

ABERDEEN AUSTRALIA EQUITY FUND INC
 Form 497
 December 09, 2010
PROSPECTUS SUPPLEMENT

(To Prospectus dated December 8, 2010)

2,500,000 Shares

Aberdeen Australia Equity Fund, Inc.

Common Stock
\$12.50 per Share

Aberdeen Australia Equity Fund, Inc. (the "Fund") is offering for sale 2,500,000 shares of its common stock ("Common Shares"). The Fund is a non-diversified, closed-end management investment company. The Fund's principal investment objective is long-term capital appreciation through investment primarily in equity securities of Australian companies listed on the Australian Stock Exchange Limited. The Fund's secondary investment objective is current income. There can be no assurance that the Fund will achieve its investment objectives.

The Fund's currently outstanding Common Shares are, and the Common Shares offered by this Prospectus Supplement and the accompanying Prospectus will be, subject to notice of issuance, listed on the NYSE Amex ("Amex") under the symbol "IAF." The last reported sale price for the Fund's Common Shares on December 8, 2010 was \$12.94 per share. The net asset value of the Fund's Common Shares at the close of business on December 8, 2010 was \$11.67 per share.

You should review the information set forth under "Risks and Special Considerations" on page 17 of the accompanying Prospectus before investing in the Fund's Common Shares.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved these securities or determined if this Prospectus Supplement or the accompanying Prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

	Per Share		Total (1)	
Public offering price	\$	12.50	\$	31,250,000
Sales load (underwriting discounts and commissions)	\$	0.50	\$	1,250,000
Proceeds, before expenses, to the Fund(2)	\$	12.00	\$	30,000,000

(1) The Fund has granted the underwriters an option to purchase up to an additional 375,000 Common Shares, within 45 days after the date of this Prospectus Supplement, at the public offering price, less the sales load, solely to cover over-allotments, if any. If the over-allotment option is exercised in full, the total public offering price would be \$35,937,500, the total sales load would be \$1,437,500 and the total proceeds, before expenses, to the Fund would be \$34,500,000.

(2) The aggregate expenses of the offering (excluding sales load) are estimated to be \$273,300.

The underwriters expect to deliver the Common Shares on or about December 14, 2010.

Citi Morgan Stanley

The date of this Prospectus Supplement is December 9, 2010.

You should rely only on the information contained in or incorporated by reference into this Prospectus Supplement and the accompanying Prospectus. This Prospectus Supplement and the accompanying Prospectus set forth certain information about the Fund that a prospective investor should carefully consider before deciding whether to invest in the Fund's Common Shares. This Prospectus Supplement, which describes the specific terms of this offering, also adds to and updates information contained in the accompanying Prospectus and the documents incorporated by reference into the accompanying Prospectus. The accompanying Prospectus gives more general information, some of which may not apply to this offering. If the description of this offering varies between this Prospectus Supplement and the accompanying Prospectus, you should rely on the information contained in this Prospectus Supplement; provided that if any statement in one of these documents is inconsistent with a statement in another document having a later date and incorporated by reference into the accompanying Prospectus or Prospectus Supplement, the statement in the incorporated document having a later date modifies or supersedes the earlier statement. Neither the Fund nor the underwriters have authorized anyone to provide you with different information. If anyone provides you with different or inconsistent information, you should not rely on it. The Fund is not making an offer to sell these securities in any jurisdiction where the offer or sale is not permitted. The information contained in or incorporated by reference into this Prospectus Supplement and the accompanying Prospectus is accurate only as of the respective dates on their front covers, regardless of the time of delivery of this Prospectus Supplement, the accompanying Prospectus, or the sale of the Common Shares. The Fund's business, financial condition, results of operations and prospects may have changed since those dates.

TABLE OF CONTENTS

Prospectus Supplement

	Page
CAUTIONARY NOTICE REGARDING FORWARD-LOOKING STATEMENTS	S-1
PROSPECTUS SUPPLEMENT SUMMARY	S-2
DISTRIBUTIONS	S-4
PORTFOLIO INVESTMENTS	S-4
SUMMARY OF FUND EXPENSES	S-5
USE OF PROCEEDS	S-5
CAPITALIZATION	S-6
UNDERWRITING	S-6
LEGAL MATTERS	S-9
ADDITIONAL INFORMATION	S-9

Prospectus

PROSPECTUS SUMMARY	3
SUMMARY OF FUND EXPENSES	10
FINANCIAL HIGHLIGHTS	11
USE OF PROCEEDS	12
THE FUND	13
DESCRIPTION OF SHARES	13
INVESTMENT OBJECTIVES	14
INVESTMENT POLICIES	14
INVESTMENT RESTRICTIONS	17

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RISKS AND SPECIAL CONSIDERATIONS	17
MANAGEMENT OF THE FUND	23
EXPENSES	28
DIVIDENDS AND DISTRIBUTIONS	28
DIVIDEND REINVESTMENT AND DIRECT STOCK PURCHASE PLAN	29
TAXATION	29
CERTAIN PROVISIONS OF THE MARYLAND GENERAL CORPORATION LAW AND THE CHARTER AND BYLAWS	31
PLAN OF DISTRIBUTION	32
LEGAL PROCEEDINGS	34
TABLE OF CONTENTS OF STATEMENT OF ADDITIONAL INFORMATION	35
APPENDIX A	A-1

You should read this Prospectus Supplement and the accompanying Prospectus before deciding whether to invest and retain them for future reference. A Statement of Additional Information, dated December 8, 2010 ("SAI"), as supplemented from time to time, containing additional information about the Fund, has been filed with the Securities and Exchange Commission ("SEC") and is incorporated by reference in its entirety into this Prospectus Supplement. You may request a free copy of the SAI or request other information about the Fund (including the Fund's annual and semi-annual reports to shareholders) or make shareholder inquiries by calling 1-866-839-5205, emailing InvestorRelations@aberdeen-asset.com or by writing to the Fund at 1735 Market Street, 32nd Floor, Philadelphia, Pennsylvania 19103. The Fund's SAI, as well as the annual and semi-annual reports to shareholders, are also available at the Fund's website at www.aberdeeniaf.com. You may also obtain copies of these documents (and other information regarding the Fund) from the SEC's website (<http://www.sec.gov>).

CAUTIONARY NOTICE REGARDING FORWARD-LOOKING STATEMENTS

This Prospectus Supplement, the accompanying Prospectus and the SAI contain "forward-looking statements." Forward-looking statements can be identified by the words "may," "will," "intend," "expect," "estimate," "continue," "plan," "anticipate," and similar terms and the negative of such terms. By their nature, all forward-looking statements involve risks and uncertainties, and actual results could differ materially from those contemplated by the forward-looking statements. Several factors that could materially affect the Fund's actual results are the performance of the portfolio of securities the Fund holds, the price at which the Fund's shares will trade in the public markets and other factors discussed in the Fund's periodic filings with the SEC.

Although the Fund believes that the expectations expressed in the forward-looking statements are reasonable, actual results could differ materially from those projected or assumed in such forward-looking statements. The Fund's future financial condition and results of operations, as well as any forward-looking statements, are subject to change and are subject to inherent risks and uncertainties, such as those disclosed in the "Risks and Special Considerations" section of the accompanying Prospectus. All forward-looking statements contained in or incorporated by reference into this Prospectus Supplement or the accompanying Prospectus are made as of the date of this Prospectus Supplement or the accompanying Prospectus, as the case may be. Except for the Fund's ongoing obligations under the federal securities laws, it does not intend, and it undertakes no obligation, to update any forward-looking statements. The forward-looking statements contained in this Prospectus Supplement, the accompanying Prospectus and the SAI are excluded from the safe harbor protection provided by Section 27A of the Securities Act of 1933, as amended.

PROSPECTUS SUPPLEMENT SUMMARY

The following information is only a summary. You should consider the more detailed information contained in this Prospectus Supplement, the accompanying Prospectus, dated December 8, 2010, and the SAI, dated December 8, 2010, especially the information under "Risks and Special Considerations" on page 17 of the accompanying Prospectus.

The Fund

The Fund is a non-diversified, closed-end management investment company organized as a Maryland corporation.

The Fund's principal investment objective is long-term capital appreciation. Its secondary objective is current income, which is expected to be derived primarily from dividends and interest on Australian corporate and governmental securities.

The Fund will normally invest at least 80% of its net assets, plus the amount of any borrowings for investment purposes, in equity securities, consisting of common stock, preferred stock and convertible stock, of Australian companies listed on the Australian Stock Exchange Limited. For these purposes, Australian companies means companies that are tied economically to Australia. The Fund may invest up to 10% of its total assets in unlisted equity securities. It may also invest in debt securities issued by Australian companies, Australian Federal and State governments and the U.S. government. Such debt securities will be rated in one of the four highest rating categories by a nationally recognized statistical rating organization or, if unrated, determined to be of comparable quality by the Investment Manager (as defined), and will typically have a maturity of 10 years or less. The Fund's investments in any one industry or group of industries are generally limited to 25% of its total assets, except that it may invest between 25% and 35% of its total assets in securities of an industry group that, at the time of investment, represents 20% or more of the S&P/ASX 200 Accumulation Index. The Fund has authority to engage in options transactions, to enter into repurchase agreements, and to lend its portfolio securities. See "Investment Policies" in the accompanying Prospectus.

The Fund's Common Shares are listed for trading on the Amex under the symbol "IAF." As of December 8, 2010, the net assets of the Fund were \$224,933,443 and the Fund had outstanding 19,277,602 Common Shares. The last reported sale price of the Fund's Common Shares, as reported on the Amex on December 8, 2010 was \$12.94 per share. The net asset value of the Fund's Common Shares at the close of business on December 8, 2010 was \$11.67 per share.

Investment Manager and Investment Adviser

The Fund's investment manager is Aberdeen Asset Management Asia Limited ("Investment Manager"), a Singapore corporation located at 21 Church Street, #01-01 Capital Square Two, Singapore 049480. The Investment Manager serves as investment manager to both equity and fixed income investment portfolios for a range of clients. The Investment Manager, in accordance with the Fund's stated investment objectives, policies and limitations and subject to the supervision of the Fund's Board of Directors, manages the Fund's investments and makes investment decisions on behalf of the Fund, including the

selection of, and being responsible for the placement of orders with, brokers and dealers to execute the Fund's portfolio transactions.

The Fund's investment adviser is Aberdeen Asset Management Limited ("Investment Adviser"), an Australian corporation affiliated with the Investment Manager. The Investment Adviser is located at Level 6, 201 Kent Street, Sydney, NSW 2000, Australia. The Investment Adviser's principal business focus is to provide investment management services with regard to equity and fixed income investments in Australian securities. The Investment Adviser makes recommendations to the Investment Manager as to specific portfolio securities to be purchased, retained or sold by the Fund and provides or obtains such research and statistical data as may be necessary in connection therewith.

The Investment Adviser is a wholly-owned subsidiary of the Investment Manager. The Investment Manager is a wholly-owned subsidiary of Aberdeen Asset Management PLC, a Scots company, that is the parent company of an asset management group managing approximately \$261.18 billion of assets as of August 31, 2010 for both institutions and private individuals from offices around the world. See "Management of the Fund The Investment Manager and the Investment Adviser" in the accompanying Prospectus.

The Offering

Common Shares Being Offered:	2,500,000shares
Common Shares To Be Outstanding After Offering:	21,777,602shares

The number of Common Shares offered and outstanding after the offering assumes the underwriters' over-allotment option is not exercised. If the over-allotment option is exercised in full, the Fund will issue an additional 375,000 Common Shares and will have 22,152,602 Common Shares outstanding after the offering.

The Fund's Common Shares have recently traded at a premium to net asset value ("NAV") per share and the price of the Common Shares being offered is expected to be above net asset value per share. Shares of closed-end investment companies, such as the Fund, frequently trade at a price below their NAV. The Fund cannot predict whether its Common Shares will trade at a premium or a discount to NAV.

Use of Proceeds

The Fund intends to invest the net proceeds of the offering in accordance with its investment objectives and policies as stated in the accompanying Prospectus. It is currently anticipated that the Fund will be able to invest substantially all of the net proceeds of the offering in accordance with its investment objectives and policies within approximately 60 days after completion of the offering. Pending such investment, the Fund anticipates investing the proceeds in short-term securities issued by the U.S. government or its agencies or instrumentalities or in high quality, short-term or long-term debt obligations or money market instruments.

Risks and Special Considerations

See "Risks and Special Considerations" beginning on page 17 of the accompanying Prospectus for a discussion of factors you should consider carefully before deciding to invest in the Fund's Common Shares.

DISTRIBUTIONS

The Board of Directors of the Fund has implemented a managed distribution policy of paying quarterly distributions at an annual rate, set once a year, that is a percentage of the rolling average of the Fund's four quarter-end net asset values. The current rolling distribution rate is 10%. This policy is subject to regular review by the Fund's Board of Directors. The distributions are made from current income, supplemented by realized capital gains and, to the extent necessary, paid-in capital. Persons who purchase Common Shares in this offering will be entitled to any regular quarterly distributions the record date for which occurs after the Common Shares are purchased. On December 8, 2010, the Board of Directors of the Fund declared a quarterly distribution of 28 cents per Common Share, payable on January 14, 2011 to all shareholders of record as of December 30, 2010.

The amounts of the last four distributions paid by the Fund are as set out below:

Payment Date	Distribution per Common Share
October 15, 2010	\$ 0.27
July 16, 2010	\$ 0.27
April 16, 2010	\$ 0.25
January 15, 2010	\$ 0.22

See "Dividends and Distributions" in the accompanying Prospectus.

PORTFOLIO INVESTMENTS

As of October 31, 2010, the Fund's top ten equity holdings (based on total assets) by issuer were:

Issuer	Percent of Total Assets
BHP Billiton limited	13.3%
QBE Insurance Group limited	7.5%
Rio Tinto Limited	7.2%
Commonwealth Bank of Australia Limited	6.5%
Woolworths Limited	5.8%
Westpac Banking Corporation Limited	5.6%
Australia & New Zealand Banking Group Limited	5.4%
Westfield Group	4.6%
AGL Energy Limited	4.5%
Woodside Petroleum Limited	4.2%
Total	64.6%

Holdings are subject to change and are provided for informational purposes only and should not be deemed a recommendation to buy or sell the securities shown.

As of October 31, 2010, the Fund held 96.3% of its net assets in equities, 0.4% in a short-term investment and 3.3% in other types of assets.

SUMMARY OF FUND EXPENSES

The following table and example are intended to assist you in understanding the various costs and expenses directly or indirectly associated with investing in Common Shares of the Fund. Some of the percentages indicated in the table below are estimates and may vary.

Shareholder Transaction Expenses	
Sales Load (underwriting discounts and commissions) (as a percentage of offering price)	4.0%
Offering Expenses Borne by the Fund (as a percentage of offering price)	0.88%
Dividend Reinvestment and Cash Purchase Plan Fees(1)	
Annual Operating Expenses (as a percentage of average net assets attributable to the Fund's Common Shares)	
Management Fee	0.82%
Other Expenses(2)(3)	0.46%
Total Annual Operating Expenses	1.28%

(1) If you participate in the Dividend Reinvestment and Direct Stock Purchase Plan sponsored and administered by Computershare Trust Company, N.A., you will be subject to any fees imposed by Computershare Trust Company, N.A.

(2) "Other Expenses" have been estimated for the current fiscal year.

(3) Includes an administration fee of 0.08% of average net assets attributable to the Fund's Common Shares.

Example

An investor would pay the following expenses on a \$1,000 investment in the Fund, assuming (1) Total Annual Operating Expenses of 1.28%, (2) a Sales Load of \$40 and estimated offering expenses of \$8.75 and (3) a 5% annual return:

	One Year	Three Years	Five Years	Ten Years
\$	61	\$ 87	\$ 116	\$ 196

The "Example" assumes that all dividends and other distributions are reinvested at net asset value and that the percentage amounts listed in the table above under Total Annual Operating Expenses remain the same in the years shown. The above table and example and the assumption in the example of a 5% annual return are required by regulations of the SEC that are applicable to all investment companies; the assumed 5% annual return is not a prediction of, and does not represent, the projected or actual performance of the Fund's Common Shares.

The example should not be considered a representation of past or future expenses, and the Fund's actual expenses may be greater than or less than those shown. Moreover, the Fund's actual rate of return may be greater or less than the hypothetical 5% return shown in the example.

USE OF PROCEEDS

The Fund estimates the net proceeds from this offering will be approximately \$29,726,700 (or \$34,226,700 if the underwriters exercise their over-allotment option to purchase additional Common Shares in full), after deducting the sales load and estimated offering expenses payable by the Fund.

The Fund intends to invest the net proceeds of the offering in accordance with its investment objectives and policies as stated in the accompanying Prospectus. It is currently anticipated that the Fund will be able to invest

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substantially all of the net proceeds of the offering in accordance with its investment objectives and policies within approximately 60 days after completion of the offering. Pending such investment, the Fund anticipates investing the proceeds in short-term securities issued by the U.S. government or its agencies or instrumentalities or in high quality, short-term or long-term debt obligations or money market instruments.

CAPITALIZATION

The following table sets forth the unaudited capitalization of the Fund as of October 31, 2010 (i) on an actual basis and (ii) and as adjusted to reflect the effects of the sale of 2,500,000 Common Shares in this offering at an offering price of \$12.50 per share.

	As of October 31, 2010 (unaudited)	
	Actual	As Adjusted
Composition of Net Assets:		
Common stock, par value \$.01 per share, 30,000,000 shares authorized (19,277,602 shares issued and outstanding as of October 31, 2010, 21,777,602 shares issued and outstanding as adjusted)(1)(2)	\$ 192,776	\$ 217,776
Paid-in capital in excess of par(2)	139,094,206	168,795,906
Distributions in excess of net investment income	(13,517,041)	(13,517,041)
Accumulated net realized gain on investment transactions	6,079,827	6,079,827
Accumulated net realized foreign exchange gains	14,672,714	14,672,714
Net unrealized appreciation on investments	76,658,595	76,658,595
Net unrealized foreign exchange loss	(8,280)	(8,280)
Net Assets	\$ 223,172,797	\$ 252,899,497

(1) The Fund does not hold any of these outstanding shares for its account.

(2) As adjusted, additional paid-in capital reflects the issuance of Common Shares offered hereby (\$31,250,000), less \$0.01 par value per Common Share (\$25,000), less the estimated offering expenses borne by the Fund (\$1,523,300) related to the issuance of shares.

UNDERWRITING

Citigroup Global Markets Inc. and Morgan Stanley & Co. Incorporated are acting as representatives of the underwriters (the "Underwriters") named below. Subject to the terms and conditions stated in the underwriting agreement, dated the date of this Prospectus Supplement, each Underwriter named below has agreed to purchase, and the Fund has agreed to sell to that Underwriter, the number of Common Shares set forth opposite the Underwriter's name.

Name of Underwriter	Number of Common Shares
Citigroup Global Markets Inc.	1,250,000
Morgan Stanley & Co. Incorporated	1,250,000
Total	2,500,000

The underwriting agreement provides that the obligations of the Underwriters to purchase the Common Shares included in this offering are subject to approval of legal matters by counsel and to other conditions. The Underwriters are obligated to purchase all the Common Shares (other than those covered by the over-allotment option described below) if they purchase any of the Common Shares. The Underwriters propose to offer some of the Common Shares directly to the public at the public offering price set forth on the cover page of this Prospectus Supplement and some of the Common Shares to dealers at the public offering price less a concession not to exceed \$0.30 per Common Share. The sales load the Fund will pay of \$0.50 per Common Share is equal to

4.0% of the public offering price. The Underwriters may allow, and the dealers may reallow, a concession not to exceed \$0.10 per Common Share on sales to other dealers. If all of the Common Shares are not sold at the public offering price, the representatives may change the public offering price and other selling terms. Investors must pay for any Common Shares purchased on or before December 14, 2010. The representatives have advised the Fund that the Underwriters do not intend to confirm any sales to any accounts over which they exercise discretionary authority.

The Fund has granted to the Underwriters an option, exercisable for 45 days from the date of this Prospectus Supplement, to purchase up to an additional 375,000 Common Shares at the public offering price per Common Share, less the sales load. The underwriters may exercise this option solely for the purpose of covering over-allotments, if any, in connection with this offering. To the extent the option is exercised, each Underwriter will be obligated, subject to certain conditions, to purchase a number of additional Common Shares approximately proportionate to such Underwriter's initial purchase commitment.

The Fund's currently outstanding Common Shares are, and the Common Shares offered by this Prospectus Supplement and the accompanying Prospectus will be, subject to notice of issuance, listed on the Amex under the trading or "ticker" symbol "IAF."

The Fund, the Investment Manager and the Investment Adviser have agreed that the Fund will not, without the prior written consent of Citigroup Global Markets Inc. and Morgan Stanley & Co. Incorporated, offer, sell, contract to sell, pledge, or otherwise dispose of, or enter into any transaction which is designed to, or might reasonably be expected to, result in the disposition (whether by actual disposition or effective economic disposition due to cash settlement or otherwise) by the Fund or any affiliate of the Fund or any person in privity with the Fund, directly or indirectly, including the filing (or participation in the filing) of a registration statement with the SEC in respect of, or establish or increase a put equivalent position or liquidate or decrease a call equivalent position within the meaning of Section 16 of the Securities Exchange Act of 1934, as amended, any other Common Shares or any securities convertible into, or exercisable, or exchangeable for, Common Shares; or publicly announce an intention to effect any such transaction for a period of 150 days after the date of the underwriting agreement. In the event that either: (a) during the last 17 days of the 150-day period referred to above, the Fund issues an earnings release or material news or material event relating to the Fund; or (b) prior to the expiration of such 150-day period, the Fund announces that it will release earning results during the 16-day period beginning on the last day of such 150-day period, the restrictions described above shall continue to apply until the expiration of the 18-day period beginning on the date of the earnings release or the occurrence of the material news or material event, as applicable.

The following table shows the sales load that the Fund will pay to the Underwriters in connection with this offering. These amounts are shown assuming both no exercise and full exercise of the Underwriters' option to purchase additional Common Shares.

	Paid by the Fund	
	No Exercise	Full Exercise
Per Share	\$ 0.50	\$ 0.50
Total	\$ 1,250,000	\$ 1,437,500

In connection with the offering, one or more of the Underwriters may purchase and sell Common Shares in the open market. These transactions may include short sales, syndicate covering transactions and stabilizing transactions. Short sales involve syndicate sales of Common Shares in excess of the number of Common Shares to be purchased by the Underwriters in the offering, which creates a syndicate short position. "Covered" short sales are sales of shares made in an amount up to the number of Common Shares represented by the Underwriters' over-allotment option. In determining the source of Common Shares to close out the covered syndicate short position, the Underwriters will consider, among other things, the price of Common Shares available for purchase in the open market as compared to the price at which they may purchase Common Shares through the over-allotment option. Transactions to close out the covered syndicate short involve either purchases

of Common Shares in the open market after the distribution has been completed or the exercise of the over-allotment option. The Underwriters may also make "naked" short sales of Common Shares in excess of the over-allotment option. The Underwriters must close out any naked short position by purchasing Common Shares in the open market. A naked short position is more likely to be created if the Underwriters are concerned that there may be downward pressure on the price of the Common Shares in the open market after pricing that could adversely affect investors who purchase in the offering. Stabilizing transactions consist of bids for or purchases of Common Shares in the open market while the offering is in progress.

The Underwriters may also impose a penalty bid. Penalty bids permit the Underwriters to reclaim a selling concession from a syndicate member when the representatives repurchase Common Shares originally sold by that syndicate member in order to cover syndicate short positions or make stabilizing purchases.

Any of these activities may have the effect of preventing or retarding a decline in the market price of the Common Shares. They may also cause the price of the Common Shares to be higher than the price that would otherwise exist in the open market in the absence of these transactions. The Underwriters may conduct these transactions on the Amex or in the over-the-counter market, or otherwise. If the Underwriters commence any of these transactions, they may discontinue them at any time.

A Prospectus Supplement and accompanying Prospectus in electronic format may be made available on the websites maintained by one or more of the Underwriters. Other than this Prospectus Supplement and the accompanying Prospectus in electronic format, the information on any such Underwriter's website is not part of this Prospectus Supplement or the accompanying Prospectus. The representatives may agree to allocate a number of Common Shares to the Underwriters for sale to their online brokerage account holders. The representatives will allocate Common Shares to Underwriters that may make Internet distributions on the same basis as other allocations. In addition, Common Shares may be sold by the Underwriters to securities dealers who resell Common Shares to online brokerage account holders.

The Fund anticipates that from time to time certain of the Underwriters may act as brokers or dealers in connection with the execution of the Fund's portfolio transactions after they have ceased to be Underwriters and, subject to certain restrictions, may act as brokers while they are Underwriters. Certain Underwriters have performed investment banking and advisory services for the Investment Manager and the Investment Adviser and their affiliates from time to time, for which they have received customary fees and expenses. Certain Underwriters may, from time to time, engage in transactions with or perform services for the Investment Manager and the Investment Adviser and their affiliates in the ordinary course of business.

The Fund, the Investment Manager and the Investment Adviser each have agreed to indemnify the Underwriters against certain liabilities, including liabilities under the Securities Act of 1933, as amended (the "Securities Act"), or to contribute to payments the Underwriters may be required to make because of any of those liabilities.

Total underwriting compensation determined in accordance with Financial Industry Regulatory Authority ("FINRA") rules is summarized as follows. The sales load the Fund will pay of \$0.50 per share is equal to 4.0% of gross proceeds.

The principal business address of Citigroup Global Markets Inc. is 388 Greenwich Street, New York, NY 10013. The principal business address of Morgan Stanley & Co. Incorporated is 1585 Broadway, New York, New York 10036.

No action has been taken in any jurisdiction (except in the United States) that would permit a public offering of Common Shares, or the possession, circulation or distribution of this Prospectus Supplement and the accompanying Prospectus or any other material relating to the Fund or the Common Shares in any jurisdiction where action for that purpose is required. Accordingly, Common Shares may not be offered or sold, directly or indirectly, and neither this Prospectus Supplement and the accompanying Prospectus nor any other offering material or advertisements in connection with the Common Shares may be distributed or published, in or from

any country or jurisdiction except in compliance with the applicable rules and regulations of any such country or jurisdiction.

Director Ownership of Underwriter Securities

As of the date of this Prospectus Supplement, Brian Sherman, a director of the Fund, beneficially owns approximately \$7 million of debt securities issued by Citigroup Global Markets Inc. or an entity directly or indirectly controlling, controlled by, or under common control with, Citigroup Global Markets Inc. and approximately \$7 million of debt securities issued by Morgan Stanley & Co. Incorporated or an entity directly or indirectly controlling, controlled by, or under common control with, Morgan Stanley & Co. Incorporated. These holdings represent a de minimis amount of the total outstanding debt of the respective parent companies of such Underwriters. As a result of such beneficial ownership, Mr. Sherman will be treated as an "interested person" (as that term is defined in Section 2(a)(19) of the 1940 Act) of the Fund, during and until the completion of this offering.

LEGAL MATTERS

Certain legal matters will be passed on by Willkie Farr & Gallagher LLP, 787 Seventh Avenue, New York, New York 10019, counsel to the Fund, in connection with the offering of the Common Shares. Certain legal matters in connection with this offering will be passed upon for the Underwriters by Simpson Thacher & Bartlett LLP, 425 Lexington Avenue, New York, New York 10017. Willkie Farr & Gallagher LLP and Simpson Thacher & Bartlett LLP will rely as to matters of Maryland law on the opinion of Venable LLP, Two Hopkins Plaza, Suite 1800, Baltimore, Maryland 21201-2978.

ADDITIONAL INFORMATION

This Prospectus Supplement and the accompanying Prospectus constitute part of a Registration Statement filed by the Fund with the SEC under the Securities Act and the Investment Company Act of 1940, as amended. This Prospectus Supplement and the accompanying Prospectus omit certain of the information contained in the Registration Statement, and reference is hereby made to the Registration Statement and related exhibits for further information with respect to the Fund and the Common Shares offered hereby. Any statements contained herein concerning the provisions of any document are not necessarily complete, and, in each instance, reference is made to the copy of such document filed as an exhibit to the Registration Statement or otherwise filed with the SEC. Each such statement is qualified in its entirety by such reference. The complete Registration Statement may be obtained from the SEC upon payment of the fee prescribed by its rules and regulations or free of charge through the SEC's web site (<http://www.sec.gov>).

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BASE PROSPECTUS

\$130,000,000

ABERDEEN AUSTRALIA EQUITY FUND, INC.

Shares of Common Stock

Aberdeen Australia Equity Fund, Inc. ("Fund," "we," "us" or "our") is a non-diversified, closed-end management investment company. The Fund's principal investment objective is long-term capital appreciation through investment primarily in equity securities of Australian companies listed on the Australian Stock Exchange Limited. The Fund's secondary investment objective is current income.

We may offer, from time to time, in one or more offerings, including through rights offerings, our shares of common stock, par value \$.01 per share ("Shares"). Shares may be offered at prices and on terms to be set forth in one or more supplements to this Prospectus (each, a "Prospectus Supplement"). You should read this Prospectus and the applicable Prospectus Supplement carefully before your invest in our Shares.

Our Shares may be offered directly to one or more purchasers, through agents designated from time to time by us, or to or through underwriters or dealers. The Prospectus Supplement relating to the offering will identify any agents or underwriters involved in the sale of our Shares, and will set forth any applicable purchase price, fee, commission or discount arrangement between us and our agents or underwriters, or among our underwriters, or the basis upon which such amount may be calculated. We may not sell any of our Shares through agents, underwriters or dealers without delivery of a Prospectus Supplement describing the method and terms of the particular offering of our Shares.

Our Shares are listed on the NYSE Amex ("Amex") under the symbol "IAF." The last reported sale price of our Shares, as reported by the Amex on November 10, 2010, was \$13.20 per Share. The net asset value of our Shares at the close of business on November 10, 2010, was \$11.93 per Share.

Investment in the Shares involves certain risks and special considerations, including risks associated with currency fluctuations. The Fund also has authority (which it has not exercised) to borrow to finance investments and to issue preferred stock. Both practices entail risks. For a discussion of these and other risks, see "Risks and Special Considerations."

Shares of closed-end investment companies frequently trade at a discount to their net asset value. If the Fund's Shares trade at a discount to its net asset value, the risk of loss may increase for purchasers in a public offering. See "Risks and Special Considerations-Net Asset Value Discount."

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved these securities or passed upon the adequacy of this Prospectus. Any representation to the contrary is a criminal offense.

This Prospectus, together with any Prospectus Supplement, sets forth concisely the information about the Fund that a prospective investor should know before investing. You should read this Prospectus and applicable Prospectus Supplement, which contain important information, before deciding whether to invest in the Shares. You should retain the Prospectus and Prospectus Supplement for future reference. A Statement of Additional Information ("SAI"), dated December 8, 2010, containing additional information about the Fund, has been filed with the Securities and Exchange Commission ("SEC") and is incorporated by reference in its entirety into this Prospectus. The Table of Contents for the SAI is on page 35 of the Prospectus. You may call 1-866-839-5205, email InvestorRelations@aberdeen-asset.com or write to the Fund at 1735 Market Street, 32nd Floor, Philadelphia, Pennsylvania 19103 to obtain, free of charge, copies of the SAI and the Fund's annual and semi-annual reports to shareholders, as well as to obtain other information about the Fund and to make shareholder inquiries. The Fund's SAI, as well as the annual and semi-annual reports to shareholders, are also available on the Fund's website at www.aberdeeniaf.com. The SEC maintains a website at <http://www.sec.gov> that contains the SAI, material incorporated by reference into the Fund's registration statement and other information about the Fund.

Our Shares do not represent a deposit or obligation of, and are not guaranteed or endorsed by, any bank or other insured depository institution, and are not federally insured by the Federal Deposit Insurance Corporation, the Federal Reserve Board or any other government agency.

Prospectus dated December 8, 2010

TABLE OF CONTENTS

	Page
PROSPECTUS SUMMARY	3
SUMMARY OF FUND EXPENSES	10
FINANCIAL HIGHLIGHTS	11
USE OF PROCEEDS	12
THE FUND	13
DESCRIPTION OF SHARES	13
INVESTMENT OBJECTIVES	14
INVESTMENT POLICIES	14
INVESTMENT RESTRICTIONS	17
RISKS AND SPECIAL CONSIDERATIONS	17
MANAGEMENT OF THE FUND	23
EXPENSES	28
DIVIDENDS AND DISTRIBUTIONS	28
DIVIDEND REINVESTMENT AND DIRECT STOCK PURCHASE PLAN	29
TAXATION	29
CERTAIN PROVISIONS OF THE MARYLAND GENERAL CORPORATION LAW AND THE CHARTER AND BYLAWS	31
PLAN OF DISTRIBUTION	32
LEGAL PROCEEDINGS	34
TABLE OF CONTENTS OF THE STATEMENT OF ADDITIONAL INFORMATION	35
APPENDIX A	A-1

You should rely only on the information contained in, or incorporated by reference into, this Prospectus and any related Prospectus Supplement in making your investment decisions. The Fund has not authorized any person to provide you with different information. If anyone provides you with different or inconsistent information, you should not rely on it. The Fund is not making an offer to sell the Shares in any jurisdiction where the offer or sale is not permitted. You should assume that the information in this Prospectus and any Prospectus Supplement is accurate only as of the dates on their covers. The Fund's business, financial condition and prospects may have changed since the date of its description in this Prospectus or the date of its description in any Prospectus Supplement.

PROSPECTUS SUMMARY

The following information is only a summary. You should consider the more detailed information contained in the Prospectus and in any related Prospectus Supplement and in the SAI before purchasing Shares, especially the information under "Risks and Special Considerations" on page 17 of the Prospectus.

The Fund The Fund is a non-diversified, closed-end management investment company organized as a Maryland corporation. See "The Fund."

The Fund's Shares are listed for trading on the Amex under the symbol "IAF." As of November 10, 2010, the net assets of the Fund were \$229,919,324 and the Fund had outstanding 19,277,602 Shares. The last reported sale price of the Fund's Shares, as reported by the Amex on November 10, 2010 was \$13.20 per Share. The net asset value of the Fund's Shares at the close of business on November 10, 2010 was \$11.93 per Share. See "Description of Shares."

The Offering We may offer, from time to time, in one or more offerings, including through rights offerings, up to \$130,000,000 of our Shares on terms to be determined at the time of the offering. The Shares may be offered at prices and on terms to be set forth in one or more Prospectus Supplements. You should read this Prospectus and the applicable Prospectus Supplement carefully before you invest in our Shares. Our Shares may be offered directly to one or more purchasers, through agents designated from time to time by us, or to or through underwriters or dealers. The Prospectus Supplement relating to the offering will identify any agents, underwriters or dealers involved in the sale of our Shares, and will set forth any applicable purchase price, fee, commission or discount arrangement between us and our agents or underwriters, or among our underwriters, or the basis upon which such amount may be calculated. See "Plan of Distribution." We may not sell any of our Shares through agents, underwriters or dealers without delivery of a Prospectus Supplement describing the method and terms of the particular offering of our Shares.

Use of Proceeds We intend to use the net proceeds from the sale of our Shares primarily to invest in accordance with our investment objectives and policies. Proceeds will be invested within approximately 60 days of receipt by the Fund. See "Use of Proceeds."

Investment Objectives The Fund's principal investment objective is long-term capital appreciation through investment primarily in equity securities of Australian companies listed on the Australian Stock Exchange Limited ("ASX"). Its secondary objective is current income, which is expected to be derived primarily from dividends and interest on Australian corporate and governmental securities. The Fund's investment objectives may not be changed without the approval of a majority of the Fund's outstanding voting securities. See "Investment Objectives."

Investment Policies The Fund will normally invest at least 80% of its net assets, plus the amount of any borrowings for investment purposes, in equity securities,

consisting of common stock, preferred stock and convertible stock, of Australian companies listed on the ASX. For these purposes, Australian companies means companies that are tied economically to Australia. The Fund may invest up to 10% of its total assets in unlisted equity securities. It may also invest in debt securities issued by Australian companies, Australian Federal and State governments and the U.S. government. Such debt securities will be rated in one of the four highest rating categories by a nationally recognized statistical rating organization or, if unrated, determined to be of comparable quality by the Investment Manager, and will typically have a maturity of 10 years or less. The Fund's investments in any one industry or group of industries are generally limited to 25% of its total assets, except that it may invest between 25% and 35% of its total assets in securities of an industry group that, at the time of investment, represents 20% or more of the S&P/ASX 200 Accumulation Index. The Fund has authority to engage in options transactions, to enter into repurchase agreements, and to lend its portfolio securities. See "Investment Policies."

Investment Restrictions The Fund has certain investment restrictions that may not be changed without approval by a majority of the Fund's outstanding voting securities. These restrictions concern issuance of senior securities, borrowing, lending, concentration, diversification and other matters. See "Investment Restrictions."

Risks (See generally "Risks and Special Considerations" for more information on these and other risks) The value of the Fund's assets, as well as the market price of its shares, will fluctuate. You can lose money on your investment. Investing in the Fund involves other risks, including the following:

- *Currency Exchange Rate Fluctuations.* The Fund invests substantially in instruments denominated in foreign currencies primarily the Australian dollar, but also the New Zealand dollar. Fluctuations in the value of these non-U.S. currencies relative to the U.S. dollar can adversely affect the U.S. dollar value of the Fund's assets. A decline in the value of such a foreign currency can require the Fund to liquidate portfolio securities to pay distributions previously calculated in U.S. dollars and can increase the relevant foreign currency cost of expenses incurred in U.S. dollars. Currency exchange losses can reduce or eliminate the Fund's ability to make ordinary income distributions.
- *Foreign Securities.* In addition to foreign currency risks, investments in non-U.S. securities involve risk of loss in the event of tax increases or adverse political, economic or diplomatic developments in Australia and New Zealand. The Australian securities market for both listed and unlisted securities may be more volatile and is less liquid than the major U.S. markets, and investing in non-U.S. securities may involve greater costs plus more uncertainty regarding legal protections. Regulatory oversight of markets and custody facilities may differ from that in the U.S.

- *Australian Securities Risk.* Because the Fund's investments are primarily in Australian securities, the Fund is particularly vulnerable to loss in the event of adverse political, economic, financial and other developments that affect Australia, including fluctuations of Australian currency versus the U.S. dollar. Also, Australia is located in a part of the world that has historically been prone to natural disasters such as drought and is economically sensitive to environmental events. Any such event could result in a significant adverse impact on the Australian economy.
- *Concentration.* The Fund may invest up to 35% of its total assets in securities of an industry group that, at the time of investment, represents 20% or more of the S&P/ASX 200 Accumulation Index. An industry sector can include more than one industry group. As of October 31, 2010, 30% of the Fund's total assets were invested in the financials sector of the Standard & Poor's Global Industry Classification Sectors. While the Fund did not concentrate its investments in the materials sector, as of October 31, 2010, 23.6% of the Fund's total assets were invested in the materials sector. Such a concentration or significant amount of investments in a single industry sector makes the Fund particularly vulnerable to adverse economic, political or other developments affecting that sector. Concentration in the financials sector may make the Fund vulnerable to risks of regulation, consolidation, financial innovation and technological progress. Significant exposure to the materials sector may also make the Fund vulnerable to risks that the issuers in such sector will underperform the market as a whole due to legislative or regulatory changes and/or increased competition affecting that sector.
- *Net Asset Value Discount.* Shares of the Fund, a closed-end investment company, may trade in the market at a discount from their net asset value.
- *Distribution Rate.* There can be no assurance that the Board will maintain the Fund's distribution rate at a particular level, or that the Board will continue a managed distribution policy. Additionally, distributions may include return of capital as well as net investment income and capital gains. If the Fund's investments do not generate sufficient income, the Fund may be required to liquidate a portion of its portfolio to fund these distributions. See "Dividends and Distributions."
- *Non-Diversified Fund.* As a "non-diversified" investment company, the Fund can invest more of its assets in fewer issuers than an investment company that is "diversified," exposing the Fund to greater risk.
- *Share Repurchases.* When the Fund repurchases its shares pursuant to the Fund's share repurchase program, the resulting decrease in shares outstanding may increase the Fund's expense ratio; any borrowing to finance repurchases would reduce net income; and any sales of portfolio securities to finance

repurchases may not be at a preferred time from a portfolio management perspective and would increase portfolio turnover and related expenses.

- *Anti-Takeover Provisions.* The Fund's charter and bylaws contain several provisions that may be regarded as "anti-takeover" because they have the effect of maintaining continuity of management. Also, Articles Supplementary approved by the Board of Directors subject the Fund to certain provisions of the Maryland General Corporation Law with respect to unsolicited takeovers. See "Certain Provisions of the Maryland General Corporation Law and the Charter and Bylaws."

- *Leverage.* The Fund has authority to issue preferred stock and to borrow to finance investments. Each of these is a form of "leverage" that entails particular risks for holders of the Fund's common stock. The issuance of preferred stock would affect the amount of income available for distribution on the Fund's common stock as well as the net asset value of the common stock and the voting rights of holders of common stock. Leverage would exaggerate the effects of both currency fluctuations and of market downturns or upturns on the net asset value and market value of the Fund's common stock, as well as on distributions to holders of common stock. Leverage can also increase the volatility of the Fund's net asset value, and expenses related to leverage can reduce the Fund's income. In the case of leverage, if Fund assets decline in value so that legal asset coverage requirements for any preferred stock or borrowings would not be met, the Fund may be prevented from paying distributions, which could jeopardize its qualification for pass-through tax treatment, make it liable for excise taxes and/ or force it to sell portfolio securities at an inopportune time. Holders of preferred stock have the right to elect two directors, and such holders, as well as Fund creditors, have the right under certain circumstances to elect a majority of the Fund's directors.

- *Unlisted Securities.* The Fund may invest up to 10% of its total assets in unlisted equity securities. Because the market for unlisted securities is not liquid, it may be difficult for the Fund to sell these securities at a desirable price. Unlisted securities are not subject to the disclosure and other investor protection requirements of Australian law applicable to listed securities.

- *Securities Lending.* With respect to loans of its portfolio securities, the Fund is exposed to risks of loss in the event of default or bankruptcy of the borrower, and in the event that the return on the loan, or on invested collateral, will be less than the related costs.

- *Options.* Options strategies may not be successful if the Investment Adviser's expectations about market trends are not fulfilled. These strategies can also increase portfolio turnover and involve costs to the Fund.

- *Repurchase Agreements.* These transactions involve risks in the event of counterparty default or insolvency.

Investment Manager and Investment Adviser The Fund's investment manager is Aberdeen Asset Management Asia Limited ("Investment Manager"), a Singapore corporation located at 21 Church Street, #01-01 Capital Square Two, Singapore 049480. The Investment Manager serves as investment manager to both equity and fixed income investment portfolios for a range of clients. The Investment Manager, in accordance with the Fund's stated investment objectives, policies and limitations and subject to the supervision of the Fund's Board of Directors, manages the Fund's investments and makes investment decisions on behalf of the Fund, including the selection of, and being responsible for the placement of orders with, brokers and dealers to execute the Fund's portfolio transactions.

The Fund's investment adviser is Aberdeen Asset Management Limited ("Investment Adviser"), an Australian corporation affiliated with the Investment Manager. The Investment Adviser is located at Level 6, 201 Kent Street, Sydney, NSW 2000, Australia. The Investment Adviser's principal business focus is to provide investment management services with regard to equity and fixed income investments in Australian securities. The Investment Adviser makes recommendations to the Investment Manager as to specific portfolio securities to be purchased, retained or sold by the Fund and provides or obtains such research and statistical data as may be necessary in connection therewith.

The Investment Adviser is a wholly-owned subsidiary of the Investment Manager. The Investment Manager is a wholly-owned subsidiary of Aberdeen Asset Management PLC ("Aberdeen PLC"), a Scots company, that is the parent company of an asset management group (the "Aberdeen Group") managing approximately \$261.18 billion of assets as of August 31, 2010 for both institutions and private individuals from offices around the world. See "Management of the Fund The Investment Manager and the Investment Adviser."

The Fund pays a fee to the Investment Manager computed at the annual rate of 1.10% of the Fund's average weekly Managed Assets (defined as net assets plus the amount of any borrowings for investment purposes) up to \$50 million, 0.90% of such assets between \$50 million and \$100 million, and 0.70% of such assets in excess of \$100 million, computed as of the end of each week and payable at the end of each calendar month.

The Investment Manager pays the fees of the Investment Adviser. These fees are computed at the annual rate of 0.30% of the Fund's average weekly Managed Assets up to \$50 million, 0.25% of such assets between \$50 million and \$100 million, and 0.15% of such assets in excess of \$100 million, computed as of the end of each week and payable at the end of each calendar month.

Portfolio Managers The following persons have day-to-day management of the Fund's portfolio Hugh Young, Managing Director of the Investment Manager; Augustine Mark Daniels, a Director of the Investment Adviser; and Michelle Lopez, Robert Penalosa and Natalie Tam. See "Management of the Fund Portfolio Management."

Administrator Aberdeen Asset Management Inc., 1735 Market Street, 32nd Floor, Philadelphia, Pennsylvania 19103, acts as the Fund's administrator ("Administrator"). The Administrator is a subsidiary of Aberdeen PLC and an affiliate of the Investment Manager and Investment Adviser. The Fund pays a fee to the Administrator at an annual rate equal to 0.08% of the Fund's average weekly Managed Assets between \$0 and \$500 million, 0.07% of such assets between \$500 million and \$1.5 billion, and 0.06% of such assets in excess of \$1.5 billion. The Administrator delegates certain of its responsibilities to a sub-administrator, State Street Bank and Trust Company. See "Management of the Fund Administrator."

Custodian and Transfer Agent State Street Bank and Trust Company, One Heritage Drive, North Quincy, Massachusetts 02171, acts as the Fund's custodian. Computershare Trust Company, N.A. and Computershare Inc., 250 Royall Street Canton, Massachusetts 02021, act as the Fund's stock transfer agent and dividend paying agent, respectively. Computershare Trust Company, N.A. also sponsors and administers a Dividend Reinvestment and Direct Stock Purchase Plan which is available to shareholders. See "Management of the Fund Custodian and Transfer Agent."

Dividends and Distributions The Board of Directors has implemented a managed distribution policy of paying quarterly distributions at an annual rate, set once a year, that is a percentage of the rolling average of the Fund's prior four quarter-end net asset values. The current rolling distribution rate is 10%, but this rate may be changed by the Board in response to, among other things, market conditions. A significant portion of the Fund's distributions for the fiscal year ended October 31, 2009 represented a return of capital (rather than income or capital gains). If the Fund's distributions were to continue to consist of a large amount of return of capital, it would result in a deterioration of the Fund's assets. There can be no assurance that the Board will continue a managed distribution policy. See "Dividends and Distributions."

Dividend Reinvestment and Direct Stock Purchase Plan Computershare Trust Company, N.A. sponsors and administers a Dividend Reinvestment and Direct Stock Purchase Plan (the "Plan") which is available to shareholders. Additional information about the Plan and a brochure that includes the terms and conditions of the Plan may be obtained at www.computershare.com/buyaberdeen or by calling Computershare Trust Company, N.A. at 1-800-647-0584. For both purchases and reinvestment purposes, shares acquired through the Plan will be purchased in the open market at the current share price and cannot be issued directly by the Fund.

Taxation Withholding and/or other taxes may apply in the countries in which the Fund invests, which will reduce the Fund's cash return in those countries. The Fund intends to elect, when eligible, to "pass-through" to the Fund's shareholders the ability to claim (subject to limitations) a deduction or credit for the amount of foreign income and similar taxes paid by the Fund. Tax considerations for an investor in the Fund are summarized under "Taxation." See also "Risks and Special Considerations."

Share Repurchase Program Under the Fund's share repurchase program, the Fund is permitted to repurchase up to 10% of its outstanding shares on the open market during any 12-month period if and when the discount from net asset value is at least 8%. The Fund may borrow to repurchase shares under this program. There have not been any repurchases of shares under this program since 2009. Applicable law may prevent such repurchases during the offering of the Shares described herein. See "Description of Shares-Share Repurchase Program."

SUMMARY OF FUND EXPENSES

Shareholder Transaction Expenses	
Sales Load (as a percentage of offering price)(1)	%
Offering Expenses Borne by the Fund (as a percentage of offering price)(1)	%
Dividend Reinvestment and Cash Purchase Plan Fees(2)	
Annual Operating Expenses (As a Percentage of Average Net Assets Attributable to the Fund's Common Stock)	
Management Fee(3)	0.84%
Other Expenses(4)(5)	0.55%
Total Annual Operating Expenses	1.39%

(1) If the Shares are sold to or through underwriters, the Prospectus Supplement will set forth any applicable sales load and the estimated offering expenses borne by the Fund.

(2) If you participate in the Dividend Reinvestment and Direct Stock Purchase Plan sponsored and administered by Computershare Trust Company, N.A., you will be subject to any fees imposed by Computershare Trust Company, N.A.

(3) See "Management of the Fund The Investment Manager and the Investment Adviser" for additional information.

(4) "Other Expenses" have been estimated for the current fiscal year.

(5) Includes an administration fee of 0.08% of average net assets attributable to the Fund's common stock. See "Management of the Fund - Administrator" for additional information.

Example

An investor would pay the following expenses on a \$1,000 investment in the Fund, assuming a 5% annual return:

	One Year	Three Years	Five Years	Ten Years
\$	14	\$ 44	\$ 76	\$ 167

The above table and example are intended to assist investors in understanding the various costs and expenses directly or indirectly associated with investing in Shares of the Fund. The "Example" assumes that all dividends and other distributions are reinvested at net asset value and that the percentage amounts listed in the table above under Total Annual Operating Expenses remain the same in the years shown. The above table and example and the assumption in the example of a 5% annual return are required by regulations of the SEC that are applicable to all investment companies; the assumed 5% annual return is not a prediction of, and does not represent, the projected or actual performance of the Fund's Shares. For more complete descriptions of certain of the Fund's costs and expenses, see "Management of the Fund" and "Expenses."

The example should not be considered a representation of past or future expenses, and the Fund's actual expenses may be greater than or less than those shown. Moreover, the Fund's actual rate of return may be greater or less than the hypothetical 5% return shown in the example.

FINANCIAL HIGHLIGHTS

The financial highlights table is intended to help you understand the Fund's financial performance. Information is shown for the Fund's last ten fiscal years and the six-months ended April 30, 2010. Certain information reflects financial results for a single Fund Share. The following information (other than the information for the six-months ended April 30, 2010) has been audited by KPMG LLP, independent registered public accounting firm for the Fund, for the fiscal year ended October 31, 2009, and by another independent registered public accounting firm for the fiscal years prior to the fiscal year ended October 31, 2009, each of whose reports thereon were unqualified. The report of KPMG LLP, together with the financial statements of the Fund, are included in the Fund's October 31, 2009 Annual Report, and are included in the SAI, which is available upon request.

	Six-Months Ended April 30, 2010	2009	2008	Year Ended October 31,		2005
				2007	2006	
Per share operating performance(1):						
Net asset value, beginning of year/period	\$ 10.96	\$ 8.37	\$ 18.53	\$ 13.25	\$ 11.75	\$ 10.64
Net investment income	0.15	0.29	0.51	0.39	0.41	.37
Net realized and unrealized gains/(losses) on investments and foreign currencies	0.78	3.34	(8.83)	6.47	2.47	1.79
Total from investment operations	0.93	3.63	(8.32)	6.86	2.88	2.16
Distributions from:						
Net investment income	(0.47)	(0.31)	(0.24)	(0.53)	(0.48)	(.51)
Long-term capital gains			(0.84)	(0.98)	(0.90)	(.54)
Tax return of capital		(0.73)	(0.76)			
Total distributions	(0.47)	(1.04)	(1.84)	(1.51)	(1.38)	(1.05)
Payment by shareholder of short-swing profit					(3)	
Capital reduction with respect to issuance of Fund shares				(0.07)		

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Increase resulting from Fund share repurchase						
Net asset value, end of year/period	\$ 11.42	\$ 10.96	\$ 8.37	\$ 18.53	\$ 13.25	\$ 11.75
Market price per share, end of year/period	\$ 11.88	\$ 11.40	\$ 8.60	\$ 18.25	\$ 14.00	\$ 12.99
Total investment return based on(2):						
Market value	8.35%	50.76%	(45.57)%	43.46%	20.09%	38.98%
Net asset value	8.34%	48.92%	(47.83)%	53.91%	25.66%	21.11%
Ratio to average net assets/ supplemental data:						
Net assets, end of year/period (000 omitted)	\$ 219,933	\$ 210,866	\$ 160,886	\$ 354,970	\$ 223,588	\$ 197,421
Average net assets (000 omitted)	\$ 221,328	\$ 163,795	\$ 282,702	\$ 283,749	\$ 209,507	\$ 194,946
Net expense	1.33%(4)	1.73%	1.26%	1.44%	1.45%	1.48%
Expenses without reimbursement expenses	1.33%(4)	1.73%	1.26%	1.51%	1.55%	1.48%
Net investment income	2.71%(4)	3.41%	3.46%	2.56%	3.31%	3.21%
Portfolio turnover	4%	16%	22%	30%	16%	28%

(1) Based on average shares outstanding.

(2) Total investment return is calculated assuming a purchase of common stock on the first day and a sale on the last day of each period reported. Dividends and distributions, if any, are assumed, for purposes of this calculation, to be reinvested at prices obtained under the Fund's dividend reinvestment plan. Total investment return does not reflect brokerage commissions.

(3) Amount is less than \$0.005 per share.

(4) Annualized.

NOTE: Contained above is operating performance for a share of common stock outstanding, total investment return, ratios to average net assets and other supplemental data for each of the periods indicated. This information has been determined based upon financial information provided in the financial statements and market value data for the Fund's shares.

FINANCIAL HIGHLIGHTS (Concluded)

	Year Ended October 31,				
	2004	2003	2002	2001	2000
Per share operating performance(1):					
Net asset value, beginning of year	\$ 9.38	\$ 6.84	\$ 5.97	\$ 6.86	\$ 8.78
Net investment income	0.28	0.12	0.15	0.12	0.14
Net realized and unrealized gains/(losses) on investments and foreign currencies	1.76	2.58	0.93	(0.33)	(1.25)
Total from investment operations	2.04	2.70	1.08	(0.21)	(1.11)
Distributions from:					
Net investment income	(0.30)	(0.10)	(0.15)		(0.12)
Long-term capital gains	(0.36)	(0.07)	(0.07)		(0.69)
Tax return of capital	(0.12)			(0.68)	
Total distributions	(0.78)	(0.17)	(0.22)	(0.68)	(0.81)
Payment by shareholder of short-swing profit					
Capital reduction with respect to issuance of Fund shares					
Increase resulting from Fund share repurchase		0.01	0.01	(3)	
Net asset value, end of year	\$ 10.64	\$ 9.38	\$ 6.84	\$ 5.97	\$ 6,564,212
Cash paid for interest	\$-	\$-	\$ 18,425		\$ 11,724,713
Supplemental Disclosure of Non-Cash Financing Activities:					
Conversion of notes payable and accrued interest to common stock	\$-	\$ 18,897,167	\$ 18,897,167		\$ 6,564,212
Reclassification of deferred financing fees to additional paid-in capital	\$-	\$ 148,014	\$ 148,014		
Stock issued to technology finders and licensors	\$-	\$-	\$ 155		
Warrants issued	\$-	\$-	\$ 748,495		

to placement
agent

Debt discount on
senior

convertible notes \$-	\$ -	\$ 4,979,461
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See Notes to Unaudited Condensed Financial Statements.

4

CORMEDIX INC.
(A Development Stage Company)

NOTES TO UNAUDITED CONDENSED FINANCIAL STATEMENTS

Note 1 — Organization, Business and Basis of Presentation:

Organization and Business:

CorMedix Inc. (“CorMedix” or the “Company”) was incorporated in the State of Delaware on July 28, 2006. CorMedix is a development-stage pharmaceutical company that seeks to fulfill selected, significant unmet medical needs in the therapeutic areas at the crossroads of cardiac and kidney (renal) disease.

Basis of Presentation:

The accompanying unaudited condensed financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America and the rules of the Securities and Exchange Commission (“SEC”) for interim financial information. Accordingly, the unaudited condensed financial statements do not include all information and footnotes required by accounting principles generally accepted in the United States of America for complete annual financial statements. In the opinion of management, the accompanying unaudited condensed financial statements reflect all adjustments, consisting of normal recurring adjustments, considered necessary for a fair presentation of such interim results. Interim operating results are not necessarily indicative of results that may be expected for the full year ending December 31, 2011 or for any subsequent period. These unaudited condensed financial statements should be read in conjunction with the audited financial statements and notes thereto of the Company which are included in the Company’s Annual Report on Form 10-K filed with the SEC on March 11, 2011. The accompanying condensed balance sheet as of December 31, 2010 has been derived from the audited financial statements included in such Form 10-K.

The Company’s primary activities since incorporation have been organizational activities, including recruiting personnel, establishing office facilities, acquiring licenses for its pharmaceutical compound pipeline, performing business and financial planning, performing research and development and raising funds through the issuance of debt and common stock. The Company has not generated any revenues and, accordingly, the Company is considered to be in the development stage.

On February 24, 2010, the Company effected a 1 for 7.836 reverse stock split of its common stock. All share and per-share information in these unaudited condensed financial statements have been adjusted to give effect to the reverse stock split.

The Company’s unaudited condensed financial statements have been prepared on a going concern basis, which contemplates the realization of assets and the settlement of liabilities and commitments through the normal course of business. The unaudited condensed financial statements do not include any adjustments to reflect the possible future effects on the recoverability and classification of assets or the amounts and classification of liabilities. The Company has sustained operating losses since its inception and expects that such losses will continue over the next several years. Management believes that the currently available capital resources will be sufficient to meet the Company’s operating needs into the first quarter of 2012. For the three months ended March 31, 2011 and the period from July 28, 2006 (inception) to March 31, 2011, the Company incurred net losses of \$1,975,038 and \$38,211,317, respectively.

CORMEDIX INC.

(A Development Stage Company)

NOTES TO UNAUDITED CONDENSED FINANCIAL STATEMENTS

Correction of Immaterial Error

The Company identified an immaterial error in its previously issued unaudited condensed financial statements for the period ended March 31, 2010, as follows:

- the improper recording of licensor escrowed shares to research and development expense when such shares were not earned.

The error in the accounting for the licensor escrowed shares resulted in an overstatement of non-cash research and development expenses of \$369,652 and an overstatement of net loss per share of \$0.34 in the first quarter of 2010. The licensor shares were not earned as of March 31, 2011.

The Company reviewed the accounting error utilizing SEC Staff Accounting Bulletin No. 99, "Materiality" ("SAB 99") and SEC Staff Accounting Bulletin No. 108, "Effects of Prior Year Misstatements on Current Year Financial Statements" ("SAB 108") and determined the impact of the errors to be immaterial to any prior period's presentation. The accompanying 2011 and 2010 unaudited condensed financial statements reflect the corrections of the aforementioned immaterial error.

Note 2 — Summary of Significant Accounting Policies:

Use of Estimates:

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America 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 reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

Loss per common share:

Basic earnings (loss) per common share excludes dilution and is computed by dividing net income (loss) by the weighted average number of common shares outstanding during the period. Diluted earnings per common share reflect the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that then shared in the earnings of the entity. Since the Company has only incurred losses, basic and diluted loss per share are the same. The amount of potentially dilutive securities excluded from the calculation was 6,572,986 and 6,410,506 shares of common stock being held in escrow, convertible notes, warrants and options at March 31, 2011 and 2010, respectively.

Stock Based Compensation:

The Company accounts for stock options granted to employees according to the Financial Accounting Standards Board Accounting Standards Codification No. 718, "Compensation — Stock Compensation" ("ASC 718"). Under ASC 718, share-based compensation cost is measured at grant date, based on the estimated fair value of the award, and is recognized as expense over the employee's requisite service period on a straight-line basis.

CORMEDIX INC.
(A Development Stage Company)

NOTES TO UNAUDITED CONDENSED FINANCIAL STATEMENTS

The Company accounts for stock options granted to non-employees on a fair value basis using the Black-Scholes option pricing method in accordance with ASC 718. The non-cash charge to operations for non-employee options with vesting is revalued at the end of each reporting period based upon the change in the fair value of the options and amortized to consulting expense over the related vesting period.

During the three months ended March 31, 2011 and 2010 options to purchase an aggregate of 506,000 and 1,581,766 shares of common stock, respectively, were granted to the Company's employees and directors.

Note 3 — Stockholders' Equity (Deficiency):

Common Stock:

During the three months ended March 31, 2011 and 2010 and the period from July 28, 2006 (inception) to March 31, 2011, the Company recorded compensation expense, in connection with common stock issued to employees, directors and consultants, of \$79,490, \$252,908 and \$1,870,230, respectively.

Common Stock Options and Warrants:

During the three months ended March 31, 2011, options to purchase an aggregate of 150,000 shares of common stock were granted to the Company's directors under the Amended and Restated 2006 Stock Incentive Plan ("Plan") with an exercise price of \$2.10 per share. These options vest on the one-year anniversary of the grant date, January 14, 2011, and have a ten-year term. Additionally, during the three months ended March 31, 2011, options to purchase 356,000 shares of common stock were granted to the Company's new Chief Medical Officer ("CMO") under the Plan with an exercise price of \$1.61 per share. These options vest in equal installments on each of the first three anniversaries of the grant date, March 1, 2011, and have a ten-year term.

During the three months ended March 31, 2010, options to purchase an aggregate of 1,581,766 shares of common stock were granted to the Company's employees and directors under the Plan with an exercise price of \$3.125 per share. The options granted to the Company's employees vest in equal installments on each of the first three anniversaries of the grant date, March 30, 2010, and the options granted to directors vest in equal installments on each of the grant date and the first two anniversaries of the grant date, March 30, 2010.

The Company records compensation expense associated with stock options and other forms of equity compensation using the Black-Scholes option-pricing model and the following assumptions:

	Three Months Ended March 31, 2011	Three Months Ended March 31, 2010
Expected Term	5 years	5 years
Volatility	109% - 114%	112%
Dividend yield	0.0%	0.0%
Risk-free interest rate	1.95% - 2.11%	2.6%

CORMEDIX INC.
(A Development Stage Company)

NOTES TO UNAUDITED CONDENSED FINANCIAL STATEMENTS

The Company estimated the expected term of the stock options granted based on anticipated exercises in future periods assuming the success of its business model as currently forecasted. Given the Company's short period of publicly-traded stock history, management's estimate of expected volatility is based on the average expected volatilities of a sampling of five companies with similar attributes to the Company, including: industry, stage of life cycle, size and financial leverage. The Company will continue to analyze the expected stock price volatility and expected term assumptions as more historical data for the Company's common stock becomes available. The expected dividend yield reflects the Company's current and expected future policy for dividends on the Company's common stock. To determine the risk-free interest rate, the Company utilized the U.S. Treasury yield curve in effect at the time of grant with a term consistent with the expected term of the Company's awards. During the first quarter ended March 31, 2011, the Company has experienced forfeitures of options issued to its former CMO and its former Chairman. Since the stock options currently outstanding are primarily held by senior management and directors of the Company, the Company will continue to evaluate the effects of such future potential forfeitures, as they may arise, to ascertain an estimated forfeiture rate.

A summary of the Company's option and warrant activity under the Plan and related information is as follows:

	Three Months Ended March 31, 2011		Three Months Ended March 31, 2010	
	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price
Outstanding at beginning of period	1,662,827	\$3.15	23,612	\$8.23
Forfeited	(362,444)	\$3.35	-	-
Granted	506,000	\$1.76	1,581,766	\$3.13
Outstanding at end of period and expected to vest	1,806,383	\$2.27	1,605,378	\$3.20
Options exercisable	454,808	\$3.21	56,380	\$4.61
Weighted-average fair value of options granted during the period		\$1.40		\$2.51

The weighted average remaining contractual life of stock options outstanding and expected to vest at March 31, 2011 is 9.2 years. The weighted average remaining contractual life of stock options exercisable at March 31, 2011 is 8.9 years. The aggregate intrinsic value is calculated as the difference between the exercise prices of the underlying options and the quoted closing price of the common stock of the Company as of March 31, 2011 for those options that have an exercise price below the quoted closing price. As of March 31, 2011, there were 406,000 options outstanding and expected to vest with an exercise price below the quoted closing price of the common stock of the Company, resulting in a \$210,440 intrinsic value. As of March 31, 2011, there were 454,808 options exercisable with an exercise price above the quoted closing price of the common stock of the Company, resulting in no intrinsic value.

As of March 31, 2011, the total compensation expense related to non-vested options not yet recognized totaled \$2,627,143. The weighted-average vesting period over which the total compensation expense related to non-vested options not yet recognized at March 31, 2011 was approximately 2.1 years.

Note 4 — Shares Issued to Licensors:

In accordance with the terms of agreements with the Company's licensors, Shiva Biomedical, LLC ("Shiva") and ND Partners, LLC ("ND Partners"), the Company was obligated to issue additional shares of common stock to each licensor sufficient to maintain an ownership percentage of 7% of the outstanding common stock of the Company on a fully-diluted basis. As a result of the automatic conversion of all of the Company's outstanding convertible notes into Units (as defined below) and shares of common stock in connection with the closing of the Company's initial public offering (the "IPO"), on March 30, 2010, the Company issued an aggregate of 828,024 shares of common stock to Shiva and ND Partners as a result of anti-dilution adjustments pursuant to their respective agreements, of which 118,289 are being held in escrow for ND Partners pending the achievement of certain regulatory and sales-based milestones. As a result of these issuances, a charge of \$2,217,924 was recorded to research and development during the first quarter of 2010. This obligation terminated upon the closing of the IPO.

CORMEDIX INC.
(A Development Stage Company)

NOTES TO UNAUDITED CONDENSED FINANCIAL STATEMENTS

Note 5 — Commitments:

Employment Agreements

On January 14, 2011, the Company entered into an amendment to the employment agreement, effective January 1, 2011, with its President and Chief Executive Officer, John C. Houghton (the “Houghton Amendment”). The Houghton Amendment amended the Amended and Restated Employment Agreement, dated as of November 25, 2009, by and between the Company and Mr. Houghton to (i) increase Mr. Houghton’s annual base salary to \$350,000 and (ii) increase the amount of the annual bonus payments Mr. Houghton may receive upon the achievement of certain financial, clinical development and business milestones, at the sole discretion of the Company’s Board of Directors (the “Board”), to up to 40% of Mr. Houghton’s annual base salary.

On January 14, 2011, the Company also entered into an amendment to the employment agreement, effective January 1, 2011, with its Chief Financial Officer, Brian Lenz (the “Lenz Amendment”). The Lenz Amendment amended the Employment Agreement, dated as of February 4, 2010, by and between the Company and Mr. Lenz to (i) increase Mr. Lenz’s annual base salary to \$250,000 and (ii) eliminate Mr. Lenz’s annual guaranteed bonus.

On February 25, 2011, the Company entered into an employment agreement with Mark A. Klausner, M.D., the Company’s new CMO (the “Klausner Employment Agreement”). Pursuant to the Klausner Employment Agreement, Dr. Klausner will serve as the Company’s CMO for an initial term of two years commencing on March 1, 2011, which term will extend automatically for additional one-year periods unless appropriate notice is given by one of the parties. Dr. Klausner will receive an annual base salary of \$310,000, and will be eligible for annual bonus payments of up to 35% of his base salary, based upon the achievement of certain milestones as established annually by the Company’s Chief Executive Officer, in consultation with the Board and Dr. Klausner.

Pursuant to the Klausner Employment Agreement, if the Company terminates Dr. Klausner as a result of his death or Disability (as defined under the Klausner Employment Agreement), Dr. Klausner or his estate, as applicable, will receive his base salary and any accrued but unpaid benefits through the termination date (the “Accrued Compensation”), plus his base salary for a period of 90 days, and all his unvested restricted shares and stock options that are scheduled to vest on or before the next succeeding anniversary of March 1, 2011 will be accelerated and vest as of the termination date. If the Company terminates Dr. Klausner for Cause (as defined under the Klausner Employment Agreement), if Dr. Klausner terminates his employment other than for Good Reason (as defined under the Klausner Employment Agreement), or if Dr. Klausner’s employment terminates by expiration of the term of the Klausner Employment Agreement, Dr. Klausner will receive the Accrued Compensation only. If the Company terminates Dr. Klausner within two months prior to or six months following the occurrence of a Change of Control (as defined under the Klausner Employment Agreement), and on the date of termination the fair market value of the Company’s common stock on a fully-diluted basis is more than \$50 million (as determined by the Board in good faith), Dr. Klausner will receive the Accrued Compensation, his base salary and benefits for a period of three months following his termination, and all his unvested restricted shares and stock options will be accelerated and vest as of the termination date. If the Company terminates Dr. Klausner for reasons other than those stated above or Dr. Klausner terminates his employment for Good Reason, Dr. Klausner will receive the Accrued Compensation and his base salary and benefits for a period of six months following his termination, and all his unvested restricted shares and stock options that are scheduled to vest within the 12 months following his termination will be accelerated and vest as of the termination date.

CORMEDIX INC.
(A Development Stage Company)

NOTES TO UNAUDITED CONDENSED FINANCIAL STATEMENTS

Revised Director Compensation Policy

On January 14, 2011, the Board adopted revisions to its director compensation policy (the “Director Compensation Policy”) based on recommendations from an independent compensation consultant retained by the Compensation Committee of the Board. The Board revised the Director Compensation Policy to provide for an increase in the amount of the annual retainer paid to non-employee directors to \$20,000, with the exception of the Chairman of the Board who will be paid \$30,000. Under the revised Director Compensation Policy, each non-employee director will be granted annually, at the first Board meeting of the calendar year, an option to purchase 30,000 shares of the Company's common stock at an exercise price equal to the closing price of the common stock on the grant date, which option will vest on the first anniversary of the grant date. In addition, pursuant to the revised Director Compensation Policy, each new non-employee director will be granted, in connection with his or her initial election to the Board, an option to purchase 30,000 shares of the Company's common stock at an exercise price equal to the closing price of the common stock on the grant date, which option will vest as follows: one-third on the grant date; an additional one-third on the first anniversary of the grant date; and the remaining one-third on the second anniversary of the grant date.

Note 6 — Initial Public Offering:

On March 30, 2010, the Company completed its IPO, whereby the Company sold 1,925,000 units, each unit consisting of two shares of its common stock and a warrant to purchase one share of common stock (each a “Unit”), at \$6.50 per Unit resulting in gross proceeds of \$12,512,500. In connection with the IPO, the Company paid underwriting discounts and commissions of \$1,063,563, corporate finance fees of \$225,250 and reimbursable legal expenses of counsel for the underwriters of \$90,000, and the Company incurred other offering costs and expenses, including legal, accounting, printing and filing fees totaling \$676,417.

All of the Company's convertible notes and all of the Company's outstanding shares of Non-Voting Subordinated Class A Common Stock automatically converted into Units or common stock upon the completion of the IPO. Management believes that the net proceeds from the IPO and existing cash will be sufficient to fund the Company's projected operating requirements into the first quarter of 2012.

Note 7 — Fair Value Measurements:

The fair value of the Company's cash and cash equivalents, accounts payable and other accrued liabilities at March 31, 2011 are estimated to approximate their carrying values due to the relative liquidity and short term nature of these instruments.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our unaudited condensed financial statements and related notes appearing elsewhere in this Quarterly Report on Form 10-Q and our Annual Report on Form 10-K filed with the Securities and Exchange Commission (the "SEC") on March 11, 2011.

Forward Looking Statements

This Quarterly Report on Form 10-Q contains "forward-looking statements" that involve risks and uncertainties, as well as assumptions that, if they never materialize or prove incorrect, could cause our results to differ materially from those expressed or implied by such forward-looking statements. The statements contained in this Quarterly Report on Form 10-Q that are not purely historical are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). Forward-looking statements are often identified by the use of words such as, but not limited to, "anticipate," "believe," "can," "continue," "could," "estimate," "expect," "intend," "may," "will," "plan," "project," "seek," "would," and similar expressions or variations intended to identify forward-looking statements. These statements are based on the beliefs and assumptions of our management based on information currently available to management. Such forward-looking statements are subject to risks, uncertainties and other important factors that could cause actual results and the timing of certain events to differ materially from future results expressed or implied by such forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those identified below, and those discussed in the section titled "Risk Factors" included in our Annual Report on Form 10-K filed with the SEC on March 11, 2011. Furthermore, such forward-looking statements speak only as of the date of this report. Except as required by law, we undertake no obligation to update any forward-looking statements to reflect events or circumstances after the date of such statements.

Overview

CorMedix Inc. (referred to herein as "we," "us," "our" and the "Company"), is a pharmaceutical company that seeks to in-license, develop and commercialize therapeutic products for the treatment of cardiac and renal dysfunction, also known as Cardiorenal disease. Specifically, our goal is to treat kidney disease by reducing the commonly associated cardiovascular and metabolic complications — in effect, "Treating the kidney to treat the heart®." To date, we have licensed all of the products in our Cardiorenal pipeline.

We have the worldwide rights to develop and commercialize several proprietary product candidates in clinical development that address significant market opportunities, including our most advanced product candidates, CRMD003 (Neutrolin®) and CRMD001 (a proprietary formulation of deferiprone).

CRMD003 is a liquid designed to prevent central venous Catheter Related Bloodstream Infections ("CRBI") and maintenance of catheter patency in central venous catheters (initially in hemodialysis catheters). We expect to submit an amendment to our Investigational Device Exemption application with the Food and Drug Administration ("FDA") for CRMD003 by the end of the first half of 2011, which if approved will enable us to start a pivotal clinical trial in the United States in 2011. We are seeking approval of Neutrolin® through a CE mark application. We have recently been informed by the notified body managing our CE mark application that the required reviews by the European regulatory authorities are expected to take several months longer than originally anticipated. As a result, although we will continue to aggressively pursue the advancement of the application process and collaborate with the European regulatory authorities, we now expect that the timing for potential receipt of CE mark approval will be during the first half of 2012. If we obtain CE mark approval in Europe, we expect to be in a position to launch Neutrolin® for the prevention of CRBI and maintenance of catheter patency in hemodialysis patients in Europe during the first half of

2012. We cannot be assured of CE mark approval of Neutrolin® on that timeline or at all. We are currently exploring the various methods of launching Neutrolin® in Europe, whether through a distributorship or partnership arrangement.

CRMD001 is our oral formulation of the drug deferiprone, which we intend to develop for use in the prevention of Contrast-Induced Nephropathy, (“CIN”), which is a common and potentially serious complication arising from the use of iodinated contrast media used in X-ray procedures to identify the status of blood vessels in the heart. Following our assessment of the data generated in connection with our development of CRMD001 for the CIN indication, we will consider whether or not to also develop CRMD001 for use in the treatment of Chronic Kidney Disease, (“CKD”), based on the support such data provides for this additional indication as well as other factors, including our access to capital, clinical and regulatory considerations regarding development of CRMD001 for the CKD indication, and our assessment of the then-current state of our intellectual property estate in CRMD001 with respect to both the CIN and the CKD indications. In June 2010, we initiated patient dosing in a phase II biomarker “proof of concept” study for the CIN indication. As of May 5, 2011, there have been 47 patients enrolled in our phase II study. We expect to have the phase II study fully enrolled with 60 patients by the end of the first half of 2011. We believe this study will generate supportive data on the ability of CRMD001 to reduce biomarker evidence of acute kidney injury and provide other information that will increase the likelihood of success of a later phase III trial for the CIN indication.

We are a development stage company. We were organized as a Delaware corporation on July 28, 2006 under the name “Picton Holding Company, Inc.” and we changed our corporate name to “CorMedix Inc.” on January 18, 2007. Since our inception, we have had no revenue from product sales. Our operations to date have been primarily limited to organizing and staffing, licensing product candidates, developing clinical trials for our product candidates, establishing manufacturing for our product candidates and maintaining and improving our patent portfolio. We have generated significant losses to date, and we expect to continue to generate losses as we progress towards the commercialization of our product candidates, including CRMD003 and CRMD001. As of March 31, 2011, we had an accumulated deficit of \$38,211,317. Since we do not generate revenue from any of our product candidates, our losses will continue as we advance our product candidates towards regulatory approval and eventual commercialization. As a result, our operating losses are likely to be substantial over the next several years. We are unable to predict the extent of any future losses or when we will become profitable, if at all.

In March 2010, we completed our Initial Public Offering (the “IPO”), whereby we sold 1,925,000 units, each unit consisting of two shares of our common stock and a warrant to purchase one share of common stock (each a “Unit”), at \$6.50 per Unit resulting in gross proceeds of \$12,512,500 and net proceeds to us of \$10,457,270 after deducting underwriting discounts and commissions and offering expenses payable by us. All of our convertible notes and accrued interest thereon and all of our outstanding shares of Non-Voting Subordinated Class A Common Stock automatically converted into Units or common stock upon the completion of the IPO. We believe that the net proceeds from the IPO and existing cash will be sufficient to fund our projected operating requirements into the first quarter of 2012.

We also effected a 1 for 7.836 reverse stock split of our common stock on February 24, 2010 in connection with the IPO. All shares and per share amounts, except as noted, have been retroactively adjusted to give effect to the reverse stock split.

Financial Operations Overview

Revenue

We have not generated any revenue since our inception. As of March 31, 2011, we have funded our operations primarily through debt financings and the IPO, and our receipt of a total of approximately \$490,000 from federal grants under the Qualifying Therapeutic Discovery Project program and a total of approximately \$280,000 from the sale of our unused net operating losses through the State of New Jersey's Economic Development Authority Technology Business Tax Certificate Transfer Program and a total of approximately \$35,000 from qualified research and development expenditures refunded to us through the New York State Department of Taxation and Finance under the Qualifying Emerging Technology Incentive Program.

If our product development efforts result in clinical success, regulatory approval and successful commercialization of any of our products, we could generate revenue from sales or licenses of any such products.

Research and Development Expense

Research and development ("R&D") expense consists of: (i) internal costs associated with our development activities; (ii) payments we make to third party contract research organizations, contract manufacturers, investigative sites, and consultants; (iii) technology and intellectual property license costs; (iv) manufacturing development costs; (v) personnel related expenses, including salaries, benefits, travel and related costs for the personnel involved in drug development; (vi) activities relating to regulatory filings and the advancement of our product candidates through preclinical studies and clinical trials; and (vii) facilities and other allocated expenses, which include direct and allocated expenses for rent, facility maintenance, as well as laboratory and other supplies. All R&D is expensed as incurred.

Conducting a significant amount of development is central to our business model. Through March 31, 2011, we incurred \$19,232,991 in R&D expenses since our inception in July 2006. Product candidates in later-stage clinical development generally have higher development costs than those in earlier stages of development, primarily due to the significantly increased size and duration of the clinical trials. We plan to increase our R&D expenses for the foreseeable future in order to complete development of our two most advanced product candidates, CRMD003 and CRMD001, and our earlier-stage R&D projects.

The following table summarizes the percentages of our R&D payments related to our two most advanced product candidates and other projects. The percentages summarized in the following table reflect payments directly attributable to each development candidate, which are tracked on a project basis. A portion of our internal costs, including indirect costs relating to our product candidates, are not tracked on a project basis and are allocated based on management's estimate.

	Three Months Ended March 31,				Period from July 28, 2006 (Inception) through March 31, 2011	
	2011	2010				
CRMD001	26	47	%	%	58	%
CRMD002	0	1	%	%	1	%
CRMD003	72	51	%	%	38	%
CRMD004	2	1	%	%	3	%

The process of conducting pre-clinical studies and clinical trials necessary to obtain FDA approval is costly and time consuming. The probability of success for each product candidate and clinical trial may be affected by a variety of factors, including, among others, the quality of the product candidate's early clinical data, investment in the program, competition, manufacturing capabilities and commercial viability. As a result of the uncertainties discussed above, the uncertainty associated with clinical trial enrollments and the risks inherent in the development process, we are unable to determine the duration and completion costs of current or future clinical stages of our product candidates or when, or to what extent, we will generate revenues from the commercialization and sale of any of our product candidates.

Development timelines, probability of success and development costs vary widely. We are currently focused on developing our two most advanced product candidates, CRMD003 for the prevention of CRBI and CRMD001 for the CIN indication. We expect to raise additional funds at a later date in order to fully complete the development of CRMD003 for CRBI and CRMD001 for the CIN indication, to further develop CRMD002 or CRMD004 through and beyond the pre-clinical stage, to develop CRMD001 for the CKD indication (should we decide to pursue such development) or to develop any new product candidates.

General and Administrative Expense

General and administrative ("G&A") expense consists primarily of salaries and other related costs, including stock-based compensation expense, for persons serving in our executive, finance and accounting functions. Other G&A expense includes facility-related costs not otherwise included in R&D expense, promotional expenses, costs associated with industry and trade shows, and professional fees for legal services and accounting services. We expect that our G&A expenses will increase if we add personnel and as a result of the reporting obligations applicable to public companies. From our inception on July 28, 2006 through March 31, 2011, we spent \$8,604,676 on G&A expense.

Interest Income and Interest Expense

Interest income consists of interest earned on our cash and cash equivalents. Interest expense consists of interest incurred on our convertible notes up to their automatic conversion into Units or common stock upon the completion of the IPO on March 30, 2010, as well as the amortization and write-off of deferred financing costs and debt discounts and a charge for the beneficial conversion relating to our convertible notes.

Results of Operations

Three months ended March 31, 2011 compared to three months ended March 31, 2010

Research and Development Expense. R&D expense was \$1,175,542 for the three months ended March 31, 2011, a decrease of \$1,551,467, from \$2,727,009 for the three months ended March 31, 2010. The decrease was primarily attributable to a charge of \$2,217,924 during the first quarter of 2010 related to our issuance of 828,024 shares of our common stock valued at \$3.125 per share to our licensors (of which 118,289 shares are being held in escrow) as a result of anti-dilution adjustments in connection with the conversion of our outstanding convertible debt to common stock upon the closing of the IPO, which anti-dilution provisions expired upon the closing of the IPO. There was no corresponding charge during the first quarter of 2011. The decrease was also a result of \$209,647 of stock-based compensation expense reversed during the first quarter of 2011, which was related to the forfeitures of unvested options to purchase 327,130 shares of common stock by our former Chief Medical Officer ("CMO") in accordance with the terms of his employment agreement upon the expiration of his employment term in February 2011. The decrease was partially offset by \$102,821 of stock-based compensation expense during the first quarter of 2011 compared to \$3,306 during the first quarter of 2010 primarily attributed to the portion of stock options granted to our President and

Chief Executive Officer (“CEO”) in connection with our IPO in March 2010 and the stock options granted to our new CMO in February 2011, as well as increased clinical, clinical research organization, manufacturing and regulatory expenses related to our Phase II clinical trial of CRMD001 that began in June 2010, higher manufacturing, regulatory and clinical research organization costs related to the development of CRMD003 and higher personnel costs as a result of hiring two employees in the areas of clinical operations and product development during the third quarter of 2010.

General and Administrative Expense. G&A expense was \$834,481 for the three months ended March 31, 2011, an increase of \$187,638 from \$646,843 for the three months ended March 31, 2010. The increase was primarily attributable to stock-based compensation expense of \$225,040 during the first quarter of 2011 compared to \$118,215 during the first quarter of 2010 primarily attributed to the portion of stock options granted to our CEO and all of the stock options granted to our Chief Financial Officer (“CFO”) and non-employee directors in connection with our IPO in March 2010 and the stock options granted to our non-employee directors in January 2011. The increase in G&A expense also reflects the increased costs of operating as a publicly-traded company following our IPO in March 2010, which includes filing fees related to the listing of our common stock, as well as increased legal, investor relations, consulting fees and increased compensation expense as a result of our hiring a CFO in February 2010. The increase was offset by \$38,724 of stock-based compensation expense reversed during the first quarter of 2011, which was related to the forfeitures of unvested options to purchase 35,314 shares of common stock by our former Chairman of the Board in accordance with our Amended and Restated 2006 Stock Incentive Plan following his resignation from our Board of Directors and from his position as Chairman.

Interest Income. Interest income was \$5,166 for the three months ended March 31, 2011, an increase of \$5,138, from \$28 for the three months ended March 31, 2010. The increase was attributable to having higher interest-bearing cash balances during the first quarter 2011 as a result of the funds received from the completion of our IPO in March 2010, compared to the first quarter of 2010.

Interest Expense. Interest expense was \$0 for the three months ended March 31, 2011, compared to \$3,093,763 for the three months ended March 31, 2010. The decrease was attributable to the conversion of all our convertible notes during the first quarter of 2010 in connection with the IPO in March 2010.

Liquidity and Capital Resources

Sources of Liquidity

As a result of our significant R&D expenditures and the lack of any approved products to generate product sales revenue, we have not been profitable and have generated operating losses since we were incorporated in July 2006. Prior to the IPO, we had funded our operations principally with \$14,364,973 in convertible notes sold in private placements and \$625,464 in related party notes, which were also convertible. All of our convertible notes were automatically converted into 1,237,293 shares of common stock and 2,338,576 Units comprised of 4,677,152 shares of common stock and 2,841,603 warrants at an exercise price of \$3.4375. We received net proceeds of \$10,457,270 from the IPO, after deducting underwriting discounts, commissions and offering expenses payable by us upon the closing of the IPO on March 30, 2010. Additionally, we received a total of approximately \$490,000 from federal grants under the Qualifying Therapeutic Discovery Project program and a total of approximately \$280,000 from the sale of our unused net operating losses through the State of New Jersey’s Economic Development Authority Technology Business Tax Certificate Transfer Program and a total of approximately \$35,000 from qualified R&D expenditures refunded to us through the New York State Department of Taxation and Finance under the Qualifying Emerging Technology Incentive Program.

Net Cash Used in Operating Activities

Net cash used in operating activities was \$1,719,472 for the three months ended March 31, 2011. The net loss of \$1,975,038 for the three months ended March 31, 2011 was higher than cash used in operating activities by \$255,566. The primary reasons for the difference is attributed to a stock-based compensation charge of \$79,490, a decrease in prepaid expenses and other current assets of \$306,357 which consists of amortized manufacturing costs, clinical research organization and insurance premiums during the first quarter of 2011, an increase in accounts payable of \$154,274 related to increased clinical development costs, offset by a decrease in accrued expenses of \$287,026 which resulted from bonus payments made during the first quarter of 2011 for performance related to 2010.

Net Cash Used in Investing Activities

Net cash used in investing activities was \$0 for the three months ended March 31, 2011.

Net Cash Provided by Financing Activities

Net cash provided by financing activities was \$0 for the three months ended March 31, 2011. Net cash provided by financing activities during the three months ended March 31, 2010 consisted of the sale of equity securities issued in our IPO, through which we received gross proceeds of \$12,512,500. The gross proceeds of \$12,512,500 were offset by underwriting discounts and commissions of \$1,063,563, corporate finance fees of \$225,250, and reimbursable legal fees for counsel to the underwriters of \$90,000, in addition to other offering costs and expenses of \$676,417, consisting primarily of legal, accounting, printing and filing fees. Net cash provided by financing activities was \$10,457,270 for the three months ended March 31, 2010.

Funding Requirements

Our total cash on hand as of March 31, 2011 was \$6,564,212, compared to \$8,283,684 at December 31, 2010. Since our business does not generate positive operating cash flow, we will need to either raise additional capital before we exhaust our current cash resources in order to continue to fund our R&D, including our long-term plans for clinical trials and new product development, as well as to fund operations generally. Our continued operations will depend on whether we are able to raise additional funds through various potential sources, such as equity, debt financing, strategic relationships, or out-licensing of our products. As of March 31, 2011, we have funded our operations primarily through debt financings, the IPO, and our receipt of a total of approximately \$490,000 from federal grants under the Qualifying Therapeutic Discovery Project program, approximately \$280,000 from the sale of our unused net operating losses through the State of New Jersey's Economic Development Authority Technology Business Tax Certificate Transfer Program and \$35,000 from qualified R&D expenditures refunded to us through the New York State Department of Taxation and Finance under the Qualifying Emerging Technology Incentive Program.

We expect to continue to fund operations from cash on hand and through either capital raising sources as previously described above, which may be dilutive to existing stockholders, or through generating revenues from the licensing of our products or strategic alliances. We plan to seek additional debt and/or equity financing, but can provide no assurances that such financing will be available on acceptable terms, or at all. Moreover, the incurrence of indebtedness in connection with a debt financing would result in increased fixed obligations and could also result in covenants that would restrict our operations.

Our actual cash requirements may vary materially from those now planned, however, because of a number of factors including the changes in the focus and direction of our R&D, the acquisition and pursuit of development of new product candidates, competitive and technical advances, costs of commercializing any of the product candidates, and costs of filing, prosecuting, defending and enforcing any patent claims and any other intellectual property rights.

We do not anticipate that we will generate any product revenue for 2011. In the absence of additional funding, we expect our continuing operating losses to result in increases in our cash used in operations over the next several quarters and years.

Based on our cash resources at March 31, 2011, and our current plan of expenditure on continuing development of our current products, we believe that we have sufficient capital to fund our operations into the first quarter of 2012, and will need additional financing until we can achieve profitability, if ever. If we are unable to raise additional funds when needed, we may not be able to market our products as planned or continue development and regulatory approval of our products, or we could be required to delay, scale back or eliminate some or all of our R&D programs. Each of these alternatives would likely have a material adverse effect on the prospects of our business.

Critical Accounting Policies

Our management's discussion and analysis of our financial condition and results of operations is based on our financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States, or GAAP. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities and expenses. On an ongoing basis, we evaluate these estimates and judgments, including those described below. We base our estimates on our historical experience and on various other assumptions that we believe to be reasonable under the circumstances. These estimates and assumptions form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results and experiences may differ materially from these estimates.

While our significant accounting policies are more fully described in our Annual Report on Form 10-K filed with the SEC on March 11, 2011, we believe that the following accounting policy is the most critical to aid you in fully understanding and evaluating our reported financial results and affect the more significant judgments and estimates that we use in the preparation of our financial statements.

Stock-Based Compensation

We account for stock options according to the Financial Accounting Standards Board Accounting Standards Codification No. 718, "Compensation — Stock Compensation" ("ASC 718"). Under ASC 718, share-based compensation cost is measured at grant date, based on the estimated fair value of the award, and is recognized as expense over the employee's requisite service period on a straight-line basis.

We account for stock options granted to non-employees on a fair value basis using the Black-Scholes option pricing method in accordance with ASC 718. The non-cash charge to operations for non-employee options with vesting are revalued at the end of each reporting period based upon the change in the fair value of the options and amortized to consulting expense over the related vesting period.

For the purpose of valuing options and warrants granted to our employees, non-employees and directors and officers during the three months ended March 31, 2011, we used the Black-Scholes option pricing model. We granted options to purchase an aggregate of 506,000 and 1,581,766 shares of common stock to our employees, non-employees and directors and officers during the three months ended March 31, 2011 and 2010, respectively. To determine the risk-free interest rate, we utilized the U.S. Treasury yield curve in effect at the time of grant with a term consistent with the expected term of our awards. We estimated the expected term of the options granted based on anticipated exercises in future periods assuming the success of our business model as currently forecasted. The expected dividend yield reflects our current and expected future policy for dividends on our common stock. The expected stock price volatility for our stock options was calculated by examining historical volatilities for publicly traded industry peers, although we do not have any trading history for our common stock. We will continue to analyze the expected stock price volatility and expected term assumptions as more historical data for our common stock becomes available. During the first quarter ended March 31, 2011, the Company has experienced forfeitures of options issued to its former CMO and Chairman. Since the stock options currently outstanding are primarily held by our senior management and directors we will continue to evaluate the effects of such future potential forfeitures, as they may arise, to ascertain an estimated forfeiture rate.

Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements.

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

Not applicable.

Item 4. Controls and Procedures.

Evaluation of Disclosure Controls and Procedures

As of the end of the period covered by this report, our management, including our principal executive officer and principal financial officer, evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended ("Exchange Act")). Based on their evaluation of our disclosure controls and procedures, our management, including our principal executive officer and principal financial officer, have concluded that our disclosure controls and procedures were effective as of March 31, 2011 to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is (a) recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms and (b) accumulated and communicated to management, including our principal executive officer and principal financial officer, as appropriate to allow for timely decisions regarding required disclosure.

Changes in Internal Control Over Financial Reporting

During the three months ended March 31, 2011, there were no changes in our internal controls over financial reporting, or in other factors that could significantly affect these controls, that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II
OTHER INFORMATION

Item 1. Legal Proceedings.

None.

Item 1A. Risk Factors.

There are no material changes from the risk factors previously disclosed in our Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 11, 2011.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.

None.

Item 3. Defaults Upon Senior Securities.

None.

Item 4. (Removed and Reserved).

Item 5. Other Information.

None.

Item 6. Exhibits.

The following is a list of exhibits filed as part of this Form 10-Q:

Exhibit Number	Description
31.1	Certification of Principal Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.*
31.2	Certification of Principal Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.*
32.1	Certification of Principal Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.*
32.2	Certification of Principal Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.*

* Filed herewith.

SIGNATURES

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

CORMEDIX INC.

Date: May 9, 2011

By: /s/ John C. Houghton
Name: John C. Houghton
Title: President and Chief Executive Officer
(Principal Executive Officer)

Date: May 9, 2011

By: /s/ Brian Lenz
Name: Brian Lenz
Title: Chief Financial Officer
(Principal Financial and Accounting Officer)

EXHIBIT INDEX

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