

Management's Discussion and Analysis of Financial Condition and Results of Operations

This management discussion and analysis was performed by management using information available as of June 20, 2007 and should be read in conjunction with our audited consolidated financial statements for the year ended March 31, 2007 and the related notes included thereto. These consolidated financial statements are prepared in accordance with Canadian generally accepted accounting principles (Canadian "GAAP"). All amounts are expressed in Canadian dollars unless otherwise indicated. Additional information relating to Pacgen Biopharmaceuticals Corporation (the "Company") can be obtained from SEDAR at www.sedar.com.

The forward-looking statements in this discussion regarding our expectations regarding our future performance, liquidity and capital resources and other non-historical statements in this discussion include numerous risks and uncertainties, as described in the "Risk Factors" section of our Prospectus dated November 28, 2006, which is available on SEDAR at www.sedar.com. The words "anticipates", "believes", "estimates", "expects", "intends", "may", "plans", "projects", "will", "would" and similar expressions are intended to identify forward-looking statements, although not all forward-looking statements contain these identifying words. Our actual results may differ materially from those contained in any forward-looking statements.

OVERVIEW

We are a life sciences company focused on development of novel therapeutics for the treatment of infectious and inflammatory diseases. Our current development efforts are focused on PAC-113, an anti-fungal for the treatment of oral Candidiasis and PAC-G31P, a novel peptide therapeutic designed to treat inflammatory diseases characterized by non-beneficial neutrophil.

Oral Candidiasis, or thrush, is usually seen as a secondary consequence arising from one of a number of primary or underlying medical conditions including HIV/AIDS, cancer, diabetes, asthma and xerostomia (abnormal dryness of the mouth). In February 2005, we completed a sublicense agreement with Demegen, Inc ("Demgem") (the "Demgen Sublicense"). The Demgen Sublicense provides us exclusive worldwide rights to develop and commercialize PAC-113 for human oral disease conditions. PAC-113 is a 12 amino-acid antimicrobial peptide derived from a naturally occurring histatin protein found in saliva. This peptide alters the permeability of fungal cell membranes causing cell death. We are developing PAC-113 in a mouthrinse formulation for the topical treatment of oral Candidiasis. In May 2007, we announced positive topline results from our Phase I/II clinical trial demonstrating that PAC-113 is generally safe, well-tolerated and effective in the treatment of oral Candidiasis. Based on these results, we plan to initiate a Phase IIb study in the second half of 2007.

Non-beneficial neutrophil recruitment is a key characteristic of a number of acute and chronic inflammatory conditions, including acute respiratory distress syndrome, severe asthma, chronic

obstructive pulmonary disease, pneumonia, Crohn's Disease, rheumatoid arthritis and ischemia/reperfusion injury. In April 2006, through acquisition of IL Therapeutics Inc. ("ILT"), we obtained exclusive worldwide rights to PAC-G31P technology for the prevention and treatment of severe inflammatory diseases characterized by neutrophil over-recruitment. We are developing PAC-G31P to treat inflammatory diseases. PAC-G31P is currently in preclinical development with animal studies and formulation work underway. We expect to continue our preclinical work to support filing of an Investigational New Drug application ("IND") and out-licensing initiatives.

We currently hold the rights to 20 patents and 17 patent applications in the United States and other jurisdictions relating to products in our development pipeline, including two other compounds, PAC-525 and PAC-745 that are in our research portfolio. We plan to invest the majority of our efforts and resources to advance PAC-113 through late stage clinical development and complete preclinical studies on PAC-G31P to support an IND and out-licensing initiatives.

CORPORATE DEVELOPMENT SINCE LAST FISCAL YEAR

- On April 4, 2006, we completed the acquisition of all outstanding shares of IL Therapeutics Inc. (the "ILT Acquisition") in exchange for our shares. The acquisition provided us with approximately \$1.5 million working capital and a technology in the prevention and treatment of severe inflammatory diseases characterized with neutrophil over-recruitment. This is the underlying technology of our PAC-G31P program. As ILT was a development stage company

Management's Discussion and Analysis of Financial Condition and Results of Operations

that did not meet the definition of a business under Canadian GAAP, the transaction was accounted for as an asset acquisition, and not as a business combination.

- On April 20, 2006, we announced the appointment of Ms. Christina Yip as Chief Financial Officer ("CFO"). Ms. Yip brings to us over twelve years of financial management experience with publicly listed companies, as well as five years public practice experience with a national accounting and auditing firm. Prior to joining us, Ms. Yip served as Vice President of Finance and Administration to Cardiome Pharma Corp.
- On July 17, 2006, we announced the appointment of Dr. Alan Moore and Mr. Kevin McGarry as our directors. Dr. Moore has over twenty-seven years of drug development and clinical expertise in pharmaceutical and biotechnology industries. Dr. Moore previously served senior management roles at Procter & Gamble and Cardiome Pharma Corp. Dr. Moore is currently the Chief Executive Officer ("CEO") at Stem Cell Therapeutics. Mr. McGarry has an extensive business and financial experience including being a founding partner and CEO of Keystone Technologies Inc which is now absorbed by Western Life Sciences Venture Fund. Mr. McGarry is currently the CEO of Lombard Life Sciences, the General Partner of Western Life Sciences, and interim CEO of Intelligent Hospital Systems.
- On December 7, 2006, we completed our initial public offering (the "IPO") raising gross proceeds of approximately \$7.1 million. Our common shares commenced trading as a Tier 1 issuer on the TSX Venture Exchange on December 11, 2006 under the trading symbol "PGA". Canaccord Capital Corporation acted as lead agent of a syndicate that also included Jennings Capital Inc.
- On February 12, 2007, we announced the appointment of Dr. J. Mark FitzGerald, Dr. William Nauseef, and Dr. Brian Rowe, all world renowned experts in inflammatory diseases, to our scientific advisory board. These experts together with Dr. John Gordon, the inventor of PAC-G31P, and Dr. Neil Reiner, our medical affairs advisor, form an advisory panel to provide input and guidance in the development of PAC-G31P.
- On March 13, 2007, we announced the appointment of Mr. Robert 'Duffy' DuFresne as President and CEO. Mr. DuFresne brings to us over 25 years of experience in the biotechnology, pharmaceutical and medical device industries. Prior to joining us, Mr. DuFresne was President and CEO of Zelos Therapeutics Inc, and previous to that he was President and CEO ConjuChem Inc.
- Subsequent to year-end, on May 7, 2007, we reported the topline results from the Phase I/II study of PAC-113 showing it is generally safe, well-tolerated, and active in the treatment of oral Candida infection with clinical cure rates comparable to the current standard of care. Based on these results, we plan to initiate a Phase IIb study to optimize PAC-113 dose and formulation.

DISCLOSURE CONTROLS AND PROCEDURES AND INTERNAL CONTROLS OVER FINANCIAL REPORTING

The Company maintains a set of disclosure controls and procedures designed to ensure information required to be disclosed in filings made pursuant to Multilateral Instrument 52-109 is recorded, processed, summarized and reported within the time periods specified in the Canadian Securities Administrators' rules and forms. Our President, Chief Executive Officer and Chief Financial Officer have evaluated the effectiveness of our disclosure controls and procedures and concluded that they provide reasonable assurance that material information relating to the Company was made known to them and reported as required.

Our Chief Executive Officer and Chief Financial Officer are also responsible for the design of internal controls required in order to provide reasonable assurance that processes used for preparation of financial statements and financial reporting for external purposes are reliable and in accordance to Canadian GAAP. They have evaluated the design of our internal controls and procedures over financial reporting as of March 31, 2007, and believe the design to provide such reasonable assurance.

CRITICAL ACCOUNTING POLICIES AND SIGNIFICANT ESTIMATES

Our audited consolidated financial statements are prepared in accordance with Canadian GAAP. These accounting principles require us to make certain estimates and assumptions. We believe that the estimates and assumptions upon which we rely are reasonable based upon information available at the time that these estimates and assumptions are made. Actual results could differ from these estimates. Significant areas requiring the use of estimates include the assessment of net recoverable value of technology licenses and rights, determination of share value in transactions where shares are issued as a consideration, assessment of clinical trial expense accruals, estimation of income tax expense and stock-based compensation. The significant accounting policies that we believe are the most critical in fully understanding and evaluating the reported financial results include those which follow:

Intangible Assets

Intangible assets are comprised of purchased technology licenses and rights. Technology licenses and rights, including those acquired in exchange for the issuance of equity instruments by us, are amortized on a straight-line basis over the estimated useful life of the underlying technologies. We determine the estimated useful lives for intangible assets based on a number of factors: legal, regulatory or contractual limitations; known technological advances; anticipated market size; and the existence or absence of competition. A significant change in any of the above factors may require a revision of the expected useful life of the intangible asset,

resulting in accelerated amortization or an impairment charge, which could have a material impact on our results of operations. We evaluate the recoverability of the net book value of our intangible assets whenever events or changes in circumstances indicate the carrying value may not be recoverable. If the carrying value of the underlying technology exceeds the estimated net recoverable value, calculated based on estimated undiscounted future cash flows, then the carrying value is written down to its fair value, based on the related estimated discounted cash flows. The amounts shown for technology licenses and rights do not necessarily reflect present or future values and the ultimate amount recoverable will be dependent upon the successful development and commercialization of products based on these rights.

Accrued Liabilities and Clinical Trial Expenses

We have entered into service agreements with various contract research organizations and other vendors that provide resources, services and expertise that complement our efforts in developing our drug candidates. These agreements may be in force over a number of accounting periods or fiscal years. Since payments under these agreements may not coincide with the period in which the services are rendered, judgment is required in estimating the amount of clinical trial expense to be recorded in each accounting period. Judgment and estimates are also involved in determining the amount of expenditures that are contractually committed under the various agreements. We consider the following factors in estimating the amount of clinical trial expense for an accounting period: the level of patient enrollment; the level of services provided and goods delivered; and the proportion of the overall contracted time that elapsed during the accounting period. In making these assessments, we monitor patient enrollment levels and related activities at a given point in time through internal reviews, correspondence and discussions with contractors and review of contractual terms. We may sometimes rely on the information provided by our contractors. A significant change in the above factors and the accuracy of information provided by our contractors may alter our estimate of our clinical trial expenditure for the accounting period and prepaid expenses or accrued liabilities as of the end of the accounting period. This could have a material impact on our results of operations and liabilities.

Research and Development Costs

Research and development costs consist of direct and indirect expenditures related to our research and development programs. Research and development costs are expensed as incurred unless they meet generally accepted accounting criteria for deferral and amortization. We assess whether these costs have met the relevant criteria for deferral and amortization at each reporting date. No development costs have been deferred to date.

Stock-based Compensation and other stock based payments

All share-based awards is measured and recognized as an expense using a fair value based method. The fair value of stock options is

estimated at the date of grant using the Black-Scholes option pricing model with the subjective assumptions of the expected life of the option, the expected volatility at the time the options are granted, and risk-free interest rate. Changes in these assumptions can materially affect the measure of the estimated fair value of our employee stock options, hence our results of operations. We amortize the fair value of stock options over the vesting terms of the options which are generally two to three years from grant.

Financial Instruments—Recognition and Measurement

In January 2005, the Canadian Institute of Chartered Accountants (“CICA”) released a new Handbook Section 3855, “Financial Instruments—Recognition and Measurement”, effective for annual and interim periods beginning on or after October 1, 2006. This new section establishes standards for the recognition and measurement of all financial instruments, provides and characteristics-based definition of a derivative financial instrument, and provides criteria to be used to determine when a financial instrument is to be extinguished. The Company is reviewing the guidance to determine the potential impact these new standards will have on its financial position and results of operation.

Comprehensive Income and Equity

In January 2005, the CICA released a new Handbook Section 1530, “Comprehensive Income”, and Section 3251, “Equity”, effective for annual and interim periods beginning on or after October 1, 2006. Section 1530 establishes standards for reporting comprehensive income. These standards require that an enterprise present comprehensive income and its components, in a separate financial statement that is displayed with the same prominence as the other financial statements. Section 3251 establishes standards for the presentation of equity and changes in equity during the reporting period. The requirements in Section 3251 are in addition to Section 1530. The Company is reviewing the guidance to determine the potential impact these new standards will have on its financial position and results of operations.

OVERALL FINANCIAL PERFORMANCE

Since we commenced operations in April 2004, we have an accumulated deficit of \$6,572,969 as at March 31, 2007. We have not generated any revenue from sales of commercial products to date and do not expect to generate any revenues until we secure a collaborative partnership or upon sales of our product candidates. We expect losses to continue as we invest in our product development, with primary focus for the next two years on our PAC-113 and PAC-G31P programs. We have funded our operations mainly by net proceeds from equity financings and the cash acquired from the ILT Acquisition. We expect to seek additional funding through public or private equity financing, corporate collaborations and/or licensing arrangements. However, if our research and development activities do not show positive progress, or if capital market conditions in

Management's Discussion and Analysis of Financial Condition and Results of Operations

general or with respect to biopharmaceutical or development stage companies such as ours are unfavorable, our ability to obtain additional funding will be negatively affected.

SELECTED CONSOLIDATED FINANCIAL INFORMATION

The following table sets forth consolidated financial data for the three fiscal periods since inception:

	For the year ended March 31, 2007	For the year ended March 31, 2006	Period from April 23, 2004 (Inception) to March 31 2005
Net loss for the period	\$ (4,353,837)	\$ (1,568,057)	\$ (651,075)
Per share loss, basic and fully diluted	\$ (0.20)	\$ (0.15)	\$ (1.55)
Total assets	\$ 7,834,666	\$ 1,419,348	\$ 1,305,194

RESULTS OF OPERATIONS

For the year ended March 31, 2007 ("Fiscal 2007"), we recorded a net loss of \$4,353,837 (\$0.20 per common share), compared to a net loss of \$1,568,057 (\$0.15 per common share) for the year ended March 31, 2006 ("Fiscal 2006"). The increase in net loss for Fiscal 2007 compared to Fiscal 2006, was largely due to the increased operational expenditures associated with our expanded operations and the adoption of stock option plan. During Fiscal 2007, we expanded our PAC-113 Phase I/II clinical trial to South Africa, acquired a new pre-clinical program, PAC-G31P, and brought the company public. We also added new personnel to support our expanded operations. In addition, following the adoption of a new stock option plan, we started recording for stock based compensation in the third quarter of 2007. The total stock based compensation recorded in Fiscal 2007 was \$580,825.

Revenues

We have not generated any revenue from sales of commercial products since our incorporation and we do not expect to generate any revenues until we secure collaborative partners who provide funding on our research and clinical development or upon sales of our product candidates.

Research and Development Expenditures

Research and development expenses were \$1,987,583 for Fiscal 2007, compared to \$791,778 for Fiscal 2006. The \$1,195,805 increase was primarily due to the clinical development cost associated with the PAC-113 Phase I/II clinical trial which was initiated in the United States in March 2006, and subsequently expanded into South Africa in October 2006. The research cost associated with the newly acquired PAC-G31P program also contributed to the

increased research and development expenditures. Specifically, we incurred higher clinical and pre-clinical research contract cost, consulting fees, patent related expenditures, and salaries and benefits during Fiscal 2007 as compared to Fiscal 2006.

Research and development expenditures for each of our research and development programs for three fiscal periods since inception are as follows:

Projects	For the year ended March 31, 2007	For the year ended March 31, 2006	Period from April 23, 2004 (Inception) to March 31 2005
PAC-113	\$ 1,292,639	\$ 719,056	—
PAC-G31P	\$ 680,464	—	—
Other Projects	\$ 14,480	\$ 72,722	\$ 70,546
	\$ 1,987,583	\$ 791,778	\$ 70,546

For the fiscal year ending March 31, 2008 ("Fiscal 2008"), we expect to incur increased research and development expenditures primarily associated with the ongoing Phase I/II clinical trial and initiation of a Phase IIb trial for our PAC-113 Program, and pre-clinical and formulation work for our PAC-G31P Program.

General and Administration Expenditures

General and administration expenses for Fiscal 2007 were \$1,790,765 compared to \$767,268 for Fiscal 2006. The increase of \$1,023,497 was primarily attributable to the increase of \$399,706 in consulting and professional fees associated with the IPO and business development; the increase of \$333,133 in salaries and wages with the additional of personnel; the increase of \$290,658 in travel and other expenditures to support the expanded operations and commercialization activities.

For Fiscal 2008, we expect our general and administration expenditures to increase in support of our expanded operational activities.

Amortization and Depreciation

Amortization and depreciation was \$242,274 for Fiscal 2007 compared to \$19,520 for Fiscal 2006. The increase of \$222,754 was primarily due to the technology licenses and rights we acquired through the ILT Acquisition. Amortization related to technology, licenses and rights was \$225,474 for Fiscal 2007 compared to \$12,399 for Fiscal 2006. The remaining amortization was related property and equipment.

Stock-based Compensation

Stock based compensation, a non-cash item included in operating expenses, was \$580,825 in Fiscal 2007 compared to nil in Fiscal 2006. The Company adopted a stock option plan in August 2006 and started to record stock based compensation expenditures starting in the third quarter of 2007.

Other

Interest and other income were \$94,610 for Fiscal 2007 compared to \$10,509 for Fiscal 2006. The increase for Fiscal 2007 was primarily due to higher interest rates and higher cash balances.

A net foreign exchange loss of \$5,872 was recorded for Fiscal 2007 compared to \$7,364 for Fiscal 2006. The net foreign exchange losses for the past two fiscal years were mainly from the impact of the depreciation of the U.S. dollar in comparison the Canadian dollar on foreign currency payables. We are exposed to market risk related to currency exchange rates in the United States because the majority of our clinical development expenditures, including majority of those in South African sites, are incurred in United States dollars. To a lesser degree, we are also exposed to market risk related to currency rates in Taiwan with some of basic research and administrative expenditures in Taiwanese new dollars.

SUMMARY OF QUARTERLY RESULTS

Set forth below is the selected consolidated financial data for each of the last eight quarters:

	4th Quarter ended	3rd Quarter ended	2nd Quarter ended	1st Quarter ended
	31-Mar-07	31-Dec-06	30-Sep-06	30-Jun-06
Research and development ⁽¹⁾	\$ (1,146,359)	\$ (459,812)	\$ (212,115)	\$ (169,297)
General and administration ⁽¹⁾	(754,348)	(358,022)	(256,886)	(421,509)
Amortization	(58,516)	(60,871)	(61,881)	(61,006)
Stock based compensation	(166,676)	(414,149)	—	—
Other income	58,343	17,561	12,204	6,502
Future income tax recovery	94,000	16,000	14,000	29,000
Net loss for the period	(1,973,556)	(1,259,293)	(504,678)	(616,310)
Basic and diluted loss per common share	\$ (0.07)	\$ (0.06)	\$ (0.03)	\$ (0.03)

	4th Quarter ended	3rd Quarter ended	2nd Quarter ended	1st Quarter ended
	31-Mar-06	31-Dec-05	30-Sep-05	30-Jun-05
Research and development ⁽¹⁾	\$ (292,431)	\$ (255,630)	\$ (203,227)	\$ (40,490)
General and administration ⁽¹⁾	(200,933)	(274,499)	(131,802)	(160,033)
Amortization ⁽¹⁾	(11,570)	(3,288)	(2,363)	(2,299)
Other income (loss)	1,694	11,195	(10,936)	8,556
Net loss for the period	(503,240)	(522,223)	(348,328)	(194,266)
Basic and diluted loss per common share	\$ (0.03)	\$ (0.03)	\$ (0.05)	\$ (0.08)

(1) Stock based compensation and amortization figures have been presented as separate line items to conform to presentation adopted in the quarter ended March 31, 2007.

Summary of Quarterly Results

The primary factors affecting the magnitude of our losses in the various quarters were (i) research and development costs associated with the PAC-113 program which we in-licensed in February 2005 and started clinical development in March 2006, the PAC-G31P program which we acquired in April 2007; (ii) general and administration expenditures to support our IPO, business development and corporate growth since inception; and (iii) stock based compensation following the adoption of our stock option plan in August 2006.

The significant increase in research and development expenditures for the 4th Quarter of 2007, when compared to other quarters, was due to the cost associated with the PAC-113 Phase I/II clinical trial and our newly acquired PAC-G31P program. The increase in general and administration expenditures 4th Quarter of 2007, when compared to other quarters, was mainly due to increased consulting and professional fees associated with the IPO and business development, added personnel, and other overhead associated with public company entity.

FOURTH QUARTER RESULTS

Net loss for the 4th Quarter of 2007 was \$1,973,556, or \$0.07 per share, compared to net loss of \$503,240, or \$0.03 per share, for the same period in Fiscal 2006. The increase in net loss was largely due to cost associated with the PAC-113 Phase I/II clinical trial, our newly acquired PAC-G31P program, and expanded operations in general.

Research and development costs for the 4th Quarter of 2007 were \$1,146,359, as compared to \$292,431 in the quarter in Fiscal 2006. The increase of \$853,928 was primarily due to the clinical development cost associated with the PAC-113 Phase I/II clinical trial which was initiated in the United States in March 2006, and subsequently expanded into South Africa in October 2006. The research cost associated with the PAC-G31P program acquired in April 2007 also contributed to the increased research and development expenditures. Specifically, we incurred higher clinical and pre-clinical research contract cost, consulting fees, patent related expenditures, and salaries and benefits during 4th Quarter of 2007 as compared to the same quarter in Fiscal 2006. General and administration expenses were \$754,348, as compared to \$200,933 in the same quarter in 2006. The increase of \$553,413 was primarily attributable to the increase of \$146,120 in consulting and professional fees associated with business development and maintenance of a public company entity, the increase of \$218,843 in salaries and wages with the additional of personnel, and the increase of \$188,450 in travel and other expenditures to support the expanded operations and commercialization activities.

Management's Discussion and Analysis of Financial Condition and Results of Operations

LIQUIDITY AND CAPITAL RESOURCES

Sources and Uses of Cash

Since inception to March 31, 2007, our operational activities were financed mainly from equity financings and the cash acquired from ILT Therapeutics Inc.

Cash used in operating activities for Fiscal 2007 was \$3,422,492 compared to \$1,454,087 for Fiscal 2006. Cash used in operating activities was composed of net loss, add-backs or adjustments not involving cash and net change in non-cash working capital items. The increase in cash used in operating activities in Fiscal 2007 as compared to Fiscal 2006 was primarily due to our expanded operational activities.

Cash provided by investing activities in Fiscal 2007 was \$1,143,012 as compared to \$62,485 cash used in investing activities in Fiscal 2006. The primary source of cash provided by investing activities in Fiscal 2007 was the ILT Acquisition. Cash was used in purchases of property and equipment in Fiscal 2007 was \$114,980, an increase of \$102,901 as compared to \$12,079 in Fiscal 2006.

Cash provided by financing activities in Fiscal 2007 was \$6,939,782 compared to \$1,131,593 in Fiscal 2006. The sources of cash provided by financing activities in Fiscal 2007 were net proceeds of \$5,920,137 from our IPO financing and cash receipts of \$1,019,645 from the issuance of common shares upon exercise of share purchase warrants. Cash provided by financing activities in Fiscal 2006 was associated with our private placement financing of our preferred shares.

In connection to our IPO, we issued 6,788,786 units (the "Units") at \$1.05 per unit for total gross proceeds of \$7,128,225. Each unit was comprised of one common share of the Company and one half of one common share purchase warrant. One whole warrant entitled the holder to purchase one common share of the Company at \$1.30 per share until December 7, 2007. We paid a cash commission of \$419,957 and issued 543,102 agent warrants (the "Agents' Warrants") to the underwriting agents (the "Agents"). The fair value of these Agents' Warrants is \$184,655. Each Agents' Warrant is exercisable for one common share of the Company at \$1.05 per share until December 7, 2008. In addition, we also paid the lead underwriting agent an administration fee of \$5,000 and issued 100,000 common shares as corporate finance fees. We incurred professional and other financing cost of \$783,131.

At March 31, 2007, we had working capital of \$5,220,456, compared to \$703,898 at March 31, 2006. We had available cash reserves comprised of cash and cash equivalents of \$5,387,366 at March 31, 2007, compared to \$727,064 at March 31, 2006. We estimate that our working capital at March 31, 2007 is adequate to fund the Company's research and development programs, capital needs and operations for approximately twelve months.

As of March 31, 2007 and in the normal course of business we have obligations to make future payments, representing contracts and other commitments that are known, committed and non-cancelable.

Contractual Obligations payment due by period					
	Total	2008-2009	2010-2011	2012	Thereafter
Operating Leases	\$ 353,770	\$ 203,637	\$ 147,112	\$ 3,021	\$ —
Clinical Research Agreements ⁽¹⁾	2,649,125	2,649,125	—	—	—
License Agreements ⁽²⁾	646,380	115,460	415,460	57,730	57,730
Total	\$3,649,275	\$2,968,222	\$ 562,572	\$ 60,751	\$ 57,730

- (1) The total commitment of \$2,649,125 reflects \$25,815 of commitments that are non-cancelable and \$2,623,310 of commitments that are cancelable should we decide to discontinue the related clinical research work.
- (2) Pursuant to the Demegen Sublicense, we have a commitment to pay minimum annual royalties of US\$50,000 described in Notes 7(a) of our annual consolidated financial statements for the fiscal year ended March 31, 2007. This commitment is converted into Canadian Dollars at the closing rate on March 31, 2007 of CAD\$1.00 = US\$0.8661. Pursuant to the US License, we have a commitment to sponsor \$500,000 for research to be performed at University of Saskatchewan, including, but not necessarily limited to research related to the licenses technology PAC-G31P, within 5 years of the term of the agreement (\$125,000 paid as of March 31, 2007).

OUTSTANDING SHARE CAPITAL

As of May 31, 2007, there were 30,521,960 common shares issued and outstanding, 7,936,401 common share purchase warrants outstanding at a weighted average price of \$1.21 per share, 500,000 share purchase option outstanding at an exercise price of \$2.25 per share, and 2,718,000 incentive stock options outstanding at a weighted average exercise price of \$0.99.

OFF-BALANCE SHEET ARRANGEMENTS

We have no off-balance sheet arrangements.

RELATED PARTY TRANSACTIONS

During Fiscal 2007, we incurred \$48,729, [2006 - \$16,500] for director consulting services, \$114,123 [2006 - \$41,236] for consulting services provided a financial consulting firm which a director is an executive, and \$42,049 [2006 - \$nil] for consulting and laboratory research services provided by an institution which a director is a professor.

FINANCIAL INSTRUMENTS AND RISKS

We are exposed to market risks related to changes in interest rates and foreign currency exchange rates. We invest our cash reserves in fixed rate and highly liquid term deposits. We have not entered into any foreign currency contracts or other financial derivatives to hedge foreign exchange risk. We are subject to foreign exchange rate changes that could have a material effect on future operating results or cash flows.

We believe that our working capital as of March 31, 2007 should be sufficient to finance our operational and capital needs for approximately twelve months. However, our future cash requirements may

vary materially from those expected due to a number of factors, including the costs associated with the completion of the clinical trials, collaborative and license arrangements with third parties, and opportunities to in-license complementary technologies. We will continue to review our financial needs and seek additional financing as required from sources that may include equity financing, and collaborative and licensing arrangements. However, there can be no assurance that such additional funding will be available or if available, whether acceptable terms will be offered.

Management's Responsibility for Financial Reporting

The accompanying consolidated financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles and have been approved by the Board of Directors. The integrity and objectivity of these consolidated financial statements are the responsibility of management.

In addition, management is responsible for all other information in this report and for ensuring that this information is consistent, where appropriate, with the information contained in the consolidated financial statements.

In support of this responsibility, management maintains a system of internal controls to provide reasonable assurance as to the reliability of financial information and the safeguarding of assets. The consolidated financial statements include amounts that are based on the best estimates and judgements of management.

The Board of Directors is responsible for ensuring that management fulfills its responsibility for financial reporting and internal control. The Board of Directors exercises this responsibility principally through the Audit Committee. The Audit Committee consists of three directors not involved in the daily operations of the Company. The Audit Committee meets with management

and the external auditors to satisfy itself that management's responsibilities are properly discharged and to review the consolidated financial statements prior to their presentation to the Board of Directors for approval.

The external auditors, Ernst & Young LLP, conduct an independent examination, in accordance with Canadian generally accepted auditing standards, and express their opinion on the consolidated financial statements. The external auditors have free and full access to the Audit Committee with respect to their findings concerning the fairness of financial reporting and the adequacy of internal controls.



Robert "Duffy" DuFresne
*President and
Chief Executive Officer*



Christina Yip
*Chief Financial Officer
and Corporate Secretary*