

ONCOLYTICS BIOTECH INC

Form 6-K

October 31, 2007

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SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

Form 6-K

Report of Foreign Private Issuer

Pursuant to Rule 13a-16 or 15d-16  
of the Securities Exchange Act of 1934

For the month of October 2007

Commission File Number 000-31062

**Oncolytics Biotech Inc.**

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*(Translation of registrant's name into English)*

**Suite 210, 1167 Kensington Crescent NW  
Calgary, Alberta, Canada T2N 1X7**

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*(Address of principal executive offices)*

Indicate by check mark whether the registrant files or will file annual reports under cover Form 20-F or Form 40-F.

Form 20-F

Form 40-F

Indicate by check mark if the registrant is submitting the Form 6-K in paper as permitted by Regulation S-T Rule 101(b)(1):

**Note:** Regulation S-T Rule 101(b)(1) only permits the submission in paper of a Form 6-K if submitted solely to provide an attached annual report to security holders.

Indicate by check mark if the registrant is submitting the Form 6-K in paper as permitted by Regulation S-T Rule 101(b)(7):

**Note:** Regulation S-T Rule 101(b)(7) only permits the submission in paper of a Form 6-K if submitted to furnish a report or other document that the registrant foreign private issuer must furnish and make public under the laws of the jurisdiction in which the registrant is incorporated, domiciled or legally organized (the registrant's home country), or under the rules of the home country exchange on which the registrant's securities are traded, as long as the report or other document is not a press release, is not required to be and has not been distributed to the registrant's security holders, and, if discussing a material event, has already been the subject of a Form 6-K submission or other Commission filing on EDGAR.

Indicate by check mark whether by furnishing the information contained in this Form, the registrant is also thereby furnishing the information to the Commission pursuant to Rule 12g3-2(b) under the Securities Exchange Act of 1934.

Yes

No

If Yes is marked, indicate below the file number assigned to the registrant in connection with Rule 12g3-2(b): 82 - \_\_\_\_\_

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**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

**Oncolytics Biotech Inc.**  
(Registrant)

Date: October 31, 2007

By: /s/ Doug Ball

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Doug Ball  
Chief Financial Officer

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**Third Quarter Report  
September 30, 2007**

**Oncolytics Biotech Inc.  
TSX: ONC  
NASDAQ: ONCY**

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### **Third Quarter Report**

*For the quarter ended September 30, 2007*

#### **Letter to Shareholders**

Clinical trial results announced in the third quarter and the commencement of enrolment in a third combination clinical trial highlighted an exciting and busy quarter for the Company. We reported positive interim clinical results from our Phase Ia/Ib combination REOLYSIN® and radiation trial and also announced the start of enrolment in a combination REOLYSIN® and docetaxel trial. In October, we received permission to begin a unique clinical trial in the U.K. that will examine REOLYSIN® in combination with cyclophosphamide, an immune system modulator. In the quarter, the Company also secured two additional U.S. patents and made presentations regarding preclinical and manufacturing processes at several international meetings.

#### **Clinical Trial Progress**

Oncolytics is currently enrolling patients in seven clinical trials in the U.S. and the U.K., and has permission to begin a combination REOLYSIN®/cyclophosphamide trial in the U.K.

##### *Positive Interim Combination REOLYSIN® and radiation results*

Our Phase Ia/Ib trial using REOLYSIN® in combination with radiation continues to report encouraging results. In September, we announced positive interim results from our clinical trial examining the combination of REOLYSIN® and radiation for patients with advanced or metastatic cancers. A total of 22 patients were treated, with 15 completing the study. Five patients withdrew from the study and two patients are still on study. Of 11 patients treated in the 1a portion of the study, three patients experienced significant partial responses in the target tumour, as well as stable disease in non-treated tumours. Of 6 patients who completed the 1b portion of the study, three patients experienced tumour regression in the target tumour, as well as stable disease in non-treated treated tumours. The Ib trial is still enrolling patients and we are continuing to evaluate the data.

The interim results were presented at the National Cancer Research Institute (NCRI) conference in Birmingham, UK on October 2, 2007, as well as at the AACR-NCI-EORTC International Conference on Molecular Targets and Cancer Therapeutics in San Francisco on October 24, 2007.

##### *Additional REOLYSIN® and chemotherapy trials move forward*

In July, we commenced patient enrolment in our third trial using REOLYSIN® in combination with standard chemotherapeutic agents in the U.K. This trial will evaluate the systemic administration of REOLYSIN® in combination with docetaxel (Taxotere®) in patients with advanced cancers including bladder prostate, lung and upper gastro-

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intestinal. Preclinical studies have demonstrated that this combination is synergistic against a variety of cancer cell lines.

A fourth clinical trial which will examine the systemic administration of REOLYSIN® in combination with cyclophosphamide, an immune modulator and chemotherapeutic agent, was approved by the U.K. health authorities in October. This is a unique trial that will deliver a standard dose of REOLYSIN® with escalating doses of cyclophosphamide to patients who have been diagnosed with advanced or metastatic solid tumours including pancreatic, lung and ovarian cancers that have not responded to standard therapy or for which no curative standard therapy exists. The primary objectives of the trial include determining the minimum effective immunomodulatory dose of cyclophosphamide to obtain successful immune modulation. Secondary objectives include the safety profile of the combination and gathering evidence of anti-tumour activity.

**Intellectual Property Advances**

To date, Oncolytics has secured more than 150 issued patents worldwide including two U.S. patents issued in the third quarter. The two new U.S. patents cover the use of modified herpes simplex viruses to treat cancer, as well as the use of REOLYSIN® with chemotherapy to prevent the development of drug resistance to chemotherapeutic agents.

**Preclinical Developments**

Preclinical work completed by our collaborators at the CR-UK Clinical Centre, Leeds, U.K. demonstrated for the first time how reovirus-infected melanoma cells stimulate dendritic cells to prime the immune system against cancer cells. The work was presented in September at the National Cancer Research Institute Conference in Birmingham. U.K. With the expansion of our clinical trial program, particularly into Phase II trials, we expect the remainder of 2007 and 2008 to be an exciting period of significant progress for the Company. As always, thank you for your continued support and encouragement.

Brad Thompson, PhD

President and CEO

October 29, 2007

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October 29, 2007

**MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL  
CONDITION AND RESULTS OF OPERATIONS**

This discussion and analysis should be read in conjunction with the unaudited financial statements of Oncolytics Biotech Inc. as at and for the three and nine months ended September 30, 2007 and 2006, and should also be read in conjunction with the audited financial statements and Management's Discussion and Analysis of Financial Condition and Results of Operations ( MD&A ) contained in our annual report for the year ended December 31, 2006. The financial statements have been prepared in accordance with Canadian generally accepted accounting principles ( GAAP ).

**FORWARD-LOOKING STATEMENTS**

The following discussion contains forward-looking statements, within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended. Forward-looking statements, including our belief as to the potential of REOLYSIN® as a cancer therapeutic and our expectations as to the success of our research and development and manufacturing programs in 2007 and beyond, future financial position, business strategy and plans for future operations, and statements that are not historical facts, involve known and unknown risks and uncertainties, which could cause our actual results to differ materially from those in the forward-looking statements. Such risks and uncertainties include, among others, the need for and availability of funds and resources to pursue research and development projects, the efficacy of REOLYSIN® as a cancer treatment, the success and timely completion of clinical studies and trials, our ability to successfully commercialize REOLYSIN®, uncertainties related to the research, development and manufacturing of pharmaceuticals, uncertainties related to competition, changes in technology, the regulatory process and general changes to the economic environment. Investors should consult our quarterly and annual filings with the Canadian and U.S. securities commissions for additional information on risks and uncertainties relating to the forward-looking statements. Forward-looking statements are based on assumptions, projections, estimates and expectations of management at the time such forward-looking statements are made, and such assumptions, projections, estimates and/or expectations could change or prove to be incorrect or inaccurate. Investors are cautioned against placing undue reliance on forward-looking statements. We do not undertake to update these forward-looking statements.

**OVERVIEW**

***Oncolytics Biotech Inc. is a Development Stage Company***

Since our inception in April of 1998, Oncolytics Biotech Inc. has been a development stage company and we have focused our research and development efforts on the development of REOLYSIN®, our potential cancer therapeutic. We have not been profitable since our inception and expect to continue to incur substantial losses as we continue research and development efforts. We do not expect to generate significant revenues until, if and when, our cancer product becomes commercially viable.

***General Risk Factors***

Prospects for biotechnology companies in the research and development stage should generally be regarded as speculative. It is not possible to predict, based upon studies in animals, or early studies in humans, whether a new therapeutic will ultimately prove to be safe and effective in humans, or whether necessary and sufficient data can be developed through the clinical trial process to support a successful product application and approval.

If a product is approved for sale, product manufacturing at a commercial scale and significant sales to end users at a commercially reasonable price may not be successful. There can be no assurance that we will generate adequate funds to continue development, or will ever achieve significant revenues or profitable



operations. Many factors (e.g. competition, patent protection, appropriate regulatory approvals) can influence the revenue and product profitability potential.

In developing a pharmaceutical product, we rely upon our employees, contractors, consultants and collaborators and other third party relationships, including our ability to obtain appropriate product liability insurance. There can be no assurance that these reliances and relationships will continue as required.

In addition to developmental and operational considerations, market prices for securities of biotechnology companies generally are volatile, and may or may not move in a manner consistent with the progress being made by Oncolytics. See also *RISK FACTORS AFFECTING FUTURE PERFORMANCE* in our 2006 MD&A.

#### ***REOLYSIN® Development Update for the Third Quarter of 2007***

We continue to develop our lead product REOLYSIN® as a possible cancer therapy. Our goal each year is to advance REOLYSIN® through the various steps and stages of development required for potential pharmaceutical products. In order to achieve this goal, we actively manage the development of our clinical trial program, our pre-clinical and collaborative programs, our manufacturing process and REOLYSIN® supply, and our intellectual property.

#### **Clinical Trial Program**

Our clinical trial program includes eight clinical trials of which seven are being conducted by us and one is being sponsored by the U.S. National Cancer Institute ( NCI ). In the third quarter of 2007, we announced positive interim results from our U.K. phase Ia/Ib combination REOLYSIN® and radiation clinical trial. As well, we commenced patient enrollment in our U.K. combination REOLYSIN®/docetaxel clinical trial, increasing our actively enrolling clinical trials to seven.

#### ***Clinical Trial Results***

In the third quarter of 2007, we announced positive interim results from our U.K. Phase Ia/Ib combination REOLYSIN® and radiation clinical trial for patients with advanced or metastatic cancers. As of September 28, 2007, 22 patients had been treated with 15 having completed the study. Five patients withdrew from the study, and two patients are still on study.

A total of 11 patients in the Ia portion of the trial have received two intratumoural treatments of REOLYSIN® at dosages of  $1 \times 10^8$ ,  $1 \times 10^9$ , or  $1 \times 10^{10}$  TCID<sub>50</sub> with a constant localized radiation dose of 20 Gy given in five fractions. Of these 11 patients, three patients (oesophageal, squamous skin carcinoma and squamous cell scalp) experienced significant partial responses.

One month following treatment, the oesophageal patient experienced a 28.5% reduction in the target tumour, with stable disease noted in four, non-treated tumours. At two and three months, the target tumour had shrunk 64%, with stable disease continuing in the four non-treated tumours, including a 15% volume reduction in non-treated mediastinal disease that was maintained for more than six months. The squamous skin cancer patient experienced a 50% reduction in the target tumour, as well as stable disease in two, non-treated tumours at one, two and three months post treatment. The squamous cell scalp patient experienced stable disease in the target tumour for two months which then became a partial response at three months. This patient also experienced stable disease in one non-treated tumour measured at three months post-treatment.

Patients in the Ib portion received either two, four or six intratumoural doses of REOLYSIN® at  $1 \times 10^{10}$  TCID<sub>50</sub> with a constant localized radiation dose of 36 Gy given in 12 fractions. Of the six patients who have completed the study to date, three patients (colorectal, melanoma and lung cancer) experienced tumour regression in the target tumour, as well as stable disease in non-treated tumours.

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The colorectal patient experienced a partial response with a more than 50% regression in the target tumour as well as stable disease in four, non-treated tumours measured at one month following treatment. A melanoma patient experienced minor regression in the target tumour as well as stable disease in two, non-treated tumours at one and two months following treatment. A lung cancer patient experienced minor regression in the target tumour, as well as stable disease in three, non-treated tumours at two months following treatment.

The treatment has been well tolerated, with mostly Grade 1 or 2 toxicities noted including fatigue, lymphopenia, fever, and neutropenia. Grade 3 toxicities including cellulitis, dysphasia and diarrhoea were related to disease progression and not to the combination treatment. Viral replication was unaffected by cellular irradiation.

The primary objective of the Phase Ia/Ib trial was to determine the maximum tolerated dose ( MTD ), dose limiting toxicity ( DLT ), and safety profile of REOLYSIN when administered intratumorally to patients receiving radiation treatment. A secondary objective is to examine any evidence of anti-tumour activity. Eligible patients include those who have been diagnosed with late stage advanced or metastatic solid tumours that are refractory ( have not responded ) to standard therapy or for which no curative standard therapy exists.

#### ***Clinical Trials Actively Enrolling***

At the end of the third quarter of 2007, we were actively enrolling in seven clinical trials. In the third quarter of 2007, we commenced enrollment in the following study:

#### ***U.K. Combination REOLYSIN<sup>®</sup> Docetaxel Clinical Trial***

We commenced patient enrolment in our U.K. clinical trial to evaluate the anti-tumour effects of systemic administration of REOLYSIN<sup>®</sup> in combination with docetaxel (Taxotere<sup>®</sup>) in patients with advanced cancers including bladder, prostate, lung and upper gastro-intestinal. In preclinical studies, the combination of REOLYSIN<sup>®</sup> and various taxanes including docetaxel has been shown to be synergistic against a variety of cancer cell lines. The trial has two components. The first is an open-label, dose-escalating, non-randomized study of REOLYSIN<sup>®</sup> given intravenously with docetaxel every three weeks. A standard dosage of docetaxel will be delivered with escalating dosages of REOLYSIN<sup>®</sup> intravenously. A maximum of three cohorts will be enrolled in the REOLYSIN<sup>®</sup> dose escalation portion. The second component of the trial will immediately follow and will include the enrolment of a further 12 patients at the maximum dosage of REOLYSIN<sup>®</sup> in combination with a standard dosage of docetaxel. Eligible patients include those who have been diagnosed with advanced or metastatic solid tumours such as bladder, prostate, lung or upper gastro-intestinal cancers that are refractory to standard therapy or for which no curative standard therapy exists. The primary objective of the trial is to determine the MTD, DLT, recommended dose and dosing schedule and safety profile of REOLYSIN<sup>®</sup> when administered in combination with docetaxel. Secondary objectives include the evaluation of immune response to the drug combination, the body's response to the drug combination compared to chemotherapy alone and any evidence of anti-tumour activity.

#### ***Pre-Clinical Trial and Collaborative Program***

In the third quarter of 2007, we announced that a poster presentation entitled "Reovirus Infection of Human Melanoma Cells Supports Priming of Anti-Tumour Cytotoxic T Cell Immunity" was presented by Dr. Robin Prestwich of CR-UK Clinical Centre, Leeds Institute of Molecular Medicine, University of Leeds, U.K. at the National Cancer Research Institute Cancer Conference in Birmingham, U.K.

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In this study, the investigators infected melanoma cell lines with reovirus. The reovirus-infected cell lines stimulated the maturation of dendritic cells, which in turn educated cancer-killing T cells to attack and kill the melanoma cells.

#### **Manufacturing and Process Development**

We continued to have REOLYSIN<sup>®</sup> manufactured in order to supply our current and future clinical trial program. In the third quarter of 2007, our manufacturing activity was focused on the completion of the vial filling and packaging of the production runs that were completed earlier in 2007. Also in the third quarter of 2007, we continued process development that examined the scale up of our manufacturing process increasing the batch size from our present GMP scale of 20-litres to 40-litres and then to 100-litres.

#### **Intellectual Property**

In the third quarter of 2007, two U.S. patents were issued. At the end of the third quarter of 2007, we had been issued over 150 patents including 23 U.S. and six Canadian patents as well as issuances in other jurisdictions. We also have over 180 patent applications filed in the U.S., Canada and other jurisdictions.

#### **Financial Impact**

We estimated at the beginning of 2007 that our monthly cash usage would be approximately \$1,400,000 for 2007. Our cash usage for the nine months ending September 30, 2007 was \$10,849,863 from operating activities and \$635,815 for the purchases of intellectual property and capital assets which is in line with our estimate. Our net loss for the nine month period ending September 30, 2007 was \$11,556,714.

#### **Cash Resources**

We exited the third quarter of 2007 with cash resources totaling \$28,191,464 (see *Liquidity and Capital Resources* ).

#### ***Expected REOLYSIN<sup>®</sup> Development for the Remainder of 2007***

We plan to continue to enroll patients in our seven clinical trials and expect to add an additional clinical co-therapy trial. We believe that the NCI sponsored melanoma clinical trial will receive approval to commence in 2007. We believe we will complete enrollment in our U.K. Phase Ia/Ib clinical trial by the end of 2007 and complete enrollment in our Phase II combination REOLYSIN<sup>®</sup>/radiation and chemotherapy co-therapy studies in 2008. Also, our process development activity will focus on scale up studies and the examination of a lyophilization process for REOLYSIN<sup>®</sup>. Based on our expected activity in 2007, we continue to estimate our average monthly cash usage to be \$1,400,000 per month (see *Liquidity and Capital Resources* ).

#### **Recent 2007 Progress**

On October 23, 2007, we announced receipt of a letter of approval to commence our clinical trial using intravenous administration of REOLYSIN<sup>®</sup> in combination with cyclophosphamide, a chemotherapeutic agent as well as immune modulator, in patients with advanced cancers.

The trial is an open-label, dose-escalating, non-randomized trial of REOLYSIN<sup>®</sup> given intravenously with escalating doses of cyclophosphamide. A standard dose of REOLYSIN<sup>®</sup> is administered intravenously over five consecutive days, while an intravenous dose of cyclophosphamide is administered three days before REOLYSIN<sup>®</sup> treatment and continues through the course of the treatment cycle. The total number of patients studied will depend on the number of dose levels tested, but it is anticipated to be approximately 30 patients.

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Eligible patients include those who have been diagnosed with advanced or metastatic solid tumours including pancreatic, lung and ovarian cancers that are refractory to standard therapy or for which no curative standard therapy exists. The primary objectives of the trial include determining the Minimum Effective Immunomodulatory Dose of cyclophosphamide to obtain successful immune modulation. Secondary objectives include the safety profile of the combination and gathering any evidence of anti-tumour activity.

### **THIRD QUARTER RESULTS OF OPERATIONS**

*(for the three months ended September 30, 2007 and 2006)*

Net loss for the three month period ending September 30, 2007 was \$3,763,901 compared to \$3,425,169 for the three month period ending September 30, 2006.

#### **Research and Development Expenses ( R&D )**

|  | <b>2007</b>      | <b>2006</b> |
|--|------------------|-------------|
|  | \$               | \$          |
| Manufacturing and related process development expenses | <b>879,937</b>   | 1,259,716   |
| Clinical trial expenses                                | <b>1,278,175</b> | 688,435     |
| Pre-clinical trial and research collaboration expenses | <b>293,785</b>   | 301,165     |
| Other R&D expenses                                     | <b>438,747</b>   | 456,430     |
| Research and development expenses                      | <b>2,890,644</b> | 2,705,746   |

For the third quarter of 2007, R&D increased to \$2,890,644 compared to \$2,705,746 for the third quarter of 2006. The increase in R&D was due to the following:

#### **Manufacturing & Related Process Development ( M&P )**

|  | <b>2007</b>    | <b>2006</b> |
|--|----------------|-------------|
|  | \$             | \$          |
| Product manufacturing expenses                         | <b>610,842</b> | 896,776     |
| Technology transfer expenses                           |                | 184,761     |
| Process development expenses                           | <b>269,095</b> | 178,179     |
| Manufacturing and related process development expenses | <b>879,937</b> | 1,259,716   |

During the third quarter of 2007, our M&P expenses decreased to \$879,937 compared to \$1,259,716 for the third quarter of 2006. In the third quarter of 2007, we continued to fill, test, and package the REOLYSIN<sup>®</sup> that was produced earlier in the year. During the third quarter of 2006, we commenced a number of cGMP production runs using our improved manufacturing process. The technology transfer of our improved process was successfully completed at the beginning of the third quarter of 2006.

Our process development studies in the third quarter of 2007 focused on increasing the scale of our production runs from batch sizes of 20 litres to 40 and then 100 litres. In the third quarter of 2006, we completed process development studies that were successful in improving virus yields.

#### **Clinical Trial Program**

|                                | <b>2007</b>      | <b>2006</b> |
|--------------------------------|------------------|-------------|
|                                | \$               | \$          |
| Direct clinical trial expenses | <b>1,201,557</b> | 639,719     |
| Other clinical trial expenses  | <b>76,618</b>    | 48,716      |

|                         |                  |         |
|-------------------------|------------------|---------|
| Clinical trial expenses | <b>1,278,175</b> | 688,435 |
|-------------------------|------------------|---------|

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During the third quarter of 2007, our direct clinical trial expenses increased to \$1,201,557 compared to \$639,719 for the third quarter of 2006. In the third quarter of 2007, we incurred direct clinical trial expenses in our seven actively enrolling trials compared to only four enrolling trials in the third quarter of 2006.

**Pre-Clinical Trial Expenses and Research Collaborations**

|   | <b>2007</b>    | <b>2006</b> |
|---|----------------|-------------|
|   | \$             | \$          |
| Research collaboration expenses                         | <b>293,785</b> | 252,460     |
| Pre-clinical trial expenses                             |                | 48,705      |
| Pre-clinical trial expenses and research collaborations | <b>293,785</b> | 301,165     |

During the third quarter of 2007, our research collaboration expenses were \$293,785 compared to \$252,460 for the third quarter of 2006. Our research collaboration activity continues to focus on the interaction of the immune system and the reovirus, the use of the reovirus as a co-therapy with existing chemotherapeutics, and to investigate new uses of the reovirus as a therapeutic.

**Other Research and Development Expenses**

|   | <b>2007</b>    | <b>2006</b> |
|---|----------------|-------------|
|   | \$             | \$          |
| R&D consulting fees                     | <b>38,152</b>  | 70,323      |
| R&D salaries and benefits               | <b>342,155</b> | 299,224     |
| Other R&D expenses                      | <b>58,440</b>  | 86,883      |
| Other research and development expenses | <b>438,747</b> | 456,430     |

Our R&D salaries and benefits costs were \$342,155 in the third quarter of 2007 compared to \$299,224 in the third quarter of 2006. The increase is a result of increases in salary and staff levels along with the addition of our Vice President of Intellectual Property in 2007.

**Operating Expenses**

|                                 | <b>2007</b>    | <b>2006</b> |
|---------------------------------|----------------|-------------|
|                                 | \$             | \$          |
| Public company related expenses | <b>635,076</b> | 507,828     |
| Office expenses                 | <b>245,082</b> | 258,790     |
| Operating expenses              | <b>880,158</b> | 766,618     |

During the third quarter of 2007, our public company related expenses were \$635,076 compared to \$507,828 for the third quarter of 2006. In the third quarter of 2007, we increased our professional fees and investor relations activity in the United States and Europe compared to the third quarter of 2006.

**Stock Based Compensation**

| <b>2007</b> | <b>2006</b> |
|-------------|-------------|
| \$          | \$          |

|                          |               |        |
|--------------------------|---------------|--------|
| Stock based compensation | <b>38,909</b> | 34,671 |
|--------------------------|---------------|--------|

Stock based compensation for the third quarter of 2007 was \$38,909 compared to \$34,671 for the third quarter of 2006. In the third quarters of 2007 and 2006, we incurred stock based compensation associated with the vesting of previously granted options.

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**YEAR TO DATE RESULTS OF OPERATIONS***(for the nine months ended September 30, 2007 and 2006)*

Net loss for the nine month period ending September 30, 2007 was \$11,556,714 compared to \$9,407,419 for the nine month period ending September 30, 2006.

**Research and Development Expenses ( R&D )**

|  | <b>2007</b>      | <b>2006</b> |
|--|------------------|-------------|
|  | \$               | \$          |
| Manufacturing and related process development expenses | <b>3,546,732</b> | 2,751,207   |
| Clinical trial expenses                                | <b>2,983,688</b> | 1,920,467   |
| Pre-clinical trial and research collaboration expenses | <b>731,445</b>   | 691,553     |
| Other R&D expenses                                     | <b>1,553,390</b> | 1,219,460   |
| Research and development expenses                      | <b>8,815,255</b> | 6,582,687   |

For the nine month period ending September 30, 2007, R&D increased to \$8,815,255 compared to \$6,582,687 for 2006. The increase in R&D was due to the following:

**Manufacturing & Related Process Development ( M&P )**

|  | <b>2007</b>      | <b>2006</b> |
|--|------------------|-------------|
|  | \$               | \$          |
| Product manufacturing expenses                         | <b>3,134,143</b> | 1,664,308   |
| Technology transfer expenses                           |                  | 457,975     |
| Process development expenses                           | <b>412,589</b>   | 628,924     |
| Manufacturing and related process development expenses | <b>3,546,732</b> | 2,751,207   |

Our M&P expenses for the nine month period ending September 30, 2007 increased to \$3,546,732 compared to \$2,751,207 in 2006. For the nine month period ending September 30, 2007, our production and vial filling activity increased compared to 2006. During this period of 2007, we completed production runs that commenced in 2006 and initiated additional production runs to manufacture REOLYSIN® at the beginning of 2007. Also, as a result of the increased viral yields from the process development activity in 2006, we have incurred additional vial filling and packaging costs compared to 2006.

For the nine month period ending September 30, 2006, we completed the production runs that were ongoing at the end of 2005 for our Phase I trials. At the same time, our process development activity helped improve the virus yields from our manufacturing process. These improvements were then transferred to our cGMP manufacturer with additional production runs initiated in the third quarter of 2006.

Our process development expenses for the nine month period ending September 30, 2007 were \$412,589 compared to \$628,924 for the nine month period ending September 30, 2006. During this period of 2007, our main process development focus has been on the scale up of our production process, which has included scale up studies at 40 and 100 litres. During the nine month period ending September 30, 2006, our process development activity included viral yield and scale up studies along with the validation of our fill process.

We still expect that our overall manufacturing and related process development expenses for 2007 will be in line with 2006. In the fourth quarter of 2007, we plan to initiate a 40-litre technology transfer, complete our 100-litre scale up studies and investigate the lyophilization of REOLYSIN®. We are also examining ways to reduce our economic dependence resulting from having only a single cGMP manufacturer. This might include building up a level of inventory, increasing the scale of each production run, engaging another cGMP manufacturer or manufacturing



REOLYSIN® ourselves. Depending on how we mitigate our risk of economic dependence our expectation of our 2007 M&P expenses may change.

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**Clinical Trial Program**

|                                | <b>2007</b>      | <b>2006</b> |
|--------------------------------|------------------|-------------|
|                                | <b>\$</b>        | <b>\$</b>   |
| Direct clinical trial expenses | <b>2,798,024</b> | 1,783,138   |
| Other clinical trial expenses  | <b>185,664</b>   | 137,329     |
| Clinical trial expenses        | <b>2,983,688</b> | 1,920,467   |

During the nine month period ending September 30, 2007, our direct clinical trial expenses were \$2,798,024 compared to \$1,783,138 for the nine month period ending September 30, 2006. In this period of 2007, we incurred direct patient costs in our seven ongoing clinical trials. As well, we incurred clinical site start up costs for our three co-therapy trials in the U.K. and our Phase II sarcoma clinical trial in the U.S. During the nine month period ending September 30, 2006, we incurred direct patient costs in four ongoing clinical trials along with clinical site start up costs associated with our U.S. recurrent malignant glioma and U.K. Phase Ia combination REOLYSIN® /radiation therapy trials.

We expect our clinical trial expenses will continue to increase for the remainder of 2007 compared to 2006 as we continue patient enrollment and expand our clinical trial program to include other trial sites and other studies.

**Pre-Clinical Trial Expenses and Research Collaborations**

|   | <b>2007</b>    | <b>2006</b> |
|---|----------------|-------------|
|   | <b>\$</b>      | <b>\$</b>   |
| Research collaboration expenses                         | <b>694,315</b> | 634,199     |
| Pre-clinical trial expenses                             | <b>37,130</b>  | 57,354      |
| Pre-clinical trial expenses and research collaborations | <b>731,445</b> | 691,553     |

During the nine month period ending September 30, 2007, our research collaboration expenses were \$694,315 compared to \$634,199 for the nine month period ending September 30, 2006. Our research collaboration activity continues to focus on the interaction of the immune system and the reovirus, the use of the reovirus as a co-therapy with existing chemotherapeutics, the use of new RAS active viruses as potential therapeutics, and to investigate new uses of the reovirus as a therapeutic.

For the remainder of 2007, we still expect that pre-clinical trial expenses and research collaborations will decline compared to 2006. We expect to continue with our various collaborations in order to provide support for our expanding clinical trial program. As well, we may expand our collaborative activities to include other viruses.

**Other Research and Development Expenses**

|  | <b>2007</b>      | <b>2006</b> |
|--|------------------|-------------|
|  | \$               | \$          |
| R&D consulting fees  | <b>180,043</b>   | 134,650     |
| R&D salaries and benefits                                      | <b>1,109,709</b> | 907,115     |
| Quebec scientific research and experimental development refund | <b>(15,927)</b>  | (52,344)    |
| Other R&D expenses   | <b>279,565</b>   | 230,039     |
| Other research and development expenses                        | <b>1,553,390</b> | 1,219,460   |

During the nine month period ending September 30, 2007, our R&D consulting fees were \$180,043 compared to \$134,650 for the nine month period ending September 30, 2006. During this period of 2007, we incurred consulting activity associated with our ongoing clinical trials and assistance with our clinical trial applications. During this period of 2006, our consulting activity related to our ongoing clinical trials.

Our R&D salaries and benefits costs were \$1,109,709 for the nine month period ending September 30, 2007 compared to \$907,115 for the nine month period ending September 30, 2006. The increase is a result of increases in salary and staff levels along with the addition of our Vice President of Intellectual Property in 2007.

We still expect that our Other Research and Development expenses for the remainder of 2007 will increase compared to 2006. We expect that salaries and benefits will increase to reflect increased compensation levels and the salary and benefit costs for our Vice President of Intellectual Property. Our R&D consulting fees are expected to remain consistent with 2006. However, we may choose to engage additional consultants to assist us in the development of protocols and regulatory filings for our additional combination therapy and phase II clinical trial studies, possibly causing our R&D consulting expenses to increase.

**Operating Expenses**

|                                 | <b>2007</b>      | <b>2006</b> |
|---------------------------------|------------------|-------------|
|                                 | \$               | \$          |
| Public company related expenses | <b>1,970,903</b> | 2,007,464   |
| Office expenses                 | <b>827,727</b>   | 782,183     |
| Operating expenses              | <b>2,798,630</b> | 2,789,647   |

During the nine month period ending September 30, 2007, our public company related expenses were \$1,970,903 compared to \$2,007,464 for the nine month period ending September 30, 2006. In this period of 2007, our financial advisory expenses decreased compared to 2006. This decrease was offset by an increase in expenses associated with our investor relations activity in the U.S. and Europe and professional fees during the nine month period ending September 30, 2007 compared to 2006.

During the nine month period ending September 30, 2007, our office expenses were \$827,727 compared to \$782,183 for the nine month period ending September 30, 2006. Our office expense activity has remained consistent in 2007 to date compared to 2006 with increases mainly due to increased compensation levels and a general increase in office costs.

**Stock Based Compensation**

| <b>2007</b> | <b>2006</b> |
|-------------|-------------|
| \$          | \$          |

|                          |                |         |
|--------------------------|----------------|---------|
| Stock based compensation | <b>142,878</b> | 293,880 |
|--------------------------|----------------|---------|

Stock based compensation for the nine month period ending September 30, 2007 was \$142,878 compared to \$293,880 for the nine month period ending September 30, 2006. During this period of 2007, we incurred

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stock based compensation associated with the vesting of options previously granted. In 2006, we incurred stock based compensation associated with the issue and immediate vesting of stock options to our two newly appointed directors and the vesting of previously granted options.

### Commitments

As at September 30, 2007, we are committed to payments totaling \$1,162,000 for the remainder of 2007 for activities related to clinical trial activity and collaborations. All of these committed payments are considered to be part of our normal course of business.

### SUMMARY OF QUARTERLY RESULTS

The following unaudited quarterly information is presented in thousands of dollars except for per share amounts:

|  | 2007    |         |         |         | 2006    |         |         | 2005    |
|--|---------|---------|---------|---------|---------|---------|---------|---------|
|  | Sept.   | June    | March   | Dec.    | Sept.   | June    | March   | Dec.    |
| <b>Revenue</b>   |         |         |         |         |         |         |         |         |
| <b>Interest income</b>                                       | 319     | 359     | 268     | 286     | 320     | 335     | 292     | 160     |
| <b>Net loss<sup>(3)</sup></b>                                | 3,764   | 3,680   | 4,156   | 4,890   | 3,425   | 2,988   | 2,995   | 3,941   |
| <b>Basic and diluted loss per common share<sup>(3)</sup></b> | \$ 0.09 | \$ 0.09 | \$ 0.11 | \$ 0.13 | \$ 0.09 | \$ 0.08 | \$ 0.08 | \$ 0.12 |
| <b>Total assets<sup>(1), (4)</sup></b>                       | 33,897  | 37,670  | 41,775  | 33,566  | 37,980  | 40,828  | 43,660  | 46,294  |
| <b>Total cash<sup>(2), (4)</sup></b>                         | 28,191  | 31,533  | 35,681  | 27,614  | 31,495  | 34,501  | 37,687  | 40,406  |
| <b>Total long-term debt<sup>(5)</sup></b>                    |         |         |         | 150     | 150     | 150     | 150     | 150     |
| <b>Cash dividends declared<sup>(6)</sup></b>                 | Nil     | Nil     | Nil     | Nil     | Nil     | Nil     | Nil     | Nil     |

(1) Subsequent to the acquisition of Oncolytics Biotech Inc. by SYNSORB in April 1999, we applied push down accounting. See note 2 to the audited financial statements for 2006.

(2) Included in total cash are cash and cash equivalents plus short-term investments.

(3) Included in net loss and loss per common share

between  
September 2007  
and  
October 2005  
are quarterly  
stock based  
compensation  
expenses of  
\$38,909,  
\$82,573,  
\$21,396,  
\$109,670,  
\$34,671,  
\$222,376,  
\$36,833, and  
\$38,152,  
respectively.

(4) We issued  
4,600,000  
common shares  
for net cash  
proceeds of  
\$12,063,394  
during 2007  
(2006 284,000  
common shares  
for cash  
proceeds of  
\$241,400; 2005  
4,321,252  
common shares  
for cash  
proceeds of  
\$18,789,596).

(5) The long-term  
debt recorded  
represents  
repayable loans  
from the Alberta  
Heritage  
Foundation. On  
January 1, 2007,  
in conjunction  
with the  
adoption of the  
CICA Handbook  
section 3855  
Financial  
Instruments , this

loan was recorded at fair value (see note 1 of the September 30, 2007 interim financial statements).

- (6) We have not declared or paid any dividends since incorporation.

#### **LIQUIDITY AND CAPITAL RESOURCES**

As at September 30, 2007, we had cash and cash equivalents (including short-term investments) and working capital positions of \$28,191,464 and \$26,343,848, respectively compared to \$27,613,748 and \$25,719,870, respectively for December 31, 2006. The increase in 2007 reflects the cash inflow from financing activities of \$12,063,394 offset by cash usage from operating activities and additions to our intellectual property of \$10,849,863 and \$586,124, respectively.

We desire to maintain adequate cash and short-term investment reserves to support our planned activities which include our clinical trial program, product manufacturing, administrative costs, and our intellectual property expansion and protection. For the remainder of 2007, we are expecting to continue to enroll patients in our existing trials and we also expect to expand our clinical trial program. As well, we expect to continue with our collaborative studies pursuing support for our future clinical trial program. We will therefore need to ensure that we have enough REOLYSIN® to supply our clinical trial and collaborative

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programs. We continue to expect our cash usage in 2007 to be \$1,400,000 per month and we believe our existing capital resources are adequate to fund our current plans for research and development activities well into 2009. Factors that will affect our anticipated monthly burn rate include, but are not limited to, the number of manufacturing runs required to supply our clinical trial program and the cost of each run, additional activities reducing our economic dependence on a single supplier, the number of clinical trials ultimately approved, the timing of patient enrollment in the approved clinical trials, the actual costs incurred to support each clinical trial, the number of treatments each patient will receive, the timing of the NCI's R&D activity, and the level of pre-clinical activity undertaken. In the event that we choose to seek additional capital, we will look to fund additional capital requirements primarily through the issue of additional equity. We recognize the challenges and uncertainty inherent in the capital markets and the potential difficulties we might face in raising additional capital. Market prices and market demand for securities in biotechnology companies are volatile and there are no assurances that we will have the ability to raise funds when required.

#### **Capital Expenditures**

We spent \$586,124 on intellectual property during the nine month period ending September 30, 2007 compared to \$552,319 during the nine month period ending September 30, 2006. The change in intellectual property expenditures reflects the timing of filing costs associated with our expanded patent base. As well, we have benefited from a stronger Canadian dollar as our patent costs are typically incurred in U.S. currency. In the third quarter of 2007, two U.S. patents were issued bringing our total patents issued to 23 in the U.S. and six in Canada.

#### **Investing Activities**

Under our Investment Policy, we are permitted to invest in short-term instruments with a rating no less than R-1 (DBRS) with terms less than two years. We have \$24,865,090 invested under this policy and we are currently earning interest at an effective rate of 4.23% (2006 3.89%).

#### **OTHER MD&A REQUIREMENTS**

We have 41,120,748 common shares outstanding at October 29, 2007. If all of our warrants (4,972,000) and options (3,497,950) were exercised we would have 49,590,698 common shares outstanding.

Additional information relating to Oncolytics Biotech Inc. is available on SEDAR at [www.sedar.com](http://www.sedar.com).

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**FINANCIAL STATEMENTS**

**Oncolytics Biotech Inc.**

September 30, 2007

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**Oncolytics Biotech Inc.**  
**BALANCE SHEETS**  
*(unaudited)*

As at,

|  | <b>September<br/>30, 2007</b> | <b>December 31,<br/>2006</b> |
|--|-------------------------------|------------------------------|
|  | \$                            | \$                           |
| <b>ASSETS</b>  |                               |                              |
| <b>Current</b>   |                               |                              |
| Cash and cash equivalents                                      | 3,326,374                     | 3,491,511                    |
| Short-term investments <i>[note 7]</i>                         | 24,865,090                    | 24,122,237                   |
| Accounts receivable  | 36,637                        | 84,003                       |
| Prepaid expenses   | 413,811                       | 638,540                      |
|  | <b>28,641,912</b>             | 28,336,291                   |
| <b>Property and equipment</b>                                  | <b>169,226</b>                | 149,596                      |
| <b>Intellectual property</b>                                   | <b>5,085,755</b>              | 5,079,805                    |
|  | <b>33,896,893</b>             | 33,565,692                   |
| <b>LIABILITIES AND SHAREHOLDERS EQUITY</b>                     |                               |                              |
| <b>Current</b>   |                               |                              |
| Accounts payable and accrued liabilities                       | 2,298,064                     | 2,616,421                    |
| <b>Alberta Heritage Foundation loan <i>[notes 1 and 8]</i></b> |                               | 150,000                      |
| <b>Shareholders equity</b>                                     |                               |                              |
| Share capital <i>[note 2]</i>                                  |                               |                              |
| Authorized: unlimited number of common shares                  |                               |                              |
| Issued: 41,120,748 (December 31, 2006 36,520,748)              | 92,708,665                    | 83,083,271                   |
| Warrants <i>[note 2]</i>                                       | 6,654,740                     | 4,216,740                    |
| Contributed surplus <i>[note 4]</i>                            | 8,672,204                     | 8,529,326                    |
| Deficit <i>[notes 1 and 5]</i>                                 | (76,436,780)                  | (65,030,066)                 |
|  | <b>31,598,829</b>             | 30,799,271                   |
|  | <b>33,896,893</b>             | 33,565,692                   |

See accompanying notes

**Oncolytics Biotech Inc.**  
**STATEMENTS OF LOSS AND COMPREHENSIVE LOSS**  
*(unaudited)*

|   | <b>Nine Month<br/>Period<br/>Ending<br/>September<br/>30, 2007</b> | <b>Nine Month<br/>Period<br/>Ending<br/>September<br/>30, 2006</b> | <b>Three Month<br/>Period<br/>Ending<br/>September<br/>30, 2007</b> | <b>Three Month<br/>Period<br/>Ending<br/>September<br/>30, 2006</b> | <b>Cumulative<br/>from<br/>inception<br/>on April 2,<br/>1998 to<br/>September 30,<br/>2007</b> |
|---|--|--|---|---|---|
|   | \$   | \$   | \$  | \$  | \$  |
| <b>Revenue</b>  |  |  |   |   |   |
| Rights revenue  |  |  |   |   | 310,000   |
|   |  |  |   |   | 310,000   |
| <b>Expenses</b>   |  |  |   |   |   |
| Research and development                                | <b>8,815,255</b>   | 6,582,687  | <b>2,890,644</b>  | 2,705,746   | 52,036,449  |
| Operating   | <b>2,798,630</b>   | 2,789,647  | <b>880,158</b>  | 766,618   | 19,569,211  |
| Stock-based compensation<br>[note 3]                    | <b>142,878</b>   | 293,880  | <b>38,909</b>   | 34,671  | 4,308,527   |
| Foreign exchange loss/(gain)                            | <b>2,829</b>   | (2,703)  | <b>18,917</b>   | 5,129   | 651,677   |
| Amortization intellectual<br>property                   | <b>713,887</b>   | 647,893  | <b>244,299</b>  | 220,774   | 4,750,721   |
| Amortization property and<br>equipment                  | <b>30,061</b>  | 43,379   | <b>10,197</b>   | 12,685  | 437,744   |
|   | <b>12,503,540</b>  | 10,354,783   | <b>4,083,124</b>  | 3,745,623   | 81,754,329  |
| <b>Loss before the following:</b>                       | <b>12,503,540</b>  | 10,354,783   | <b>4,083,124</b>  | 3,745,623   | 81,444,329  |
| <b>Interest income</b>                                  | <b>(946,826)</b>   | (947,364)  | <b>(319,223)</b>  | (320,454)   | (5,749,831)   |
| <b>Gain on sale of BCY<br/>LifeSciences Inc.</b>        |  |  |   |   | (299,403)   |
| <b>Loss on sale of Transition<br/>Therapeutics Inc.</b> |  |  |   |   | 2,156,685   |
| <b>Loss before taxes</b>                                | <b>11,556,714</b>  | 9,407,419  | <b>3,763,901</b>  | 3,425,169   | 77,551,780  |
| <b>Future income tax recovery</b>                       |  |  |   |   | (1,115,000)   |

|  |                   |            |                   |            |            |
|--|-------------------|------------|-------------------|------------|------------|
| <b>Net loss and comprehensive loss for the period</b>        | <b>11,556,714</b> | 9,407,419  | <b>3,763,901</b>  | 3,425,169  | 76,436,780 |
| <b>Basic and diluted loss per share</b>                      | <b>0.29</b>       | 0.26       | <b>0.09</b>       | 0.09       |            |
| <b>Weighted average number of shares (basic and diluted)</b> | <b>40,181,777</b> | 36,317,687 | <b>41,120,748</b> | 36,368,270 |            |

*See accompanying notes*

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**Oncolytics Biotech Inc.**  
**STATEMENTS OF CASH FLOWS**  
*(unaudited)*

|   | Nine Month<br>Period Ending<br>September 30,<br>2007<br>\$ | Nine Month<br>Period<br>Ending<br>September 30,<br>2006<br>\$ | Three Month<br>Period<br>Ending<br>September<br>30, 2007<br>\$ | Three Month<br>Period<br>Ending<br>September<br>30, 2006<br>\$ | Cumulative<br>from inception<br>on April 2,<br>1998 to<br>September 30,<br>2007<br>\$ |
|---|--|---|--|--|---|
| <b>OPERATING ACTIVITIES</b>                             |  |   |  |  |   |
| Net loss for the period                                 | (11,556,714)   | (9,407,419)   | (3,763,901)  | (3,425,169)  | (76,436,780)  |
| Add/(deduct) non-cash items                             |  |   |  |  |   |
| Amortization intellectual property                      | 713,887  | 647,893   | 244,299  | 220,774  | 4,750,721   |
| Amortization property and equipment                     | 30,061   | 43,379  | 10,197   | 12,685   | 437,744   |
| Stock-based compensation                                | 142,878  | 293,880   | 38,909   | 34,671   | 4,308,527   |
| Other non-cash items <i>[note 6]</i>                    |  |   |  |  | 1,383,537   |
| Net changes in non-cash working capital <i>[note 6]</i> | (179,975)  | (34,485)  | 239,121  | 261,875  | 1,724,946   |
|   | <b>(10,849,863)</b>  | <b>(8,456,752)</b>  | <b>(3,231,375)</b>   | <b>(2,895,164)</b>   | <b>(63,831,305)</b>   |
| <b>INVESTING ACTIVITIES</b>                             |  |   |  |  |   |
| Intellectual property                                   | (586,124)  | (552,319)   | (99,066)   | (187,283)  | (6,085,404)   |
| Property and equipment                                  | (49,691)   | (29,342)  | (11,386)   | (8,294)  | (673,039)   |
| Purchase of short-term investments                      | (742,853)  | (801,358)   | (255,688)  | (261,480)  | (48,862,320)  |
| Redemption of short-term investments                    |  | 10,158,000  |  |  | 23,578,746  |
| Investment in BCY LifeSciences Inc.                     |  |   |  |  | 464,602   |
| Investment in Transition Therapeutics Inc.              |  |   |  |  | 2,532,343   |
|   | <b>(1,378,668)</b>   | <b>8,774,981</b>  | <b>(366,140)</b>   | <b>(457,057)</b>   | <b>(29,045,072)</b>   |
| <b>FINANCING ACTIVITIES</b>                             |  |   |  |  |   |
| Proceeds from exercise of warrants and stock options    |  | 127,500   |  | 85,000   | 15,208,468  |

|   |                   |           |                    |             |            |
|---|-------------------|-----------|--------------------|-------------|------------|
| Proceeds from private placements  |                   |           |                    |             | 38,137,385 |
| Proceeds from public offerings [note 2]                                   | <b>12,063,394</b> |           |                    |             | 42,856,898 |
|   | <b>12,063,394</b> | 127,500   |                    | 85,000      | 96,202,751 |
| <b>Increase (decrease) in cash and cash equivalents during the period</b> | <b>(165,137)</b>  | 445,729   | <b>(3,597,515)</b> | (3,267,221) | 3,326,374  |
| <b>Cash and cash equivalents, beginning of the period</b>                 | <b>3,491,511</b>  | 3,511,357 | <b>6,923,889</b>   | 7,224,307   |            |
| <b>Cash and cash equivalents, end of the period</b>                       | <b>3,326,374</b>  | 3,957,086 | <b>3,326,374</b>   | 3,957,086   | 3,326,374  |

*See accompanying notes*

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**Oncolytics Biotech Inc.**  
**NOTES TO FINANCIAL STATEMENTS**

September 30, 2007 *(unaudited)*

**1. ACCOUNTING POLICIES**

These unaudited interim financial statements have been prepared in accordance with Canadian generally accepted accounting principles. The notes presented in these unaudited interim financial statements include only significant events and transactions occurring since the Company's last fiscal year end and are not fully inclusive of all matters required to be disclosed in the Company's annual audited financial statements. Accordingly, these unaudited interim financial statements should be read in conjunction with the Company's most recent annual financial statements. The information as at and for the year ended December 31, 2006 has been derived from the Company's audited financial statements.

The accounting policies used in the preparation of these unaudited interim financial statements conform with those used in the Company's most recent annual financial statements except for the following:

**Adoption of New Accounting Policies**

***Financial Instruments***

On January 1, 2007, the Company prospectively adopted, without restatement, CICA Handbook Section 3855 *Financial Instruments - Recognition and Measurement* and Section 1530 *Other Comprehensive Income*. Pursuant to the transitional provisions of Section 3855, the Company classified its short-term investments as held-to-maturity fixed income securities and recorded its Alberta Heritage Foundation interest free loan at fair value. As a result, there were no adjustments made to short-term investments or other comprehensive income and there was a decrease in the Alberta Heritage Foundation loan of \$150,000 with a corresponding decrease of \$150,000 in the Company's deficit.

***Financial Assets***

Financial assets are comprised of cash and cash equivalents, accounts receivable (mainly goods and service tax receivable), and short-term investments.

***Cash and cash equivalents***

Cash and cash equivalents consist of cash on hand and interest bearing deposits with the Company's bank.

***Short-term investments***

The Company determines the appropriate classification of its short-term investments at the time of purchase and reevaluates such designation as of each balance sheet date. Short-term investments can be classified as held-for-trading, available-for-sale or held-to-maturity. Currently, the Company has classified all of its short-term investments as held-to-maturity as it has the positive intent and ability to hold the securities to maturity. Held-to-maturity securities are stated at original cost, adjusted for amortization of premiums and accretion of discounts to maturity computed under the effective interest rate method. Such amortization and interest on securities classified as held-to-maturity are included in interest income.

***Financial Liabilities***

Financial liabilities are comprised of trade accounts payable and accrued liabilities.

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**Oncolytics Biotech Inc.**  
**NOTES TO FINANCIAL STATEMENTS**

September 30, 2007 *(unaudited)***2. SHARE CAPITAL****Authorized:**

Unlimited number of common shares

| <b>Issued:</b>  | <b>Shares</b>     | <b>Amount</b>     | <b>Warrants</b>  | <b>Amount</b>    |
|---|-------------------|-------------------|------------------|------------------|
|   | <b>Number</b>     | <b>\$</b>         | <b>Number</b>    | <b>\$</b>        |
| Balance, December 31, 2005  | 36,236,748        | 82,841,871        | 2,784,800        | 4,429,932        |
| Exercise of options   | 284,000           | 241,400           |                  |                  |
| Expired warrants  |                   |                   | (112,800)        | (213,192)        |
| Balance, December 31, 2006  | 36,520,748        | 83,083,271        | 2,672,000        | 4,216,740        |
| Issued for cash pursuant to February 22,<br>2007 public offering <sup>(a)</sup> | 4,600,000         | 11,362,000        | 2,300,000        | 2,438,000        |
| Share issue costs   |                   | (1,736,606)       |                  |                  |
| <b>Balance, September 30, 2007</b>  | <b>41,120,748</b> | <b>92,708,665</b> | <b>4,972,000</b> | <b>6,654,740</b> |

(a) Pursuant to a public offering, 4,600,000 units were issued at an issue price of \$3.00 per unit for gross proceeds of \$13,800,000. Each unit included one common share (ascribed value of \$2.47) and one-half of one common share purchase warrant (ascribed value of \$0.53) for a



total of  
2,300,000  
warrants. The  
ascribed value  
was determined  
using the  
relative fair  
value method.  
Each whole  
common share  
purchase  
warrant entitles  
the holder to  
acquire one  
common share  
in the capital of  
the Company  
upon payment  
of \$3.50 per  
share until  
February 22,  
2010. Share  
issue costs for  
this offering  
were  
\$1,736,606.

The following table summarizes the weighted average assumptions used in the Black-Scholes Model with respect to the valuation of warrants:

|                                  | <b>2007</b>    |
|----------------------------------|----------------|
| Risk-free interest rate          | <b>4.08 %</b>  |
| Expected hold period to exercise | <b>3 years</b> |
| Volatility                       | <b>62.8 %</b>  |
| Dividend yield                   |                |

There were no warrants issued during the nine month period ending September 30, 2006.

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**Oncolytics Biotech Inc.**  
**NOTES TO FINANCIAL STATEMENTS**

September 30, 2007 *(unaudited)*

The following table summarizes the Company's outstanding warrants as at September 30, 2007:

| <b>Exercise Price</b> | <b>Outstanding, Beginning of the Period</b> | <b>Granted During the Period</b> | <b>Exercised During the Period</b> | <b>Expired During the Period</b> | <b>Outstanding, End of Period</b> | <b>Weighted Average Remaining Contractual Life (years)</b> |
|-----------------------|---|----------------------------------|------------------------------------|----------------------------------|-----------------------------------|--|
| \$3.50                |   | 2,300,000                        |                                    |                                  | 2,300,000                         | 2.40   |
| \$5.65                | 320,000                                     |                                  |                                    |                                  | 320,000                           | 1.25   |
| \$6.15                | 1,600,000                                   |                                  |                                    |                                  | 1,600,000                         | 1.25   |
| \$8.00                | 752,000                                     |                                  |                                    |                                  | 752,000                           | 0.15   |
|                       | 2,672,000                                   | 2,300,000                        |                                    |                                  | 4,972,000                         | 1.62   |

**3. STOCK BASED COMPENSATION****Stock Option Plan**

The Company has issued stock options to acquire common stock through its stock option plan of which the following are outstanding:

|                                   | <b>2007</b>          | <b>Weighted Average Share Price</b> | <b>2006</b>          | <b>Weighted Average Share Price</b> |
|-----------------------------------|----------------------|-------------------------------------|----------------------|-------------------------------------|
|                                   | <b>Stock Options</b> | <b>\$</b>                           | <b>Stock Options</b> | <b>\$</b>                           |
| Outstanding, January 1            | <b>3,537,950</b>     | <b>4.88</b>                         | 3,634,550            | 4.66                                |
| Granted during period             | <b>100,000</b>       | <b>3.28</b>                         | 100,000              | 3.85                                |
| Exercised during period           |                      |                                     | (150,000)            | 0.85                                |
| Cancelled                         | <b>(140,000)</b>     | <b>2.90</b>                         |                      |                                     |
| Outstanding, September 30         | <b>3,497,950</b>     | <b>4.84</b>                         | 3,584,550            | 4.79                                |
| Options exercisable, September 30 | <b>3,290,450</b>     | <b>4.94</b>                         | 3,352,050            | 4.91                                |

**Oncolytics Biotech Inc.**  
**NOTES TO FINANCIAL STATEMENTS**

September 30, 2007 *(unaudited)*

The following table summarizes information about the stock options outstanding and exercisable at September 30, 2007:

| Range of Exercise<br>Prices | Number<br>Outstanding | Weighted<br>Average<br>Remaining<br>Contractual<br>Life (years) | Weighted<br>Average<br>Exercise<br>Price<br>\$ | Number<br>Exercisable | Weighted<br>Average<br>Exercise<br>Price<br>\$ |
|-----------------------------|-----------------------|---|--|-----------------------|--|
| \$0.75 - \$1.00             | 318,550               | 2.1   | 0.85   | 318,550               | 0.85   |
| \$1.65 - \$2.37             | 358,400               | 6.1   | 1.95   | 338,400               | 1.95   |
| \$2.70 - \$3.50             | 800,250               | 6.7   | 3.15   | 625,250               | 3.13   |
| \$4.00 - \$5.00             | 1,208,250             | 7.0   | 4.86   | 1,195,750             | 4.86   |
| \$6.77 - \$9.76             | 684,500               | 4.4   | 8.66   | 684,500               | 8.66   |
| \$12.15 - \$13.50           | 128,000               | 3.1   | 12.63  | 128,000               | 12.63  |
|                             | 3,497,950             | 5.7   | 4.84   | 3,290,450             | 4.94   |

Options granted vest immediately or annually over one, three or four years at the discretion of the Board. The outstanding options vest annually or after the completion of certain milestones. The Company has reserved 4,052,075 common shares for issuance relating to outstanding stock options.

As the Company is following the fair value based method of accounting for stock options, the Company recorded compensation expense of \$38,909 and \$142,878 for the three and nine month periods ending September 30, 2007, respectively (September 30, 2006 \$34,671 and \$293,880, respectively) with respect to the granting of options in the period and vesting of options issued in prior periods with an offsetting credit to contributed surplus.

The estimated fair value of stock options issued during the nine month period ending September 30, 2007 was determined using the Black-Scholes Model using the following weighted average assumptions and fair value of options:

|  | <b>2007</b>          | <b>2006</b> |
|--|----------------------|-------------|
| Risk-free interest rate                | <b>4.11%</b>         | 4.24%       |
| Expected hold period to exercise       | <b>3.5<br/>years</b> | 3.5 years   |
| Volatility                             | <b>63%</b>           | 64%         |
| Dividend yield                         |                      |             |
| Weighted average fair value of options | <b>\$1.56</b>        | \$1.86      |

**Oncolytics Biotech Inc.**  
**NOTES TO FINANCIAL STATEMENTS**

September 30, 2007 *(unaudited)***4. CONTRIBUTED SURPLUS**

|                                    | <b>Amount</b><br><b>\$</b> |
|------------------------------------|----------------------------|
| Balance, December 31, 2005         | 7,912,584                  |
| Expired warrants                   | 213,192                    |
| Stock based compensation           | 403,550                    |
| Exercise of stock options          |                            |
| Balance, December 31, 2006         | 8,529,326                  |
| Stock based compensation           | 142,878                    |
| <b>Balance, September 30, 2007</b> | <b>8,672,204</b>           |

**5. DEFICIT**

|   | <b>Amount</b><br><b>\$</b> |
|---|----------------------------|
| Balance, December 31, 2005                                  | 50,732,542                 |
| Net loss for the year                                       | 14,297,524                 |
| Balance, December 31, 2006                                  | 65,030,066                 |
| Adjustment Alberta Heritage Foundation loan <i>[note 1]</i> | (150,000)                  |
| Net loss and comprehensive loss, September 30, 2007         | 11,556,714                 |
| <b>Balance, September 30, 2007</b>                          | <b>76,436,780</b>          |

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**Oncolytics Biotech Inc.**  
**NOTES TO FINANCIAL STATEMENTS**

September 30, 2007 *(unaudited)***6. ADDITIONAL CASH FLOW DISCLOSURE****Net Change In Non-Cash Working Capital**

|   | <b>Nine<br/>Month<br/>Period<br/>Ending<br/>September<br/>30, 2007</b> | <b>Nine<br/>Month<br/>Period<br/>Ending<br/>September<br/>30, 2006</b> | <b>Three<br/>Month<br/>Period<br/>Ending<br/>September<br/>30, 2007</b> | <b>Three<br/>Month<br/>Period<br/>Ending<br/>September<br/>30, 2006</b> | <b>Cumulative<br/>from<br/>inception<br/>on April 2,<br/>1998 to<br/>September<br/>30, 2007</b> |
|---|--|--|---|---|---|
|   | \$   | \$   | \$  | \$  | \$  |
| <i>Change in:</i>                               |  |  |   |   |   |
| Accounts receivable                             | <b>47,366</b>  | 9,750  | <b>10,080</b>   | 16,507  | (36,637)  |
| Prepaid expenses                                | <b>224,729</b>   | (691,329)  | <b>384,380</b>  | (233,919)   | (413,811)   |
| Accounts payable and accrued liabilities        | <b>(318,357)</b>   | 671,927  | <b>(147,926)</b>  | 457,687   | 2,298,064   |
| Net change in non-cash working capital          | <b>(46,262)</b>  | (9,652)  | <b>246,534</b>  | 240,275   | 1,847,616   |
| Portion related to investing activities         | <b>(133,713)</b>   | (24,833)   | <b>(7,413)</b>  | 21,600  | (122,670)   |
| Net change associated with operating activities | <b>(179,975)</b>   | (34,485)   | <b>239,121</b>  | 261,875   | 1,724,946   |

| <b>Other Non-Cash Items</b>  | <b>Nine<br/>Month<br/>Period<br/>Ending<br/>September<br/>30, 2007</b> | <b>Nine<br/>Month<br/>Period<br/>Ending<br/>September<br/>30, 2006</b> | <b>Three<br/>Month<br/>Period<br/>Ending<br/>September<br/>30, 2007</b> | <b>Three<br/>Month<br/>Period<br/>Ending<br/>September<br/>30, 2006</b> | <b>Cumulative<br/>from<br/>inception on<br/>April 2,<br/>1998 to<br/>September<br/>30, 2007</b> |
|--|--|--|---|---|---|
|  | \$   | \$   | \$  | \$  | \$  |
| Foreign exchange loss  |  |  |   |   | 425,186   |
| Donation of medical equipment  |  |  |   |   | 66,069  |
| Loss on sale of Transition Therapeutics Inc.                           |  |  |   |   | 2,156,685   |
| Gain on sale of BCY LifeSciences Inc.                                  |  |  |   |   | (299,403)   |
| Cancellation of contingent payment obligation settled in common shares |  |  |   |   | 150,000   |
| Future income tax recovery   |  |  |   |   | (1,115,000)   |
|  |  |  |   |   | 1,383,537   |

**7. SHORT-TERM INVESTMENTS**

Short-term investments, consisting of Government of Canada treasury bills, are liquid investments that are readily convertible to known amounts of cash and are subject to an insignificant risk of changes in value. The objectives for holding short-term investments are to invest the Company's excess cash resources in investment vehicles that provide a better rate of return compared to the Company's interest bearing bank

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**Oncolytics Biotech Inc.**  
**NOTES TO FINANCIAL STATEMENTS**

September 30, 2007 *(unaudited)*

account with limited risk to the principal invested. The Company also intends to match the maturities of these short-term investments with the cash requirements of the Company's activities.

|                        | <b>Original<br/>Cost</b> | <b>Accrued<br/>Interest</b> | <b>Carrying<br/>Value</b> | <b>Fair<br/>Value</b> | <b>Effective<br/>Interest<br/>Rate</b> |
|------------------------|--------------------------|-----------------------------|---------------------------|-----------------------|--|
| September 30, 2007     |                          |                             |                           |                       |  |
| Short-term investments | 24,413,733               | 451,357                     | 24,865,090                | 24,868,366            | 4.23%                                  |
| December 31, 2006      |                          |                             |                           |                       |  |
| Short-term investments | 23,672,719               | 449,518                     | 24,122,237                | 24,124,810            | 3.95%                                  |

Fair value is determined by using published market prices provided by the Company's investment advisor.

**8. ALBERTA HERITAGE FOUNDATION LOAN**

The Company received an interest free loan of \$150,000 from the Alberta Heritage Foundation for Medical Research. Pursuant to the terms of the agreement, the Company is required to repay this amount in annual installments from the date of commencement of sales in an amount equal to the lesser of: (a) 5% of the gross sales generated by the Company; or (b) \$15,000 per annum until the entire loan has been paid in full.

**9. COMPARATIVE FIGURES**

Certain comparative figures have been reclassified to conform with the current period's presentation.

**Shareholder Information**

For public company filings please go to [www.sedar.com](http://www.sedar.com) or contact us at:

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**Officers**

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Chairman, President and CEO

**Doug Ball, CA**

Chief Financial Officer

**Matt Coffey, PhD**

Chief Scientific Officer

**Karl Mettinger, MD, PhD**

Chief Medical Officer

**George Gill, MD**

Senior Vice President, Clinical and Regulatory Affairs

**Mary Ann Dillahunty, JD, MBA**

Vice President, Intellectual Property

**Directors**

**Brad Thompson, PhD**

Chairman, President and CEO, Oncolytics Biotech Inc.

**Doug Ball, CA**

CFO, Oncolytics Biotech Inc.

**Ger van Amersfoort**

Biotech Consultant

**William. A. Cochrane, OC, AOE, MD, FRCP(C)**

Biotech Consultant

**Jim Dinning, BCom, MPA**

Chairman, Western Financial Group

**Ed Levy, PhD**

Adjunct Professor, University of British Columbia

**J. Mark Lievonon, CA**

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Corporate Director

**Fred A. Stewart, QC**

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