

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 July 9, 2009 and should be read in conjunction with our audited consolidated financial statements for the year ended March 31, 2009 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 ("Pacgen" or the "Company") can be obtained from SEDAR at www.sedar.com.

The forward-looking statements in this discussion regarding our expectations of our future performance, liquidity and capital resources and other non-historical statements include numerous risks and uncertainties, as described in the "Risk Factors" section of our Annual Information Form, which is available on SEDAR at www.sedar.com. The words "anticipates", "believes", "estimates", "expects", "intends", "may", "could", "plans", "projects", "will", "would" and similar expressions are intended to identify forward-looking statements, although not all forward-looking statements contain these identifying words. Such statements involve known and unknown risks, uncertainties and other factors that may cause actual results, level of activity, performance or achievements to be materially different from those implied by such statements. Such factors include, among others, our stage of development, lack of product revenues, additional capital requirements, risk associated with completion of clinical trials and obtaining regulatory approval, dependence on collaborative partners, and our ability to protect our intellectual property. We undertake no obligation to revise or update forward looking statement in this discussion whether as a result of new information, future events or otherwise. Accordingly, readers should not place undue reliance on forward looking statements in this discussion.

OVERVIEW

We are a life science technology transfer company focused on the commercial development of novel therapeutic drug candidates up to Phase II, proof of concept efficacy in human. We identify innovative therapeutic drug candidates globally, and develop these drug candidates in accordance to the United States Food and Drug Administration (the "FDA") regulatory standards to feed the product development pipelines of the pharmaceuticals industry. We currently have two product pipelines in our technology portfolio: 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.

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. 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). We obtained our rights to PAC-113 through a sublicense agreement with Demegen, Inc. (the "Demegen Sublicense") in February 2005. The Demegen Sublicense provides us with exclusive worldwide rights to develop and commercialize PAC-113 for human oral disease conditions. Since obtaining these rights, we have completed formulation optimization work, a Phase I/II proof of concept clinical study, as well as a Phase IIb dose-ranging study. The data from our clinical studies demonstrates that PAC-113 is effective in the treatment of oral Candidiasis. The data also suggests that PAC-113 compares favourably to the efficacy demonstrated by Nystatin, a current standard of care. We are currently seeking for a collaborative partner to advance PAC-113 into pivotal Phase II/III clinical development.

PAC-G31P is a small recombinant protein that is a synthetic analogue of the human cytokine called Interleukin-8 which is the key chemokine involved in neutrophil recruitment. We are developing PAC-G31P to treat inflammatory diseases. 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. We obtained exclusive worldwide rights to PAC-G31P technology for the prevention and treatment of severe inflammatory diseases characterized by neutrophil over-recruitment in April 2006, through the acquisition of IL Therapeutics Inc. ("ILT"). Since taking over the PAC-G31P program, we conducted a number of preclinical and mechanistic studies,

and initiated formulation development work. PAC-G31P is currently in preclinical development. We are currently seeking for a joint-venture / co-development partner to conduct preclinical and toxicology studies, as well as manufacturing work necessary to enable a filing of Investigational New Drug application (“IND”) with the FDA.

We currently hold the rights to 29 patents and 32 patent applications in the United States and other jurisdictions relating to products in our development pipeline. We also hold 2 granted patents and 8 patent applications and intellectual properties to two other research compounds that we no longer develop.

CORPORATE DEVELOPMENT SINCE LAST FISCAL YEAR

On June 5, 2008, we released positive topline results from our Phase IIb dose-ranging trial of PAC-113. The results demonstrated that PAC-113 is effective in the treatment of oral Candidiasis and compares favourably to the efficacy demonstrated by Nystatin.

On October 24, 2008, we entered into a letter of intent for a business combination with Medigen Biotechnology Corp. (“Medigen”), a biotech company in Taiwan. In connection with the transaction, we would acquire all of the issued and outstanding shares of Medigen by way of share purchase or through such other transaction structure as may be determined by the mutual agreement of Pacgen and Medigen. In connection with the proposed transaction, Mr. Duffy DuFresne departed Pacgen as our President, CEO and director to pursue other interests.

On October 31, 2008, we appointed Mr. Chung Yu Wang, Chairman and director, as our interim President and Chief Executive Officer and Mr. Kevin McGarry, director, as lead independent director of the Board. These appointments followed the departure of Mr. Duffy DuFresne as President and Chief Executive Officer and director to pursue other interests.

On December 29, 2008, we announced that we have terminated our letter of intent for a business combination with Medigen. In accordance with the letter of intent signed in October 2008, the closing of the proposed business combination was subject to certain terms and conditions, including obtaining necessary approvals to enter into a definitive agreement. The parties determined that, in a share for share exchange transaction, the regulatory requirements in Taiwan would require an issuer to redeem dissenting shareholder interests for cash. Both parties anticipated that this requirement would negatively affect the liquidity and capital resources of the combined company, and that the proposed merger would be a significant undertaking given current financial market conditions. As a result, both parties have mutually elected not to proceed with the signing of a definitive agreement.

On January 30, 2009, we announced that we intended to offer, through one or more tranches of closings of a non-brokered private placement, convertible debentures in an aggregate principal amount of up to approximately \$610,000 (the “Offering”). We closed this Offering in two tranches in February 2009 and March 2009 for an aggregate principal amount of \$614,500.

On March 6, 2009, we finalized our negotiation with a vendor to settle our outstanding account of approximately US\$1.3 million (\$1.65 million). We received a credit note and recovered approximately US\$604,000 (\$747,000) of research and development expenditures from this vendor. For the remaining balance of US\$708,000 (\$893,000), we made an initial payment of US\$128,000 (\$157,000) and agreed to pay the balance of US\$580,000 (\$731,000) by installments. We have been in constant communication with this vendor to keep them apprised of the Company’s developments.

On June 8, 2009, we signed a share purchase agreement with the shareholders of Xphase Pharmaceuticals Inc. (“Xphase”) as part of our efforts to leverage our technology portfolio and enhance our ability to raise capital in the recent global financial market downturn. Xphase, a privately held pharmaceutical company, has the right to acquire the exclusive global rights, excluding China, of AF-05, a novel anti-anxiety drug candidate currently in Phase I clinical trial in China. Xphase also provides consulting and project management services to assist small to medium pharmaceutical and biotechnology companies globally. We obtained regulatory approval to complete the acquisition of Xphase in July 2009. Following the acquisition of Xphase, we have positioned ourselves to become a global life science technology transfer company focused on the commercial development of novel therapeutic drug candidates up to Phase II human proof of concept.

RESEARCH AND DEVELOPMENT UPDATE

PAC-113

During the fiscal year ended March 31, 2009, our development efforts were focused primarily on completing the Phase IIb dose-ranging trial initiated in the preceding fiscal year. In June 2008, we completed and announced results from this clinical trial. The results demonstrated that PAC-113 was effective in the treatment of oral Candidiasis and compared favourably to the efficacy demonstrated by Nystatin, a current standard of care.

The Phase IIb dose-ranging trial involved 223 seropositive HIV patients with oral Candidiasis, and was conducted at sites in the United States and South Africa. The objectives of the trial were to identify an optimal dose of PAC-113 from among the three doses studied, and to determine the relative efficacy of this PAC-113 dose as compared to Nystatin in eliminating clinical signs and symptoms of oral Candidiasis. Additionally, safety and tolerance and the microbiological response of *Candida albicans* to treatment were also measured.

The optimal dose of PAC-113 demonstrated a 34% increase in the primary endpoint efficacy level (complete clinical cure rate at Day 19) for the Per Protocol analysis as compared to Nystatin, and a 50% increase in the corresponding Intent to Treat analysis. Secondary efficacy endpoints showed similar trends among the three PAC-113 doses and the Nystatin group. Results also confirmed that PAC-113 was generally safe and well-tolerated.

The next development milestone is to meet with the FDA to discuss pivotal Phase II/III development plan. We are currently seeking for a partner to collaborate with us to advance PAC-113 into final stage of clinical development and to commercialize the product.

PAC-G31P

During the fiscal year ended March 31, 2009, we conducted certain preclinical studies primarily through our collaboration with the University of Saskatchewan, St. Michael's Hospital and the University of Iowa. The results from these studies provided additional preclinical data to confirm the mechanism of action of PAC-G31P and the potential use of PAC-G31P in different animal models. Due to financial constraints, no large scale study was conducted on PAC-G31P during the fiscal year ended March 31, 2009.

The next development milestone is to conduct necessary studies to enable an IND filing with the FDA. We expect these studies to include preclinical safety and toxicology studies at Good Laboratory Standards ("GLP") level, as well as manufacturing and formulation work at Good Manufacturing Practice Standards ("GMP") level. We are currently seeking for a partner to co-develop PAC-G31P.

SELECTED CONSOLIDATED FINANCIAL INFORMATION

The following table sets forth consolidated financial data for the fiscal years ended March 31, 2009, 2008 and 2007:

	For the year ended March 31,		
	2009	2008	2007
Net loss for the period	\$(2,282,640)	\$(5,974,712)	\$(4,353,837)
Per share loss, basic and fully diluted	\$(0.06)	\$(0.19)	\$(0.20)
Total assets	\$1,676,523	\$3,024,237	\$7,834,666
Long-term liabilities	\$216,459	—	—

RESULTS OF OPERATIONS

For the year ended March 31, 2009 ("Fiscal 2009"), we recorded a net loss of \$2,282,640 (\$0.06 per common share), compared to a net loss of \$5,974,712 (\$0.19 per common share) for the year ended March 31, 2008 ("Fiscal 2008"). The decrease of \$3,777,072 in net loss in Fiscal 2009, as compared to Fiscal 2008, was largely due to a reduction in our operating expenses following our cost control programs and a recovery of research and development expenditures.

The recent global financial market downturn has led to an overall tightening in the credit markets and a substantial reduction in capital available to companies in the development stage. This financial market condition has significantly affected smaller life science technology companies which are generally viewed as higher risk investments. We undertook a comprehensive review of our product development programs, operations and projected cash requirements with the view of conserving cost and deferring cash outflows. During the fiscal year ended March 31, 2009, we implemented further cost reduction programs in addition to those implemented in the preceding fiscal year. We also ceased research and development activities and focused our operations in business development to secure collaborative partners for our technology pipelines and undertook a number of financing initiatives including a small bridge financing and negotiation with our major vendors for defer payments .

Starting in November 2007 in the preceding fiscal year, we eliminated two administrative positions, reduced management salaries by 30% and focused our development efforts primarily on our lead program, PAC-113. A further reduction in management salaries was implemented in February 2008. Following the completion of our Phase IIIb clinical trial of PAC-113 in June 2008, we further reduced our research and development activities and focused our operational activities in financing and business development.

During the quarter ended March 31, 2009, we closed our convertible debenture financing for an aggregate proceed of \$614,500. We also finalized our negotiation with a vendor to settle our outstanding account of approximately US\$1.3 million (\$1.65 million). As part of our negotiation, we received a credit note and recovered approximately US\$604,000 (\$747,000) of research and development expenditures from this vendor and made arrangement to settle the remaining balance of US\$708,000 (\$893,000). Of this amount, we made an initial payment of US\$128,000 (\$157,000) in February 2009 and agreed to pay the balance of US\$580,000 (\$731,000) by installments.

Since we commenced operations in April 2004, we have not generated any revenue from our operations and have accumulated a deficit of \$14,830,321 as at March 31, 2009.. Therefore, we are considered to be in the development stage. As at March 31, 2009, we had \$308,871 of cash and cash equivalents and a working capital deficiency of \$1,023,213. We believe the remaining cash on hand will finance our operations into second half of calendar year 2009. However, given our working capital deficiency as at March 31, 2009, we may be unable to continue to realize our assets and discharge our obligations in the normal course, which cast substantial doubt about our ability to continue as a going concern.

We are currently seeking additional funding to finance our operations and obligations. Management is considering all possible financing alternatives, including equity financing, debt financing, joint-venture, corporate collaboration and licensing arrangement, and has initiated preliminary discussions on some of these alternatives. While we have been successful in securing financings in the past, there can be no assurance that such financing will be materialized or be completed on a timely basis and on favorable terms. If we are unable to obtain additional financing or complete a collaborative transaction, we may have to further scale back our operations, consider business combinations or shut down some or all of our operations.

Our financial statements have been prepared in accordance with generally accepted accounting principles applicable to a going concern, which assumes that we will be able to meet its obligations and continue our operations for the next fiscal year. Realization values may be substantially different from the carrying values as shown and these financial statements which do not give effect to adjustments that would be necessary to the carrying values and classifications of assets and liabilities should we unable to continue as a going concern. If the going concern assumption was not used, adjustments required to report our assets and liabilities, as well as to report on our net loss, on a liquidation basis could be material.

Revenues

We have not generated any revenue from sales of commercial products since our incorporation and we do not expect to generate any revenue 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 for Fiscal 2009 were \$1,451,884 which was further reduced by a recovery from a credit note of a vendor of \$747,214 (approximately US\$604,000) and an underlying accretion of interest of \$118,073 resulting in net expenditures of \$586,597, compared to \$3,480,523 for Fiscal 2008. The decrease in research and development expenditures was primarily due to our reduced development activities for all projects following our comprehensive review. We also eliminated two full-time positions and replaced these positions with one consultant position.

The following provides a summary of the research and development expenditures by programs for the two most recent fiscal years and since inception:

Project	For the year ended March 31, 2009	2008	Cumulative from Inception to March 31, 2009
PAC-113 (2005 – 2009)			
Expense	\$1,154,902	\$2,302,548	\$5,469,146
Recovery	(865,287)	—	(865,287)
	289,615	2,302,548	4,603,859
PAC-G31P (2007 – 2009)	272,306	1,146,834	2,099,603
Other Projects	24,676	31,141	213,565
	\$586,597	\$3,480,523	\$6,917,027

PAC-113

Development expenses for this program decreased by \$1,147,646 in Fiscal 2009 as compared to those in Fiscal 2008. In addition, we recovered \$747,214 associated with the Phase IIB clinical trial as part of our settlement with a vendor. Inclusive of this expense recovery and an underlying accretion of interest of \$118,073, development expenditures incurred for PAC-113 declined by \$2,012,933. The reduced development expenditures was mainly due to the decision, following our comprehensive review, to defer further development of PAC-113 until a collaborative partner is secured. We completed our Phase IIB clinical study in June 2008 and obtained favorable results from this clinical study. Using these results and data accumulated to date, we are seeking for a partner to collaborate with us to advance PAC-113 into final stage of clinical development and to commercialize the product.

The development expenditures in Fiscal 2009 covered primarily the costs associated with wrapping up our Phase IIB study. The development expenditures in Fiscal 2008 included the costs associated with the initiation of the Phase IIB study as well as those linked to the completion of the Phase I/II study. The external cost for the Phase IIB study, which involved 223 patients, was approximately \$2.5 million and was incurred over two fiscal years ended March 31, 2009. The Phase IIB study was initiated in November 2007 and completed in June 2008. The external cost for the Phase I/II study, which involved 107 patients, was approximately \$1.6 million and was spread over three fiscal years ended March 31, 2008. The Phase I/II trial was initiated in March 2006 and completed in May 2007.

For the fiscal year ending March 31, 2010 (“Fiscal 2010”), we expect to incur minimal research and development expenditures for PAC-113 until a collaborative partner is secured. The expected research and development cost is those related stability studies and license maintenance.

PAC-G31P

Research expenditures for PAC-G31P decreased by \$874,528 in Fiscal 2009, as compared to those in Fiscal 2008. As discussed earlier, following the initiation of our cost control program in November 2007, we devoted our research and development efforts primarily on our other program, PAC-113.

Research expenditures in Fiscal 2009 covered primarily the costs related to preclinical studies conducted through our collaborations with the University of Saskatchewan, St. Michael's Hospital and the University of Iowa. Research expenditures in Fiscal 2008 covered primarily the costs associated with preclinical studies conducted through various commercial research organizations, as well as manufacturing and formulation development work.

For Fiscal 2010, we expect to incur minimal research and development expenditures for PAC-G31P until a joint-venture / co-development partner is secured. The expected research and development cost is those related license maintenance.

General and Administration Expenditures

General and administration expenditures for Fiscal 2009 were \$1,052,414, compared to \$1,901,567 for Fiscal 2008. The decrease of \$849,153 was primarily attributable to the implementation of our cost control programs. The following provides a summary of the general and administration expenditures for the two most recent fiscal years and since inception:

General and Administration Expenditures	For the year ended March 31,		Cumulative from
	2009	2008	Inception to March 31, 2009
Salaries and benefits	\$307,808	\$811,353	\$2,440,714
Consulting and professional fees	466,382	539,543	1,823,279
Travel and accommodation	48,202	87,530	337,408
Market research for product candidate	—	125,981	136,149
Other general overhead	230,022	337,160	1,341,832
	<u>\$1,052,414</u>	<u>\$1,901,567</u>	<u>\$6,079,382</u>

In comparative to the same line item in Fiscal 2008:

- Salaries and benefits declined by \$503,545 in Fiscal 2009 as a result of our reduced workforce and management salaries. During Fiscal 2009, we eliminated five full-time positions and replaced these positions with two consultant positions. In addition, on October 31, 2008, we appointed Chairman of our board of directors, Mr. Chung-Yu Wang, to act as our interim President and Chief Executive Officer to oversee our operations. No salary or management fee was paid to Mr. Wang.
- Consulting and professional fees declined by \$73,161 in Fiscal 2009, primarily due to an elimination of all director fees effective February 2008. These cost savings were offset by an increase in professional fees associated with various business development activities including the previously proposed merger with Medigen.
- No market research expenditure was incurred in Fiscal 2009 given the completion of PAC-113 market research in the preceding year.
- The reduced travel and accommodation expenses, as well as reduced general overhead in Fiscal 2009 were due to our cost control programs including sub-letting part of our office facilities.

For Fiscal 2010, we expect our general and administration expenditures to be lower than those incurred in Fiscal 2009. As part of our proposed Xphase acquisition, in addition to 100% equity interest of Xphase, we would receive management and business development services from Xphase principals.

Stock-based Compensation

Stock-based compensation, a non-cash item included in operating expenses, reduced to \$160,687 in Fiscal 2009, compared to \$346,348 in Fiscal 2008. Stock-based compensation attributable to research and development operations and general administration for Fiscal 2009 was \$62,391 [2008 - \$131,702] and \$98,296 [2008 - \$214,646], respectively. The decrease in stock-based compensation was primarily due to the increased number of options forfeited or cancelled, as well as the reduced number of stock options granted during Fiscal 2009 as compared to Fiscal 2008.

Amortization

Amortization was \$263,816 in Fiscal 2009, compared to \$269,245 in Fiscal 2008. Amortization related to technology, licenses and rights was \$236,974 in Fiscal 2009, compared to \$236,975 in Fiscal 2008. The remaining amortization was related to property and equipment.

Other Loss

Other loss in Fiscal 2009 was \$219,126, compared to \$62,029 in Fiscal 2008. The increase of \$157,097 in other loss was mainly due to a decline in interest income by \$55,715 and an increase of foreign exchange loss by \$103,951 in Fiscal 2009, as compared to those in Fiscal 2008. The decrease in interest income was due to lower interest rates and lower cash balances. The increase in net foreign exchange loss was primarily due to the appreciation of the United States dollar, in comparison with the Canadian dollar, on our US denominated retainer payments, accounts payable and accrued liabilities. We are exposed to market risk related to currency exchange rates in the United States because the majority of our clinical development and manufacturing development expenditures are incurred in United States dollars.

SUMMARY OF QUARTERLY RESULTS

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

	4th Quarter Ended March 31, 2009 ("Q4 2009")	3rd Quarter Ended December 31, 2008 ("Q3 2009")	2nd Quarter Ended September 30, 2008 ("Q2 2009")	1st Quarter Ended June 30, 2008 ("Q1 2009")
Research and development	\$(87,804)	\$537,658	\$(155,264)	\$(881,187)
General and administration	(171,039)	(277,673)	(298,815)	(304,887)
Stock based compensation	40,879	(51,410)	(91,346)	(58,810)
Amortization	(64,895)	(66,307)	(66,307)	(66,307)
Other income (loss)	(28,128)	(163,966)	(30,722)	3,690
Future income tax recovery	—	—	—	—
Net loss for the period	(310,987)	(21,698)	(642,454)	(1,307,501)
Basic and diluted loss per common share	\$(0.01)	\$(0.00)	\$(0.02)	\$(0.04)

	4th Quarter Ended March 31, 2008 ("Q4 2008")	3rd Quarter Ended December 31, 2007 ("Q3 2008")	2nd Quarter Ended September 30, 2007 ("Q2 2008")	1st Quarter Ended June 30, 2007 ("Q1 2008")
Research and development	\$(1,071,903)	\$(431,197)	\$(912,203)	\$(1,065,220)
General and administration	(307,439)	(406,920)	(550,878)	(636,330)
Stock based compensation	(119,597)	(68,928)	(71,418)	(86,405)

Amortization	(63,905)	(68,661)	(68,569)	(68,110)
Other income (loss)	(129,095)	(7,358)	28,015	46,409
Future income tax recovery	27,722	12,079	30,199	15,000
Net loss for the period	(1,664,217)	(970,985)	(1,544,854)	(1,794,656)
Basic and diluted loss per common share	\$(0.05)	\$(0.03)	\$(0.05)	\$(0.06)

Summary of Quarterly Results

The primary factors affecting the magnitude of our losses in the various quarters were (i) expenditures associated with our PAC-113 Phase I/II and Phase IIb clinical trials (ii) recovery of part of our Phase IIb clinical expenditures and an underlying accretion of interest, and (iii) the implementation of our cost programs in different stages.

Research and development expenditures were in a declining trend throughout Fiscal 2009 as a result of (i) our decision in November 2007 to focus our development efforts primarily on the completion of PAC-113 Phase IIb clinical study and to scale down of PAC-G31P research and development activities (ii) further reduction in research and development activities following the completion of the Phase IIb study in June 2008, and (iii) a recovery of \$747,214 (approximately US\$604,000) of expenditure associated with PAC-113 Phase IIb in the second half of 2009 and an underlying accretion of interest of \$118,073. General and administration expenditures were also in a declining trend as a result of our cost control programs. The cost control programs in Fiscal 2009 involved (i) elimination of five full-time positions with a replacement of two consultant positions (ii) appointment of Chairman of our board of directors to act as our interim President and Chief Executive Officer, and (iii) elimination of all director fees effective February 2008.

Research and development expenditures were relatively the same throughout the Fiscal 2008 except in Q3 2008. The decline in research and development expenditures in Q3 2008 was primarily due to (i) the reduced development activities for PAC-113 as we prepared to advance this project into Phase IIb and (ii) the completion of PAC-G31P GLP manufacturing development. The significant timelines impacting our research and development cost in Fiscal 2008 were: the completion of PAC-113 Phase I/II clinical trial in May 2007, the completion of PAC-G31P manufacturing development at GLP level in July 2007, and the initiation of PAC-113 Phase IIb trial in November 2007. General and administration expenditures were in a declining trend throughout Fiscal 2008. This was primarily due to (i) one-time expenditures associated with PAC-113 market research in Q1 2008, and (ii) the initiation of our cost control programs in November 2007.

FOURTH QUARTER RESULTS

Net loss for Q4 2009 was \$310,987 (\$0.01 per share), compared to net loss of \$1,664,217 (\$0.05 per share) for Q4 2008. The decrease of \$1,353,230 in net loss was primarily due to a decline of \$1,279,985 in operating expenditures and a decline of \$100,967 in other loss; these were offset by a decline of \$27,722 in future income tax recovery.

Research and development costs for Q4 2009 were \$87,804, compared to \$1,071,903 for Q4 2008. The decrease of \$984,099 was primarily due to the reduced research and development activities following the completion of PAC-113 Phase IIb study and an underlying accretion of interest. As mentioned earlier, as part of our cost control programs, further development on PAC-113 and PAC-G31P would be initiated once collaborative partners or joint-venture partners are secured.

General and administration expenses for Q4 2009 were \$171,039, compared to \$307,439 for Q4 2008. The decrease of \$136,400 was primarily attributable to the implementation of our cost control programs. As compared to the same quarter in the preceding year, we incurred lower salaries and benefits as a result of the reduced internal workforce and the appointment of Chairman of our board as interim CEO arrangement. We also incurred lower professional fees. These cost savings were offset by higher travel and accommodation expenses associated with various business development activities, as well as general overhead.

LIQUIDITY AND CAPITAL RESOURCES

Sources and Uses of Cash

Since inception to March 31, 2009, our operational activities were financed mainly from equity financings, other than the recent issuance of convertible debentures, and the cash acquired from ILT.

Cash used in operating activities for Fiscal 2009 was \$1,740,545, compared to \$4,700,919 for Fiscal 2008. 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 decrease of \$2,960,374 in cash used in operating activities in Fiscal 2009 as compared to Fiscal 2008 was primarily due to the decreased operating loss.

Cash used in investing activities in Fiscal 2009 was \$3,775, compared to \$4,734 of cash provided by investing activities in Fiscal 2008. The increase of cash used in investing activities was primarily due to the one-time leasehold inducement received in Fiscal 2008. Cash used in Fiscal 2009 was composed of costs associated with the Xphase acquisition. Cash provided by the disposal of property and equipment and leasehold inducement was offset by cash used in the purchases of property and equipment in Fiscal 2008.

Cash provided by financing activities in Fiscal 2009 was \$614,500, compared to \$747,510 in Fiscal 2008. Cash provided by financing activities in Fiscal 2009 was associated with our private placement financing of convertible debentures. Cash provided by financing activities in Fiscal 2008 was associated with our private placement financing of units in March 2008.

We closed a private placement of convertible debentures in two tranches in February 2009 and March 2009 for an aggregate principal amount of \$614,500. The convertible debentures will bear interest from the date of issuance at a rate of prime plus 4% per annum and will mature one year from the date of issuance. The principal amount under the convertible debentures plus any accrued interest will be repayable in cash or convertible, at the option of the holder, into units of the Company (the "Units") at a conversion price of \$0.10 per Unit. Each Unit will consist of one common share of the Company (a "Common Share") and one common share purchase warrant (a "Warrant"), each Warrant entitling a non-insider holder to purchase one Common Share at an exercise price of \$0.10 per Common Share at any time prior to 24 months following the date of issuance of the Warrant upon conversion of the convertible debenture. The Warrants comprising the Units issuable upon conversion of convertible debentures issued to insiders of the Company will expire upon the earlier of the maturity date of the convertible debentures and the date that is 24 months following the date of issuance of the Warrants upon conversion of the convertible debentures.

In connection with the private placement financing in March 2008, we closed a private placement of 4,515,003 units (the "Units") at \$0.20 per Unit for total gross proceeds of \$903,000. Each Unit was comprised of one common share of the Company (a "Common Share") and one common share purchase warrant (a "Warrant"). One Warrant entitles the holder to purchase one Common Share at \$0.30 per Common Share until March 16, 2013. In connection with this private placement, we issued 107,730 units as compensation (the "Compensation Units") and 34,200 broker warrants (the "Broker's Warrants") to an agent. Each Compensation Unit was comprised of one Common Share and one Warrant. Each Broker's Warrant is exercisable into one Unit at \$0.22 per Unit until March 16, 2010. Upon exercise, each Broker Warrant will convert to one Common Share and one Warrant exercisable into one additional Common Share at \$0.30 per Common Share until March 16, 2013. The Compensation Units and Broker's Warrants have an estimated value of \$40,960.

At March 31, 2009, we had a negative working capital of \$1,023,213, compared to a working capital of \$535,149 at March 31, 2008. We had available cash reserves comprised of cash and cash equivalents of \$308,871 at March 31, 2009, compared to \$1,438,691 at March 31, 2008. We estimate that our cash reserves at March 31, 2009 is adequate to fund our operations and capital needs into the second half of calendar year 2009.

As of March 31, 2009 and in the normal course of business we have obligations to make future payments, representing contracts and other commitments that are known, committed, cancellable and non-cancellable.

	Contractual Obligations payment due by period				
	Total	2010	2011-2012	2013-2014	Thereafter
Operating Leases	\$157,363	\$101,372	\$55,991	—	—
Clinical Research Agreements ⁽¹⁾	2,923,950	2,923,950	—	—	—
License Agreements ⁽²⁾	484,294	168,969	126,130	126,130	63,065
Total	\$3,565,607	\$3,314,887	\$182,121	\$126,130	\$63,065

⁽¹⁾ The total commitment of \$2,923,950 reflects \$490,966 of commitments that are non-cancellable and \$2,432,984 of commitments that are cancellable 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 *note 9(a)* of our annual consolidated financial statements for the fiscal year ended March 31, 2009. This commitment is converted into Canadian Dollars at the closing rate on March 31, 2009 of CAD\$1.00 = US\$0.7928. Pursuant to a license agreement between ILT and the University of Saskatchewan (the “US License”), we have a commitment to sponsor \$500,000 for research to be performed at the University of Saskatchewan, including, but not necessarily limited to, research related to the licensed technology PAC-G31P, within 5 years of the term of the agreement (\$334,097 has been paid as of March 31, 2009).

OUTSTANDING SHARE CAPITAL

As of June 30, 2009, there were 35,144,693 common shares issued and outstanding, 4,656,933 common share purchase warrants outstanding at a weighted average exercise price of \$0.30 per common share, and 1,403,333 incentive stock options outstanding at a weighted average exercise price of \$0.99.

OFF-BALANCE SHEET ARRANGMENTS

We have no off-balance sheet arrangements.

RELATED PARTY TRANSACTIONS

During Fiscal 2009, we incurred \$503 [2008 - \$3,186] for consulting services provided by directors, \$nil [2008 - \$1,000] for research services provided by a consulting firm of which a director is the principal; \$nil [2008 - \$120,988] for research services provided by a consulting firm of which an officer is the principal; and \$nil [2008 - \$5,645] for research services provided by a university laboratory of which an officer is a professor.

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 relate to the assessment for impairment and useful lives of intangible assets, determination of share value in transactions where shares are issued as a consideration, accrued liabilities, estimation of income tax expense and determination of fair value of 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 technology licenses and rights acquired from third parties. Technology licenses and rights are initially recorded at the fair value based on consideration paid and are amortized on a straight-line basis over the estimated useful lives 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.

Research and Development Costs

Research costs, including costs for new patents and patent applications, are expensed in the period in which they are incurred. Development costs are expensed in the period in which they are incurred unless such development costs meet the criteria under Canadian GAAP for deferral and amortization. No development cost has been deferred to date.

Contract research and development expenses, including fees paid to contract research organizations, investigators and other vendors who conduct certain product development activities on our behalf, are recognized in an accounting period based on estimates of the work performed during the period using an accrual basis of accounting. Since the service agreements with these vendors may be in force over a number of accounting periods and payments may not coincide with the period in which the services are rendered, judgment is required in estimating the amount of research and development 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 enrolment; 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 enrolment 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 accrued liabilities.

Amounts advanced to third parties in connection with planned future research and development activities are deferred as prepaid expenses and are expensed as research and development costs based on estimates of the activities.

Stock-based Compensation and other stock-based payments

We grant stock options to employees, directors, and consultants pursuant to a stock option plan. We use the fair value method to account for all stock-based awards granted, modified or settled, and the Black-Scholes option pricing model to determine the fair value of stock options granted. A compensation expense is recorded based on the estimated fair value of options with a corresponding credit to contributed surplus. Any consideration received on the exercise of stock options is credited to share capital. The fair value of stock-based awards to employees and directors is measured on the date of grant and amortized over the vesting period. The fair value of stock-based awards to consultants is measured at the performance commitment date or the date that the service is delivered. We amortize the fair value of stock options over the vesting terms of the options which are generally two to three years from grant.

The estimation of the fair value of stock options using the Black-Scholes option pricing model involves subjective assumptions of the expected life of the option, the expected volatility at the time the options are granted, and the risk-free interest rate. Changes in these assumptions can materially affect the measure of the estimated fair value of our stock options, hence our results of operations.

CHANGE OF ACCOUNTING POLICIES

General Standards of Financial Statement Presentations

In May 2007, the Canadian Accounting Standards Board (the “AcSB”) amended CICA Handbook Section 1400, “General Standards of Financial Statement Presentation”, to change the guidance related to management’s responsibility to assess the ability of the entity to continue as a going concern.

The main features of the changes are as follows:

- (i) management is required to make an assessment of an entity’s ability to continue as a going concern;
- (ii) in making its assessment, management takes into account all available information about the future, which is at least, but is not limited to, twelve months from the balance sheet date;
- (iii) financial statements must be prepared on a going concern basis unless management either intends to liquidate the entity, to cease trading or cease operations, or has no realistic alternative but to do so;
- (iv) disclosure is required of material uncertainties related to events or conditions that may cast significant doubt upon the entity’s ability to continue as a going concern; and
- (v) when financial statements are not prepared on a going concern basis, that fact should be disclosed, together with the basis on which the financial statements are prepared and the reason the entity is not regarded as a going concern.

This section became effective for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2008. We adopted these standards commencing April 1, 2008. The new disclosure requirements pertaining to this section are contained in *note 1* of our consolidated financial statements.

Capital Disclosures

The AcSB issued Section 1535, “Capital Disclosures”. This section establishes standards for disclosing information about an entity’s capital and how it is managed in order that a user of the financial statements may evaluate the entity’s objectives, policies and processes for managing capital. This section became effective for interim and annual financial statements relating to fiscal years beginning on or after October 1, 2007. We adopted these standards commencing April 1, 2008. The adoption of these new standards did not have a material impact on our consolidated financial statements. The new disclosure requirements pertaining to this section are contained in *note 4* of our audited annual consolidated financial statements.

Financial Instruments – Disclosure and Presentation

The AcSB issued two new sections in relation to financial instruments: Section 3862, “Financial Instruments – Disclosure” and Section 3863, “Financial Instruments – Presentation”. The new disclosure standard increases the emphasis on the risks associated with both recognized and unrecognized financial instruments and how these risks are managed. The new presentation standard carries forward the former presentation requirements. Both sections became effective for interim and annual financial statements relating to fiscal years beginning on or after October 1, 2007. We adopted these standards commencing April 1, 2008. The adoption of these new standards did not have a material impact on our consolidated financial statements. The new disclosure requirements pertaining to these sections are contained in *note 5* of our audited annual consolidated financial statements.

New Accounting Pronouncements

In February 2008, the AcSB confirmed that Canadian GAAP for public companies will be converged with International Financial Reporting Standards (“IFRS”) for accounting periods commencing on or after January 1, 2011. IFRS uses a conceptual framework similar to Canadian GAAP, but there are some significant differences on recognition, measurement and disclosures. We will be required to report under IFRS for interim and annual financial statements beginning April 1, 2011 and provide IFRS comparative figures for the preceding fiscal year, including an opening balance sheet as at April 1, 2010. We are currently planning for the conversion to IFRS and conducting a high-level preliminary assessment of the differences between Canadian GAAP and IFRS and the potential impact of IFRS to our financial reporting systems and processes.

In February 2008, the CICA issued Section 3064, “Goodwill and Intangible Assets”, which replaces Section 3062, “Goodwill and Other Intangible Assets” and Section 3450, “Research and Development Costs”. Various changes have been made to other sections of the CICA Handbook for consistency purposes. Section 3064 establishes standards for the recognition, measurement, presentation and disclosure of goodwill subsequent to its initial recognition and of intangible assets. The new section will be applicable to our consolidated financial statements beginning April 1, 2009. We are evaluating the impact of the adoption of this new section on our consolidated financial statements and currently expect no significant impact from this adoption.

In January 2009, the CICA issued Section 1601 “*Consolidations*” and Section 1602 “*Non-controlling Interests*”. Section 1601 establishes standards for the preparation of consolidated financial statements. Section 1602 establishes standards for accounting for a non-controlling interest in a subsidiary in consolidated financial statements subsequent to a business combination. These standards are applicable to our interim and annual financial statements beginning April 1, 2011. We are in the process of evaluating the impact of these standards.

In January 2009, the CICA issued Section 1582 “*Business Combinations*” replacing Section 1581 “*Business Combinations*”. The new section improves the relevance, reliability and comparability of the information that a reporting entity provides in its financial statements about a business combination and its effects. The section is applicable to our annual and interim financial statements beginning April 1, 2011, with early adoption permitted. We are in the process of evaluating the impact of this standard.

In January 2009, the CICA issued EIC 173 “*Credit Risk and the Fair Value of Financial Assets and Financial Liabilities*”. This guidance requires that an entity's own credit risk and the credit risk of the counterparty be taken into account in determining the fair value of financial assets and financial liabilities including derivative instruments. This guidance is applicable to our annual and interim financial statements beginning April 1, 2009 with retrospective application without restatement of prior periods. We are in the process of evaluating the impact of this new guidance.

RISKS AND UNCERTAINTIES

Due to the inherent nature of our business, investing in our securities involves a high degree of risk and uncertainties. Such risk factors include, among others, our stage of development, lack of product revenues, additional capital requirements, risk associated with completion of clinical trials and obtaining regulatory approval, lack of collaborative partners at this time, dependence on collaborative partners to develop and commercialize our products once partners are secured, our ability to protect our intellectual property and our ability to stay competitive in a rapid changing industry environment.

We are in the early stage of development and have limited operating history. We have not generated any revenues to date from product sales, nor do we expect any product revenues for the immediate future. To achieve profitable operations, we must successfully develop our products that are currently in the research and development phase on our own or with collaborative partners. These product developments may take a number of years and involve significant risks and uncertainties. As a result, we require substantial additional capital to finance our product developments.

We are currently seeking additional capital to finance our operations. Management is considering all financing alternatives, including equity financing, debt arrangement, merger and acquisition, corporate collaboration and licensing arrangement, and has engaged in discussions with multiple parties on some of these alternatives. There can be no assurance that such financing will materialize on a timely basis or obtained on favorable terms. If we are unable to obtain additional financing, we may be required to curtail or discontinue our operations.

We are exposed to credit risk, interest rate risk, currency risk and liquidity risk as described in *note 5* in our audited consolidated financial statements. We are also subject to other significant risks and uncertainties listed in the section entitled “Risk Factors” in our Annual Information Form dated July 31, 2008.