HYDROMER INC
Form 10KSB
September 29, 2006

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON D. C. 20549

FORM 10-KSB

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended June 30, 2006

Commission File Number 0-10683

HYDROMER, INC.

(Exact name of registrant as specified in its charter)

New Jersey (State of incorporation)	22-2303576 (I.R.S. Employer Identification No.)
35 Industrial Parkway, Branchburg, New Jersey (Address of principal executive offices)	08876-3424 (Zip Code)
Registrant's telephone number, including area code:	(908) 722-5000
Securities registered pursuant to Section 12 (b) of the Act:	None
Securities registered pursuant to Section 12 (g) of the Act:	
Common Stock Without Par Value (Title of class)	

Check whether the issuer (1) has filed all reports required to be filed by Section 13 or 15 (d) of the Securities Exchange Act of 1934 during the preceding 12 months
(or for such shorter period that the registrant was required to file such report(s) and (2) has been subject to such filing requirements for the past 90 days. Yes x Noo

Check if there is no disclosure of delinquent filers in response to Item 405 of Regulation S-B is not contained in this form, and no disclosure will be contained, to the best of
registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-KSB or any amendment to this Form 10-KSB x

The aggregate market value of the voting stock held by non-affiliates of the Registrant at September 1, 2006 was approximately $3,947,539.

The number of shares of Registrant's Common Stock outstanding on September 1, 2006 was 4,644,164.

Portions of the Audited Financials Statements for the year ended June 30, 2006 are incorporated by reference in Part II of this report. Portions of the Proxy Statement of
Registrant dated September 15, 2006 are incorporated by reference in Part III of this report.

PART I

Item 1. BUSINESS

General

Hydromer, Inc (the "Company") is a bio-polymer research and development company organized as a New Jersey Corporation in 1980 for the purposes of developing polymeric complexes for commercial use in the medical, commercial, cosmetics and veterinary sciences markets.

Until September 1982, approximately 99% of the outstanding common stock, without par value (the "Common Stock"), of the Company, was owned by Biosearch Medical Products Inc. ("BMPI"), which in turn was controlled by Manfred Dyck, who is the Company's current Chief Executive Officer, Director and the Chairman of the Board.
On September 16, 1982, BMPI distributed its shareholdings in the Company pro rata to the holders of its common stock. In connection with this distribution, the Company granted to BMPI an exclusive, worldwide perpetual, royalty-free license for the use of Hydromer technology in connection with the development, manufacture and marketing of biomedical devices for enteral feeding applications. On February 4, 2000, the Company acquired all outstanding stock of BMPI for $0.20 per share, and now manages BMPI as a subsidiary.

The Company owns several process and applications patents for Hydromer® coatings ("Hydromer"). These polymers become extremely lubricious (slippery) when wet.
Techniques have been developed for grafting or applying this substance onto a broad variety of materials, including other polymers like polyurethane, polyvinyl chloride, and silicone elastomers, ceramics and metals. The Company has also been issued patents for permanent anti-fog materials, hydrophilic polyurethane foams, hydrophilic polyurethane blends, hydrophilic polyvinylbutyral alloys, several biocompatible hydrogels and an anti-bacterial medical material. Currently, the Company has two patent applications pending. The Company continues to actively evaluate other new market opportunities for its polymer technology specifically in neurology and cardiology.

The Company also owns various trademarks, including AQUADAPT®, a medical hydrogel, AQUAMERE®, a water resistant film former product with cosmetic applications, AQUATRIX®, a cosmetic hydrogel, Dermaseal®, a dermal barrier film product for the prevention of contact dermatitis, Sea-Slide®, a coating for watercraft hulls, and T-HEXX®, a barrier teat dip product for the prevention of mastitis in dairy animals.

The Company's patents are typically broad based, having a multitude of different applications across various industries. Accordingly, the Company currently operates in the medical, commercial, cosmetics and veterinary sciences markets.

MEDICAL

From its inception in 1980 to mid-1984, the Company was primarily engaged in R&D activities related to Hydromer coatings used on medical devices. Since then and until the acquisition of BMPI, the Company's business in the medical field consisted of the sale of lubricious coatings and the licensing of its lubricious coating technologies. With the acquisition of BMPI in February 2000, the Company now offers a horizontally integrated breadth of services including medical device

manufacturing, contract coating, equipment building and design, and as of more recently, R&D servicing and government contracts.

The Company continues to focus on its coatings technologies as the nucleus of its participation in the medical field. As of June 30, 2006, the Company has three
patents pending, one on an anti-microbial coating and two on teat dip technology. The Company was granted a patent on water-based lubricious coatings in fiscal 2006.

HYDROMER® Lubricious Coatings

When treated with Hydromer polymers, a medical device becomes very slippery when wet, allowing for easy insertion into any orifice of the body, in penetration of the
skin or for device-on-device (i.e. guidewire-catheter) use. Hydromer coatings are permanently bonded to the device unlike silicone lubricants, which must be applied
after each use and are often left behind in the bloodstream and body cavities. Hydromer coatings can also be coated on complex surfaces and on the inside walls of
devices, unlike the treatments by major competition. Hydromer has also been shown in numerous studies to reduce the risk of thrombogenesis or clot formation on devices.
Drugs and other substances can be readily incorporated into Hydromer, both in a bound and unbounded fashion, allowing for controlled release from the device for
therapeutic purposes or the creation of permanent biocidal or biostatic surfaces. The Company believes that the polymer-water interface of Hydromer provides surface
lubricity superior to the quality of other currently marketed silicone-based lubricants to treat medical devices.

Option and License Agreements

A portion of the Company's revenues is derived from option and license agreements (see “Patents and Trademarks” section). Option agreements provide customers the
right for a finite period of time (i) to use the Hydromer process to determine whether the customer's products lend themselves to treatment with the process and (ii)
to test market such products. The option agreements have also given the customers the right to subsequently enter into a license agreement with the Company
and to the market product(s) treated with Hydromer, which typically provides the Company an initial flat fee, followed by periodic royalty payments based on sales.

The Company has previously reported license agreements in effect and expiring relating to applications of the Hydromer as follows: Annual Report on Form 10-K for the
fiscal years ended June 30, 1983 through 1996 and Form 10-KSB for fiscal years ended 1997 through 2005.

As of June 30, 2006, the Company has license agreements with seven companies covering the application of Hydromer coatings to the following devices: enteral feeding
products, guidewires, certain urological devices, infusion microcatheters, central venous catheters, guiding and umbilical catheters, razor

cartridges (non-medical related), orthodontic accessories, angioplasty balloon catheters, embolization delivery devices, inter/intra-ocular lenses and biliary
and pancreatic stents. The Company is actively seeking new licensing opportunities.

Licensee/Application
Applied Medical - certain urological and vascular devices

Corneal, Ltd. - inter-ocular lenses

Eveready - Schick / Warner / Wilkinson Sword Ltd. - razor cartridges

Gallini - certain urological devices

MXM - intraocular lens inserter systems

Nemed - inter-ocular lenses

Tyco International / Kendall HealthCare Products - certain urological devices and enteral feeding systems

Supply and Support Agreements

In order to avail our customers to a continued material source or of technical support on our products, certain supply or support agreements may be entered into.
Depending on the specific requirements of each agreement, the Company would provide continued support in terms of product availability or technical know-how,
some including the escrow of formulas or data with independent agents.

Hydrogels, Drug Delivery, Wound Dressing

Applications of the Company's Hydrogels are being developed for wound care, implants, drug delivery, burn care, conductive hydrogel electrodes, ultrasonic
couplants and cosmetic uses for several customers. The Company is also identifying strategic partners to offer hydrogel coating services to clients who does
not have rolled goods coating capability and to license Hydrogel technology for cosmetic and medical use, including drug release.

The Company's hydrogel technology offers biocompatibility, flexibility, and ease of use and processing. It also allows for the stabilization of biomolecules, cell cultures,
drugs and other active substances without potentially damaging external energy sources. It is absorbent, inherently self-adhesive but peels away cleanly and is naturally
soothing. Other than our bio-adhesives and medical coatings, which are one part systems, to form the gel entails simply to mix the two parts together - no heat, no chemical
cross linkers nor expensive high energy processing is required. Many competitive technologies are much more process intensive and require external energy to crosslink.
The Company believes these products are synergistic to our existing hydrogel technologies, and offer further opportunities in electrodes and internal and topical
actives delivery. The Company has a pilot coating machine to facilitate the commercialization of its hydrogel technologies. The Company is exploring other medical and
dental as well as cosmetic applications for this technology.

Aquadapt® is the Company's hydrophilic polyurethane foam technology. The Company has 510K approvals from the FDA for medical use applications in the U.S.
The Company also has a patent on its chitosan-PVP hydrogel technology as well as patents granted in 2000 and 2002 on polyaldehyde hydrogels.

OEM Medical Devices

Through its Biosearch Medical Products subsidiary, ISO 13485 certified and FDA registered, the Company offers 510K/CE marked medical devices. The current product
portfolio includes: bipolar coagulation probes; jejunal, enteral and biliary catheters and stents; feeding accessories; guidewires; biofeedback devices for fecal and urinary
incontinence; and endoscopic accessories. The Company also contract manufactures products for several large multi-national marketers of medical devices on an OEM basis.

HYDROMER® Coating Services

The acquisition of BMPI allowed for the Company to realize another venue of revenues: Coating Services. Utilizing the acquired medical device manufacturing know how
and by applying its coatings technologies, the Company began offering Coating services, in which the Company coats third party devices with its own lubricious coatings.
The Company's knowledge in coatings technologies allows for it to coat various types of material, such as silicone, stainless steel, Pebax and polypropylene cost effectively,
whereas some of the competition is unable to. A global client is using this service in the urology market.

The Company continues to expand its activity in Coating services and is actively seeking new opportunities to provide contract development, coating and manufacturing
services to the medical, commercial and personal care industry, utilizing its Hydromer and Anti-Fog coating technology and expertise. The Company further continues to
believe that these services will enable a broader range of customers to use our materials in market on accelerated timelines in a more cost effective manner.

R&D and Engineering Services

The medical device market continues to undergo a shift toward consolidation by very large multi-national players with small, entrepreneurial start-up companies looking to
exploit niche opportunities or unique device designs. The Company's experience and knowledge can significantly speed development, assessment and market readiness for
our clients, large and small through its research and development and engineering services.

For example, for medical devices such as coronary stents and brain catheters, the Company can develop the coatings, including drug eluting coatings, establish the manufacturing
protocols, design and build the coating equipment, start up scale prototype production and eventually transfer the process assisting the customer in the transition.

The Company believes that offering prototyping, process development and small-medium scale coating/ manufacturing services is fundamental to the expansion of the
Hydromer coatings business, and a strategic imperative. The Company will endeavor to become a "one stop" supplier of high performance coatings and services.

INDUSTRIAL/COMMERCIAL

Hydromer Anti-Fog/Condensation Control is an optical coating which prevents the accumulation of vision-obscuring condensation under high humidity conditions.
The Company is selling this material in bulk to manufacturers of greenhouse panels, refrigerator freezer doors, industrial and medical safety and swim goggles,
aircraft windows, automotive headlight assemblies and gauge and meter manufacturers in the U.S. and internationally, including China.

The Company also offers Sea-Slide®, a Hydromer-based drag reducing coating that reduces friction between hull and water, and can be used over most anti-fouling paints.
A U.S. patent covering this coating and other potential uses was issued in 1987. Independent testing has confirmed that this technology significantly improves fuel
economy and the hull speed of watercraft. Sea-Slide is marketed through HammerHead Products, Inc., via an exclusive distribution agreement.

COSMETICS

The Aquamere® series of the Company's cosmetic intermediaries are sold to major cosmetic companies worldwide for use in hair dyes, hair conditioners, mascaras, eye shadows,
sunscreens and body lotions. They are currently in test for use in shampoos, hair styling aids, OTC dermal drug delivery and topical disinfectants. The Aquamere series of
cosmetic polymer solutions, introduced in 1988, are both aqueous and hydro-alcoholic based systems. They are also offered with cationic and silicone grafted modifications.
Formulations have also been developed internally utilizing this technology and are being offered for sale as turnkey products to smaller marketers of personal care products.

The Company's Dermaseal® line, a patented film-forming hydrogel technology, is currently being sold to major cosmetic companies as a base for foundations and other skin
care products. It is also being tested for use in broader skin care, cosmetic and OTC drug delivery. Dermaseal is the registered trademark for barrier film compositions,
patented in fiscal 2000 along with the method for preventing contact dermatitis. Clinical testing has demonstrated that these compositions protect the user from the effects
of contact with poison ivy, oak or sumac plant allergens. Technical testing has also demonstrated protection from latex proteins, nickel and other contact allergens.

In 2006, the Company added a unique anti-microbial polymer to its product line. When used for beauty cosmetics, contamination and infections can be reduced.

VETERINARY SCIENCES

In Fiscal Year 1999, the Company's polymer technology was used to launch the Company's entry into the Animal Health field to combat clinical and sub-clinical mastitis, a
problem that costs U.S. Dairy farmers an estimated $3-5 billion per year. Marketed under the *T-HEXX*® brand, initially through U.S. licensees, the *T-HEXX* Barrier Dips and Sprays
offer dairy farmers exceptional value and unsurpassed protection as the first no-drip and water resistant barrier products on the market preventing environmental water
containing mastitis-causing organisms, including mycoplasma, from reaching the teat surface. The Company has received three patents for its unique barrier teat dip compositions
with an application on a fourth patent pending.

The annual U.S. market for barrier teat dips is estimated to be $100-130 million at the farm level. The *T-HEXX* Barrier products contain protocol-proven active ingredients that kill mastitis-causing bacteria within 30 seconds of contact while continuing to remain active up to 12 hours later. *T-HEXX* Barriers are superior performers in its niche market while priced comparably or less than barrier dip products manufactured by the leading sanitary chemical companies in the world. Our products are compatible with existing mechanical equipment and milking procedures and most importantly, are easily removed using traditional pre-milking methods. Based on field tests, our product has been demonstrated to stay on the cow teat better than the competition, protecting the cow during the complete 8-12 hour milking cycle.

In fiscal 2002, the Company launched a complementary product, *T-HEXX*® Dry Teat Protection Sealant, to protect cows during the non-lactation ("dry cow") period. *T-HEXX* Dry is used as a non-irritating low-cost sealant during the dry-off and the critical pre-calving period where it is estimated that over 50% of new mastitis cases are believed to start. *T-HEXX* Dry is the first dry cow dip product with an antimicrobial that remains on the teat for 3-7 days. Clinical studies show that *T-HEXX* Dry is impervious to National Mastitis Council (NMC) recognized mastitis-causing organisms for seven days, yet is comparably priced to existing dry cow teat sealants that does not offer such protection. Our product is suggested to be used on cows just prior to their release to the dry cow pen, in conjunction with existing antibiotic therapy or internal teat sealants. In fiscal 2004, two customers launched our Dry product under their private-label name, reflecting the strength of our product.

Patent pending and under development is a *T-HEXX* teat plug, which when launched, would allow the Company to provide complete protection against mastitis for the entire bovine working cycle.

The Company has invested significantly in clinical research, patents, promotion, vendor partnerships and advertising via print media, trade shows and the Internet to support this business and continues to do so. In fiscal 2004, the Company initiated a claim against a former licensee and other parties citing infringement on the Company's patented technology in this area. In total, through June 30, 2006, the Company spent approximately $510,000 ($257,000 in fiscal 2006) in direct legal costs, which has been expensed in the related year's results. Settlement was made in early calendar 2006, with the discounted value on $300,000 recorded in Other Income.

Products

Coating solutions for use on medical devices, cosmetic intermediaries, hydrogels and teat barrier dips/sprays are manufactured and sold by the Company to its licensees and others. The Company is selling bulk quantities of anti-fog solution to manufacturers of greenhouse panels, refrigerator freezer doors, swim goggles, industrial safety equipment, aircraft

windows and meter covers, both in the U.S. and foreign countries. The Company also sells OEM medical devices through its Biosearch Medical Products subsidiary.

The Company has no long-term contracts with any of its suppliers and believes that there are adequate alternative sources of supply available for all raw materials that it currently uses.

Dependence Upon Customers

The Company derives its revenues from two primary business segments: (1) polymer research and the products derived there from, and (2) the sales of medical products.
During the fiscal years ended June 30, 2006 and June 30, 2005, the Company recognized revenues from two major customers: Johnson & Johnson's Cordis Division and
Cook Endoscopy, formerly Wilson Cook Medical, Inc.

Product sales and/or royalty payments and support fees from these customers accounted for 32% and 29% of the Company's total revenues for the years ended June 30, 2006
and June 30, 2005, respectively.

Potential Applications

The Company continues to explore other applications of the complexing capabilities of polymeric substances, such as anti-microbial agents. The Company currently is
working on further applications of its patented technologies to existing products of other companies, including cosmetics, wound dressings, personal care and a wide
variety of medical devices, including vascular stents. Some of these products and applications are in the preliminary development stage and are subject to substantial
further development before their feasibility can be verified.

On the basis of its market analyses, as well as laboratory and in-vitro testing of certain applications of Hydromer, the Company believes that Hydromer's potential product
applications, classified with reference to salient Hydromer characteristics, are as follows:

1. *Low Coefficient of Friction*. Hydromer is a hydrophilic coating which when contacted by water becomes extremely lubricious. The Company believes that this unique
feature would prove beneficial to any medical device that is inserted into the body. Medical products that would so benefit include:

urinary products - urethral catheters, stents and urinary drainage systems;

rectal products - enemas, rectal tubes, examination gloves and proctoscopy devices (disposable);

nasal/oral products - suction catheters, oxygen catheters and endotracheal tubes;

cardiovascular and related products - grafts, cardiac assist catheters heart-lung tubing, stents.

2. *Ability to be Complexed with Other Functional Chemicals.* The Hydromer hydrophilic polymer coating can be complexed with other chemicals. For example,
Hydromer coating complexed with iodine forms an effective anti-microbial barrier. The Company believes that this unique feature would lend itself to application on a

wide variety of currently marketed medical products, including vascular stents, Foley catheters, wound drains, wart and corn dressings, burn dressings, intravenous catheters, surgical dressings and adhesive bandages. One of the Company's recent patents in the coating area, issued in April 2000, involves the covalent bonding of infection resistant materials into the coating, providing a non-leaching, anti-infective surface. The Company was also granted a patent in July 2003 for covalently bonded radio-opaque polymeric compositions to improve the radio-opacity of materials without needing high solid loading, metal plating or ion implantation for applications like stents and vascular catheters.

3. *Cross-link Density Can be Controlled.* The Hydromer hydrophilic polymer coating, through controlled cross-linking, has been further developed into a special anti-fog coating. Such a coating is (a) resistant to fogging under a wide range of temperature/humidity conditions; (b) transparent and has heat/light stability; (c) long lasting, i.e., will not chip or peel and offers more scratch resistance than do most commercial plastics; (d) inert to most commercial glass cleaners; (e) less prone to static dirt pickup; and (f) applicable by dip, spray or roll coating. A U.S. Patent for this material was first issued to the Company in August 1984 (patent expired). This anti-fog product has use on greenhouse panels, refrigerator freezer doors, sports goggles, windows, mirrors and other products, either by direct application or by coating of an adhesive backed film.

Research and Development

The Company's research and development activities presently are, and during the next year are expected to be devoted primarily to the development and enhancement of the products described above and to the design and development of new products, either for its own account, jointly with another company or strictly as a sub-contractor. The Company sponsors all of such activities from its own internal funding or through charges to the contracting company. The major portion of R&D expenses was applied toward salaries and other expenses of personnel employed on a regular basis in such work. See the "Employees" section.

Competition

The Company considers the most significant competitive factors in its market for its patented coatings to be product capability and performance (including reliability and ease of use), in addition to price and terms of purchase.

The Company currently owns nineteen process and applications patents for Hydromer coatings (see "Patents and Trademarks"). Although the medical products market is highly competitive, the Company does not believe that there is any other product available which performs functions significantly better than those which are performed by the Company in terms of lubricity, complexing capabilities, durability and cost.

While management believes the Company has a strong position in the market for medical device coatings in which it competes, and that its hydrophilic foam, anti-fog coatings and hydrogel products are technologically superior to other products in the market, there can be no assurance that alternatives, with similar

properties and applications, could not be developed by other companies. The Company is aware that there are other similar technologies available and/or being developed by others. The industry in which the Company competes is characterized by rapid technological advances and includes competitors that possess significantly greater financial resources and research and manufacturing capabilities, larger marketing and sales staffs and longer established relationships with customers than the Company does, at present or will for the foreseeable future.

Marketing

The Company markets its products and services through five principal means:

1. *Commercialization of its existing technologies:* The Company intends to expand its efforts to market its current technology to the medical, industrial, personal care and veterinary sciences markets. The Company has expanded its capabilities to prototype and manufacture for customers to demonstrate the value of Hydromer technology. The Company will also seek opportunities to apply its technology in new applications where the technology will offer a benefit. Further, the Company will seek customers for technologies that have been developed but are not currently generating revenue, capitalize on the technology that has been created through its R&D efforts and to expand the application of current technologies.

2. *Sale of Development Services:* The Company intends to continue moving its effort away from straight technology licensing and toward contract product development, contract manufacturing and coating services (see “5. Coating Services”). The Company has significant expertise in polymer development and applications. By exhibiting at an increased number of trade shows in the medical device fields, the Company expects to generate interest in its technology and products, with a view toward acting as an outside product development arm and development supplier for companies in these fields.

3. *Joint Development:* The Company will continue to seek joint development programs, co-marketing programs and other business arrangements with potential partners.

4. *Licensing:* The Company will continue its endeavors to license its technology to current market leaders in the medical device, pharmaceutical and other fields, whereby the Company will grant exclusive or non-exclusive rights for the Hydromer coating treatment of existing or new products, and the development of specific products utilizing its foam and hydrogel technology under its patents. In return, the Company generally would earn royalties based on sales of such treated or new products. Such licenses will usually be very narrow. The activities leading to the consummation of a license agreement normally are lengthy and require establishing a scientific dialogue with potential customers, treating samples supplied by that customer with Hydromer coatings, determining if the treatment is feasible and cost effective, testing the coated products in a laboratory and then negotiating a mutually acceptable option agreement. An option fee may be paid by the customer which would give the customer exclusive rights to use the Hydromer treatment on the specified product for a specified period. During such period, the optionee can test market the coated product and/or determine its ability to treat the product in its own manufacturing process. If the customer determines that the subject product should be treated

with Hydromer coating on a commercial basis, it may either perform the Hydromer coating treatment itself under a license agreement with the Company, through the
Company's Contract Coating unit or it may have a third party perform the Hydromer coating treatment.

5. *Coating Services:* The Company will serve the customer who needs products coated with lubricious or anti-fog coatings in production runs that are economically
feasible without substantial investments in fixturing and automation. Typically this would be prototypes or runs of low volume, high value products. Higher volume
products could be accommodated if they were physically small and did not require extensive fixturing or because for technical reasons they could not be automated
and were of high enough value to warrant the added cost. The Company will pursue large volume projects if they fall within a technical area where the Company has
particular expertise.

Business segments in Coating Services which are of particular interest include medical devices (catheters and guidewires) and transparencies (lenses, face shields).
Contacts will be pursued in conjunction with marketing of Hydromer coatings, at trade shows, in mass mailings and advertisement in appropriate trade publications.
The Company is continually upgrading its advertising copy and promotional literature as needed to graphically highlight the properties and advantages of its technologies.

The same marketing tools (traditional means of tradeshow contacts, mass mailings, advertising, promotional activities, etc.) as well as alternative methods (such as the Internet)
are used by the Company in its focus of expanding sales globally to the medical, commercial, personal care and veterinary sciences community.

Patents and Trademarks

Management believes that the protection afforded by the Hydromer patents will be a significant factor in the Company's ability to market its products. Anticipating
patent expiration, the Company has focused on licensing and developing products based upon its newer technologies. A U.S. patent was issued in October 1985 for a
hydrophilic polyurethane foam that is expected to have numerous medical applications. Foreign patents covering this material were issued in July 1990. A U.S. patent for
hydrophilic polymer blends, which covers the Company's coating for boats and the cosmetic formulations, was issued in February 1987. U.S. and foreign patents have
also been issued for an anti-bacterial medical material that can be incorporated in foam or as a coating. The Company was issued a U.S. patent for non-leaching biostatic
coatings and three United States patents for its new composition, barrier film, and method for preventing contact dermatitis developed by the Company's research and
development staff. The Company has also been issued United States and foreign patents for a permanent anti-fog. The Company also has two patents for Chitosan gels,
which expires in 2014. These patents are part of the new gel technology with applications in medical, industrial, cosmetic and personal care markets. The Company was issued
three U.S. Patents for barrier teat dip compositions.

One U.S. patent that contributed approximately $2,100,000 in annual royalties expired on May 6, 2005. The Company was successful in reaching new supply or support agreements with all four former licensees of the expired patent for an approximate annual value of $1,500,000. These new supply/support agreements have varying terms and cancellation provisions. It is the Company's practice to replace any discontinuances of income stream with other sources, including new product revenues, new service revenues and other license or contract revenues.

One new patent was awarded to the Company during the fiscal year ended June 30, 2006. This patent covers the application of water based surface modifications for use in lubricity, anti-microbial, drug release, hydrogel, radio-opaque, animal care and unique anti-fog/anti-frost applications.

As of June 30, 2006, the Company has 19 U.S. patents, three U.S. applications and various foreign counterparts.

The Company owns the registered trademarks "Aquadapt", "Aquamere", "Aquatrix", "Dermaseal", "Hydromer", "Sea-Slide" a "T-HEXX" in the United States and other countries.

Employees

As of June 30, 2006, the Company and its subsidiary had eighty-five active full-time employees. The Chief Executive Officer is Manfred F. Dyck, who is also Chairman of the Board.
The Company does not have a collective bargaining agreement with any of its employees and considers its relationship with its employees to be very good.

Government Regulations

The uses of the Company's medical, agricultural and cosmetic products come under the jurisdiction of the FDA, as well as other federal, state and local agencies, and similar agencies in other countries.

In connection with the Company's license agreements, it is generally the obligation of the licensee to conform to any required FDA pre-market notification or other regulations.
To the Company's knowledge, all such licensees who are marketing FDA regulated licensed products are in such compliance. The Company may in the future desire to market additional applications of Hydromer to existing products, or products introduced by it, which may be subject to such FDA approval procedures as proof of safety and effectiveness of the applications or products, or adherence to prescribed design standards. There can be no assurance that such approvals would be forthcoming or of compliance with such standards. Any such failure to obtain approvals or non-compliance might have a significant adverse effect on the Company. However, the Company intends to make every effort to obtain all necessary approvals and to comply with such standards, and in the case of its licensed applications, to require the licensees to obtain such approvals.

The Company manufactures medical products through its Biosearch Medical Products subsidiary ("Biosearch"), whose activities come under the jurisdiction of the FDA.
It is the policy of the Company to use the FDA regulations as guidelines during manufacturing of Hydromer coatings.

The Company is also subject to federal and state regulations dealing with occupational health and safety and environmental protection. It is the policy of the Company to

comply with these regulations and be responsive to its obligations to its employees and the public.

The Company's electronically filed reports are available at www.sec.gov.

Executive Officers

The executive officers of the Company are as follows: Name	Position with Company	Age as of Aug 31, 2006
Manfred F. Dyck -	Chairman of the Board, Chief Executive Officer and President	71
Martin C. Dyck -	Executive Vice-President, Operations and President Biosearch Medical Products subsidiary	44
Rainer Gruening -	Vice-President, Intellectual Property	63
John Konar -	Vice-President, Quality Assurance and Director of Human Resources	57
Robert Y. Lee -	Vice-President, Finance, Chief Financial Officer and Treasurer	40
Robert J. Moravsik	Senior Vice-President,	63

Manfred F. Dyck has been Chairman of the Board of the Company since June 1983 and a Director of the Company since its inception. Mr. Dyck served as
Chief Executive Officer of the Company from its inception until October 1986, and as of August 1989, reassumed the duties of Chief Executive Officer. Mr. Dyck was
President of Biosearch Medical Products Inc. from 1975 until 1998 and a Director of Biosearch Medical Products Inc. from 1975 until 2000.

Martin C. Dyck has been Executive Vice-President, Operations since June of 2001. He was previously Vice-President of Operations since February 2000 when the

Company purchased Biosearch Medical Products. Mr. Dyck has been President of Biosearch since 1998, a position which he still maintains. Mr. Dyck has been employed by
Biosearch since 1986 and has served in various capacities including Director of New Product Development, where he developed several new medical devices and authored
six FDA 510(k) pre-market submissions. After becoming President of Biosearch in 1998, Mr. Dyck changed the focus of Biosearch to become a contract medical coatings service
provider using proprietary technology unique to Biosearch.

Rainer Gruening joined the Company as Vice-President of Research and Development in June 2001, and in May 2006 became VP of Intellectual Property. With a PhD in
Chemistry from the University of Marburg in Germany, his background

includes service with Bayer AG/Deutsche Solvay Werke, Troy, G+G International and AM Cosmetics in areas including international regulatory affairs, coatings technology
and anti-microbials. Mr. Gruening authored and/or co-authored 17 patents and 35 publications on synthesis and formulation of anti-microbials for paint and coatings,
cosmetics, personal care products, adhesives, marine anti-fouling and metal working fluids and developed dossiers, safety assessments and GMP documentation.
Additionally, he implemented FDA/CTFA, European and Japanese compliance requirements for raw materials and formulation restrictions.

John Konar has been the Vice-President of Quality Assurance since February 2004 and Director of Human Resources since February 2000. Mr. Konar joined Biosearch in 1986
and served as the Director of Human Resources with Biosearch from 1996 until its acquisition by the Company in 2000, when he then assumed responsibilities for both
companies. He also served, with Biosearch, as the Director of Sales from 1996 until 2000, Director of Manufacturing from 2000 to 2001 and Director of QA from 1998 until 2004.

Robert Y. Lee joined the Company in the capacities of Vice-President of Finance, Chief Financial Officer and Treasurer in June 2001. He earned a MBA in Finance and
International Business, and a Bachelors of Science in Accounting and Information Systems, both from New York University's Stern School of Business. His professional
experience includes tenure with the New York office of Coopers & Lybrand (currently Pricewaterhouse Coopers) in their Emerging Business Group, the Bristol Myers
Squibb Internal Auditing group, ASARCO's Southern Peru Copper Corporation, now Southern Copper Corporation, part of Grupo Mexico, and Citigroup.

Robert J. Moravsik has been Senior Vice-President, General Counsel and Secretary since February 2000. He holds a B.S. in Aerospace Engineering, an M.S. in Computer
Science and a Doctorate in Law. He was Vice-President and General Counsel since April 1998. He also serves in the same capacity for Biosearch Medical Products, Inc. an
affiliated company since 1987. Prior to that, he was Vice-President and General Counsel to Fisher Stevens, Inc., a subsidiary of the Bureau of National Affairs. He is an attorney
admitted in the state of New Jersey and New York.

Item 2. PROPERTIES

In June 1998, the Company purchased the building and land at 35 Industrial Parkway, Branchburg, NJ from Biosearch Medical Products, then an affiliated party. The facility,
currently its sole facility, is secured by mortgages through banks. See the financial statements included herein for the terms of the agreements.

In 2002, the Company completed its 10,400 square feet expansion at its primary location of 35 Industrial Parkway. This allowed the Company to consolidate certain
manufacturing and quality assurance functions operations formerly located on leased space.

The expanded facility will be adequate for the Company’s operations for the foreseeable future.

Item 3. LEGAL PROCEEDINGS

The Company has been named as a defendant in two product liability actions. Both actions are covered within the Company’s Product Liability Insurance policy.

Item 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

Not applicable.

PART II

Item 5. MARKET FOR THE REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

Prior to January 9, 1986, the Company's Common Stock was traded in the over-the-counter market on the National Association of Securities Dealer's Automated
Quotation System (NASDAQ) under the symbol "HYDI". Subsequent to January 9, 1986, reporting of trading was transferred to the National Daily Quotation Service
(commonly known as the "Pink Sheets"). For the past twenty years, trading in the Company's stock has been limited.

On February 13, 2002 the Company became a listed security on the Boston Stock Exchange ("BSX") under the trading symbol "HDO". Hydromer remains listed as "HYDI"
on the OTC reporting services.

The Company's common stock traded at prices ranging between $0.75 and $1.35 in the fiscal year 2006 and between $0.80 and $3.05 in the fiscal year 2005. These prices
may not include retail mark-ups or mark-downs or any commission to the broker dealer.

The approximate number of holders of record of the Common Stock on September 1, 2006 was 232. There are approximately 700 individual shareholders of the common stock.

Item 6. MANAGEMENT DISCUSSION AND ANALYSIS

The below discussion analyzes major factors and trends regarding the results of operations and the financial condition of the Company as of June 30, 2006,
and its results of operations for the prior fiscal period. It should be read in conjunction with the Financial Statements and Notes thereto.

Revenues for the year ended June 30, 2006 were $7,869,729 as compared to $8,501,374 for the same period last year, a decrease of $631,645 (-7.4%).

Product sales and services revenues were $5,933,167 for the 2006 fiscal year as compared to $6,200,992 the prior fiscal year, a 3.4% decrease or $207,825.

License royalties and option payments were $1,876,562 in fiscal 2006, down 18.4% from fiscal 2004's results of $2,300,382.

Management Comment: Lower customer orders in the medical device business negated the fiscal 2006 growth from our contract coating services and medical coating sales.
In fiscal 2006, there were two medical device customers with reduced volume: one which is transferring their orders to in-house production and the second, who purchased the
OEM product line from another of our customers, lost focus on the product line during the transition. The Company expects a turn around from these particular customers,
as in the former, the Company will replace lost medical device revenues with the sales of lubricious coatings (along with a cost reduction to staffing from to the elimination of a
product line). With regards to the second customer, the Company has brought to their attention of the business reduction and we are currently working on re-establishing

volume. In addition, there was an one-time $250,000 in technology transfer revenues in fiscal 2005.

The Company's patent 4,642,267 expired on May 6, 2005. It was the subject of four licenses which provided approximately $1.9 million of royalty and option income in fiscal 2005. The Company was able to enter into supply agreements or support fees, with varying terms and termination conditions, with all four of the licensees, recovering $1.6 million of the former royalty stream in fiscal 2006.

Total Expenses for the year ended June 30, 2006 were $8,649,106, $416,913 or 5.1% higher than fiscal year 2005's results of $8,232,123.

Cost of Goods Sold was $3,526,039 for fiscal 2006 as compared to $3,228,875 for fiscal 2005. Operating expenses were $5,494,366 and $4,783,188, for the years ended June 30, 2006 and 2005, respectively. There was a $238,172 impairment of goodwill charge in fiscal 2006. Fiscal 2006 includes Other income of $143,974 compared with Other Expenses of $109,995 in fiscal 2005. There was a Benefit from Income Taxes of $465,497 in fiscal 2006 as compared with a provision for Income taxes of $110,065 for the twelve months ended June 30, 2005.

Management Comment: A change in the Company's inventory standard costs impacted the beginning fiscal 2006 inventory value by $138,459, which is included in the fiscal 2006 Cost of Sales. Higher wages and benefits paid added another $99,879 to Cost of Sales in fiscal 2006. A portion of the capital expenditures incurred have been for equipment to automate production -- to increase productivity. The redesign of various medical devices, including that of the component materials used, is expected to reduce a portion of Cost of Sales in the future. This initiative is underway and first requires the acceptance of the redesign by our customers.

The capitalization of [inventory] overhead on higher June 30, 2005 ending inventory levels reduced fiscal 2005 Operating Expenses by $290,112. A SBIR (Small Business Innovation Research) grant of $93,650 further reduced fiscal 2005 costs. These reductions to the fiscal 2005 costs were compounded with higher fiscal 2006 expenses, primarily of $82,885 in higher litigation expenses related to our patent infringement claim (see below and the following page) and a $74,900 bad debt write-off relating to R&D services performed in 2005 which is now deemed uncollectible, yielding the large swing that we see in Operating Expenses year-over-year. Our patent infringement claim against a former licensee and other parties has been settled, entailing over $509,000 expended in legal fees since 2004. Taking this action not only substantiated the validity of our patents, but put the world on notice that we would not allow for infringement of our intellectual property. With the settlement, we are now able to focus on selling our products with reduced concerns of counterfeit products stealing our markets once we establish them. We do not anticipate any significant amounts to be spent further on this matter. Also included in Operating Expenses is the Company's investment into Research and Development (primarily salaries and benefits) of $1,000,987 and $1,012,091, or 18.2% and 21.2% of total Operating Expenses,

for the years ended June 30, 2006 and 2005, respectively, and the amortized investment on the patent estate ($144,327 and $151,175 for the years ended June 30, 2006 and 2005, respectively).

After years of realized synergies, the most recent evaluation of the Company's carrying value of goodwill, created from the acquisition of Biosearch in 2000, determined an impairment of goodwill of $238,172, recorded in the year ended June 30, 2006, eliminating the remaining balance of goodwill carried. There was no required charge for the year ended June 30, 2005. This charge in fiscal 2006 did not provide for a current tax benefit resulting in a lower tax benefit realized.

Other income in fiscal 2006 includes $284,238, the discounted value on $300,000, from the settlement of a patent infringement case against a former licensee and other parties.
Reducing Other income is interest expense from the Company's mortgage loans and Line-of-Credit borrowings, which is the primary component of Other Expenses for fiscal 2005.

An Income Tax Benefit was recorded for the year ended June 30, 2006 based on the pre-tax loss. This benefit includes provisions for federal income taxes, state income taxes and R&D tax credits as offset by the non-current deductibility of the impairment of goodwill charge (which resulted in a deferred tax asset, however as realization is highly unlikely, a valuation allowance fully reserving for the benefit has been recorded). This compares with a tax provision for the year ended June 30, 2005.

A Net Loss of $779,377 is reported for the 2006 fiscal year compared with Net Income of $269,251 for the 2005 fiscal year.

A Net Loss of $779,377 or $0.17 per share is reported for fiscal 2006 as compared with Net Income of $269,251 or $0.06 per share for fiscal 2005.

Management Comment: Lower revenues combined with higher expenses, including an impairment charge of $238,172 to goodwill, as reduced by a tax benefit arising from the operating loss, resulted in a net loss of $779,377.

The conclusion of various matters (patent infringement costs, impairment of goodwill charges) and the cost reduction initiatives underway along with new developments and projects, is expected to improve the Company's results down the road.

Liquidity and Capital Resources

Working Capital as of June 30, 2006 was $970,112, down from $2,471,207 the prior year.

Long-term investments (capital expenditures and the funding of the patent estate) along with the working capital needs arising from operations decreased working capital during the 2006 fiscal year.

Management Comment: We continue our re-investment back into the Company, primarily in terms of R&D (personnel as well as equipment) and to our patent estate, to support future growth of our business. During the fiscal year ended June 30, 2006, the Company expended $338,283 for capital expenditures and $213,449 in patent and trademarks costs.
In addition, long-term debt was reduced by $177,679.

Item 7. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

For information concerning this item, see pages F-1 through F-8 of the "Audited Financial Statements for the year ended June 30, 2006," which information is incorporated herein by reference.

Item 8. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

Not applicable.

Item 8a. DISCLOSURE CONTROLS AND PROCEDURES

As of the period covered by this report, the Company carried out an evaluation, under the supervision and with the participation of our management, including the Chief Executive Officer and President and the Chief Financial Officer, of the effectiveness of the design and operation of the disclosure controls and procedures.

Based upon this evaluation, our Chief Executive Officer and Chief Financial Officer concluded that, our disclosure controls and procedures were effective and that there were no changes to our Company's internal control over financial reporting that have materially affected, or is reasonably likely to materially affect the Company's internal control over financial reporting during the period covered by the Company's annual report.

PART III

Item 9. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT

For information concerning this item, see "Item 1. Business - Executive Officers" and pages 3 through 9 in the Proxy Statement filed with respect to the 2006
Annual Meeting of Shareholders (the “Proxy Statement”), which information is incorporated herein by reference.

Item 10. EXECUTIVE COMPENSATION

For information concerning this item, see page 7 of the Proxy Statement, which information is incorporated herein by reference.

Item 11. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

For information concerning this item, see page 8 of the Proxy Statement, which information is incorporated herein by reference.

Item 12. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

During the past fiscal year, there have been no related party transactions.

PART IV

Item 13. EXHIBITS, FINANCIAL STATEMENT SCHEDULES AND REPORTS ON FORM 8-K

(a) 1. Financial Statements:

The financial statements of the Company incorporated by reference in this Report are listed in the attached Index to the Financial Statements and Supplementary Data.

(a) 2. Financial Statement Schedules:

The financial statement schedules of the Company filed in this Report are listed in the attached Index to Financial Statements and Supplementary Data.

(a) 3. Exhibits (not included)

The exhibits required to be filed as part of this Report are listed in the attached Index to Exhibits.

(b) Current Reports on Form 8-K:

The Company did not file any Form 8-K during the quarter ended June 30, 2006.

POWER OF ATTORNEY

The Company and each person whose signature appears below hereby appoint Manfred F. Dyck and Robert Y. Lee as attorneys-in-fact with full power of substitution,
severally, to execute in the name and on behalf of the registrant and each such person, individually and in each capacity stated below, one or more amendments to the
annual report which amendments may make such changes in the report as the attorney-in-fact acting deems appropriate and to file any such amendment to the report with the
Securities and Exchange Commission.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) 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.

HYDROMER, INC.

/s/ Manfred F. Dyck	President, Principal Executive Officer,	August 23, 2006
Manfred F. Dyck	Chairman of the Board of Directors	
/s/ Robert Y. Lee	Chief Accounting Officer	August 23, 2006
Robert Y. Lee		

Pursuant to the requirements of the Securities and Exchange Act of 1934, this report has been signed below by the
following persons on behalf of the registrant and in the capacities and on the dates indicated:

/s/ Manfred F. Dyck	President, Principal Executive Officer,	August 23, 2006
Manfred F. Dyck	Chairman of the Board of Directors	
/s/ Robert H. Bea	Director	August 23, 2006
Robert H. Bea		
/s/ Maxwell Borow	Director	August 23, 2006
Maxwell Borow, MD		
/s/ Ursula M. Dyck	Director	August 23, 2006
Ursula M. Dyck		
/s/ Dieter Heinemann	Director	August 10, 2006
Dieter Heinemann		

/s/ Klaus J.H. Meckeler Klaus J.H. Meckeler, MD	Director	August 23,2006
/s/ Frederick L. Perl Frederick L. Perl, MD	Director	August 23, 2006
/s/ Michael F. Ryan Michael F. Ryan, PhD	Director	August 23, 2006

INDEX TO 2005 10-KSB CERTIFICATIONS

Exhibit No.	Description
31.1	Certification of Manfred F. Dyck, Chief Executive Officer, pursuant to Securities Exchange Act Rule 13a-14(a).
31.2	Certification of Robert Y. Lee, Chief Financial Officer, pursuant to Securities Exchange Act Rule 13a-14(a).
32.1	Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, signed by Manfred F. Dyck, Chief Executive Officer of Hydromer, Inc.
32.2	Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, signed by Robert Y. Lee, Chief Financial Officer of Hydromer, Inc.

Hydromer, Inc. & Subsidiary

Consolidated Financial Statements

June 30, 2006 and 2005

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholders of
Hydromer, Inc. and Subsidiary

We have audited the accompanying balance sheets of Hydromer, Inc. and Subsidiary as of June 30, 2006 and 2005 and the related statements of income, stockholders' equity and cash flows for each of the years in the two year period ended June 30, 2006. These financial statements are the responsibility of the company's management.
Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Hydromer, Inc. and Subsidiary as of June 30, 2006 and 2005, and the results of its operations and its cash flows for each of the two in the two-year period ended June 30, 2006 in conformity with accounting principles generally accepted in the United States of America.

Rosenberg Rich Baker Berman & Company

Rosenberg Rich Baker Berman & Company

Rosenberg Rich Baker Berman & Company

Rosenberg Rich Baker Berman & Compan

Bridgewater, New Jersey
September 27, 2006

Hydromer, Inc. & Subsidiary
Index to the Consolidated Financial Statements
June 30, 2006 and 2005

Hydromer, Inc. & Subsidiary
Consolidated Balance Sheets

.	June 30, **2006**	2005
Assets		
Current Assets:		
Cash and cash equivalents	**$ 434,865.**	$ 1,376,656.
Trade receivables less allowance for doubtful accounts of $44,479 and $32,753 as of June 30, 2006 and 2005, respectively	**1,198,089.**	1,220,258.
Inventory	**988,086.**	1,094,927.
Prepaid expenses	**118,436.**	126,762.
Deferred tax asset	**8,976.**	8,976.
Income Tax Refund Receivable	**91,436.**	38,801.
Other	**127,776.**	14,841.
Total Current Assets	**2,967,664.**	3,881,221.
Property and equipment, net	**3,377,473.**	3,276,258.
Deferred tax asset, non-current	**507,426.**	83,013.
Intangible Assets, net	**849,262.**	780,140.
Goodwill	**-**	238,172.
Other, non-current	**114,377.**	**-**
Total Assets	**$ 7,816,202.**	$ 8,258,804..
Liabilities and Stockholders' Equity		
Current Liabilities:		
Accounts payable	**$ 635,010.**	$ 466,993.
Short-term borrowings	**656,255.**	206,663.
Accrued expenses	**374,043.**	287,417.
Bonus payable	**-..**	77,267.
Current portion of deferred revenue	**128,941.**	161,317.
Current portion of mortgage payable	**202,204.**	178,029.
Income tax payable	**1,100.**	32,328.
Total Current Liabilities	**1,997,553.**	1,410,014.
Deferred tax liability	**271,058.**	243,864.
Long-term portion of deferred revenue	**93,176.**	176,979.
Long-term portion of mortgage payable	**2,093,437.**	2,295,292.
Total Liabilities	**4,455,224.**	4,126,149.
Contingencies	-	-
Stockholders' Equity		
Preferred stock - no par value, authorized 1,000,000 shares, no shares issued and outstanding	-	-
Common stock - no par value, authorized 15,000,000 shares;		

as of June 30, 2006, 4,655,081 shares issued and 4,644,164 shares outstanding; as of June 30, 2005, 4,634,859 shares issued and 4,623,942 shares outstanding	**3,639,315.**	3,631,615.
Contributed capital	**577,750.**	577,750.
Accumulated deficit	**(849,947)**	(70,570)
Treasury stock, 10,917 common shares at cost	**(6,140)**	(6,140)
Total Stockholders' Equity	**3,360,978.**	4,132,655.
Total Liabilities and Stockholders' Equity	**$ 7,816,202.**	$ 8,258,804.

See notes to the consolidated financial statements.

Hydromer, Inc. & Subsidiary
Consolidated Statements of Income

	Year Ended	
	2006	2005
Revenues		
Sale of products	**$ 4,752,991.**	$4,871,283
Service revenues	**1,240,176.**	1,329,709
Royalties and Contract Revenues	**1,876,562.**	2,300,382
Total Revenues	**7,869,729.**	8,501,374
Expenses		
Cost of Sales	**3,526,039.**	3,228,875
Operating Expenses	**5,494,366.**	4,783,188
Impairment of Goodwill	**238,172.**	-
Other (Income) / Expenses, net	**(143,974)**	109,995
(Benefit from)/Provision for Income Taxes	**(465,497)**	110,065
Total Expenses	**8,649,106.**	8,232,123
Net (Loss) Income	**$ (779,377)**	**$** 269,251
(Loss) / Earnings Per Common Share	**$ (0.17)**	**$** 0.06
(Loss) / Earnings Per Common Share - Assuming Dilution	**$ (0.17)**	**$** 0.06
Weighted Average Number of Common Shares Outstanding	**4,638,843**	4,614,500
Weighted Average Number of Common Shares Outstanding - Assuming Dilution	**4,638,843**	4,781,500

For the year ended June 30, 2006, common stock equivalents were not included in computing diluted earnings per share as their effect would be anti-dilutive.

See notes to the consolidated financial statements.

Hydromer, Inc. & Subsidiary
Consolidated Statements of Stockholders' Equity

	Common Stock		Contributed Capital	Accumulated Deficit	Treasury Stock		
	Shares	Amount			Shares	Amount	Total
Balance June 30, 2004	4,608,904	$ 3,615,615	573,750	(338,821)	10,917	$ (6,143,845)	707,404.
Exercise of Stock Options	25,955	16,000		269,251.			16,000. 269,251.

Net Income													
Balance June 30, 2005	4,634,859	$	3,631,615	577	3,750	(78	9,570)		10,917	$	(6,140,1	1,082,655.	
Exercise of Stock Options	20,222		7,700									7,700.	
Net Loss						(779,377)						(779,377)	
Balance June 30, 2006	**4,655,081**	**$**	**3,639,315**	**577**	**3,750**	**(849**	**9,947)**		**10,917**	**$**	**(6,14**	**1,08**	**8,978.**

See notes to the consolidated financial statements.

Hydromer, Inc. & Subsidiary
Consolidated Statements of Cash Flows

	Year Ended June 30,	
	2006	2005
Cash Flows From Operating Activities:		
Net (Loss) / Income	**$ (779,377)**	$ 269,251.
Adjustments to reconcile net income to net cash provided by operating activities		
Depreciation and amortization	**381,395.**	360,117.
Impairment of Goodwill	**238,172.**	-.
Deferred income taxes	**(397,219)**	102,173.
Changes in Assets and Liabilities		
Trade receivables	**22,169.**	495,051.
Inventory	**106,841.**	(285,938)
Prepaid expenses	**8,327.**	(1,963)
Other assets	**(234,679)**	24,570.
Accounts payable and accrued liabilities	**177,374.**	(133,367)
Deferred revenues	**(116,179)**	208,296.
Income taxes payable	**(83,863)**	(95,090)
Net Cash (Used for) Provided by Operating Activities	**(677,039)**	943,100.
Cash Flows From Investing Activities:		
Cash purchases of property and equipment	**(338,283)**	(560,277)
Cash payments on Patents and Trademarks	**(213,449)**	(258,387)
Cash purchases of Short-term investments	**(392,633)**	-
Maturity of Short-term investments	**400,000.**	-
Net Cash Used for Investing Activities	**(544,365)**	(818,664)
Cash Flows From Financing Activities:		
Net borrowings/(payments) against Line of Credit	**449,592.**	75,653.
Proceeds from long-term borrowings	**-.**	1,990,000.
Repayment of long-term borrowings	**(177,679)**	(971,909)
Proceeds from the issuance of common stock	**7,700.**	16,000.
Net Cash Provided by Financing Activities	**279,613.**	1,109,744.
Net (Decrease) Increase in Cash and Cash Equivalents:	**(941,791)**	1,234,180.
Cash and Cash Equivalents at Beginning of Period	**1,376,656.**	142,476.
Cash and Cash Equivalents at End of Period	**$ 434,865.**	$ 1,376,656.

Cash paid during the year for:		
Interest	**$ 172,823.**	$ 115,216.
Income taxes	**$ 32,907.**	$ 102,500.

See notes to the consolidated financial statements.

Hydromer, Inc. & Subsidiary
Notes to the Consolidated Financial Statements

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Operations
Hydromer, Inc. & Subsidiary (the "Company") is a bio-polymer research and development company based in Branchburg, New Jersey. The Company develops polymer complexes for commercial markets in both the United States and abroad for the medical, cosmetics, veterinary sciences and industrial fields. The Company obtains patent rights on certain products from which royalty revenues are received. Its wholly owned subsidiary, Biosearch Medical Products, Inc., a U.S. based corporation, is an OEM manufacturer for various medical products companies as well as the manufacturer of its own line of endoscopic products sold to hospitals, domestically and internationally, through a network of dealers. The Company also offers R&D, engineering and contract coating services in its array of capabilities.

Principles of Consolidation
The consolidated financial statements include the accounts of Hydromer, Inc. and its wholly owned subsidiary. All significant intercompany balances and transactions have been eliminated.

Cash and Cash Equivalents
Cash and cash equivalents consist of short-term investments with original maturities of three months or less.

Short-Term Investments
Short-term investments consist of investments other than cash and cash equivalents with original maturities of greater than three months and less than one year. There were no short-tem investments as of June 30, 2006 and June 30, 2005.

Inventories
Inventories are valued at the lower of cost, determined by the first-in, first-out method, or market and include appropriate amounts of labor and overhead.

Depreciation
The cost of property and equipment, which includes a reasonable portion of labor costs for equipment built in-house, is depreciated on a straight-line method over the estimated useful lives of the assets: 5-10 years for machinery and equipment, 3-5 years for furniture and office equipment and 40 years for the building. When assets are retired or otherwise disposed of, the cost and related accumulated depreciation are removed from the accounts, and any resulting gain or loss is reflected in income for the period. Repairs and maintenance which do not extend the useful lives of the related assets are expensed as incurred.

Patents
Expenses associated with patents are prepaid and amortized over the expected life of the patent, typically 20 years. Prepaid expenses associated with patents which are not approved or abandoned are expensed in the period in which such patents are not approved or abandoned. Maintenance fees associated with existing patents are written off over 12 months. Amortization expense for the years ended June 30, 2006 and 2005 were $144,327 and $151,175, respectively. One new patent was granted during

the year ended June 30, 2006.

Goodwill

Goodwill represents the excess of the purchase price of Biosearch Medical Products, Inc. over the fair market value of their net assets at the date of acquisition and through June 30, 2002, was amortized on the straight line method over 40 years. The Company adopted Statement of Financial Accounting Standards ("SFAS") No. 142, *Goodwill and Other Intangible Assets*, on July 1, 2002 in which goodwill is no longer amortized but tested for impairment on at least an annual basis. The carrying value is reviewed if the facts and circumstances, such as significant declines in sales, earnings or cash flows or material adverse changes in the business climate, suggest that it may be impaired.

If this review indicates that goodwill will not be recoverable, the impairment is determined by comparing the carrying value of goodwill to fair value. Fair value can be determined based on quoted market values, discounted cash flows or appraisals. The Company uses the present value of expected future cash inflows method.

During the year ended June 30, 2006, the Company determined that the carrying amount of the goodwill exceeded its fair value. A goodwill impairment loss of $238,172 was recognized. As of June 30, 2006, the original goodwill balance has been fully written off.

Long-Lived Assets

The Company assesses long-lived assets for impairment as required under SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*. The Company reviews for impairment whenever events or circumstances indicate that the carrying amount of these assets may not be recoverable. The Company assesses these assets for impairment based on estimated future cash flows from these assets.

Revenue Recognition

Revenues from product and services sales are recognized at the time of shipment or services rendered provided that collection of the resulting receivable is probable. Revenues from royalties are recognized upon the sale of certain products by licensees with whom the Company has licensing agreements. Contract Revenues, which includes payments from Option, Supply or Support agreements that are typically based on time frames, are recognized in the periods to which it pertains. Deferred revenues are recorded when agreements call for payment ahead of when the amounts are earned.

Shipping and Handling Charges

The Company includes costs of shipping and handling billed to customers in Revenues and the related expense of shipping and handling costs in Cost of Sales.

Advertising

Advertising costs are expensed as incurred except for tangible assets, such as printed advertising materials, which are expensed as consumed. Advertising expense was $42,671 and $47,267 for the years ended June 30, 2006 and 2005, respectively.

Research and Development

Research and development costs, primarily employee salaries and benefits, are charged to operations when incurred and are included in operating expenses. The amounts charged to expense for the years ended June 30, 2006 and 2005 were approximately $1,000,987 and $1,040,110, respectively.

Stock-Based Compensation

As permitted by SFAS No. 123, *Accounting for Stock-Based Compensation*, the Company has elected to follow Accounting Principle Board Opinion No. 25, *Accounting for Stock Issued to Employees,* ("APB 25") and related interpretations in accounting for its employee stock option plans. Under APB 25, no compensation expense is recognized at the time of option grant when the exercise price of the Company's employee stock options equals the fair market value of the underlying common stock on the date of grant. Effective January 1, 2006, the Company is accounting for stock options under SFAS No. 123(R) (see footnote 2. "New Accounting Pronouncements**"**)

Income Taxes

Income taxes are provided for the tax effects of transactions reported in the financial statements and consist of taxes currently due plus deferred taxes related primarily to differences between the bases of assets and liabilities for financial and income tax reporting. The deferred tax assets and liabilities represent the future tax return

Hydromer, Inc. & Subsidiary
Notes to the Consolidated Financial Statements

consequences of those differences, which will either be taxable or deductible when the assets and liabilities are recovered or settled.
Deferred taxes are also recognized for operating losses that are available to offset future federal and state income taxes.

Earnings Per Share
Earnings per share, in accordance with the provisions of SFAS No. 128, Earnings Per Share, is computed by dividing net income by the weighted average number of common
stock shares outstanding during the period.

Use of Estimates
The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect
the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues
and expenses during the reporting period. Actual results could differ from those estimates.

Reclassification
Certain amounts previously reported have been reclassified to conform to the 2006 presentation.
[Missing Graphic Reference]

2. NEW ACCOUNTING PRONOUNCEMENTS

The Company adopted SFAS No. 123(R), *Share-Based Payment*, on January 1, 2006. SFAS No. 123(R) establishes the standards for transactions where an entity exchanges its
equity instruments for goods or services. This standard requires an issuer to measure the cost of employee services received in exchange for an award of equity instruments
based on the grant-date fair value of the award and eliminated the exception to account for such awards using the intrinsic method previously allowable under APB No. 25.
SFAS No. 123(R) requires all equity compensation to be expensed during the related periods. There were no transactions subject to the accounting of SFAS No. 123(R) this year.
[Missing Graphic Reference]

3. CONCENTRATION OF CREDIT AND BUSINESS RISK

The Company is exposed to additional credit and business risks due to its concentration of activity with certain parties. For example, at times throughout the year, the Company
may maintain certain bank accounts in excess of FDIC insured limits.

In addition, the Company provides credit in the normal course of business to customers. Ongoing credit evaluations of its customers are performed, and allowances for
doubtful accounts are based on factors surrounding the credit risk of specific customers, historical trends and other information.

For the year ended June 30, 2006, the Company sold products and services and collected royalty income, totaling 29% of its total revenues, to two customers, Cordis
Neurovascular Systems and Cook Endoscopy (formerly Wilson Cook Medical, Inc.) who individually accounted for 18% and 14%, respectively, of the consolidated revenues.

There were no outstanding accounts receivable from these customers at June 30, 2006.

During the fiscal year ended June 30, 2005 Cordis Neurovascular Systems and Cook Endoscopy individually accounted for 15% and 14%, respectively, of total revenues.

Accounts receivable from these customers accounted for 22% of total accounts receivable at June 30, 2005.

The Company's patent 4,642,267 expired on May 6, 2005. This patent was the subject of four licenses with a total annual royalty income to the Company of approximately $2.1
million. The Company was able to enter into supply agreements or support fees, with varying terms and termination conditions, with all four of the licensees, valued at $1.5
million annually. Patent no. 4,769,013, the subject of three royalty licenses, expired during the fiscal year ended June 30, 2006 and another patent (no. 4,875,287 with one royalty
license) is to expire in November 2006. The total annual royalty income from these two patents approximated $0.1 million.
[Missing Graphic Reference]

4. INVENTORY

Inventory consists of:

	June 30,	
	2006	2005
Finished goods	**$ 328,777**	$ 336,078
Work in process	**211,422**	314,345
Raw materials	**447,887**	444,504
	$ 998,086	$ 1,094,927

[Missing Graphic Reference]

5. OTHER ASSETS

Included in Other assets as of June 30, 2006 is $123,776 and $114,377, current and non-current portion, respectively, representing the $250,000 remaining receivable
\ from the legal settlement arising from the Company's patent infringement claim settled in February 2006. The receivable, $125,000 each due in January 2007 and January 2008, is
discounted at 5%.
[Missing Graphic Reference]

6. PROPERTY AND EQUIPMENT

Property and equipment consists of the following:

	June 30,	
	2006	2005
Land	**$ 472,410..**	$ 472,410.
Building	**2,148,681..**	2,121,092.
Machinery and equipment	**3,819,631..**	3,556,839.
Furniture and fixtures	**605,558..**	733,595.

	7,046,280..		. 6,883,936.	
Less: Accumulated depreciation and amortization	**(3,668,807).**		(3,607,678)	
Property and Equipment, net	**$ 3,377,473..**	$	3,276,258.	

Depreciation expense charged to operations was $236,558 and $205,579 for the years ended June 30, 2006 and 2005, respectively.
[Missing Graphic Reference]

7. INTANGIBLE ASSETS

Intangible Assets are comprised of the following:

	June 30,		
	2006		2005
Patents	**$ 1,101,153.**	$	975,940.
Trademarks	**72,955.**		72,412.
Less: Accumulated amortization	**(324,846)**		(268,212)
Intangible Assets, net	**$ 849,262.**	$	780,140.

Future amortization of the Intangible Assets, as of June 30, 2006, are as follows:

Year ending June 30,		
2007	$	81,567
2008		77,323
2009		73,310
2010		69,366
2011		68,727
Thereafter		478,9690
	$	849,262

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8. LONG-TERM DEBT AND CREDIT FACILITY

The Company's facility is financed by a ten-year mortgage note bearing interest at a 6.52% fixed rate. The note amortizes with monthly payments and is secured by the real estate and improvements and all rents from leases subsequently entered into. As of June 30, 2006, the book value of the real estate and improvements was $2,327,405. The last complete appraisal was conducted in 2003 and reflected a market value of $3,200,000.

On June 30, 2005, the Company closed on a long-term financing facility of $1,990,000 in the form of a second mortgage on its property. This facility has a ten year term with a 6.38% fixed rate. $886,414 was used to pay off a construction loan/continuing loan provided by New Millennium Bank with the remainder put in short-term investments or to be used for working capital and possible acquisitions. The facility was financed through Wachovia Bank, NA which also holds a $555,000 first Mortgage on the Company's property.

As of June 30, 2006, the Company did not meet certain financial ratios required under the loan documents. A waiver has been granted by the lender.

The Company also has a revolving line of credit agreement with a financial institution, which allows borrowings of up to $750,000, secured by all trade receivables and inventories. The line bore interest, payable monthly at LIBOR plus 3.15% until June 2005 at which was then reduced to LIBOR plus 2.25%. As of June 30, 2006, the interest rate was 7.59%. This line had a maturity date of July 31, 2006 which was extended until January 31, 2007 during the year at the same terms. As of June 30, 2006 and 2005, $656,255 and $206,663 were outstanding on the line of credit respectively.

Long-term debt is comprised of the following:

	June 30,	
	2006	2005
Mortgage note	**$ 438,234.**	$ 483,321.
Second Mortgage Loan	**1,857,407.**	1,990,000.
Less: Current Maturities	**(202,204)**	(178,029)
Long-term Debt, Net of Current Maturities	**$ 2,093,437.**	$ 2,295,292.

Total maturities of long-term debt are as follows:

Year ending June 30,	
2007	$ 202,204
2008	215,393

2009		230,182
2010		245,604
2011		262,060
Thereafter		1,140,198
	$	2,295,641

[Missing Graphic Reference]

9. FAIR VALUE OF FINANCIAL INSTRUMENTS

The carrying amount of cash and cash equivalents, short-term investments, accounts receivable, accounts payable and accrued expenses approximates fair value because
of the short maturity of these instruments. The fair value of the Company's long-term debt approximates its carrying value as it is based on or about the current rates
offered to the Company for debt of the same remaining maturities with similar collateral requirements.

Limitations

Fair value estimates are made at a specific point in time, based on relevant market information about the financial instrument. These estimates are subjective in nature
and involve uncertainties and matters of significant judgment and therefore cannot be determined with precision. Changes in assumptions could significantly affect the
estimates.

10. INCOME TAXES

The income tax (benefit) provision is comprised of the following:

		Federal		State		Total	
Year Ended June 30, 2006							
Current	**$**	**(71,185)**	**$**	**2,907.**	**$**	**(68,278)**	
Deferred		**(296,253)**		**(100,966)**		**(397,219)**	
	$	**(367,438)**	**$**	**(98,059)**	**$**	**(465,497)**	
Year Ended June 30, 2005							
Current	$	1,513	$	5,764.	$	7,277	
Deferred		90,843		11,945.		102,788	
	$	92,356	$	17,709.	$	110,065	

The Company's deferred tax asset and liability as presented in the Company's financial statements are comprised of the following temporary differences:

	June 30,		
	2006		2005

Deferred Tax Asset					
Net Operating Losses	**$**	**345,510.**	$	201,628.	
Adjustment of Goodwill		**196,069.**		100,800.	
Research & Development Credits		**346,643.**		9,829.	
Valuation allowance		**(371,820)**		(220,268)	
Total Deferred Tax Assets		**516,402.**		91,989.	
Deferred Tax Liability					
Depreciation		**(271,058)**		(243,864)	
Total Deferred Tax Liability	**$**	**(271,058)**	$	(243,864)	

Deferred taxes are recognized for temporary differences between the bases of assets and liabilities for financial statement and income tax purposes. The differences
relate primarily to depreciable assets (using accelerated depreciation methods for income tax purposes). The Company's adjustment to Goodwill in 2004 and 2006 created
a deferred tax asset, which although has an indefinite life, has been fully reserved for as realization of its benefit is unlikely.

The Company has net operating loss carry forwards of approximately $144,051 and $508,813 for Federal and State tax purposes respectively. These net operating loss carry
forwards may be used to reduce federal and state taxable income and tax liabilities in future years and expire in various years through June 30, 2019 and June 30, 2011 for
Federal and State tax purposes, respectively. In addition, the Company has Research and Development Tax Credits for State tax purposes of approximately $329,643 which
expires in various years through June 30, 2019.

The Company's provision for income taxes differs from applying the statutory U.S. federal income tax rate to the income before income taxes. The primary differences
result from providing for state income taxes, generation of allowable tax credits and from deducting certain expenses for financial statement purposes but not for federal
income tax purposes.

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A reconciliation between taxes computed at the federal statutory rate and the consolidated effective tax rate follows:

	June 30,				
	2006 .			2005 .	
Federal statutory tax rate	**(34.0)**	**%**		34.0	%
State income tax - net of federal tax benefit	**(4.5)**			3.2	
R & D credits	**(7.8) .**			-	
Adjustment to prior year accrual for income tax	**.-.**			(8.2)	
Permanent and other differences	**8.9. .**			0.9	
	(37.4)	**%**		29.9	%

11. STOCK OPTIONS AND AWARDS

On February 22, 2000 the Board of Directors approved an option plan that granted each active director 2,000 options for each meeting attended, awarded at the annual meeting at the 5-day market price average.

The following options were awarded to the Board of Directors under this plan:

Issuance Date	Options Issued	Exercise Price	Expiration Date	Options Exercised
Oct 24, 2000	62,000	$0.55	Oct 23, 2005	23,700
Nov 14, 2001	64,000	$1.11	Nov 13, 2006	-
Nov 13, 2002	80,000	$0.45	Nov 13, 2007	-
Nov 19, 2003	52,000	$1.10	Nov 19, 2008	-
	56,000	$2.10		-

Nov 17, 2004			Nov 17, 2009	
Nov 16, 2005	62,000	$0.95	Nov 16, 2010	-

There were no other stock option issuances during the 2005 and 2006 fiscal years.

A summary of activity under the plan for the years ending June 30, 2006 and 2005 is as follows:

	Common Stock Options Outstanding	
	Shares	Weighted Average Exercise Price
Balance, June 30, 2004	501,524.	$ 0.94
Granted	56,000.	2.10
Exercised	(30,000)	0.83
Canceled	(5,000)..	0.80
Balance, June 30, 2005	522,524.	$ 1.08
Granted	62,000.	0.95
Exercised	(23,700)..	0.55
Canceled	(158,824)..	1.18
Balance, June 30, 2006	**402,000.**	**$ 1.04**

Following is a summary of the status of options outstanding as of June 30, 2006:

	Outstanding Options .			Exercisable Options .	
Exercise Price Range	Number	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Number	Weighted Average Exercise Price
$0.45 - $0.85	100,000	1.2 years	$0.49	100,000	$0.49
$0.86 - $1.68	246,000	1.9 years	$1.03	246,000	$1.03
$1.69 - $2.10	56,000	3.4 years	$2.10	56,000	$2.10
	402,000	1.9 years	$1.04	402,000	$1.04

PRO FORMA INFORMATION

Prior to January 1, 2006, the Company followed the disclosure only provisions of SFAS No. 123, *Accounting for Stock Based Compensation.* Accordingly, no
compensation expense has been recognized for stock options issued. Had compensation expense for the options which vested in 2006 and 2005 been determined based
on the fair value at the grant date commensurate with the provisions of SFAS No. 123, the Company's net income and net income per share for 2006 and 2005, respectively,

would have been reflected as to the pro forma amounts indicated below:

		2006		2005
Net (Loss) Income:				
As reported	**$**	**(779,377)**	$	269,251
Pro forma		**(809,460)**		209,396
Basic (Loss) Income per Share:				
As reported	**$**	**(0.17)**	$	0.06
Pro forma		**(0.17)**		0.05

The fair value of each option grant is estimated on the date of grant using the Black-Scholes pricing model with the following weighted average assumptions for
grants in 2006 and 2005, respectively: dividend yield of 0% and 0%; expected volatility of 115% and 115%; risk-free interest rate of 5.1% and 4.1%; and expected lives of
5 years in both years.

12. RETIREMENT PLAN

The Company sponsors a qualified 401(k) plan covering substantially all full time employees under which eligible employees can defer a portion of their annual compensation.
The Company determines annually, the amount of matching contributions, which recently has been 25% on 6% of the employees' salary. The Company's matching
contribution made to the plan during the years ended June 30, 2006 and 2005 were $35,094 and $22,929, respectively.

[Missing Graphic Reference]

13. LEASES

There were no material non-cancelable lease terms in excess of one year as of June 30, 2006.

14. EARNINGS PER SHARE

The following table sets forth the computation of earnings per share and earnings per share - assuming dilution:

		2006		2005
Numerator:				
Net (loss) income	**$**	**(779,377)**	$	269,251
Denominator:				
Denominator for earnings per share - weighted average shares outstanding		**4,638,843**		4,614,500
Effect of dilutive securities - stock options		**n/a .**		167,000

Denominator for earnings per share assuming dilution - adjusted weighted average shares outstanding		**4,638,843**		4,781,500
(Loss) Earnings per share	**$**	**(0.17)**	$	0.06
(Loss) Earnings per share - assuming dilution	**$**	**(0.17)**	$	0.06

Common stock equivalents of 402,000 and 355,524 for the years ended June 30, 2006 and 2005, respectively, were not included in computing diluted earnings per share as their effect would be anti-dilutive.

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15. INDUSTRY SEGMENT INFORMATION

The Company operates two primary business segments: (1) Polymer Research and (2) Medical Products.

Products included in the polymer research segment are Aquadapt®, Aquamere®, Aquatrix®, Dermaseal®, Hydromer® Anti-Fog/Condensation Control Coatings,
Hydromer® Lubricious Coatings, Sea-Slide® and T-Hexx® Barrier Dips and Sprays. Research and Development services and all of the Company's royalties, options and
license revenues are reported in this segment.

The medical products segment includes an OEM product line of bipolar coagulation probes, bilary catheters and stents, jejunal and enteral feeding accessories, guidewires,
biofeedback devices for fecal and urinary incontinence and other endoscopic accessories. Service revenues, including coating services and engineering services, are included
in this segment.

Due to the multitude of products offered and the product gross margins, the Company does not track sales volumes by products.

The Company operates globally in its segments with several large customers that are important to their operating results. One such customer accounted for 26% and 23%
of the polymer research segment sales for the 2006 and 2005 fiscal years, respectively. For the medical products segment, the top three customers accounted for 48% and 50%
of that segment's 2006 and 2005 sales, respectively.

The Company evaluates the segments by revenues, total expenses and earnings before income taxes. The Company's assets are not reviewed by business segment.
The accounting policies of these segments are described in the summary of significant accounting policies.

Corporate Overhead, primarily the salaries and fringes of senior management, support services (Accounting, Legal, Human Resources and Purchasing) and other
shared services (Building maintenance and warehousing), is reflected separately from the results of the business segments in the following:

	Polymer Research*	Medical Products	Corporate Overhead	Total
Year Ended June 30, 2006				
Revenue	**$ 4,315,794.**	**$ 3,547,574.**		**$ 7,863,368.**
Expenses	**(3,623,388)**	**(3,761,704)**	**($ 1,484,978)**	**(8,870,070)**
Earnings (Loss) before Income Taxes	**$ 692,406.**	**$ (214,130).**	**($ 1,484,978)**	**$ (1,006,702)..**
Year Ended June 30, 2005				
Revenue	$ 4,878,364.	$ 3,607,640.		$ 8,486,004..

Expenses		(3,536,202)	(3,140,312)	($	430,174)		(8,106,688)
Earnings (Loss) before Income Taxes	$	1,342,162..	$ 467,328.	($	430,174)	$	379,316..

* Excludes the Fiscal 2006 Impairment of Goodwill of $238,172 as such charge-off is not included in the periodic reporting segment evaluations.

Geographic revenues were as follows for the years ended June 30,

	2006	2005
Domestic	**82%**	84%
Foreign	**18%**	16%

16. CONTINGENCIES

Royalty revenues recorded by the Company's are based on the sales of licensee products as reported by the Company's licensees which has the risk of being under- or over-reported. To minimize such risks, the Company's management utilizes its knowledge and understanding of the licensee's business, the market and other pertinent factors in assessing the validity of reported royalties. In addition, the Company has a right to audit the amounts reported.

The Company has not received any claims by licensees for possible overpayment of royalties.

17. SUBSEQUENT EVENTS

In July 2006, the Company renewed its $750,000 revolving line of credit agreement extending the maturity from July 31, 2006 to January 31, 2007.

INDEX TO EXHIBITS

3.a Certificate of Incorporation of the Company, as amended to date

3.b By-Laws of the Company, as amended to date

10.a Minutes of Meeting of the Board of Directors of the Company held on March 5, 1981 with respect to stock options granted to Manfred F. Dyck (Incorporated by reference to Exhibit 10.i to the Registration Statement).

10.b Agreement dated August 11, 1981 between Horizon Concepts, Inc., and the Company (Incorporated by reference to Exhibit 10.c to the Registration Statement).

10.c Agreement dated January 27, 1982 between Reliable Pharmaceutical Company, Inc. and the Company (Incorporated by reference to Exhibit 10.d to the Registration Statement).

10.d License Agreement dated July 14, 1982 between Biosearch Medical Products Inc. and the Company (Incorporated by reference to Exhibit 10.g to the Registration Statement).

10.e Management Services Agreement dated July 14, 1982 between Biosearch Medical Products Inc. and the Company (Incorporated by reference to Exhibit 10.h to the Registration Statement).

10.f Amendment dated October 7, 1982 to Agreement dated January 27, 1982 between Reliable Pharmaceutical Company, Inc. and the Company, together with letter dated October 14, 1982 from Reliable Pharmaceutical Company, Inc. to the Company (Incorporated by reference to Exhibit 10.f to the 1983 Annual Report).

10.g Hydromer Coating agreement dated February 11, 1983 between Pacesetter Systems, Inc. and the Company (Incorporated by reference to Exhibit 10.g to the 1983 Annual Report).

10.h Lease Agreement dated April 5, 1983 between Salem Realty and the Company (Incorporated by reference to Exhibit 10.h to the 1983 Annual Report).

10.i License Agreement dated April 25, 1983 between CardioSearch Inc. and the Company (Incorporated by reference to Exhibit 10.i to the 1983 Annual Report).

10.j Trademark License Agreement dated April 25, 1983 between CardioSearch Inc. and the Company (Incorporated by reference to Exhibit 10.j to the 1983 Annual Report).

10.k Agreement dated August 31, 1983 between Becton, Dickinson & Company and the Company (Incorporated by reference to Exhibit 10.l to the 1983 Annual Report).

10.l Current Report on Form 8-K filed May 30, 1986

10.m Hydromer Coating License Agreement dated September 30, 1984 between Axiom Medical, Inc. and the Company (Incorporated by reference to Exhibit 10.m to the 1984 Annual Report).

10.n 1982 Stock Option Plan of the Company (Incorporated by reference to Exhibit 10.m to the 1983 Annual Report).

10.o Amendment dated June 26, 1984 to Agreement dated August 3, 1983 between Becton, Dickinson & Company and the Company (Incorporated by reference to
Exhibit 10.o to the 1984 Annual Report).

10.p License Agreement dated July 31, 1984 between Kendall Company and the Company (Incorporated by reference to Exhibit 10.p to the 1984 Annual Report).

10.q License Agreement dated March 1, 1985 between Van-Tec Inc. and the Company and Letter of Amendment thereto dated June 13, 1985 (Incorporated by reference
to Exhibit 10.o to the 1985 Annual Report).

10.r Telex dated June 24, 1985 terminating License Agreement with CardioSearch Inc. (Incorporated by reference to Exhibit 10.p to the 1984 Annual Report).

10.s Amendment dated as of December 31, 1984 to Management Services Agreement dated July 14, 1982 between Biosearch Medical Products Inc. and the Company
(Incorporated by reference to Exhibit 10.q to the 1985 Annual Report).

10.t Lease Renewal Agreement dated April 15, 1985 between Salem Realty and the Company (Incorporated by reference to Exhibit 10.r to the 1985 Annual Report).

10.u Lease Agreement dated December 4, 1984 between Biosearch Medical Products Inc. and the Company (Incorporated by reference to Exhibit 10.s to the 1985
Annual Report).

10.v License Agreement dated April 11, 1986 between Axiom Medical, Inc. and the Company (Incorporated by reference to Exhibit 10.i to the 1986 Annual Report).

10.w License Agreement dated September 13, 1985 between U. S. Viggo and the Company (Incorporated by reference to Exhibit 10.c to the 1986 Annual Report).

10.x License Agreement dated March 27, 1986 between Wilkinson Sword Limited and the Company (Incorporated by reference to Exhibit 10.f of the 1986 Annual Report).

10.y Lease Renewal Agreement dated April 15, 1987 between Salem Realty and the Company (Incorporated by reference to Exhibit 10.y to the 1987 Annual Report).

10.z License Agreement dated April 30, 1986 between HPK International and the Company (Incorporated by reference to Exhibit 10.j to the 1986 Annual Report).

10.aa License Agreement dated August 1, 1986 between Film Specialties, Inc. and the Company (Incorporated by reference to Exhibit 10.aa to the 1987 Annual Report).

10.ab Lease Renewal Agreement dated April 15, 1988 between Salem Realty and the Company (Incorporated by reference to Exhibit 10.ab to the 1988 Annual Report).

10.ac License Agreement dated June 30, 1987 between Richards Medical Company and the Company (Incorporated by reference to Exhibit 10.ac to the 1988 Annual Report).

10.ad License Agreement dated December 1, 1987 between Mallinckrodt, Inc. and the Company (Incorporated by reference to Exhibit 10.ad to the 1988 Annual Report).

10.ae Option Agreement dated January 28, 1988 between Cordis Corporation and the Company (Incorporated by reference to Exhibit 10.ae to the 1988 Annual Report).

10.af Lease Agreement dated April 15, 1988 between Biosearch Medical Products Inc. and the Company (Incorporated by reference to Exhibit 10.ag of the 1988 Annual Report).

10.ag Letters dated June 11, 1987 and September 22, 1987 to U. S. Viggo, Inc. modifying License Agreement dated September 13, 1985, to cover only central venous
catheters (Incorporated by reference to Exhibit 10.ag to the 1988 Annual Report).

10.ah Lease Renewal Agreement dated April 15, 1989 between Salem Realty and the Company (Incorporated by reference to Exhibit 10.ah to the 1989 Annual Report).

10.ai Amendment dated October 1, 1988 to License Agreement dated September 13, 1985, between U. S. Viggo and the Company (Incorporated by reference to Exhibit 10.ai to the
1989 Annual Report).

10.aj License Agreement dated October 20, 1988 between Cordis Corp. and the Company (Incorporated by reference to Exhibit 10.aj to the 1989 Annual Report).

10.ak License Agreement dated March 31, 1989 between Cathlab Corp. and the Company (Incorporated by reference to Exhibit 10.ak to the 1989 Annual Report).

10.al Amendment dated December 1, 1988 to License Agreement dated August 1, 1986 between Film Specialties, Inc. and the Company (Incorporated by reference to
Exhibit 10.al to the 1989 Annual Report).

10.am Finders Agreement dated August 20, 1987 between Phoenix Chemical, Inc. and the Company (Incorporated by reference to Exhibit 10.am to the 1989 Annual Report).

10.an License Agreement dated September 10, 1989 between the Stent Division of Schneider and the Company (Incorporated by reference to Exhibit 10.an to the 1990 Annual Report).

10.ao License Agreement dated March 30, 1990 between Cosmo Ikko Company and the Company (Incorporated by reference to Exhibit 10.ao to the 1990 Annual Report).

10.ap License Agreement dated April 12, 1990 between Interventional Therapeutics, Inc. and the Company and amendment dated May 7, 1990 to the Agreement dated April 12, 1990 between Interventional Therapeutics, Inc. and the Company (Incorporated by reference to Exhibit 10.ap to the 1990 Annual Report).

10.aq Amended License Agreement dated January 1, 1990 between the Wilkinson Sword group of companies and the Company (Incorporated by reference to Exhibit 10.aq the 1990 Annual Report).

10.ar Lease Agreement dated April 15, 1990 between Salem Realty and the Company (Incorporated by reference to Exhibit 10.ar to the 1990 Annual Report).

10.as Amendment to the Agreement dated July 31, 1984 between Kendall Company and the Company (Incorporated by reference to Exhibit 10.as to the 1990 Annual Report).

10.at License Agreement dated January 11, 1991 between Biosearch Medical Products Inc. and the Company (Incorporated by reference to Exhibit 10.at to the 1991 Annual Report).

10.au License Agreement dated May 16, 1991 between I E Sensors and the Company (Incorporated by reference to Exhibit 10.au to the 1991 Annual Report).

10.av Lease Renewal Agreement dated April 15, 1991 between Salem Realty and The Company (Incorporated by reference to Exhibit 10.av to the 1991 Annual Report).

10.aw License Agreement dated July 25, 1991 between Johnson & Johnson Orthopaedics and the Company (Incorporated by reference to Exhibit 10.aw to the 1992 Annual Report).

10.ax License Agreement dated August 19, 1991 between Navarre Laboratories Ltd. and the Company (Incorporated by reference to Exhibit 10.ax to the 1992 Annual Report).

10.ay Amended License Agreement dated September 15, 1991 between Boston Scientific Corp. and the Company (Incorporated by reference to Exhibit 10.ay to the 1992 Annual Report).

10.az Option/License Agreement dated September 23,1991 between Elan Corp. PLC and the Company (Incorporated by reference to Exhibit 10.az to the 1992 Annual Report).

10.ba Lease Agreement dated November 1, 1991 between Morton Street Realty and the Company (Incorporated by reference to Exhibit 10.ba to the 1992 Annual Report).

10.bb License Agreement dated August 17, 1992 between SCIMED Peripheral Interventions, division of SCIMED Life Systems, Inc. and the Company. (Incorporated by reference to Exhibit 10.bb to the 1993 Annual Report).

10.bc License Agreement dated March 9, 1993 between Arrow International, Inc. and the Company. (Incorporated by reference to Exhibit 10.bc to the 1993 Annual Report).

10.bd License Agreement dated April 28, 1993 between St. Jude Medical, Inc. and the Company. (Incorporated by reference to Exhibit 10.bd to the 1993 Annual Report).

10.be License Agreement dated November 11, 1993 between Katoh Hatsujyo Kaisha, Ltd. and the Company. (Incorporated by reference to Exhibit 10.be to the 1994 Annual Report).

10.bf Lease Agreement dated June 9, 1995 between Salem Realty and the Company (Incorporated by reference to Exhibit 10.bf to the 1995 Annual Report).

10.bg Amendment dated September 20, 1995 to License Agreement dated April 28, 1993 between St. Jude Medical, Inc. and the Company. (Incorporated by reference to Exhibit 10.bg to the 1996 Annual Report).

10.bh License Agreement dated April 12, 1990 between Interventional Therapeutics and the Company was terminated effective December 22, 1995. (Incorporated by reference to Exhibit 10.bh to the 1996 Annual Report).

10.bi License Agreement dated May 16, 1991 between I E Sensors and the Company was terminated effective December 31, 1995. (Incorporated by reference to Exhibit 10.bi to the 1996 Annual Report).

10.bj Consented to the assignment of license agreement dated April 28,1993 between St. Jude Medical, Inc. and the Company to CR Bard dated January 18, 1996. (Incorporated by reference to Exhibit 10.bj to the 1996 Annual Report).

10.bk License Agreement dated April 30, 1986 between HPK International and the Company was terminated effective February 19, 1996. (Incorporated by reference to Exhibit 10.bk to the 1996 Annual Report).

10.bl License Agreement dated June 6, 1996 between Biosearch Medical Products Inc. and the Company. (Incorporated by reference to Exhibit 10.bl to the 1996 Annual Report).

10.bm License Agreement dated August 1, 1996 between Biosearch Medical Products Inc. and the Company.

10.bn Amended License Agreement dated September 4, 1996 between SCIMED (Boston Scientific Corporation) and the Company.

10.bo License Agreement dated January 6, 1997 between Sherwood Davis & Geck and the Company.

10.bp Use permit for certain designated area dated May 4, 1997 between Biosearch Medical Products Inc. and the Company

10.bq Contract of sale between Biosearch Medical Products and the Company for the sale of 35 Industrial Parkway dated 3/31/98

10.br Note and mortgage with PNC Bank dated 6/12/98

10.bs 3 year lease agreement with Biosearch Medical Products dated 6/12/98 for 35 Industrial Parkway

10.bt License of technology, supply and stock purchase agreement with C.R.Bard dated 2/25/99

10.bu Trademark and technology license agreement with AST dated 3/9/99

10.bv License of two gel patents from Ridge Scientific dated 11/1/98

10.bw License and Supply agreement with Gallini SRL dated 6/28/00

10.bx Standstill agreement with license option with IMED Pharma Inc. dated 3/30/00

10.by License of technology with Symbiotech Medical Inc. dated 3/28/00

10.bz License and supply agreement with TP Orthodontics Inc. dated 3/30/00

10.ca License Agreement dated July 1, 2000 between Becton Dickinson and Company, Inc. and the Company.

10.cb License Agreement dated January 1, 2001 between LHS Limited and LHS Holding Limited, English dba KLEENCARE and the Company.

10.cc License Agreement dated April 17, 2001 between Tyco Healthcare Group LP and the Company.

10.cd Construction Contract dated April 19, 2001 between REDCO Engineering & Construction Corp and the Company.

10.ce Service Agreement dated April 23, 2001 between Tyco Healthcare Group LP and the Company.

10.cf Loan Agreement dated June 7, 2001 between New Millenium Bank and the Company.

10.cg By-Laws Articles of Incorporation.

10.ch Loan Agreement dated June 30, 2005 between Wachovia Bank, N.A. and the Company.

24. Power of Attorney (see "Power of Attorney" in the Annual Report on Form 10-KSB).

31.1 Certification of Manfred F. Dyck, Chief Executive Officer, pursuant to Securities Exchange Act Rule 13a-14(a).

31.2 Certification of Robert Y. Lee, Chief Financial Officer, pursuant to Securities Exchange Act Rule 13a-14(a).

32.1 Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, signed by Manfred F. Dyck, Chief Executive Officer of Hydromer, Inc.

32.2 Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, signed by Robert Y. Lee, Chief Financial Officer of Hydromer, Inc.

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