Vectura Group plc Interim Report 2007/08

vectura

A leader in inhaled pharmaceuticals

About Vectura

Vectura Group plc is a pulmonary product development company focused principally on the development of a range of inhaled therapies for the treatment of respiratory and neurological diseases. Vectura develops products to treat respiratory diseases such as asthma, chronic obstructive pulmonary disease (COPD) and cystic fibrosis, the market for which is forecast to achieve sales of $32 billion by 2011. Vectura also develops products for non-respiratory diseases where optimised delivery via the lungs into the blood stream can provide significant benefits, such as a rapid onset of action, improved efficacy and improved tolerability compared with current therapies.

Vectura has eight marketed products and a portfolio of drugs in clinical and pre-clinical development, some of which have been licensed to major pharmaceutical companies. The Company seeks to develop certain programmes further through development to optimise value at a later licensing stage. Vectura also offers its formulation and inhalation technologies to other pharmaceutical companies on a licensing basis where this complements Vectura's business strategy.

Vectura has development collaborations with several pharmaceutical companies including Boehringer Ingelheim, Novartis and Chiesi. The acquisition of Innovata in January 2007 brought established alliances with a number of additional companies, such as Baxter, GlaxoSmithKline (GSK), Merck Generics (part of Mylan Inc), UCB and Otsuka, as well as providing revenue streams, complementary products and critical mass.

For further information, please visit Vectura's website at **www.vectura.com**

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Vectura's forward-looking statement
This interim report contains "forward-looking statements," including statements about the discovery, development and commercialisation of products. Various risks may cause Vectura's actual results to differ materially from those expressed or implied by the forward-looking statements, including adverse results in clinical development programs; failure to obtain patent protection for discoveries; commercial limitations imposed by patents owned or controlled by third parties; dependence upon strategic alliance partners to develop and commercialise products and services; difficulties or delays in obtaining regulatory approvals to market products and services resulting from development efforts; the requirement for substantial funding to conduct research and development and to expand commercialisation activities; and product initiatives by competitors. As a result of these factors, prospective investors are cautioned not to rely on any forward-looking statement. We disclaim any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

Interim Highlights for the Six Months ended 30 September 2007

Recent Achievements

Milestone on collaboration with Boehringer Ingelheim – Vectura will receive €10 million cash payment, and an additional €5 million equity investment

Corporate Highlights

- Innovata integration complete with cost savings in excess of expectations
- Successful move from AIM to the Official List of the London Stock Exchange in July 2007

Financial Highlights

Revenues increased
by 102%
to £12.3 million
(2006 H1: £6.1 million)

Gross profit
up by 116%
to £9.8million
(2006 H1: £4.5 million)

Investment in Research and Development
up by 120%
to £14.6million
(2006 H1: £6.7 million)

Cash of
£71.4 million
at 30 September 2007
(£77.5 million at 31 March 2007)

Product Highlights

VR315 for asthma (partnered with major generics companies)
- Milestone successfully achieved; €3 million received October 2007

NVA237 and QVA149 for COPD (partnered with Novartis)
- Initiation of three Phase II clinical studies

VR040 for Parkinson's disease
- Successful completion of second Phase II study

VR147 for migraine
- Initiation of Phase I trial

VR004 for erectile dysfunction
- Successful completion of second Phase IIb study

VR776 for premature ejaculation
- Successful completion of Phase IIa study

QDose inhaled insulin programme for diabetes
- Successful completion of Phase I glucose clamp study

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This is an exciting time at Vectura as we continue to build momentum by delivering on our commercial, development and operational goals. We have made significant advances across our product portfolio and we are very pleased to announce that we have achieved an important development milestone on our collaboration with Boehringer Ingelheim. We believe Vectura will play a key role in the rapidly growing respiratory market and we are approaching some significant growth catalysts for the Company with the start of pivotal studies in our asthma and COPD programmes.

Dr Chris Blackwell Chief Executive of Vectura

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Chairman’s and Chief Executive’s report

Overview

We are pleased to report progress across all aspects of our business. Success on the corporate front was demonstrated by the completion of the integration of Innovata, where we achieved cost savings of £2 million in the six months, which were ahead of our expectations. The Innovata business contributed an impressive £3.9 million of EBITDA in the six months. We also successfully moved from AIM to the Official List of the London Stock Exchange in July 2007. These successes have been accompanied by excellent clinical trial results and milestones across a number of our products and collaborations.

Our partner, Novartis has initiated two Phase II trials with NVA237, a once-daily muscarinic antagonist for COPD, in addition to a Phase II trial for QVA149, the combination therapy of NVA237 with indacaterol. Also in the respiratory therapy area, we have generated milestone payments on both our Boehringer Ingelheim collaboration and our asthma programme, VR315.

A number of our proprietary programmes have made significant progress, including VR040 for Parkinson’s disease, which has successfully completed a second Phase II study, and our migraine programme, VR147, which has entered clinical trials. We have also achieved good clinical trial results for the three products we are seeking to out-license; VR004 for erectile dysfunction, VR776 for premature ejaculation and our inhaled insulin.

Product pipeline

Franchise	Product name	Indication	Pre-clinical	Phase I	Phase II	Phase III	Partner
Respiratory	Budesonide Clickhaler®	asthma					Japanese partner
	NVA237	COPD					Novartis
	QVA149	COPD					Novartis
	VR315	asthma					US and EU partners
	Duohaler® Project 1	asthma/COPD					EU partner
	Duohaler® Project 2	asthma/COPD					EU partner
	BI collaboration	respiratory products					Boehringer Ingelheim
	VR496	CF and COPD					
Neurology	VR040	Parkinson’s disease					
	VR147	migraine					
Other	VR004	erectile dysfunction					
	VR776	premature ejaculation					
	QDose Insulin	diabetes					

Chairman's and Chief Executive's report (continued)

Product pipeline

Respiratory

Boehringer Ingelheim collaboration

In November 2007 Vectura achieved a pre-agreed milestone payment under our collaboration with Boehringer Ingelheim to develop a new dry powder inhaler (DPI). Vectura will receive in December a cash payment of €10 million and a €5 million equity investment.

In April 2006, Vectura entered a worldwide collaboration, development and licence agreement with Boehringer Ingelheim to develop a DPI as a tailored Boehringer Ingelheim device to deliver a range of their proprietary respiratory products, primarily for treating asthma and COPD. Boehringer Ingelheim ultimately will be responsible for further development, manufacturing and clinical trial use of the DPI with their proprietary compounds, and the commercialisation of these products. Vectura will receive development milestones and royalties on sales of each product that uses the device. The non-exclusive nature of the agreement with Boehringer Ingelheim provides Vectura with an excellent opportunity to deliver further value from our inhaled therapy technologies.

NVA237 and QVA149 for COPD

NVA237 is a once-daily, rapid onset, long-acting muscarinic antagonist (LAMA), which Novartis intends to launch as a differentiated treatment for COPD, with improved benefits for patients compared with existing therapies. QVA149 comprises the combination of NVA237 with Novartis's once-daily, long-acting beta agonist (LABA), indacaterol (or QAB149), which is currently in Phase III development. We believe that QVA149 is one of the most advanced once-daily LAMA/LABA combinations in development, and that it could be the first such combination to come to market for COPD.

Vectura developed NVA237 in collaboration with Sosei Co Ltd, applying PowderHale®, Vectura's proprietary technology, to improve the formulation for delivery to the lungs. Vectura and Sosei licensed NVA237 to Novartis in April 2005.

Over the past six months, Novartis has initiated additional Phase II trials including a dose-ranging study and a US IND (Investigational New Drug) regulatory authorisation to support the safety of NVA237, as well as a Phase II safety study with QVA149. Novartis announced in September 2007 that it expects to initiate Phase III trials in 2008, with an expectation to file NDAs (New Drug Applications) in 2010.

VR315 for asthma

VR315 is an inhaled combination asthma therapy that is being developed as a generic product using GyroHaler® as the delivery device. Vectura licensed the European rights for VR315 to an undisclosed leading international pharmaceutical company in March 2006. The US rights were licensed to an undisclosed leading international pharmaceutical company in December 2006. As at 30 September 2007, Vectura was due to receive €3 million in cash from its European partner in relation to milestones achieved during the six months to 30 September 2007. Vectura expects VR315 to enter clinical registration studies in 2008.

VR496 treatment for Cystic Fibrosis (CF) and COPD

VR496 is being developed as an inhaled, locally-acting treatment for CF, with the potential to be developed as a therapy for COPD. The active component of VR496 is a drug that has been approved worldwide as an injected or infused treatment for other indications. The European Medicines Evaluation Agency (EMEA) and US Food and Drug Administration (FDA) have designated VR496 an orphan drug. It is expected that this product will enter Phase II studies in early 2008.

Duohaler®

Vectura has two exclusive agreements with a leading European pharmaceutical company for the, development marketing and distribution in Europe and other specified countries (excluding the US and Japan) of two Duohaler® products, each of which co-delivers two established respiratory drugs. Vectura expects one of these products to enter clinical registration studies during 2008.

Neurology

VR040 treatment for Parkinson's disease (PD)

VR040 is an inhaled, systemically acting product for treating "off" episodes associated with advanced PD that do not respond to oral treatment. The active ingredient in VR040, apomorphine hydrochloride, has previously been approved as an injectable formulation in Europe, and more recently in the US, for treating "off" episodes. VR040 is Vectura's formulation of apomorphine, delivered by inhalation using the Company's proprietary DPI technology.

In October 2007 Vectura announced successful completion of a second Phase II clinical study for VR040 in patients with PD. The study demonstrated that VR040 was safe, well-tolerated, and successfully recovered patients from an induced "off" episode with a rapid onset of action; this effect was also durable. Importantly, the novel delivery via inhalation could offer patients an improved alternative to the currently available formulations of apomorphine.

VR147 for migraine

VR147 is an undisclosed inhaled compound with the potential to provide a rapid onset of action, which is expected to provide key benefits to migraine patients. In the third quarter of 2007, Vectura initiated a Phase I clinical trial of VR147 for the treatment of migraine.

Other development products

VR004 for the treatment of erectile dysfunction (ED)

VR004 is an inhaled, systemic product for treating mild, moderate and severe ED. As with VR040, the active ingredient is apomorphine, previously approved in Europe for treating ED as a sublingual tablet. VR004 is formulated in a proprietary Vectura formulation and delivered using Vectura's Aspirair® device.

Vectura has demonstrated efficacy and a rapid onset of action in ED patients in a Phase IIa clinical study. In subsequent Phase IIb clinical trials, completed in June 2006 and April 2007, Vectura demonstrated in an "at home" setting that VR004 was effective in a larger population and also identified an effective dose range associated with an acceptable side-effect profile. Vectura is now seeking licensing partners for the product.

VR776 for the treatment of premature ejaculation (PE)

VR776 is a Vectura proprietary inhaled, systemic treatment for PE in which the active ingredient is an off-patent neuro-active drug approved worldwide for treating other indications. VR776 is formulated using PowderHale® and delivered with Aspirair®.

Vectura has completed pre-clinical toxicology studies and a "first-time-in-man study". A successful Phase IIa proof-of-concept study was announced in May 2007. Vectura is now seeking licensing partners for the product.

Inhaled insulin

In August 2007 Vectura announced the successful completion of a glucose clamp study on the QDose inhaled insulin programme. QDose Limited is a 50/50 joint venture with MicroDose Technologies Inc. The study demonstrated a faster onset of action with the inhaled formulation compared with that of subcutaneous insulin. In addition, the relative bioavailability observed in this study compares favourably with available information on competitor inhaled insulin programmes. QDose is now seeking licensing partners for the product.

Marketed products

ADVATE®

In 2000 Baxter was granted worldwide rights to use Vectura's stabilisation patents and has utilised the technology in its serum-free recombinant Factor VIII, ADVATE®. ADVATE® is indicated for the treatment of haemophilia A and is marketed worldwide by Baxter. Vectura receives royalties on sales of ADVATE®. Baxter has projected that sales for calendar year 2007 will be in excess of $1.1 billion.

Adept®

Adept® is a 4% icodextrin solution used during surgery to reduce post-surgical adhesions, a frequent and major complication following gynaecological and other abdominal surgery. It has been used for this purpose in Europe since 2000. Vectura signed a global licence deal with Baxter in December 2005 for the manufacture and distribution of Adept®.

On 1 August 2006, Baxter announced that the FDA had approved Adept® adhesion reduction solution for intraperitoneal use as an adjunct to good surgical technique for the reduction of post-surgical adhesions in patients undergoing gynaecological laparoscopic adhesiolysis. Adept® was launched by Baxter in the US in October 2006. We announced the publication of the Phase III clinical trial results for this product in the November 2007 US issue of Fertility and Sterility and this should assist Baxter with their marketing campaign in the US.

Extraneal®

Extraneal® is a peritoneal dialysis solution containing icodextrin, licensed to Baxter in 1996 and now marketed worldwide. The product has been launched in over 45 countries worldwide including, in 2003, the major markets of the US and Japan. Since September 2006, Vectura no longer receives royalties on the sales of Extraneal® in Europe, but continues to receive royalties on sales in the US, Japan and the rest of the world.

Asmasal® and Asmabec®

Two products for the treatment of asthma, Asmasal® containing salbutamol and Asmabec® containing beclometasone, are marketed by UCB S.A. in the UK, France and Ireland. These products are delivered using Vectura's Clickhaler®, a multi-dose, single reservoir DPI.

Budesonide Clickhaler® and Formoterol Clickhaler®

Two further Clickhaler® products for the treatment of asthma, the Budesonide Clickhaler® and the Formoterol Clickhaler®, are marketed by Merck Generics (now part of Mylan Inc.) in some European countries. The product dossiers are currently with other European regulatory authorities awaiting approval. On 30 October 2007, the EMEA published further guidelines on the requirements for DPI regulatory dossiers and we believe this guidance should assist these products in gaining a more rapid approval in key European territories.

Meptin Clickhaler®

Meptin® Clickhaler® is marketed in Japan by Otsuka Pharmaceutical Co Ltd and is for the delivery of its beta-agonist asthma treatment, procaterol.

Vectura receives royalties and/or product margin on these five Clickhaler® products and continues to explore licensing opportunities for Clickhaler® products in other countries. Budesonide Clickhaler® is licensed to an unnamed partner in Japan and it is hoped that marketing authorisation for this product will be achieved in 2009.

Vectura also supplies the Clickhaler® devices to these licensees and earns a margin on their sales.

Chairman's and Chief Executive's report (continued)

Outlook

Vectura has a broad, innovative clinical pipeline that combines valuable mid- and late-stage pharmaceutical products and earlier stage opportunities with high commercial potential. These are supported by a wide range of devices, technologies and expertise that allow Vectura to address fast-growing market sectors. Vectura expects to continue to invest in advancing its product pipeline from a position of financial strength and plans on taking selected proprietary products through to registration, whilst maintaining a balanced risk/reward strategy of pursuing product and technology collaborations with large pharmaceutical partners where appropriate.

The key drivers over the remainder of the year relate to the continued success of Vectura's development work, particularly on the respiratory programmes partnered with Novartis and the asthma programmes licensed to undisclosed partners and the Company expects some important pivotal trials to initiate on these projects over the course of 2008.

Vectura also expects to announce clinical data from VR147 for migraine during 2008, which has the potential to provide a rapid onset of action and which it is hoped will provide key benefits to migraine patients. The Company has opportunities for new licensing deals from its sexual dysfunction programmes, VR004 in erectile dysfunction and VR776 for premature ejaculation and expects to see advancement in the royalties earned on its licensed products, particularly ADVATE®.

In relation to trading in second half of the year, Vectura expects to be cash generative in the six months to 31 March 2008. This will be achieved as a result of the receipt of £10 million from Boehringher Ingelheim due in December 2007 and the £2 million received from our VR315 partner in October 2007. These receipts will off-set the continued increase in our investment in research and development activities.

With eight marketed products, one Phase III product, eight Phase II products and four products entering registration studies in the next 12-18 months Vectura is well placed to deliver valuable returns for shareholders. With stable revenues from marketed products and £71.4 million in cash Vectura is also making good progress on its goal to become a sustainable, self-funding principal player in the development of pulmonary pharmaceutical products.

Jack Cashman
Chairman

Chris Blackwell
Chief Executive

23 November 2007

Financial review

Total revenue

07 H1 £12.3m

06 H1 £6.1m

Gross profit

07 H1 £9.8m

06 H1 £4.5m

R&D development expenses

07 H1 £14.6m

06 H1 £6.7m

Summary of Results

The results for the six months ended 30 September 2007 show total revenue of £12.3 million (H1 2006–£6.1 million) with gross profit of £9.8 million (H1 2006–£4.5 million). The operating loss for the period was £13.0 million (H1 2006–£3.6 million). The loss before tax was £11.3 million (2006–£2.7 million) and the loss after tax £9.6 million (2006–£1.9 million). The increase in losses is mainly due to the £7.9 million increase in investment in research and development.

Risks and uncertainties

There are a number of potential risks and uncertainties which could have a material impact on the Group's performance over the remaining six months of the financial year and could cause actual results to differ materially from expected and historical results. Particular risks include industry risk, clinical and regulatory risk, competition and intellectual property risk, economic risk and financial risk (cash flow, credit, liquidity and price).

Innovata acquisition

Comparison of the results with the previous year is affected by the acquisition of Innovata in January 2007. Innovata is a profitable cash generative business with revenues of £8.3 million for the six months to 30 September 2007 and EBITDA of £3.9 million. This compares to revenues of £8.6 million for the six months to 31 March 2007 and an EBITDA before exceptionals of £1.9 million. Vectura generated savings in excess of £2 million from the combination of the two businesses in the six-month period which is ahead of our expectations. We now expect to generate over £5 million per annum in cost savings from the Innovata business.

Revenue

Revenue includes fee income from product licensing, technology licensing, development fees, royalties and device sales. In the six-months to 30 September 2007, revenue increased compared to the six-months to 30 September 2006 by 102% to £12.3 million, and included a contribution of £8.3 million from Innovata. The underlying revenue for the existing Vectura Group decreased by 34%, from £6.1 million to £4 million due to the recognition of one-off milestone payments in the six months to 30 September 2006.

Product licensing revenues in the period were £2.2 million, and include £1.4 million for VR315, £0.5 million of which was released from deferred income and £0.9 million relates to a new milestone recognised in the period. Licensing revenues also include £0.5 million released from deferred income and generated from the 2003 licensing agreement between Innovata and GSK relating to formulation and delivery patents for DNA vaccine delivery. As at 30 September 2007, Vectura was due to receive £2 million in cash from its VR315 European partner in relation to achievement of a milestone in the period. £0.9 million has been recognised as revenue in the period and £1.1 million relates to the sale of a blister filling machine. The total £2 million was received in October 2007 and is included in trade debtors at 30 September 2007.

Technology licensing revenues of £0.9 million were released from deferred income during the period. This was the access fee from Boehringer Ingelheim, which is being recognised over a two-year period in line with the period in which services are being provided. The milestone payment of €10 million announced today (due to be received in December 2007) will also be recognised over a two-year period.

Pharmaceutical Development Services (PDS) revenues were £4.1 million. These revenues represent principally contractual development fees charged to licensing partners for work carried out during the period, particularly in relation to work with our European partner on VR315. It is expected that these revenues will decrease in the second half of the year following the achievement of a milestone in September 2007.

Total royalties for the period were £4.5 million and relate to products in the portfolio acquired from Innovata. The principal royalty income streams were from ADVATE® and Extraneal®, with smaller contributions from Adept® and products delivered in Clickhaler®.

Financial review (continued)

Product sales revenue of £0.6 million was derived from the sale of devices to licensees.

Gross profit

The gross profit in the period to 30 September 2007 was £9.8 million, a £5.3 million improvement on the same period in the prior period (£4.5 million). Gross profit in the period to 30 September 2007 represents 79% of revenue (2006 – 74%).

Research and development expenses

Total investment in research and development was £14.6 million, a 120% increase on the same period in the prior year (£6.7 million). We expect our investment in this area to continue to increase as some of our key products move to late-stage development.

Other Administrative expenses

Other administrative expenses for the period were £1.7 million, a £0.5 million increase on the prior period mainly due to the expanded operations.

Loss after taxation and loss per share

The loss for the year after taxation was £9.6 million (2006 – £1.9 million) giving a loss per ordinary share of 3.1p (2006 – 1.5p).

Non-current assets

Non-current assets were £146.2 million, compared with £156.2 million at 31 March 2007, including goodwill (£71.1 million), intangible assets (£67.7 million), a deferred tax asset (£1.9 million) and property, plant and equipment (£3.8 million). In accordance with accounting practice, the calculation of the fair value of the assets acquired with the Innovata business is provisional and may be adjusted at any time up to the anniversary of the acquisition in January 2008.

Deferred tax liability

Liabilities include £19.0 million of deferred tax, which is equivalent to 28% (current UK corporation tax rate) of the value of the intangible assets acquired with Innovata as at 30 September 2007. The write down of this liability will reduce the tax charge in the income statement annually. The annual reduction in this liability will equate to 28% of the annual amortisation charge on these Innovata intangible assets.

Financial liability

Current liabilities include £3.9 million of a total £15.8 million financial liability, which represents an Innovata liability to a third party in respect of a loan secured on Adept® and Extraneal® royalty streams.

Deferred income

Deferred income relates to milestones received but not yet recognised as revenue. The £9.2 million to be recognised as revenue in later periods includes £2.5 million for VR315, £0.9 million relating to Boehringer Ingelheim, £3.4 million for Clickhaler® and £2.4 million for Duohaler®.

Operating cash flow

Net cash outflow from operating activities in the period was £7.9 million compared to a cash inflow of £1.5 million in the 6 months to 30 September 2006. At 30 September 2007, Vectura had cash and short-term deposits of £71.4 million (31 March 2007 – £77.5 million). As discussed in the Chairman and Chief Executive's review Vectura expects to be cash generative in the six months to 31 March 2008.

Anne Hyland
Chief Financial Officer

23 November 2007

Responsibility statement

We confirm that to the best of our knowledge:

a) the condensed set of financial statement has been prepared in accordance with IAS 34 "Interim Financial Reporting";

b) this report includes a fair review of the information required by the Disclosure and Transparency Directive DTR 4.2.7R (indication of important events during the first six months and description of principal risks and uncertainties for the remaining six months of the year); and

c) this report includes a fair review of the information required by DTR 4.2.8R (disclosure of related party transactions and changes therein).

By order of the Board

Anne Hyland
Company Secretary

23 November 2007

Financial statements for the six months ended 30 September 2007

Consolidated income statement

for the six months ended 30 September 2007 (unaudited)

	Notes	6 months ended 30 September 2007 (unaudited) £000	6 months ended 30 September 2006 (unaudited) £000	Year ended 31 March 2007 (audited) £000
Revenue	2	**12,270**	6,079	**14,051**
Cost of sales		(2,517)	**(1,561)**	(3,295)
Gross profit		**9,753**	4,518	**10,756**
Research and development expenses		(14,637)	(6,660)	(16,994)
Administrative expenses		(1,694)	(1,161)	(2,615)
Amortisation		(4,786)	–	(1,995)
Share-based compensation		(1,471)	(463)	(1,633)
Total administrative expenses		(7,951)	(1,624)	(6,243)
Share of loss of associate		(153)	(61)	(208)
Other income		–	199	1,423
Operating loss	3	**(12,988)**	(3,628)	**(11,266)**
Finance income		2,137	932	2,816
Finance costs		(467)	(2)	(242)
Loss before taxation		**(11,318)**	(2,698)	**(8,692)**
Taxation	4	1,696	776	1,865
Loss after taxation attributable to equity holders of the company		**(9,622)**	(1,922)	**(6,827)**
Loss per ordinary share basic and diluted	5	(3.1p)	(1.5p)	(4.4p)

All results are derived from continuing activities.

Consolidated balance sheet

at 30 September 2007 (unaudited)

	Notes	30 September 2007 (unaudited) £000	30 September 2006 (unaudited) £000	31 March 2007 (audited) £000
Assets				
Intangible assets, including goodwill	11	138,775	2,012	146,784
Property, plant and equipment		3,839	3,535	5,635
Investments accounted for using the equity method		1,074	–	1,228
Trade investment		250	–	250
Deferred tax asset		1,871	–	1,871
Other non-current assets		428	428	428
Non-current assets		**146,237**	5,975	**156,196**
Inventories		122	–	202
Trade and other receivables	6	8,740	3,278	8,230
Short-term investments		–	–	500
Cash and cash equivalents		71,422	68,614	77,029
Current assets		**80,284**	71,892	**85,961**
Total assets		**226,521**	77,867	**242,157**
Liabilities				
Trade and other payables	7	(7,988)	(5,569)	(8,060)
Obligations under finance leases		–	–	(410)
Deferred income	8	(2,918)	(4,567)	(4,400)
Financial liabilities	9	(3,882)	–	(3,216)
Current liabilities		**(14,788)**	(10,136)	**(16,086)**
Deferred income	8	(6,312)	(2,662)	(6,888)
Financial liabilities	9	(11,905)	–	(15,163)
Deferred tax	11	(18,961)	–	(21,752)
Non-current liabilities		**(37,178)**	(2,662)	**(43,803)**
Total liabilities		**(51,966)**	(12,798)	**(59,889)**
Net assets		**174,555**	65,069	**182,268**
Equity				
Share capital	10	113	76	113
Share premium		73,327	72,768	72,889
Shares to be issued		–	918	–
Other reserves		137,657	13,322	136,186
Retained loss		(36,542)	(22,015)	(26,920)
Total equity		**174,555**	65,069	**182,268**

These financial statements were approved by the Board of Directors on 23 November 2007 and were signed on its behalf by:

Dr C P Blackwell
Director

A P Hyland
Director

Consolidated cash flow statement

for the six months ended 30 September 2007 (unaudited)

	6 months ended 30 September 2007 (unaudited) £000	6 months ended 30 September 2006 (unaudited) £000	Year ended 31 March 2007 (audited) £000
Cash flow from operating activities			
Loss before tax	(11,318)	(2,698)	(8,692)
Finance income and expense	(1,670)	(930)	(2,574)
Depreciation, amortisation and share based compensation	7,101	1,017	4,893
Increase in working capital	1,773	3,936	1,938
(Decrease)/increase in deferred income	(2,058)	305	(2,236)
(Decrease) in financial liabilities	(2,049)	–	–
Other	153	(138)	(1,235)
Cash (outflow)/inflow from operating activities	(8,068)	1,492	(7,906)
Taxation paid	(52)	–	–
Research and development tax credits received	228	–	1,396
Net cash (outflow)/inflow from operating activities	**(7,892)**	1,492	**(6,510)**
Cash flows from investing activities			
Cash acquired as part of Innovata	–	–	19,882
Costs in association with acquisition of Innovata	–	–	(2,830)
Interest received	2,137	930	2,816
Investment in associate	–	(10)	(160)
Purchase of property plant and equipment	(366)	(523)	(2,438)
Receipts from sale of property, plant and equipment	–	–	22
Net cash flows from investing activities	**1,771**	397	**17,292**
Cash flows from financing activities			
Proceeds from issue of ordinary shares	438	51,985	52,143
Share issue costs	–	(2,072)	(2,072)
Payment of finance lease liabilities	(410)	(14)	(139)
Interest element of payments under finance leases	(14)	(2)	(10)
Repayment of loans	–	–	–
Interest on loans	–	–	(3)
Net cash flows from financing activities	**14**	49,897	**49,919**
Decrease)/increase in cash and cash equivalents	**(6,107)**	51,786	**60,701**
Cash and cash equivalents at beginning of period	77,529	16,828	16,828
Cash and cash equivalents at end of period	**71,422**	68,614	**77,529**

Consolidated statement of changes in equity

for the six months ended 30 September 2007 (unaudited)

	Share capital £000	Share premium £000	Shares to be issued £000	Special reserve £000	Merger reserve £000	Share-based compensation reserve £000	Retained loss £000	Total equity £000
At 1 April 2006	62	22,869	918	8,245	3,211	1,403	(20,093)	16,615
Loss for the period	–	–	–	–	–	–	(1,922)	(1,922)
Total recognised income and expense for the period	–	–	–	–	–	–	(1,922)	(1,922)
Issue of ordinary shares	14	51,889	–	–	–	–	–	51,903
Share issue costs	–	(2,072)	–	–	–	–	–	(2,072)
Share-based compensation	–	–	–	–	–	463	–	463
Exercise of warrants and options	–	82	–	–	–	–	–	82
At 30 September 2006	76	72,768	918	8,245	3,211	1,866	(22,015)	65,069
Loss for the period	–	–	–	–	–	–	(4,905)	(4,905)
Total recognised income and expense for the period	–	–	–	–	–	–	(4,905)	(4,905)
Issue of ordinary shares	37	–	(918)	–	121,694	–	–	120,813
Share-based compensation	–	–	–	–	–	1,170	–	1,170
Exercise of warrants and options	–	121	–	–	–	–	–	121
At 31 March 2007	113	72,889	–	8,245	124,905	3,036	(26,920)	182,268
Loss for the period	–	–	–	–	–	–	(9,622)	(9,622)
Total recognised income and expense for the period	–	–	–	–	–	–	(9,622)	(9,622)
Issue of ordinary shares	–	438	–	–	–	–	–	438
Share-based compensation	–	–	–	–	–	1,471	–	1,471
At 30 September 2007	**113**	**73,327**	–	**8,245**	**124,905**	**4,507**	**(36,542)**	**174,555**

Notes to the financial statements

1 Basis of preparation of interim financial statements

The unaudited interim financial statements have been prepared in accordance with International Financial Reporting Standards and International Accounting Standards (collectively IFRS) as adopted by the European Union. Details of the accounting policies applied are those set out in Vectura Group plc's Annual Report for the year ended 31 March 2007. These interim financial statements have been prepared in accordance with International Accounting Standard 34 "Interim Financial Reporting" they do not include all the statements required for full annual financial statements, and should be read in conjunction with the consolidated financial statements of the group as at the year ended 31 March 2007.

These interim financial statements are unaudited and do not constitute statutory accounts of the group as defined in section 240 of the Companies Act 1985. The auditors, Deloitte & Touche LLP, have carried out a review of the financial information in accordance with the guidance contained in International Standard on Review Engagements (UK and Ireland) 2410 'Review of Interim Financial Information Performed by the Independent Auditor of the Entity' and their review report is set out at the end of this report.

The financial information for the year ended 31 March 2007 has been extracted from the group's published financial statements for that year, which contain an unqualified audit report from Ernst & Young LLP, which did not contain statements under section 237of the Companies Act 1985 and which have been filed with the Registrar of Companies.

2 Revenue

Revenue by category:	6 months ended 30 September 2007 £000	6months ended 30 September 2006 £000	Year ended 31 March 2007 £000
Product licensing	2,182	2,327	4,592
Technology licensing	860	809	1,713
Pharmaceutical Development Services	4,138	2,943	5,838
Royalties	4,450	–	1,443
Product sales	640	–	465
	12,270	6,079	14,051

Revenue by customer location:	6 months ended 30 September 2007 £000	6months ended 30 September 2006 £000	Year ended 31 March 2007 £000
United Kingdom	4,511	848	3,246
Rest of Europe	2,735	5,231	9,371
United States of America	4,839	–	1,397
Rest of World	185	–	37
	12,270	6,079	14,051

Interest income is disclosed separately in the income statement and has been excluded from this note.

For management purposes the group is currently organised into one business segment, which is the development of pharmaceutical products. Since this is the only primary reporting segment, no further information has been shown. All revenue and losses before taxation originate in the United Kingdom.

3 Operating loss

This is stated after charging/(crediting):	6 months ended 30 September 2007 £000	6months ended 30 September 2006 £000	Year ended 31 March 2007 £000
Amortisation of intangibles	4,786	–	1,995
Depreciation of property, plant and equipment:			
– owned	829	547	1,242
– held under finance leases and hire purchase contracts	15	7	23
Share-based compensation	1,471	463	1,633
Share of loss of associate (after taxation)	153	–	208
Auditor's remuneration:			
– Audit fees to Ernst & Young LLP	–	6	71
– Audit related services to Deloitte & Touche LLP	15	–	–
– Other services to Ernst & Young LLP	47	30	120
– Other services to Deloitte & Touche LLP	30	–	–
Operating lease rentals:			
– land and buildings	395	174	456
– plant and machinery	76	39	86
Net foreign exchange (gain)/loss	(73)	70	32

4 Taxation

	6 months ended 30 September 2007 £000	6months ended 30 September 2006 £000	Year ended 31 March 2007 £000
Current income tax:			
Current income tax charge	(52)	–	(41)
Utilisation of Innovata tax losses	(777)	–	(130)
Research and development tax credits	1,185	776	1,437
	356	776	1,266
Deferred income tax:			
Deferred tax relating to 28% of amortisation charge	1,340	–	599
	1,696	776	1,865

Utilisation of Innovata tax losses is a non-cash charge which will be charged to the income statement until the estimated tax losses of £88 million acquired with the business are utilised. The utilisation of these tax losses will reduce the goodwill acquired with the business by an amount equivalent to the tax losses utilised each year. Included in the research and development tax credits above is £957,000 yet to be received.

Notes to the financial statements (continued)

5 Loss per ordinary share

The calculation of loss per share is based on the following losses and number of shares:	6 months ended 30 September 2007 £000	6months ended 30 September 2006 £000	Year ended 31 March 2007 £000
Retained loss for the period	(9,622)	(1,922)	(6,827)
Weighted average number of ordinary shares (No. 000)	315,106	129,038	155,205
Loss per share	(3.1p)	(1.5p)	(4.4p)

The loss per share is based on the weighted average number of shares in issue during the period. IAS 33, "Earnings per Share", requires presentation of diluted earnings per share when a company could be called upon to issue shares that would decrease net profit or increase net loss per share. No adjustment has been made to the basic loss per share, as the exercise of share options and warrants would have the effect of reducing the loss per ordinary share, and is therefore not dilutive.

6 Trade and other receivables

	30 September 2007 £000	30 September 2006 £000	31 March 2007 £000
Trade receivables	3,853	561	2,099
Other receivables	2,223	2,096	14
Prepayments and accrued income	2,497	359	5,538
VAT recoverable	167	262	579
	8,740	3,278	8,230

7 Trade and other payables

	30 September 2007 £000	30 September 2006 £000	31 March 2007 £000
Trade payables	1,435	1,156	1,063
Other taxes and social security costs	342	236	416
Other payables	408	-	438
Accruals	5,803	4,177	6,143
	7,988	5,569	8,060

8 Deferred income

Deferred income relates to amounts received under licensing agreements where Vectura Group plc continues to provide services to these licensing partners over a period of time. Revenue arising from milestone receipts under such licensing agreements is recognised over the period of time the services are being provided. Deferred income is as follows:

	30 September 2007 £000	30 September 2006 £000	31 March 2007 £000
Amounts due in more than one year	6,312	2,662	6,888
Amounts due within one year	2,918	4,567	4,400
	9,230	7,229	11,288

9 Financial liabilities

	6 months ended 30 September 2007 £000	6 months ended 30 September 2006 £000	Year ended 31 March 2007 £000
Opening balance	18,379	–	–
Acquired as part of Innovata	–	–	18,657
Utilised	(3,046)	–	(507)
Interest	454	–	229
Closing balance	15,787	–	18,379
Due after more than one year	11,905	–	15,163
Due within one year	3,882	–	3,216
Closing balance	15,787	–	18,379

10 Share capital

	30 September 2007 £000	30 September 2007 No.000	30 September 2006 £000	30 September 2006 No.000	31 March 2007 £000	31 March 2007 No.000
Authorised:						
Ordinary shares of 0.025p each	110	441,200	65	261,200	110	441,200
Redeemable preference shares of £1 each	34	34	34	34	34	34
Allotted, called up and fully paid:						
Ordinary shares of 0.025p each	79	315,446	42	168,581	79	314,518
Redeemable preference shares of £1 each	34	34	34	34	34	34

Between 1 April 2007 and 30 September 2007 the company issued 816,660 (2006 – 370,831) ordinary shares of 0.025p each on exercise of employee share options at an average exercise price of 53.6p per share (2006 – 22.1p).

Notes to the financial statements (continued)

11 Innovata acquisition

On 18 January 2007, Vectura Group plc ("Vectura") acquired Innovata plc ("Innovata") and its subsidiaries for a consideration of £123.6 million. This was satisfied by the issue of 143.8 million new Ordinary shares in Vectura whereby Innovata's share capital was acquired by Vectura and Innovata shareholders were allotted new shares in Vectura.

Innovata earned revenues of £8.3 million for the six months to 30 September 2007 (year to 31 March 2007 – £23.1 million), and achieved an operating profit of £2.0 million (year to 31 March 2007 – £4.7 million before exceptional costs). Innovata retained profit for the six months to 30 September 2007 was £3.3 million (year to 31 March 2007 – £5.5 million loss). An analysis of the EBITDA for the two operations for the period is shown below:

	6 months ended 30 September 2007	6 months ended 30 September 2007	6 months ended 30 September 2007
	Group	Vectura excld. IOV	Innovata excld. VEC
	£000	£000	£000
Revenues	12,270	3,996	8,274
Cost of sales	(2,517)	(813)	(1,704)
Gross profit	9,753	3,183	6,570
Research and development costs	(13,946)	(11,545)	(2,401)
Administrative costs	(1,694)	(1,392)	(302)
EBITDA	(5,887)	(9,754)	3,867
Depreciation	(844)		
Amortisation	(4,786)		
Share-based compensation	(1,471)		
Net interest income	1,670		
Loss before taxation	(11,318)		
Taxation	1,696		
Loss after taxation	(9,622)		

In accordance with International Financial Reporting Standard 3 "Business Combinations", the fair values assigned to the identifiable assets, liabilities and contingent liabilities acquired with the Innovata business on 18 January 2007 were determined provisionally on that date and these provisional estimates may be subject to revision in the period to 17 January 2008.

Independent review report to Vectura Group plc

We have been engaged by the company to review the condensed set of financial statements in the half-yearly financial report for the six months ended 30 September 2007 which comprises the income statement, the balance sheet, the statement of changes in equity, the cash flow statement and related notes 1 to 11. We have read the other information contained in the half-yearly financial report and considered whether it contains any apparent misstatements or material inconsistencies with the information in the condensed set of financial statements.

This report is made solely to the company in accordance with International Standard on Review Engagements 2410 issued by the Auditing Practices Board. Our work has been undertaken so that we might state to the company those matters we are required to state to them in an independent review report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company, for our review work, for this report, or for the conclusions we have formed.

Directors' responsibilities
The half-yearly financial report is the responsibility of, and has been approved by, the directors. The directors are responsible for preparing the half-yearly financial report in accordance with the Disclosure and Transparency Rules of the United Kingdom's Financial Services Authority.

As disclosed in note 1, the annual financial statements of the group are prepared in accordance with International Financial Reporting Standards as adopted by the European Union. The condensed set of financial statements included in this half-yearly financial report has been prepared in accordance with International Accounting Standard 34, "Interim Financial Reporting", as adopted by the European Union.

Our responsibility
Our responsibility is to express to the company a conclusion on the condensed set of financial statements in the half-yearly financial report based on our review.

Scope of the review
We conducted our review in accordance with International Standard on Review Engagements (UK and Ireland) 2410, "Review of Interim Financial Information Performed by the Independent Auditor of the Entity" issued by the Auditing Practices Board for use in the United Kingdom. A review of interim financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing (UK and Ireland) and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion
Based on our review, nothing has come to our attention that causes us to believe that the condensed set of financial statements in the half-yearly financial report for the six months ended 30 September 2007 is not prepared, in all material respects, in accordance with International Accounting Standard 34 as adopted by the European Union and the Disclosure and Transparency Rules of the United Kingdom's Financial Services Authority.

Deloitte & Touche LLP
Chartered Accountants and Registered Auditor
Cambridge, UK

23 November 2007

Shareholder information

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Dr Christopher P Blackwell (Chief Executive)
Dr John R Brown (Non-Executive)
Dr Susan E Foden (Non-Executive)
Anne P Hyland (Chief Financial Officer)
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