosed with the notice of the AGM a proxy card for use at the AGM. Whether or not you propose to attend the AGM in person, you are requested to complete and return the proxy card to the Company's Registrars in accordance with the instructions printed thereon as soon as possible and in any event, so as to be received no later than 48 hours before the meeting. Please note that completion and return of the proxy cards will not preclude you from attending the AGM and voting in person if you wish.

By order of the Board
David Smith
 Secretary

25th January 2005



Remuneration Committee (non-auditable)

The Remuneration Committee (the "Committee") comprises the independent Non-Executive Directors on the Board, Dr. T. Medinger and Professor A. D. Dayan and is chaired by Dr. Medinger. The Committee held one meeting during the past financial year, which was attended by both Non-Executive Directors. The principal functions of the Committee are to make recommendations to the Board on the Company's policy for executive remuneration and to determine, on behalf of the Board, the remuneration, including the terms and conditions of service, for the Executive Directors and appropriate other senior executives. The full terms of reference for the Committee are available on request. The Committee has been advised in its work during the past financial year by the Executive Chairman except in matters relating to his own remuneration. The Committee has also appointed New Bridge Street Consultants LLP ("NBSC") to provide them with independent remuneration advice. NBSC provides no other services to the Company.

Remuneration Policy (non-auditable)

The Committee's policy is to set remuneration packages for Executive Directors and senior management that are competitive with the market, allowing the Company to attract, motivate and retain executives of the highest calibre. Remuneration packages are designed to incentivise and reward executives for improved performance via annual bonus payments and awards of share options, which together constitute a potentially significant proportion of the total remuneration opportunity.

The remuneration of Executive Directors comprises the following five elements:

(i) Basic salary

A salary which reflects the market rate for each position and the individual Director's experience and value to the business and takes into consideration levels of remuneration and increases awarded to other employees. Salaries are reviewed annually as from 1st April, taking into account personal performance, and are bench-marked against a comparator group.

(ii) Taxable benefits

Taxable benefits represent the provision of a car, including (with the exception of Dr. R. N. Boyes) fuel benefit, and private medical insurance.

(iii) Share options

Executive share options are granted to Directors (other than the independent Non-Executive Directors), senior management and the majority of other employees within the Group under the M L Laboratories PLC 1999 Executive Share Option Scheme and are normally exercisable between 3 and 10 years from the date of the grant, subject to continued employment and the satisfaction of performance conditions.

Executives may be granted options over shares with a value of up to two times their total remuneration in any year. Grants may be made in excess of this limit, however, if the Committee decides that this is justified in the circumstances of recruitment or to reflect prevailing market practices outside the UK where an Executive carries on his duties overseas or in other exceptional circumstances.

Grants made to Executive Directors so far under this scheme are only exercisable subject to the achievement of stretching share price growth targets (as outlined later in this Report). It is the Committee's current intention that future option grants will also be subject to share price growth targets that it considers to be appropriately demanding at the date of grant. The Committee believes that the use of share price targets clearly aligns the interests of the Executives with the interests of shareholders. The share options granted to individual Executive Directors to date are disclosed later in this Report and include grants made in prior years under a previous option scheme.

(iv) Bonus

In the case of senior management the Company operates a non-pensionable discretionary bonus scheme based upon individual performance and achievement of personal and corporate objectives. In the case of Executive Directors the scheme recognises exceptional performance. The bonus paid to Mr. P.J. Shennan for the past financial year was related to the Rights Issue and the Issue for Cash and represented 12.25% of his basic salary in that year. No other Executive Director received a bonus for the past financial year. It is the intention to revise these schemes in the forthcoming year to ensure that over time a greater proportion of executive remuneration is performance related.

(v) Pension arrangements

The Company currently makes pension contributions equal to 15% of salary for Executive Directors, all of whom are members of the M L Laboratories PLC Staff Non-Contributory Pension Scheme, a defined contribution scheme, details of which are given in note 28 on page 50, with the exceptions of Mr. Ballington and Professor Davies, whose contributions are payable into their own pension schemes.

Executive Directors service contracts (non - auditable)

	Date of Contract
S. W. Sim	27th July 1992
P. J. Ballington	1st July 2004
Dr. R. N. Boyes	31st March 1993
Prof. D. S. Davies	21st January 2003
P. J. Shennan	23rd May 1997

Each of Mr. S.W. Sim and Dr. R.N. Boyes has a service contract which is terminable by the Company on two years notice. Each of Mr. P.J. Shennan and Professor D.S. Davies has a service contract with the Company which is terminable by the Company on not less than one and not more than two years notice. Mr. P.J. Ballington has a service contract which is terminable by the Company on twelve months notice. The Company is obliged to compensate a Director if his contract is terminated with less than the specified notice periods, by payments of up to the notice period's worth of salary, pension and other benefits. Where possible, the Company would mitigate the cost of termination by negotiation.

The service contracts of Mr. S.W. Sim and Dr. R.N. Boyes each contain a term which entitles the relevant individual, within six months after a change of control of the Company, to serve three months notice of termination of his service contract and, on expiry of that notice, to receive a termination payment equal to twice his annual salary at the time of termination.

The Company has awarded certain Directors service contracts in excess of one year where it has been necessary to do so in order to attract and retain those executives, in competition with larger and more established companies.

Non-executive directors (non - auditable)

The Non-Executive Directors are subject to a notice period of six months and receive fees which are determined by the Board.

Retirement by rotation (non - auditable)

All Directors are subject to the requirements of the Articles of Association which state that at least one third of the Directors will retire by rotation each year.

Directors' remuneration (auditable)

The information on Directors' remuneration in the financial year ended 30th September 2004 set out below should be read in conjunction with the Directors' Report and note 9 on page 41 which also constitute part of this Remuneration Report.

	Basic Salary £000	Bonus £000	Taxable Benefits £000	Pension Contributions £000	Fees £000	Total 2004 £000	Total 2003 £000
Executive Directors							
S.W. Sim	321	-	43	48	-	412	394
P.J. Ballington (from 29th June 2004)	45	-	5	6	-	56	-
Dr. R.N. Boyes	121	-	15	18	-	154	173
Prof. D.S. Davies	111	-	19	17	-	147	144
P.J. Shennan	204	25	15	30	-	274	263
Non-Executive Directors							
Prof. A.D. Dayan	-	-	-	-	43	43	41
Dr. T. Medinger	-	-	-	-	37	37	32
Total	802	25	97	119	80	1,123	1,047

Mr. G.P. Fothergill, a former Director who remains employed by ML in a part-time capacity, had remuneration in the period of £260,000 (2003 £269,000) comprising basic salary £226,000 (2003 £217,000) and pension contributions £34,000 (2003 £52,000).

Dr. C.B. Brown, a former Director who remains employed by ML in an executive role as Medical Director, had remuneration in the period of £217,000 (2003 £223,000) comprising basic salary £187,000 (2003 £171,000), taxable benefits £3,000 (2003 £20,000) and pension contributions £27,000 (2003 £32,000).

Remuneration Report

Directors' share options (auditable)

Share options have been granted to Directors under two schemes, being the M L Laboratories PLC Executive Share Option Scheme, which was set up originally in 1989, and the M L Laboratories PLC 1999 Executive Share Option Scheme.

The M L Laboratories PLC Executive Share Option Scheme adopted in 1989 had a fixed life of 10 years and no further options may now be granted under it. There was no performance condition attaching to the outstanding options granted and they are therefore exercisable at the discretion of the option holder.

The Executive Directors have outstanding options over the ordinary shares of 1p each of the Company under the M L Laboratories PLC Executive Share Option Scheme as follows :-

Name of Director	1st October 2003	Granted in the year	Adjustment for rights issue	Exercised	Lapsed	30th September 2004	Subscription Price	Exercise Date	Expiry Date
S. W. Sim	39,408	-	509	-	(39,917)	-	£2.01	26/08/97	26/08/04
	23,529	-	304	-	-	23,833	£1.68	04/09/98	04/09/05
	36,676	-	474	-	-	37,150	£3.69	23/07/99	23/07/06
	412,560	-	5,334	-	-	417,894	£1.24	09/02/01	09/02/08
	39,548	-	511	-	-	40,059	£0.88	06/07/01	06/07/08
	50,000	-	646	-	-	50,646	£1.06	08/03/02	08/03/09
	601,721	-	7,778	-	(39,917)	569,582			
P. J. Ballington	29,556	-	382	-	(29,938)	-	£2.01	26/08/97	26/08/04
	47,059	-	608	-	-	47,667	£1.68	04/09/98	04/09/05
	21,229	-	274	-	-	21,503	£3.69	23/07/99	23/07/06
	181,451	-	2,346	-	-	183,797	£1.24	09/02/01	09/02/08
	25,000	-	323	-	-	25,323	£1.06	08/03/02	08/03/09
	304,295	-	3,933	-	(29,938)	278,290			
Dr. R. N. Boyes	19,704	-	254	-	(19,958)	-	£2.01	26/08/97	26/08/04
	23,529	-	304	-	-	23,833	£1.68	04/09/98	04/09/05
	3,190	-	41	-	-	3,231	£3.69	23/07/99	23/07/06
	118,480	-	1,532	-	-	120,012	£1.24	09/02/01	09/02/08
	51,977	-	672	-	-	52,649	£0.88	06/07/01	06/07/08
	50,000	-	646	-	-	50,646	£1.06	08/03/02	08/03/09
	266,880	-	3,449	-	(19,958)	250,371			
Prof. D. S. Davies	11,765	-	152	-	-	11,917	£1.68	04/09/98	04/09/05
	2,159	-	27	-	-	2,186	£3.69	23/07/99	23/07/06
	43,094	-	557	-	-	43,651	£1.24	09/02/01	09/02/08
	15,911	-	205	-	-	16,116	£0.88	06/07/01	06/07/08
	50,000	-	646	-	-	50,646	£1.06	08/03/02	08/03/09
	122,929	-	1,587	-	-	124,516			
P. J. Shennan	320,000	-	4,137	-	-	324,137	£1.24	09/02/01	09/02/08
	22,599	-	292	-	-	22,891	£0.88	06/07/01	06/07/08
	50,000	-	646	-	-	50,646	£1.06	08/03/02	08/03/09
	392,599	-	5,075	-	-	397,674			
Total	1,688,424	-	21,822	-	(89,813)	1,620,433			

The M L Laboratories PLC 1999 Executive Share Option Scheme (the "1999 Scheme") is administered by the Board of Directors and governed by the 1999 Scheme Rules, adopted in 1999 and amended in 2001 and 2004. There are two parts to the 1999 Scheme, an "Approved" element, which has been approved by the Inland Revenue, which is primarily used for the grant of options to employees at all levels, and an "Unapproved" part which is intended primarily to be used where Executives have more than £30,000 worth of outstanding approved options. The 1999 Scheme has a fixed life of ten years. The price at which a participant may acquire ordinary shares is to be not less than the higher of nominal value and the mid-market quotation on the date of grant. Options may be exercised only on the satisfaction of the associated performance conditions.

For all options granted under the scheme prior to 2001, the performance condition for Basic Options (vesting after 3 years) to be exercisable requires the share price to achieve a level at least twice the option price on or after the vesting date. For larger awards of Super Options (vesting after 5 years) to be exercisable requires the share price to achieve a level at least three times the option price on or after the vesting date. In 2001 the scheme was amended to discontinue Basic and Super options and to allow for annual grants of options.

Since the 1999 Scheme was amended in 2001, (i) for options granted over shares with a value of up to 100% of total remuneration in a year to be exercisable the Company's share price (based on a 30 day average) must have achieved a level of at least 50% growth (rising by 10% a year from the fifth anniversary of grant) from the option price at some time in the period from 3 years from the date of grant until option exercise, (ii) for options granted over shares with a value over 100% of total remuneration in a year to be exercisable the Company's share price (based on a 30 day average) must have achieved a level of at least 100% growth (rising by 20% a year from the fifth anniversary of grant) from the option price at some time in the period from 3 years from the date of grant until option exercise.

Since the amendment of the 1999 Scheme in 2001, options granted on an all employee basis need not be subject to a performance condition if the Committee considers this appropriate, although the Committee has not, as yet, exercised this discretion. The maximum number of ordinary shares which may be issued under the 1999 Scheme is 10% of the issued ordinary shares. The 1999 Scheme makes special provision for the grant of options to newly recruited members of staff.

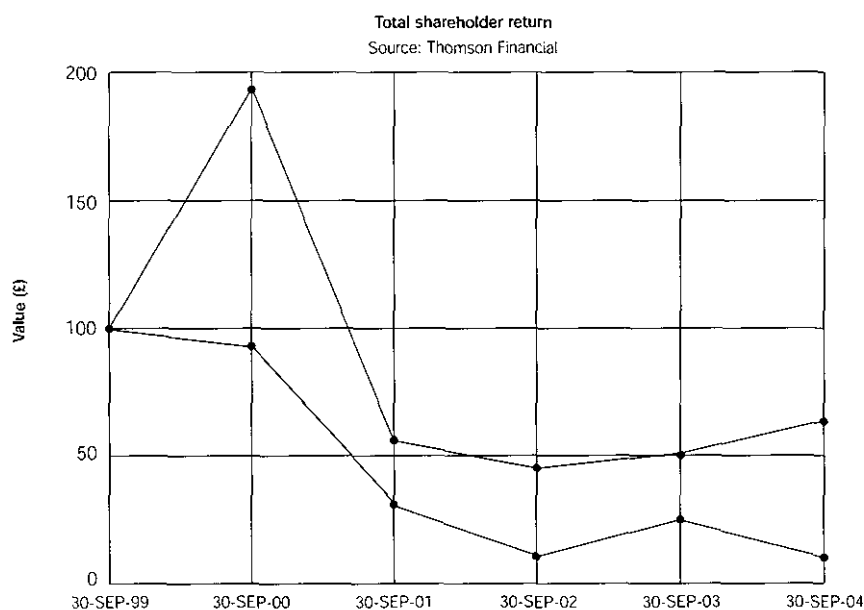
The Executive Directors have outstanding options over the ordinary shares of 1p each of the Company under the M L Laboratories PLC 1999 Executive Share Option Scheme as follows:-

Name of Director	1st October 2003	Granted in the year	Adjustment for rights issue	Exercised	Lapsed	30th September 2004	Subscription Price	Exercise Date	Expiry Date
S. W. Sim	113,571	-	1,468	-	-	115,039	£1.39	20/08/04	20/08/09
	483,108	-	6,247	-	-	489,355	£0.37	02/11/04	02/11/11
	1,015,282	-	13,128	-	-	1,028,410	£0.15	17/04/06	17/04/13
	-	869,387	-	-	-	869,387	£0.19	19/04/07	19/04/14
	1,611,961	869,387	20,843	-	-	2,502,191			
P. J. Ballington	48,127	-	622	-	-	48,749	£1.39	20/08/02	20/08/09
	47,587	-	615	-	-	48,202	£1.39	20/08/04	20/08/09
	214,358	-	2,771	-	-	217,129	£0.37	02/11/04	02/11/11
	347,766	-	4,496	-	-	352,262	£0.15	17/04/06	17/04/13
	-	298,080	-	-	-	298,080	£0.19	19/04/07	19/04/14
	657,838	298,080	8,504	-	-	964,422			
Dr. R. N. Boyes	1,106	-	14	-	-	1,120	£1.39	20/08/02	20/08/09
	37,466	-	483	-	-	37,949	£1.39	20/08/04	20/08/09
	181,419	-	2,345	-	-	183,764	£0.37	02/11/04	02/11/11
	381,254	-	4,929	-	-	386,183	£0.15	17/04/06	17/04/13
	-	326,468	-	-	-	326,468	£0.19	19/04/07	19/04/14
	601,245	326,468	7,771	-	-	935,484			
Prof. D. S. Davies	9,643	-	124	-	-	9,767	£1.39	20/08/04	20/08/09
	152,518	-	1,971	-	-	154,489	£0.37	02/11/04	02/11/11
	353,579	-	4,572	-	-	358,151	£0.15	17/04/06	17/04/13
	-	302,770	-	-	-	302,770	£0.19	19/04/07	19/04/14
	515,740	302,770	6,667	-	-	825,177			
P. J. Shennan	28,571	-	369	-	-	28,940	£1.39	20/08/04	20/08/09
	253,378	-	3,276	-	-	256,654	£0.37	02/11/04	02/11/11
	645,620	-	8,348	-	-	653,968	£0.15	17/04/06	17/04/13
	-	552,845	-	-	-	552,845	£0.19	19/04/07	19/04/14
	927,569	552,845	11,993	-	-	1,492,407			
Total	4,314,353	2,349,550	55,778	-	-	6,719,681			

The market price of the shares at 30th September 2004 was £0.1575 and the range during the financial year was £0.1575 to £0.3529.

Performance Graph (non-auditable)

The graph below illustrates the relative Total Shareholder Return performance of the Company and the FTSE Techmark 100 Index over the last five financial years. Total Shareholder Return comprises the impact of share price movements and dividends paid. The FTSE Techmark 100 Index has been used as a comparator because the Committee considers it to be the most appropriate index of which the Company is currently a constituent.



This graph shows the value, by 30th September 2004, of £100 invested in M L Laboratories on 30th September 1999 compared with the value of £100 invested in the FTSE Techmark 100 Index. The other points plotted are the values at intervening financial year-ends.

—●— M L Laboratories —●— FTSE techmark 100 Index

Signed on behalf of the Board

Dr. T. Medinger

Chairman, Remuneration Committee

25th January 2005

In July 2003 the revised Combined Code on Corporate Governance was issued which supersedes the original Combined Code published in 1998. The revised Combined Code applies for reporting years beginning on or after 1st November 2003 and will accordingly form the basis of the Group's corporate governance statement in the Annual Report for the next financial year. This report has been prepared by reference to the original Combined Code.

The Group has applied the principles set out in Section 1 of the Combined Code as currently applicable to the Group as explained below. In doing so it has complied with the provisions of Section 1 of the Combined Code with the following exceptions. As explained in the Remuneration Report, certain Executive Directors have contracts with notice periods of more than one year. In view of the small size of the Board, a Nomination Committee has not been established to deal with the appointment of new Directors and this function is exercised by the Board. The Audit Committee is comprised of two rather than three Non-Executive Directors, as the Company has only two Non-Executive Directors.

Since the appointment of Mr. P. J. Ballington to the Board on 29th June 2004 the Board has comprised five Executive Directors, including the Executive Chairman, and two Non-Executive Directors Professor A. D. Dayan and Dr. T. Medinger, both of whom are considered to be independent Non-Executive Directors. Dr. T. Medinger, who acts as Chairman of both the Remuneration and Audit Committees, has been nominated as senior independent Director. The Board meets regularly, normally six times a year, to consider appropriate matters, including matters specifically reserved to the Board for consideration. All Directors are provided with the necessary information to enable them to carry out their duties and have access to the Company Secretary and to independent professional advice at the Company's expense.

The Board has established a Remuneration Committee, comprising the independent Non-Executive Directors, Professor A. D. Dayan and Dr. T. Medinger, to determine matters relating to the remuneration of Executive Directors and other senior executives, and an Audit Committee, which comprises the same individuals, to discuss the work of the Auditors and the adequacy of internal controls. Both committees have written terms of reference.

Report on internal control

The Board is responsible for maintaining an effective system of internal control. There is an ongoing process for identifying, evaluating and managing the significant risks facing the Group. Such an internal control framework is designed to manage rather than eliminate risk and can only provide reasonable, not absolute, assurance against material misstatement or loss. The Board considers that the size of the Group does not require an internal audit function at present but will continue to keep the matter under review. The Directors have reviewed the effectiveness of internal control, including internal financial control, during the year and to the date of approval of these financial statements.

The main features of the internal control framework implemented are :

Board review

At each Board meeting standing agenda items are discussed covering the principal areas of the Group's activities, including corporate development, regulatory and product development issues, financial performance and cash adequacy, commercialisation progress, intellectual property and investor relations.

Management involvement

The Group has recruited suitably experienced Directors and senior management to take responsibility for key areas of the Group's activities.

Risk reporting

There is a system of formal reporting on a regular basis on the review and management of a matrix of specific risks by members of senior management and Directors to whom responsibilities for such risks has been allocated.

Financial reporting

There is a detailed budgeting system with a two year rolling forecast of trading results, cash flow and balance sheet positions on a monthly basis, approved by the Board and updated regularly during the year. Monthly trading results and working capital requirements are reported against the corresponding figures for the budget and the previous year with corrective action taken by the Board as appropriate. Further detailed financial information is also provided on a monthly basis. In addition, a rolling ten year strategic projection of income anticipated from product commercialisation is reviewed and approved by the Board.

Treasury management

The treasury function is operated within Board-approved guidelines. Facilities are approved by the Board and all transactions are controlled and monitored. The cash position is monitored on a daily basis and monthly summaries are prepared for the Board. Speculative transactions are not undertaken.

Insurance

As explained above, the identification of major business risks is carried out in conjunction with operating management and is reviewed by the Board. In addition, the Group has insurance cover where it is considered appropriate.

Capital expenditure and project appraisal

The Group has clearly defined guidelines for the review and approval of capital expenditure and other major projects. These include annual budgets and designated levels of authority.

Going concern

As explained in the Chairman's Statement and note 1 to the financial statements the Directors have a reasonable expectation that the Group will have adequate resources to continue in operational existence for the foreseeable future. For this reason they continue to adopt the going concern basis in preparing the Group's financial statements.

Company law requires the Directors to prepare financial statements for each financial year that give a true and fair view of the state of affairs of the Company and the Group and of the profit or loss of the Group for that period. In preparing those financial statements the Directors are required to :

- Select suitable accounting policies and then apply them consistently.
- Make judgements and estimates that are reasonable and prudent.
- State whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements.
- *Prepare the financial statements on the going concern basis, unless it is inappropriate to presume that the Group will continue in business.*

The Directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the Company and the Group and enable them to ensure that the financial statements comply with the Companies Act 1985. They are also responsible for safeguarding the assets of the Company and the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The maintenance and integrity of the M L Laboratories PLC website is the responsibility of the Directors; the work carried out by the Auditors does not involve consideration of these matters and, accordingly, the Auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

S. W. Sim

Executive Chairman

25th January 2005

We have audited the financial statements which comprise the consolidated profit and loss account, the balance sheets, the consolidated cash flow statement, the statement of accounting policies and the related notes. We have also audited the disclosures required by Part 3 of Schedule 7A to the Companies Act 1985 contained in the Remuneration Report and identified as "auditable".

Respective responsibilities of directors and auditors

The Directors' responsibilities for preparing the Annual Report and the financial statements in accordance with applicable United Kingdom law and accounting standards are set out in the statement of Directors' Responsibilities. The Directors are also responsible for preparing the Remuneration Report.

Our responsibility is to audit the financial statements and the auditable part of the Remuneration Report in accordance with relevant legal and regulatory requirements and United Kingdom Auditing Standards issued by the Auditing Practices Board. This report, including the opinion, has been prepared for and only for the Company's members as a body in accordance with Section 235 of the Companies Act 1985 and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

We report to you our opinion as to whether the financial statements give a true and fair view and whether the financial statements and the auditable part of the Remuneration Report have been properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the Directors' Report is not consistent with the financial statements, if the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding Directors' remuneration and transactions is not disclosed.

We read the other information contained in the Annual Report and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. The other information comprises only the Directors' Report, the unaudited part of the Remuneration Report, the Chairman's Statement, the Operational Review, the Financial Review, the "Our pharmaceutical products" listing and the Corporate Governance statement.

We review whether the Corporate Governance statement reflects the Company's compliance with the seven provisions of the Combined Code specified for our review by the Listing Rules of the Financial Services Authority, and we report if it does not. We are not required to consider whether the Board's statements on internal control cover all risks and controls, or to form an opinion on the effectiveness of the Company's or Group's corporate governance procedures or its risk and control procedures.

Basis of audit opinion

We conducted our audit in accordance with Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements and the auditable part of the Remuneration Report. It also includes an assessment of the significant estimates and judgements made by the Directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements and the auditable part of the Remuneration Report are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Uncertainty-going concern

In forming our opinion, we have considered the adequacy of the disclosure made in note 1 to the financial statements concerning the uncertainty as to the Group's future financial position. For the reasons explained in the note the financial statements do not include any adjustments that would arise if they were not drawn up on a going concern basis. In view of the significance of this fundamental uncertainty we consider that it should be drawn to your attention, but our opinion is not qualified in this respect.

Opinion

In our opinion:

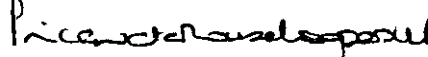
- the financial statements give a true and fair view of the state of affairs of the Company and the Group at 30 September 2004 and of the loss and cash flows of the Group for the year then ended;
- the financial statements have been properly prepared in accordance with the Companies Act 1985; and
- those parts of the Remuneration Report required by Part 3 of Schedule 7A to the Companies Act 1985 have been properly prepared in accordance with the Companies Act 1985.

PricewaterhouseCoopers LLP

Chartered Accountants and Registered Auditors,

Liverpool

25 January 2005



Consolidated Profit and Loss Account

for the year ended 30th September 2004

	NOTES	2004	2004	2004	2003	2003	2003
		Continuing	Discontinued	Total	Restated Continuing	Restated Discontinued	Restated Total
		£000	£000	£000	£000	£000	£000
Turnover	4	7,696	198	7,894	3,726	2,804	6,530
Cost of sales		(2,369)	(98)	(2,467)	(863)	(1,737)	(2,600)
Gross profit		5,327	100	5,427	2,863	1,067	3,930
Research and development expenditure		(12,903)	-	(12,903)	(14,223)	-	(14,223)
Selling, marketing and distribution costs		(487)	(7)	(494)	(422)	(58)	(430)
Administrative expenses		(4,273)	(247)	(4,520)	(4,096)	(1,130)	(5,226)
Other operating income	5	508	-	508	7,346	-	7,346
Operating loss		(11,828)	(154)	(11,982)	(8,532)	(121)	(8,653)
Profit on divestments	3			755			5,686
Loss before interest				(11,227)			(2,967)
Interest receivable	6(a)			390			254
Interest payable	6(b)			(68)			(117)
Loss on ordinary activities before taxation	4, 7			(10,905)			(2,830)
Taxation	8			1,859			234
Loss on ordinary activities after taxation				(9,046)			(2,596)
Minority interests				-			-
Loss for financial year	20(a)			(9,046)			(2,596)
Loss per ordinary share	24			(4.48)p			(1.61)p

There were no recognised gains or losses other than those shown in the above profit and loss account and therefore no separate statement of total recognised gains and losses has been presented.

There is no difference between the loss on ordinary activities before taxation and the loss for the year stated above, and their historical cost equivalents.

Consolidated Balance Sheet

at 30th September 2004

	NOTES	2004 £000	2003 Restated £000
Fixed Assets			
Intangible assets	10	3,100	3,300
Tangible assets	11	2,858	1,885
Investments	12	250	477
		6,208	5,662
Current Assets			
Stocks	13	329	737
Debtors	14	5,534	3,222
Investments	15	-	1
Cash and short term deposits	16	10,868	6,581
		16,731	10,541
Current Liabilities			
Creditors: amounts falling due within one year	17(a)	(9,012)	(7,534)
Net Current Assets		7,719	3,007
Total Assets less Current Liabilities		13,927	8,669
Creditors: amounts falling due after more than one year	17(b)	(322)	(233)
		13,605	8,436
Deferred income	18	(673)	(815)
Net Assets		12,932	7,621
Capital and Reserves			
Share capital	19, 20(a)	2,287	1,582
Share premium account	20(a)	50,155	36,503
Merger reserve	20(a)	8,336	8,336
Profit and loss account	20(a)	(47,846)	(38,800)
Equity Shareholders' Funds	20(a)	12,932	7,621
Minority interests		-	-
		12,932	7,621

The financial statements on pages 31 to 51 were approved by the Board of Directors on 25th January 2005 and were signed on its behalf by :

S. W. Sim Director



at 30th September 2004

	NOTES	2004 £000	2003 Restated £000
Fixed Assets			
Intangible assets	10	3,100	3,300
Tangible assets	11	996	910
Investments	12	4,428	5,243
		8,524	9,453
Current Assets			
Stocks	13	10	61
Debtors - due within one year	14(a)	3,019	1,940
Debtors - due after more than one year	14(b)	170	18
Total debtors		3,189	1,958
Investments	15	-	1
Cash and short term deposits		36,440	28,902
		39,639	30,922
Current Liabilities			
Creditors: amounts falling due within one year	17(a)	(2,458)	(2,818)
Net Current Assets		37,181	28,104
Total Assets less Current Liabilities		45,705	37,557
Creditors: amounts falling due after more than one year	17(b)	(411)	(335)
		45,294	37,222
Deferred income	18	(4)	(508)
Net Assets		45,290	36,714
Capital and Reserves			
Share capital	19,20(b)	2,287	1,582
Share premium account	20(b)	50,155	36,503
Special reserve	20(b)	4,049	4,049
Merger reserve	20(b)	8,336	8,336
Profit and loss account	20(b)	(19,537)	(13,756)
Equity Shareholders' Funds	20(b)	45,290	36,714

The financial statements on pages 31 to 51 were approved by the Board of Directors on 25th January 2005 and were signed on its behalf by:

S. W. Sim Director



Consolidated Cash Flow Statement

for the year ended 30th September 2004

	NOTES	2004 £000	2003 £000
Net Cash Outflow from Operating Activities	29	(10,802)	(11,277)
Returns on Investments and Servicing of Finance			
Interest received		355	290
Interest paid		(16)	(10)
Interest paid on finance leases		(48)	(106)
Net Cash Inflow from Returns on Investments and Servicing of Finance		291	174
Taxation			
UK Corporation tax recovered		816	806
Capital Expenditure and Financial Investment			
Purchase of tangible fixed assets		(1,438)	(714)
Receipts from sale of current asset investments		2	-
Receipts from sale of tangible fixed assets		78	91
Net Cash Outflow for Capital Expenditure and Financial Investment		(1,358)	(623)
Disposals			
Net receipts from disposal of shares	3(a)	1,231	3,851
Disposal of subsidiary	30(b)	(402)	-
Net receipts from disposal of manufacturing business	3(c)	-	5,736
Net Cash Inflow from Disposals		829	9,587
Net Cash Outflow before Management of Liquid Resources and Financing		(10,224)	(1,333)
Management of Liquid Resources			
Cash (placed on)/withdrawn from short term deposits		(4,208)	3,504
Net Cash (Outflow)/Inflow from Management of Liquid Resources		(4,208)	3,504
Financing			
Issue of ordinary share capital		15,519	-
Expenses paid in connection with share issue		(1,162)	-
		14,357	-
Capital element of finance lease rental payments		(432)	(1,433)
Lease finance acquired		162	125
New unsecured loan finance		473	-
Capital element of unsecured loan payments		(49)	(79)
Increase/(decrease) in debt and lease financing	31	154	(1,387)
Net Cash Inflow/(Outflow) from Financing		14,511	(1,387)
Increase in Net Cash in Year	31	79	784

Principal accounting policies

The financial statements have been prepared in accordance with the Companies Act 1985 and Accounting and Financial Reporting Standards applicable in the United Kingdom. A summary of the most significant accounting policies, which have been applied consistently, is set out below. Certain debtor and creditor balances in the comparative figures have been offset to give a fairer presentation, consistent with the current year's treatment.

Basis of accounting

The financial statements have been prepared under the historical cost basis of accounting. The going concern basis continues to be adopted for the reasons explained in note 1.

Basis of consolidation

The consolidated profit and loss account and balance sheet include the financial statements of the Company and all its subsidiary undertakings made up to 30th September in each year. The results of any subsidiaries acquired are included from the date that control was acquired. The results of any subsidiaries disposed of are included up to the date of disposal or loss of control. Intra-group sales, profits and losses and intra-group balances outstanding at the year end are eliminated fully on consolidation.

Minority interests

Minority interests represent the share of the net assets, liabilities and financial results attributable to the interests of the minority shareholders in subsidiaries which are not wholly owned by the Company or its subsidiaries. Minority interests share of subsidiary companies' losses have been fully provided against.

Goodwill

Goodwill arises on the acquisition of a business and represents the excess of the fair value of consideration over the fair value of the net assets acquired. Goodwill arising up to 30th September 1998 was written off on acquisition against reserves. Goodwill arising from 1st October 1998 is capitalised and amortised over its useful life, not exceeding 20 years.

Research and development

Research and development expenditure is written off in the period in which it is incurred and includes, inter alia, all internal and external costs incurred in patenting, developing manufacturing processes, manufacturing materials to be used in clinical trials, the cost of conducting those trials, external studies, analysis and consultants, the cost of obtaining regulatory approvals and the cost of third party licence fees.

The categorisation of internal costs as between research and development expenditure and administrative expenses has been revised during the year ended 30th September 2004 to include within research and development costs certain indirect costs, such as the costs of employees engaged in research and development not charged to a specific project and establishment and other expenses related to research and development activities, which have previously been classified as administrative costs. The Group believes that this broader definition of research and development expenditure more appropriately reflects the nature of the Group's activities and is more comparable with practice elsewhere in the sector. The classification of these costs for 2003 has been restated on a comparable basis. The effect of this restatement is to reclassify as research and development costs £3.2m (2003 £3.3m) previously categorised as administrative expenses. There is no impact on the net loss for the year.

Tangible fixed assets

Tangible fixed assets are stated at their purchase cost to the Group less depreciation. Depreciation is provided on a straight line basis to write off the cost of the tangible fixed assets over their estimated useful lives at the following rates:

Plant and machinery	20.00% - 33.3% per annum
Computer and office equipment	20% - 25% per annum
Motor vehicles	33.3% per annum

Assets under construction are classified separately and depreciated from the date they are brought into use at appropriate rates.

Finance leases

Finance leases are defined as those which transfer the majority of the risks and rewards of ownership to the Group/Company. Tangible fixed assets include assets held under finance leases which are capitalised at their purchase cost with a corresponding amount treated as a liability. Interest is charged to the profit and loss account over the period of the lease agreements by reference to the capital balance outstanding.

Operating leases

Rentals payable in respect of operating leases are charged to the profit and loss account as incurred.

Fixed asset investments (including investments in subsidiaries)

Investments are stated at cost, but are written down to their net realisable or recoverable value if the Directors consider that there has been an impairment of their value.

Stocks

Stocks are valued at the lower of cost and net realisable value. Cost is determined on a first in, first out basis.

Deferred taxation

Deferred tax is recognised, without discounting, in respect of all timing differences which have originated but not reversed by the balance sheet date, except as otherwise required by FRS 19, at rates expected to apply when they reverse, based on current tax rates and law. Deferred tax assets are recognised to the extent that it is regarded as more likely than not that they will be recovered.

Pension costs

The Company makes defined contributions to money purchase pension schemes. Contributions are charged to the profit and loss account on an accruals basis.

Foreign currency translation

Foreign currency transactions are translated into sterling at the rate prevailing at the date of the transaction. Assets and liabilities at the year end are translated into sterling at the rate prevailing at the balance sheet date. The resulting exchange differences are dealt with in the profit and loss account.

Turnover

Turnover, which excludes value added tax, comprises:

- Licensing and evaluation fees are recognised once it can be determined with reasonable certainty that such amounts will be received and that they are not returnable and are taken to turnover when the associated conditions are satisfied, pending which they are treated as deferred income. Licence fees which are returnable if contractually specified conditions are not met are treated as creditors until such conditions are fully satisfied.
- Development fees are recognised in the period in which the development work is undertaken for third party licensees under the terms of licence agreements. Expenditure incurred in relation to development fees is treated as a cost of sale rather than classified as research and development expenditure.
- Royalties are recognised in the period in which the sales by third parties that give rise to the royalties take place.
- Product sales are recognised when the goods are despatched to customers.
- Turnover does not include that proportion of the royalty and revenue streams arising from the Group's products which is receivable by Paul Capital Royalty Acquisition Fund under the transactions referred to in note 5.

Other operating income

Other operating income comprises income which falls outside the definition of turnover.

1. Basis of preparing the financial statements – going concern

The financial statements have been prepared on a going concern basis. This basis is supported by the cash flow projections of the Group. The projections include receipt of significant milestone and similar income the Group anticipates will arise on the commercialisation of its products and divestment proceeds arising from the potential disposal of assets. The Directors recognise that the timing and amount of such receipts is uncertain and not guaranteed and that as a result the Group's financial position cannot be certain. However, the Directors have a reasonable expectation that the Group will have sufficient working capital for the foreseeable future and consequently believe that it is appropriate for the financial statements to be prepared on a going concern basis. The financial statements do not contain any adjustments that would arise if the financial statements were not drawn up on a going concern basis. If required these adjustments would be made to the balance sheets of the Company and the Group to increase or reduce the balance sheet values of assets to their recoverable amounts, to provide for further liabilities that might arise and to reclassify fixed assets and long term liabilities as current assets and liabilities.

2. Discontinued activities

On 6th February 2004 the Group completed the disposal of its subsidiary, Healthcare Education Services Limited. The results of this business have been included in the Group's consolidated profit and loss account for the year ended 30th September 2003 and, up until the date of disposal, for the year ended 30th September 2004, as a discontinued activity.

On 15th April 2003 the Group completed the disposal of its Icodextrin manufacturing business to Baxter Healthcare Limited. The results of this business have been included in the Group's consolidated profit and loss account, up until the date of disposal, for the year ended 30th September 2003, as a discontinued activity.

3. Profit on divestments

(a) An exceptional profit arose during the year on the sale of the Group's remaining holding of one million Cobra Biomanufacturing Plc ("CBM") shares at a price of £1.25 per share, generating net proceeds, after expenses, of £1,231,000 and a profit for the Group of £755,000.

(b) The disposal of Healthcare Education Services Limited during the year gave rise to neither a profit nor a loss as the consideration received in the form of shares in Bridgehead International Limited ("Bridgehead") has a fair value in the balance sheet equal to the net assets divested (see notes 30 and 33).

(c) The profit on divestments in the period ended 30th September 2003 of £5,686,000 arose on the disposal of the Icodextrin manufacturing business (£4,218,000) and on the sale of five million CBM shares (£1,468,000), full details of which were disclosed in the Group's Annual Report for the year ended 30th September 2003.

Notes to the Financial Statements

for the year ended 30th September 2004

4. Segmental analysis by class of business

The analysis by class of business of the Group's turnover, research and development expenditure, other expenses, other operating income, loss before taxation and net assets is set out below:

Segmental reporting - All activities

2004	Turnover £000	Research and development expenditure £000	Other expenses £000	Other operating income £000	Loss before taxation £000	Net assets £000
Licensing and evaluation fees	2,738	-	-	-	-	-
Development fees	1,558	-	-	-	-	-
Royalties	2,540	-	-	-	-	-
Product sales	602	-	-	-	-	-
Total pharmaceutical activities	7,438	(12,890)	(6,753)	508	(10,665)	12,780
Other activities	456	(13)	(728)	-	(240)	152
Total	7,894	(12,903)	(7,481)	508	(10,905)	12,932

2003	Turnover £000	Research and development expenditure £000	Other expenses £000	Other operating income £000	Loss before taxation £000	Net assets £000
Licensing and evaluation fees	933	-	-	-	-	-
Development fees	-	-	-	-	-	-
Royalties	1,977	-	-	-	-	-
Product sales	2,219	-	-	-	-	-
Total pharmaceutical activities	5,129	(14,169)	(6,411)	7,346	(2,358)	7,765
Other activities	1,401	(54)	(1,895)	-	(472)	(144)
Total	6,530	(14,223)	(8,306)	7,346	(2,830)	7,621

Geographical segments

2004	Turnover by destination £000	Turnover by origin £000	Loss before taxation £000	Net assets £000
United Kingdom	3,853	7,894	(10,905)	12,932
North America	222	-	-	-
Europe	3,173	-	-	-
Rest of the World	646	-	-	-
Group	7,894	7,894	(10,905)	12,932

2003	Turnover by destination £000	Turnover by origin £000	Loss before taxation £000	Net assets £000
United Kingdom	1,776	6,530	(2,830)	7,621
North America	1,103	-	-	-
Europe	2,682	-	-	-
Rest of the World	969	-	-	-
Group	6,530	6,530	(2,830)	7,621

Segmental reporting re Discontinued Activities

2004	Turnover £000	Other expenses £000	Loss before taxation £
Other activities	198	(352)	-
Total	198	(352)	-

2003	Turnover £000	Other expenses £000	Loss before taxation £
Product sales	1,602	-	-
Total pharmaceutical activities	1,602	(1,430)	-
Other activities	1,202	(1,495)	-
Total	2,804	(2,925)	(854.97)

4. Segmental analysis by class of business (continued)**Geographical segments re discontinued activities**

2004

	Turnover by destination £000	Turnover by origin £000
United Kingdom	131	198
North America	38	-
Europe	52	-
Rest of the World	(23)	-
Group	198	198

2003

	Turnover by destination £000	Turnover by origin £000
United Kingdom	925	2,804
North America	882	-
Europe	712	-
Rest of the World	285	-
Group	2,804	2,804

5. Other operating income

Other operating income comprises the release to the consolidated profit and loss account of the remaining portion of monies received from Paul Capital Royalty Acquisition Fund ("PCRAF") in earlier years and carried in the balance sheet either as deferred income, in order to match its release with associated spending obligations, or, where there were no associated spending obligations, within creditors, pending the satisfaction of a potential repayment condition.

A total of £22.5m was received from PCRAF under two transactions in 2001 and 2002 as a result of which PCRAF is entitled to receive until 30th September 2010 a proportion of the royalties and revenue streams arising from Adept and Extraneal. As at 30th September 2004, the amounts received from PCRAF have been released in full to the consolidated profit and loss account.

While the risk relating to that proportion of the future royalty and revenue streams receivable by PCRAF has effectively been transferred to PCRAF, under certain specified circumstances (including change of control of M L Laboratories PLC, certain major corporate transactions, and events of default material in the context of the PCRAF transaction) PCRAF has the right to require the Group to re-purchase PCRAF's interests in the royalty and revenue streams concerned for a consideration calculated to give PCRAF an agreed minimum rate of return.

6. Interest receivable and payable**(a) Interest receivable**

	2004 £000	2003 £000
Bank interest receivable	390	254
	390	254

(b) Interest payable

	2004 £000	2003 £000
On bank overdraft - repayable within 5 years, not by instalments	4	2
On unsecured loans	17	9
On finance leases	47	106
	68	117

Notes to the Financial Statements

for the year ended 30th September 2004

7. Loss on ordinary activities before taxation

	2004 £000	2003 £000
<i>Loss on ordinary activities before taxation is stated after charging:</i>		
Depreciation - tangible owned fixed assets	328	235
- tangible fixed assets held under finance leases	439	840
Amortisation of intangible fixed assets	200	200
Auditors' remuneration for:		
- Audit (Company £20,000) (2003 £20,000)	45	39
Operating leases - hire of other assets	1	45
- hire of plant and machinery	20	7
- rental of premises	410	487
<i>Loss on disposal of tangible fixed assets</i>	-	19
<i>And after crediting:</i>		
Profit on disposal of tangible fixed assets	50	54

Remuneration of the Company's Auditors for provision of non-audit services to the Company and its subsidiary undertakings was £147,000 (2003 £108,000). This comprised fees in respect of taxation compliance £27,000 (2003 £20,000) and transaction assistance fees £120,000 (2003 £88,000).

8. Taxation

The current year tax credit represents refundable R & D tax credits less withholding taxes suffered. There is no charge to corporation tax during the year nor is there any provision required for deferred taxation. Accumulated tax losses have not been recognised as deferred tax assets as there is insufficient certainty as to their future recoverability.

As at 30th September 2004, the total tax losses in Group companies amounted to £54m (2003 £53m). These losses are available for offset against future profits in the companies concerned, subject to agreement with the Inland Revenue.

(a) Analysis of credit in year	2004	2003
UK corporation tax	£000	£000
R & D tax credit		
Current year	1,414	518
Prior years	629	(160)
Withholding taxes	(184)	(124)
	1,859	234
(b) Factors affecting the tax credit for the year	£000	£000
Loss on ordinary activities before taxation	10,905	2,830
Loss on ordinary activities at 30%	3,271	849
Effects of :		
Adjustments to tax credit in respect of prior periods	629	(160)
Carry forward of tax losses	(1,783)	(1,545)
Other timing differences	15	27
Amortisation of goodwill	(60)	(60)
Expenses not deductible for tax purposes	6	(335)
Non taxable income arising on consolidation	226	785
Adjustment in respect of R & D tax credits	(261)	797
Withholding taxes suffered	(184)	(124)
	1,859	234

9. Directors and employees

	2004 Number	2003 Restated Number
Employees		
Average weekly number of persons (including Directors) employed by the Group during the year		
Research and development	78	88
Administration and marketing	31	40
Production and educational training	6	27
	115	155
	2004	2003
	£000	£000
Staff costs (for the above persons)		
Wages and salaries	5,800	6,954
Social security costs	623	706
Other pension costs (note 28)	412	426
	6,835	8,086
Directors' Remuneration		
Remuneration paid to the Directors of the holding company	£000	£000
Aggregate emoluments	1,004	912
Contributions to money purchase pension schemes	119	135
	1,123	1,047
Emoluments payable to the highest paid Director	£000	£000
Aggregate emoluments	364	348
Contributions to money purchase pension scheme	48	46
	412	394

5 Directors (2003 : 4) have benefits accruing under money purchase pension schemes.

No Director waived emoluments in respect of the year ended 30th September 2004 (2003 None).

Further details of the remuneration and Share Options of Directors are given in the Remuneration Report on pages 22 to 26.

Notes to the Financial Statements

for the year ended 30th September 2004

10. Intangible fixed assets

Goodwill relates to the research and development activities originally acquired by the Group on its acquisition of Cobra Therapeutics Limited ("Cobra") which were transferred into the direct ownership of M L Laboratories PLC when Cobra left the Group as a result of the flotation on AIM of Cobra Biomanufacturing PLC. Goodwill continues to be amortised over the remainder of the period of 20 years from the original date of the acquisition of Cobra by the Group, this being the Directors' estimate of its useful economic life.

GROUP COST	Goodwill £000
At 1st October 2003	4,000
Additions	-
At 30th September 2004	4,000
AGGREGATE AMORTISATION	£000
At 1st October 2003	700
Charge for the year	200
At 30th September 2004	900
Net book value at 30th September 2004	3,100
Net book value at 30th September 2003	3,300
COMPANY COST	Goodwill £000
At 1st October 2003	3,550
Additions	-
At 30th September 2004	3,550
AGGREGATE AMORTISATION	£000
At 1st October 2003	250
Charge for the year	200
At 30th September 2004	450
Net book value at 30th September 2004	3,100
Net book value at 30th September 2003	3,300

11. Tangible fixed assets

Group COST	Plant & machinery £000	Computer & office equipment £000	Motor vehicles £000	Assets under construction £000	Total £000
At 1st October 2003	3,430	1,599	842	180	6,051
Additions	305	82	396	1,019	1,802
Disposal of subsidiary	-	(166)	-	-	(166)
Disposals	(68)	-	(250)	-	(318)
At 30th September 2004	3,667	1,515	988	1,199	7,369
DEPRECIATION					
At 1st October 2003	2,501	1,235	431	-	4,167
Charge for year	354	147	266	-	767
Disposal of subsidiary	-	(133)	-	-	(133)
Disposals	(68)	-	(222)	-	(290)
At 30th September 2004	2,787	1,249	475	-	4,511
NET BOOK VALUE					
At 30th September 2004	880	266	513	1,199	2,858
At 30th September 2003	929	364	411	180	1,885

The net book value of tangible fixed assets includes £1,038,000 (2003 £959,000) in respect of assets held under finance leases.

Company
COST

At 1st October 2003	1,158	894	674	-	2,726
Additions	294	47	198	-	539
Transfer to subsidiaries	-	-	(26)	-	(26)
Disposals	(68)	-	(180)	-	(248)
At 30th September 2004	1,384	941	666	-	2,991
DEPRECIATION					
At 1st October 2003	773	703	340	-	1,816
Charge for year	148	76	200	-	424
Transfer to subsidiaries	-	-	(25)	-	(25)
Disposals	(68)	-	(152)	-	(220)
At 30th September 2004	853	779	363	-	1,995
NET BOOK VALUE					
At 30th September 2004	531	162	303	-	996
At 30th September 2003	385	191	334	-	910

The net book value of tangible fixed assets includes £697,000 (2003 £611,000) in respect of assets held under finance leases.

12. Fixed asset investments

Group COST	Investment £000
At 1st October 2003	477
Disposal of CBM shares (see note 3(a))	(477)
Investment in Bridgehead (see note 3(b) and note 30(a))	250
At 30th September 2004	250

The Group's investment in Bridgehead, an unquoted company, represents 12% of its issued ordinary share capital.

Notes to the Financial Statements

for the year ended 30th September 2004

12. Fixed asset investments (continued)

Company CARRYING VALUE	Investments £000	Subsidiaries £000	Total £000
At 1st October 2003	1,000	4,243	5,243
Disposal of CBM shares (see note 3(a))	(1,000)	-	(1,000)
Disposal of investment in subsidiary	-	(44)	(44)
Impairment charges against carrying value of subsidiaries	-	(21)	(21)
Investment in Bridgehead (see note 3(b) and note 30)	250	-	250
At 30th September 2004	250	4,178	4,428

Principal Subsidiary Companies	Country of Incorporation	Description of Holding	Proportion Held %	Nature of Business
Benest Engineering Limited	England	Ordinary Shares	75	Research, development & commercialisation of agronomic chemical delivery systems
Biofil Limited	England	Ordinary Shares	100	Research, development & commercialisation of microbiological water purification systems
Bioinnovation Limited	England	Ordinary Shares	75	Research, development & commercialisation of a novel approach to treatment of various diseases, including cancer
Innovata Biomed Limited	Scotland	Ordinary Shares Preference Shares	81 100	Research, development & commercialisation of respiratory drug delivery technologies
M.A.T.S. (UK) Limited	England	Ordinary Shares	51	Applied surface science
Movement Control Systems Limited	England	Ordinary Shares	90	Development and commercialisation of infant monitoring systems
Traversall Limited	England	Ordinary Shares	100	Research, development & commercialisation of patient transfer systems

With the exceptions of Innovata Biomed Limited and M.A.T.S. (UK) Limited, the operations of the above subsidiaries have been discontinued or substantially reduced in scale.

Investment

Bridgehead International Limited	England	Ordinary Shares	12	Consultancy services
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13. Stocks

	Group		Company	
	2004 £000	2003 £000	2004 £000	2003 £000
Raw materials & consumables	329	737	10	61
	329	737	10	61

14. Debtors

	Group		Company	
	2004	2003	2004	2003
	£000	£000	£000	£000
(a) Amounts falling due within one year:				
Trade debtors	1,609	379	242	229
Other debtors	356	386	221	274
Corporation tax	2,561	1,479	1,656	682
Prepayments and accrued income	1,008	978	900	755
	5,534	3,222	3,019	1,940
(b) Amounts falling due after more than one year:				
Amounts owed by subsidiary undertakings	-	-	170	18
	5,534	3,222	3,189	1,958

The amounts due from subsidiary undertakings are unsecured and interest free.

15. Current asset investments

	2004	2003
Group & Company	£000	£000
Investments quoted on a recognised stock exchange, at cost	39	39
Sale of current asset investment	(1)	-
Provision for impairment of value	(38)	(38)
At 30th September 2004	-	1
Aggregate market value of quoted investments	-	1

Current asset investments include a holding of 2,177,400 shares (2003 1,451,600 shares, the increase resulting from a 3 for 2 stock split) in Enhance Biotech, Inc. held at nil book value. These shares are traded on an "over the counter bulletin board" in the US. Trades in the three months prior to the date of these financial statements have been at prices ranging between \$2.40 and \$1.70. However, the shares are extremely illiquid and the Group is currently restricted under US securities regulations from disposing of these shares, on which basis the Directors have determined that no value should be attributed to the investment at this stage. Current asset investments also include 4,354 shares in Advance Media Training, Inc. received as a distribution from Enhance Biotech, Inc. There is no public market for these shares and the Directors have determined that no value should be attributed to this investment.

16. Cash and short term deposits

Cash and short term deposits of £10,868,000 (2003 £6,581,000) includes short term deposits amounting to £10,452,000 (2003 £6,244,000) including £500,000 held as security for an overdraft facility of that amount from Barclays Bank PLC.

17. Creditors

	Group		Company	
	2004	2003	2004	2003
	£000	£000	£000	£000
(a) Amounts falling due within one year:				
Bank overdraft	-	-	-	13
Obligations under finance leases	310	281	177	183
Unsecured loans	478	49	5	49
Trade creditors	2,640	2,639	1,332	1,598
Taxation and social security	220	218	166	161
Other creditors	4,004	3,069	3	24
Accruals	1,360	1,278	775	790
	9,012	7,534	2,458	2,818

Notes to the Financial Statements

for the year ended 30th September 2004

17. Creditors (continued)

	Group		Company	
	2004 £000	2003 £000	2004 £000	2003 £000
(b) Amounts falling due after more than one year:				
Obligations under finance leases	322	228	210	129
Unsecured loans	-	5	-	5
Amounts owed to subsidiary undertakings	-	-	201	201
	322	233	411	335

The Company has provided unlimited multilateral guarantees in respect of the bank overdrafts of its subsidiaries, which at 30th September 2004 amounted to £25,573,000 (2003 £22,318,000)

18. Deferred income

Deferred income at 30th September 2004 comprised licensing fees received but not yet credited to the consolidated profit and loss account, in accordance with our accounting policy on turnover. Deferred income at 30th September 2003 also included PCRAF monies not yet credited to other operating income (see note 5).

	2004 £000	2003 £000
Group		
PCRAF balance outstanding	-	508
Licensing fees not yet credited	673	307
	673	815
	£000	£000
Company		
PCRAF balance outstanding	-	508
Licensing fees not yet credited	4	-
	4	508

19. Called-up share capital

	2004 £000	2003 £000
Authorised		
350,000,000 Ordinary Shares of 1p each	3,500	2,000
Allotted, called-up and fully paid		
228,710,703 Ordinary Shares of 1p each (2003: 158,168,563 Ordinary Shares)	2,287	1,592
Pursuant to the Rights Issue and Issue for Cash announced in the circular to shareholders dated 28th January 2004, the following Ordinary Shares were issued for cash at 22p per share to raise working capital for the Group.		
	No. of Shares	£000
Rights Issue	39,542,140	8,699
Issue for Cash	31,000,000	6,820
	70,542,140	15,519

Contingent rights to the allotment of shares :

Under the M L Laboratories PLC Executive Share Option Scheme, options which have been granted to Directors and Executives to subscribe for Ordinary Shares and which remain unexercised as at 30th September 2004 are as follows:

19. Called-up share capital (continued)

Number of shares	Subscription Price	Exercise Date	Expiry Date
132,221	£1.68	04/09/98	04/09/05
71,226	£3.69	23/07/99	23/07/06
477,712	£2.27	06/01/00	06/01/07
1,854,625	£1.24	09/02/01	09/02/08
68,722	£1.19	18/03/01	18/03/08
640,508	£0.88	06/07/01	06/07/08
329,199	£1.06	08/03/02	08/03/09
3,574,213			

Under the M L Laboratories PLC 1999 Executive Share Option Scheme, options which have been granted to Directors, Executives and employees to subscribe for Ordinary Shares and which remain unexercised as at 30th September 2004 are as follows:

Number of shares	Subscription Price	Exercise Date	Expiry Date
302,349	£1.39	20/08/02	20/08/09
286,202	£1.39	20/08/04	20/08/09
510,932	£1.40	10/11/03	10/11/10
3,582,673	£0.37	02/11/04	02/11/11
6,974,510	£0.15	17/04/06	17/04/13
6,390,379	£0.19	19/04/07	19/04/14
18,047,045			

In accordance with the rules of both schemes, following the Rights Issue, an adjustment was applied to share options, increasing the number of shares by 1.29% (rounded down to the nearest whole number) and reducing the subscription price by 1.29% (rounded up to the nearest whole penny).

Details of Directors' interests in Ordinary Shares of the Company are shown in the Directors' Report on pages 18 to 21.

Details of Directors' Share Options are shown in the Remuneration Report on pages 22 to 26.

20. Movements in capital and reserves and equity shareholders' funds

The movements in capital and reserves during the year were as follows :

	Share Capital	Share Premium Account	Merger Reserve	Profit & Loss Account	Equity Shareholders' Funds
(a) Group	£000	£000	£000	£000	£000
At 1st October 2003	1,582	36,503	8,336	(38,800)	7,621
Loss for financial year	-	-	-	(9,046)	(9,046)
Issue of ordinary share capital on Rights Issue and Issue for cash	705	14,814	-	-	15,519
Expenses paid in connection with the issue of ordinary share capital	-	(1,162)	-	-	(1,162)
At 30th September 2004	2,287	50,155	8,336	(47,846)	12,932

	Share Capital	Share Premium Account	Special Reserve	Merger Reserve	Profit & Loss Account	Equity Shareholders' Funds
(b) Company	£000	£000	£000	£000	£000	£000
At 1st October 2003	1,582	36,503	4,049	8,336	(13,756)	36,714
Loss for financial year	-	-	-	-	(5,781)	(5,781)
Issue of ordinary share capital on Rights Issue and Issue for cash	705	14,814	-	-	-	15,519
Expenses paid in connection with the issue of ordinary share capital	-	(1,162)	-	-	-	(1,162)
At 30th September 2004	2,287	50,155	4,049	8,336	(19,537)	45,290

The special reserve was created in 1999 following a reduction of the share premium account. In the Group accounts, the goodwill which had arisen on consolidation up to 30th September 1998 of £4,049,000 has been offset against the special reserve rather than against the profit and loss account.

Notes to the Financial Statements

for the year ended 30th September 2004

21. Finance lease obligations and unsecured loans

	Group		Company	
	2004 £000	2003 £000	2004 £000	2003 £000
At 30th September 2004 the Group and Company had obligations under finance leases as follows:				
Payable within one year	310	281	177	183
Payable between one and two years	227	186	136	112
Payable between two and five years	95	42	74	17
	632	509	387	312

	Group		Company	
	2004 £000	2003 £000	2004 £000	2003 £000
At 30th September 2004 the Group and Company had obligations under unsecured loans as follows:				
Payable within one year	478	49	5	49
Payable between one and two years	-	5	-	5
	478	54	5	54

22. Financial instruments

The Group has taken advantage of the exemption available under FRS13 in respect of short term debtors and creditors and accordingly, where permitted by the FRS, details in respect of such debtors and creditors are excluded from the disclosures dealt with in this note.

Primary financial instruments employed by the Group, other than short-term debtors and creditors, comprise cash, short term deposits, unsecured loans, current asset investments and finance leases. The Group's activities involve some currency exposure arising from the fact that certain royalties are calculated and paid in US dollars and that certain operating costs are incurred in currencies other than sterling, principally US dollars. The Group's general policy is to convert dollar revenues to sterling when received and to convert sterling to foreign currencies at the transaction date. The Group does not trade in financial instruments. The Group's policy during the year ended 30th September 2004 was to place the majority of its cash on short term deposits with its bankers and to finance the purchase of tangible fixed assets through finance leases, where possible, for cash flow purposes.

The Group's exposure to interest rate risk is limited to its finance leases and unsecured loans which are typically fixed rate and its overdraft and cash deposits which are typically floating rate.

The interest rate profile of financial assets was :

	Floating rate financial assets and overdraft		
	Cash and current bank accounts £000	Short term bank deposits £000	Total £000
Currency			
Sterling	(105)	10,452	10,347
US dollars	521	-	521
At 30th September 2004	416	10,452	10,868
Currency			
Sterling	(55)	6,244	6,189
US dollars	403	-	403
Euros	(11)	-	(11)
At 30th September 2003	337	6,244	6,581

The current year's cash and current bank accounts comprise cash book overdrafts which are represented substantially by unpresented cheques.

The fair value of short term deposits approximates to the book value reported in the balance sheet because of the short maturity dates of these deposits.

22. Financial instruments (continued)

The interest rate profile of financial liabilities was :

	Financial liabilities			
	Fixed rate		Floating rate	
	2004 £000	2003 £000	2004 £000	2003 £000
Sterling				
Finance leases	632	509	-	-
Unsecured loans	478	54	-	-
	1,110	563	-	-

The weighted average interest rate on finance leases at 30th September 2004 was 5.5% (2003 8.8%).

	Group		Company	
	2004 (Months)	2003 (Months)	2004 (Months)	2003 (Months)
The weighted average period to maturity of finance leases was:	25	20	26	18

The weighted average interest rate on the unsecured loans at 30th September 2004 was 5.5% (2003 9.7%) and the period to maturity was 2 months (2003 8 months).

The fair value of finance leases at 30th September 2004, calculated by discounting cash flows at prevailing interest rates, was £704,000 (2003 £650,000).

The currency analysis of the Group's net monetary assets and liabilities (including short term debtors and creditors) at 30th September was :

	2004 £000	2003 £000
Sterling	6,695	1,513
Other currencies, principally US dollars	373	524
	7,068	2,037

As at 30th September 2004 the Group had committed undrawn overdraft facilities amounting to £500,000 (2003 £973,000).

23. Loss for the financial year

As permitted by Section 230 of the Companies Act 1985, the parent company's profit and loss account has not been included in these financial statements. The parent company's loss for the financial year was £5,781,000 (2003 £2,457,000).

24. Loss per ordinary share

The calculation of basic earnings per share is based on the loss on ordinary activities after taxation and minority interests and on 201,948,984 (2003 161,345,005) ordinary shares, being the weighted average, calculated on a time basis, of the number of ordinary shares in issue. For this purpose the calculation of the number of ordinary shares in issue prior to the Rights Issue and Issue for Cash takes account of the notional bonus element arising on the Rights Issue and Issue for Cash from the difference between the mid-market price on the last day on which shares were quoted cum-rights and the theoretical ex-rights price. Earnings per share for comparative periods have also been re-stated to take account of this notional bonus issue element.

The effect of dilutive share options outstanding and not yet exercised at 30th September 2004 would be to reduce the loss per ordinary share.

25. Other financial commitments

At 30th September 2004 the Group had annual commitments under non-cancellable operating leases as follows:

	Land & buildings £000	Other £000	Land & buildings £000	Other £000
Expiring within one year	48	2	183	7
Expiring between one and two years	38	1	130	3
Expiring between two and five years	213*	11	38*	6
Expiring in over five years	214**	-	116**	-
	513	14	467	16

* Subject to a three year rent review ** Subject to a five year rent review

Notes to the Financial Statements

for the year ended 30th September 2004

26. Capital commitments

	Group		Company	
	2004 £000	2003 £000	2004 £000	2003 £000
Capital expenditure on tangible fixed assets that had been contracted for but has not been provided for in the financial statements	1,400	64	43	-

27. Contingent liabilities

Group & Company

As explained in note 5, under agreements entered into in July 2001 and February 2002, in certain circumstances the Group may be required to make payments to PCRAF to repurchase its interests in the royalty and revenue streams concerned.

In June 2004 the Group commenced arbitration proceedings against Novex Limited in which it is seeking damages pursuant to its claim that, inter alia, Novex failed to perform its obligations in respect of marketing Adept during 2000 and 2001. Novex has filed a response seeking to dismiss the Group's claim with costs and making an unparticularised and unquantified counterclaim which the Group has received legal advice it is in a strong position to defend.

As explained in note 17, the Company has provided unlimited multilateral guarantees in respect of the bank overdrafts of its subsidiaries.

A milestone payment of £1.5m was received in the year to 30th September 2004 which, while taken to income as turnover in accordance with our accounting policy, is potentially repayable in the event of termination of the relevant licensing agreement through the breach thereof by the Group, insolvency of the Group, or as a result of actions within the Group's control.

At 30th September 2004 there were no other contingent liabilities other than those arising from the ordinary course of business in respect of which no material losses are expected to arise.

28. Pensions

The Group operates defined contribution pension schemes comprising the M L Laboratories PLC Staff Non-Contributory Pension Scheme and the M L Laboratories PLC Staff Contributory Pension Scheme, which is a Group Personal Plan established with Scottish Equitable PLC. The assets of the schemes are held separately from those of the Group and are independently administered. The pension cost charge represents contributions payable by the Group under the schemes and amounted to £412,000 (2003 £426,000). Contributions totalling £43,000 (2003 £65,000) were payable at the year end.

29. Reconciliation of operating loss to net cash flow from operating activities

	2004 £000	2003 Restated £000
Operating loss	(11,982)	(8,653)
Depreciation of tangible fixed assets	768	1,075
Amortisation of goodwill	200	200
Net profit on disposal of current asset investment	(1)	-
Net profit on disposal of tangible fixed assets	(50)	(35)
Decrease in stocks	408	181
(Increase)/decrease in debtors	(1,307)	3,883
Increase/(decrease) in creditors	1,304	(5,888)
Decrease in deferred income	(142)	(2,040)
Net cash outflow from operating activities	(10,802)	(11,277)

30. Working capital and cash effect of disposal of Healthcare Education Services Limited**(a) Working capital effect**

£000

Tangible fixed assets	34
Cash	302
Debtors	114
Creditors	(300)
Net assets disposed of for shares in Bridgehead	150
Additional cash investment pursuant to sale agreement	100
Fair value of investment in Bridgehead	250

(b) Cash effect

Cash included in net assets disposed of	302
Additional cash investment pursuant to sale agreement	100
	402

31. Reconciliation of net cash flow to movement in funds

	2004 £000	2003 £000
Increase in cash in year	79	784
Movement in short term deposits	4,208	(3,504)
Movement in borrowings	(154)	1,387
Change in Net Funds Resulting from Cash Flows	4,133	(1,333)
New finance leases	(393)	(208)
Movement in Net Funds	3,740	(1,541)
Opening Net Funds	6,018	7,559
Closing Net Funds	9,758	6,018

32. Analysis of net funds

	2003 £000	Cash flow £000	Other non cash changes £000	2004 £000
Cash at bank and in hand	337	79	-	416
Short term deposits	6,244	4,208	-	10,452
Unsecured loans	(54)	(424)	-	(478)
Finance leases due within one year	(281)	136	(165)	(310)
Finance leases due in more than one year	(228)	134	(228)	(322)
	6,018	4,133	(393)	9,758

The majority of finance leases are arranged in respect of sale and leaseback transactions. Accordingly new finance leases are shown as a separate component of cash flow in the cash flow statement.

33. Related party transactions

Prior to the disposal of Healthcare Education Services Limited, details of which are set out in note 3, the Group acquired the minority interest of 18.75% in that company which was owned by Dr. R.N. Boyes, a Director of M.L. Laboratories PLC, for a consideration of £1.

The Directors have taken advantage of the exemption conferred by Financial Reporting Standard 8 not to disclose transactions with other Group companies as they are eliminated on consolidation.